TO:	**CHAIR AND MEMBERS CORPORATE SERVICES COMMITTEE MEETING ON OCTOBER 19, 2020**
FROM:	**ANNA LISA BARBON MANAGING DIRECTOR, CORPORATE SERVICES AND CITY TREASURER, CHIEF FINANCIAL OFFICER**
SUBJECT:	**CITY OF LONDON'S CREDIT RATING**

RECOMMENDATION

That, on the recommendation of the Managing Director, Corporate Services and City Treasurer, Chief Financial Officer, the City of London's Credit Rating Report, providing a summary of Moody's Investors Service Credit Opinion of the City of London, **BE RECEIVED** for information.

LINK TO 2019-2023 STRATEGIC PLAN

Council's 2019-2023 Strategic Plan for the City of London (the "City") identifies "Leading in Public Service" as a strategic area of focus. Continuing to ensure the strength and sustainability of London's finances is a strategy to maintain London's finances in a well-planned manner to balance equity and affordability over the long term. The City's adherence to financial policies and practices has helped the City maintain positive operating results, stable debt levels, and strong liquidity, reflected in the credit rating assigned by Moody's.

BACKGROUND

Moody's Investors Service (Moody's) is a leading provider of credit ratings, research, and risk analysis. The firm's ratings and analysis track debt covering more than 130 countries, 11,000 corporate issuers, 21,000 public finance issuers and 76,000 structured finance obligations. Typically, Moody's reviews the credit worthiness of the City of London annually and then assigns the City a credit rating.

The rating process involved a review of the City's 2019 Financial Statements, 2019 Financial Information Return, approved 2020-2023 Multi-Year Budget and recent relevant reports to Council (e.g. Budget Monitoring Reports). Moody's also utilizes independent research from a variety of sources such as Statistics Canada, comparisons with other municipalities, and news from local media. Along with reviewing and analyzing documents, Moody's arranges a site visit to the City and interviews with senior management and the Mayor.

The credit opinion of the City published September 30, 2020 from Moody's is attached to this report. Consistent with prior years, the City has maintained its Aaa credit rating with a stable outlook. The City has held the Aaa rating since 1977, making 2020 the 44th consecutive year of the Aaa rating and reaffirming that the City's debt has the highest rating possible. The Aaa rating was integral in securing buyers for the City's debentures on June 5, 2020 at favourable interest rates ($36 million at an average all-in-rate of 1.673% over a ten-year term). The stable outlook reflects Moody's expectation *"that liquidity will remain strong and debt will remain at the current low levels. While the coronavirus pandemic will weaken operating results in 2020, this is not expected to result in a material multi-year change in the City's ability to post strong positive operating balances."*

The Moody's Credit Opinion Report summarizes the City's credit strengths and challenges. The City's credit strengths include;

1. High levels of cash and investments providing strong liquidity;
2. Low debt levels supported by conservative debt management practices;
3. Mature, supportive, institutional framework governing municipalities in Ontario; and
4. Track record of generating positive fiscal outcomes highlights robustness of fiscal planning

Moody's comments regarding the City's track record of generating positive fiscal outcomes are as follows:

"…the City of London displays strong governance and management practices, such as the application of multi-year budgets, which helps promote stable operations. London's history of posting positive operating results, application of strict controls on debt issuance, and conservative debt and investment policies which limit their exposure to market related risks and help ensure relatively smooth debt servicing costs all act as evidence of the city's strong management and governance."

The comments provided by Moody's in their review of the City of London's credit rating further supports the strategy taken by Council to ensure the strength and sustainability of London's finances. The application of multi-year budgeting signifies that the City is looking beyond a short term focus when planning its finances. The City's multi-year budget provides alignment of longer-term goals with longer-term funding plans, improved accountability and transparency over spending changes. Taking a long-term view with respect to financial matters has led to fiscally responsible decisions, as reflected in the City's credit rating.

