Research Update:

City of Greater Sudbury 'AA+' Ratings Affirmed; Outlook Is Stable

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Overview

- We expect the City of Greater Sudbury's reliance on debt to fund its large capital plan will increase and peak in 2026; we also expect this will raise the city's after-capital deficits over the next two years.
- That said, we expect the city's operating surpluses will remain healthy owing to the expanding property tax base and user fee revenues.
- S&P Global Ratings affirmed its 'AA+' long-term issuer credit and senior unsecured debt ratings on Sudbury.
- The stable outlook reflects our expectation that in the next two years, although the city will continue to generate healthy operating surpluses, advancements in its large capital program will result in high after-capital deficits, but that these will correct after 2026 with a decline in the debt burden.

Rating Action

On Sept. 10, 2024, S&P Global Ratings affirmed its 'AA+' long-term issuer credit and senior unsecured debt ratings on the City of Greater Sudbury, in the Province of Ontario. The outlook is stable.

Outlook

The stable outlook reflects our expectation that in the next two years, a healthy mining sector and increasing immigration will help expand the economy. We also expect Sudbury's asset renewal needs and large projects will continue to require significant capital investments, resulting in higher after-capital deficits and a rise in the debt burden. However, we expect the city will still generate strong operating surpluses and that it doesn't intend to issue debt beyond 2026, as per our base-case expectations.

Downside scenario

We could lower the rating in the next two years if Sudbury's revenue growth is materially lower than expected, with increasing capital needs resulting in after-capital deficits greater than 10% of total revenue on a sustained basis and a higher-than-expected tax-supported debt burden due to additional debt financing requirements of the capital plan.

Upside scenario

We could raise the ratings in the next two years if Sudbury's revenue increases faster than expected while the city achieves and sustains after-capital surpluses and holds tax-supported debt below 30% of operating revenue. However, we view this scenario as unlikely during the next two years.

Rationale

We expect Sudbury will continue to post healthy operating surpluses throughout the forecast horizon. However, its large projects and asset renewal plans will result in elevated capital requirements for the next several years, which the city intends to finance with additional debt issuances. We expect this will result in significant after-capital deficits in the near future and a debt burden peaking at about 67% in 2026. We also expect the debt burden to improve steadily after 2026 according to our base-case expectations, as capital spending moderates. Nevertheless, we believe that Sudbury's strong economy, robust liquidity, and the extremely supportive and predictable institutional framework for Canadian municipalities, remain key strengths that support the city's creditworthiness.

A healthy resource sector complemented by a sizable public-sector presence, built on an extremely predictable and supportive institutional framework, bolsters the ratings.

We expect Sudbury's economy and population will continue to expand and diversify moderately in the next two years, with high median incomes and estimated GDP per capita in line with that of the national economy at about US$55,000 in 2024. The city's population continues to increase, aided by immigration and programs such as the federal Rural and Northern Immigration Pilot.

We view Sudbury's public sector as a stabilizing force, aiding economic diversification from the city's historical concentration in the resource sector--primarily nickel mining as well as related support services. Although the resource sector accounts for a significant proportion of total local employment, the city is a major retail, health care, finance, and educational center for northern Ontario.

The city continues to face challenges meeting the demand for skilled labor. Its unemployment rate increased to 5.9% in July 2024, albeit lower than the provincial and national rates. Furthermore, the regional economy's relatively high reliance on mining, and in particular, its exposure to the volatility of nickel prices, could affect Sudbury's revenue growth and expenditure needs. In addition, innovations in battery technology could reduce demand for regionally mined metals. In our view, this partially constrains the city's economic profile. Nevertheless, high demand for nickel from the energy transition and electric vehicle battery manufacturers will support the mining sector and help spur employment opportunities in the city.

Sudbury's financial management practices are strong and