While the City continues to maintain its strong fiscal performance, one credit challenge that Moody's mentions is the potential for near term fiscal pressures including the coronavirus pandemic and provincial funding changes. Moody's states that *"although London will receive additional funds from both the provincial and federal government to offset additional budget pressure, the City will continue to face budget pressure throughout the pandemic."*

Moody's also states that a sustained loss of fiscal discipline leading to a material increase in debt or a substantial reduction in accessible financial reserves could place downward pressure on the City's credit rating. A credit rating downgrade or change in outlook to negative by Moody's would cause investors to lose confidence in the quality of the City's debt and financial management practices, affecting the City's ability to raise future financing. This would also increase interest rates at which the City issues debt, which would increase debt servicing costs for the City.

CONCLUSION

The City's achievement of the Aaa credit rating for 44 consecutive years is a testament to the success of the City's prudent, conservative approach to fiscal planning.

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Attachment - City of London's Credit Opinion Report by Moody's Investors Service

Cc: Ian Collins, Director, Financial Services
Sharon Swance, Manager, Accounting

MOODY'S
INVESTORS SERVICE

CREDIT OPINION
30 September 2020

Update

Rate this Research

RATINGS

London, City of

Domicile	London, Ontario, Canada
Long Term Rating	Aaa
Type	Senior Unsecured - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Japan	81-3-5408-4100
EMEA	44-20-7772-5454

City of London (Canada)

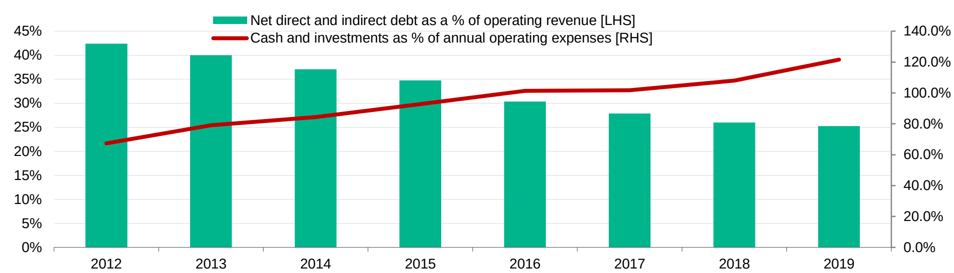
Update to credit analysis

Summary

The credit profile of the City of London (Aaa stable) reflects the strong protection to bondholders stemming from a relatively low debt burden, low interest expense and sizeable levels of reserves relative to outstanding debt. Through an increased use of reserves and decreased reliance on debt issuance to fund capital projects, London's net direct and indirect debt relative to operating revenue has steadily fallen from 42.4% in 2012 to 25.2% in 2019. Concurrently, the city's holdings of cash and investments, including those to be used for financing capital projects in lieu of debt, has increased to 3.8x net debt and 1.2x operating expenses as of December 31, 2019. The rating also reflects the city's strong track record of achieving positive operating results and the generation of internal financing for capital expenditures.

Exhibit 1

Recent improvements in the city's debt burden and reserves will provide support to London's credit profile should fiscal challenges arise



Source: Moody's Investors Service, City of London financial statements

Credit strengths

» High levels of cash and investments provide strong liquidity

» Low debt levels supported by conservative debt management practices

» Mature, supportive, institutional framework governing municipalities in Ontario

» Track record of generating positive fiscal outcomes highlights robustness of fiscal planning

Credit challenges

» Near-term fiscal pressures including the coronavirus pandemic, ambitious council agenda and provincial funding changes will impact operating balances

Rating outlook

The outlook for London's Aaa debt rating is stable, reflecting our expectation that liquidity will remain strong, debt will continue to remain at the current low levels. While the coronavirus pandemic will weaken operating results in 2020, this is not expected to result in a material multi-year change in the city's ability to post strong positive operating balances.

Factors that could lead to a downgrade

Downward pressure could arise if the city were to experience a sustained loss of fiscal discipline leading to a material increase in debt or substantial reduction in accessible financial reserves.

Key indicators

Exhibit 2

London, City of

(Year Ending 12/31)	2015	2016	2017	2018	2019
Net Direct and Indirect Debt/Operating Revenue (%)	34.8	30.4	27.8	26.0	25.2
Gross Operating Balance/Operating Revenue (%)	18.1	22.4	21.2	21.2	21.2
Cash Financing Surplus (Requirement)/Total Revenue (%)	7.4	8.6	6.2	8.2	13.2
Interest Payments/Operating Revenue (%)	1.0	0.9	0.8	0.8	0.7
Debt Service/Total Revenue (%)	5.2	5.3	5.0	4.6	4.7
Capital Spending/Total Expenditures (%)	19.8	24.8	25.5	21.7	19.1
Self-Financing Ratio	1.4	1.4	1.3	1.5	1.8

Source: Moody's Investors Service, City of London financial statements

Detailed credit considerations

The City of London's Aaa rating combines (1) a baseline credit assessment (BCA) of aaa, and (2) a high likelihood of extraordinary support coming from the Province of Ontario (Aa3 stable) in the event London faced acute liquidity stress.

Baseline credit assessment

High levels of cash and investments provide strong liquidity

London's credit profile is supported by a strong liquidity position which provides a significant measure of safety for bondholders. In 2019 the city's cash and investments were equal to 3.8x net debt and 1.2x annual operating expenses. These levels represent a transformational shift in the manner in which the city views its debt and reserves which has taken place consistently over a number of different municipal councils. These metrics have risen to their current levels from 0.47x net direct and indirect debt and only 0.3x operating expenses in 2005, highlighting the continued adherence to prudent fiscal management and liquidity strength that London possesses.

The city's cash and reserve holdings will remain healthy even as the city moves forward with the construction of three of five budgeted rapid transit components and related transit supportive capital works totaling CAD375 million, of which the city is expected to fund CAD148 million from property tax supported sources and development charges. The remaining funding contributions have been approved by both the Canadian and Ontario governments.

London's investment policies ensure that the city minimizes credit risk and maintains liquidity of its investment portfolio. The city's policies outline various limits placed on investment decisions, such as limiting the concentration of investments in specific sectors or issuers, limiting investments to only highly rated securities and ensuring a variety of maturities. The presence and adherence to these policies offers reassurance that the city's investment management policies provide security to liquidity, which along with the level of liquidity, is a strong credit positive.

Low debt levels supported by conservative debt management practices

London's net direct and indirect debt expressed as a percentage of operating revenues measured 25.2% in 2019. While Canadian municipalities can only issue debt for capital reasons, this is nonetheless a low level relative to domestic peers as Canadian municipalities' revenue structure and high level of operating expense tend to not favour funding capital needs from operations. The low debt burden is propelled by the conservative debt policies that the city employs such as a self-imposed "debt cap" which limits the amount of debt that can be issued for capital projects as well as the move to a greater reliance on pay-as-you-go financing. Debt issuance is also reduced through the use of multiple policies overseeing the use of excess funds at year end: the city applies all year-end debt service savings, 50% of unallocated assessment growth as well as 50% of any operating surplus that it generates towards financing needs that would have otherwise be funded from authorized debt issuance. The city also has a target to eliminate debt for life cycle maintenance by 2022, a target which is expected to be achieved and remains unchanged even in the face of the coronavirus pandemic.

The low debt burden also translates into a relatively low interest expense. In 2019, interest expense consumed only 0.7% of operating revenues. Given the efforts to minimize debt issuance, the city's debt service costs as a percentage of revenue are expected to remain low in the intermediate term.

Mature, supportive institutional framework governing municipalities in Ontario

The institutional framework governing municipalities in Ontario is mature and highly developed. The division of roles and responsibilities between the province and municipalities is clearly articulated. Historically, changes to the institutional framework have occurred at a measured, evolutionary pace, following discussions between both parties. Nevertheless, in certain cases, changes have occurred more rapidly.

London's creditworthiness benefits from the stability inherent in the provincial institutional framework. Provincial legislation dictates a high degree of oversight, including limits on debt servicing costs, while policy flexibility, on both the revenue and expenditure sides of the ledger, helps London to manage pressures as they arise.

Track record of generating positive fiscal outcomes highlights robustness of fiscal planning

Similar to other highly rated Ontario municipalities, the City of London displays strong governance and management practices, such as the application of multi-year budgets, which helps to promote stable operations. London's history of posting positive operating results, application of strict controls on debt issuance, and conservative debt and investment policies which limit their exposure to market related risks and help ensure relatively smooth debt servicing costs all act as evidence of the city's strong management and governance.

The city manages its plans using a four-year budget that is prepared during the first year of a new council and extends into the first year of the following council period. Through this process, annual departmental expenditures for the four years are determined in the initial budget year, and in theory only expenditures that are supported through additional assessment growth can be passed outside of the initial budget. City Council can still raise property taxes above the four-year planned approved rates as part of the annual budget review process. This approach successfully allowed the city to maintain strong operating outcomes, posting gross operating balances averaging 21.5% of operating revenues over the 2016-2019 four-year budget plan.

Near-term fiscal pressures including the coronavirus pandemic, ambitious council agenda and changes to provincial funding levels will impact operating balances

While we anticipate that the city will continue to post positive operating outcomes, a number of challenges will result in these outcomes being lower than that recently recorded.

As with all Canadian municipalities, London faces fiscal pressure from the onset of the coronavirus pandemic which has led to lower operating revenue, primarily from user fees and fines, and higher costs to accommodate the increased need for health and safety protection of workers and service delivery. The largest single source of financial pressure is from the city's public transit network, which faces lower ridership levels, and therefore lower fare revenue, but concurrently needs to continue to offer a relatively high level of service to promote both social distancing and to ensure reliable service to those customers dependent on public transit for their mobility needs. Although London will receive additional funds from both the provincial and federal government to offset additional budget pressure, the city will continue to face budget pressure throughout the duration of the pandemic.

Adding to the fiscal challenge facing the city, London's 2020-2023 budget includes a number of new initiatives which will increase permanently the level of service provided by the city. To help fund these initiatives, along with the need to offset funding changes introduced by the province, the property tax levy is expected to increase annually by an average 3.9% over the 2020-2023 budget plan, with the planned increase in 2021 reaching 4.5%. This is relatively high currently for Canadian municipalities which have typically focused on keeping property tax levy increases at or below the level of inflation (2%). With the onset of the coronavirus pandemic and related negative impacts on the economy, the ability to move forward with these tax increases may be pressured. However, once the new initiatives are implemented, they will result in a permanent addition to spending of the city and will need to be supported by ongoing revenue generation, which will further limit the ability of the city to lower tax rate increases in the future.

The Province of Ontario announced in its 2019/20 Budget that it would reduce transfers to municipalities for a variety of programs as the province faces material deficits and seeks to reduce its spending. Although some changes have been delayed and the onset of the coronavirus pandemic is leading to further uncertainty on timing of further proposed measures, London is well positioned to accommodate these reductions, they do nonetheless impose a fiscal burden on the city.

Ontario's changes primarily relate to cost-sharing arrangements between the province and municipalities. These changes either directly reduce funds for municipalities or require municipalities to increase their share of funding commitments for programs which have mandated service levels. In some cases, such as the regionalization of ambulance services, London may find that its ability to control costs are reduced as it will share service delivery with a larger number of partners and therefore face increased considerations on services that are offered. Reductions to capital funds and the cancelation of a previously planned doubling of the provincial gas tax directed to municipalities are also among items that have been impacted.

Furthermore, the province passed legislation that will delay the amount of funds municipalities can raise via development charges (fees that housing developers are mandated to pay to help fund growth related and community services). This will likely impact the timing and level of debt requirements for London in the short and medium-term, although the long-term impact should be broadly neutral.

Extraordinary support considerations

Moody's assigns a high likelihood of extraordinary support from the Province of Ontario (Aa3 stable), reflecting Moody's assessment of the incentive provided to the provincial government of minimizing the risk of potential disruptions to capital markets if London, or any other Ontario municipality, were to default.

ESG considerations

How environmental, social and governance risks inform our credit analysis of the City of London

Moody's takes into account the impact of environmental (E), social (S) and governance (G) factors when assessing sub-sovereign issuers' economic and financial strength. In the case of the City of London, we assess the materiality of ESG to the credit profile as follows:

Environmental considerations are not material to the credit profile and the risk is therefore low. Neither the city's infrastructure nor economic base are subject to material risks stemming from environmental concerns. As such, both spending and revenue are not expected to be impacted by environmental changes at this time.

Social considerations are not material to the credit profile and the risk is therefore low. The city provides key public services such as public safety (police, fire and paramedic) and environmental (water and waste collection), but these services do not face material social risks given the stable population levels and predictable demographic trends which allows for long-term forecasting of such service requirements. We view the coronavirus as a social risk given the substantial implications for public health and safety, but primary health care is not the responsibility of municipalities in Canada. While the city will face fiscal challenges over lost revenue and higher spending associated with the coronavirus pandemic, the city's overall financial strength and governance will minimize any risk.

Governance is considered quite important and London provides for strong governance characteristics resulting in low risk. The city utilizes prudent financing planning, including the establishment of a 4-year budget plan, and makes use of forward looking assumptions which provides the city with the ability to identify potential pressures and allows for sufficient time to adjust plans accordingly to mitigate any credit implications. The city provides transparent, timely financial reports and adheres to strict policies on debt and investment management.

Further details are provided in the "Detailed credit considerations" section above. Our approach to ESG is explained in our cross-sector methodology General Principles for Assessing Environmental, Social and Governance Risks.

Rating methodology and scorecard factors

In the case of London, the BCA of aaa assigned by the rating committee is close to the scorecard-indicated outcome of aa1. The scorecard-indicated outcome reflects (1) an idiosyncratic risk score of 2 (presented below) on a 1 to 9 scale, where 1 represents the strongest relative credit quality and 9 the weakest; and (2) a systemic risk score of Aaa, as reflected in the sovereign bond rating (Aaa stable).

For details of our rating approach, please refer to the methodology Regional and Local Governments, 16 January 2018

Exhibit 3

London, City of

Baseline Credit Assessment	Score	Value	Sub-factor Weighting	Sub-factor Total	Factor Weighting	Total
Scorecard						
Factor 1: Economic Fundamentals						
Economic strength	5	98.56	70%	3.8	20%	0.76
Economic volatility	1		30%			
Factor 2: Institutional Framework						
Legislative background	1		50%	1	20%	0.20
Financial flexibility	1		50%			
Factor 3: Financial Performance and Debt Profile						
Gross operating balance / operating revenues (%)	1	21.20	12.5%	1.5	30%	0.45
Interest payments / operating revenues (%)	1	0.75	12.5%			
Liquidity	1		25%			
Net direct and indirect debt / operating revenues (%)	1	25.40	25%			
Short-term direct debt / total direct debt (%)	3	17.90	25%			
Factor 4: Governance and Management - MAX						
Risk controls and financial management	1			1	30%	0.30
Investment and debt management	1					
Transparency and disclosure	1					
Idiosyncratic Risk Assessment						**1.71(2)**
Systemic Risk Assessment						**Aaa**
Suggested BCA						**aa1**

Source: Moody's Investors Service, City of London

Ratings

Exhibit 4

Category	Moody's Rating
LONDON, CITY OF	
Outlook	Stable
Senior Unsecured -Dom Curr	Aaa

Source: Moody's Investors Service

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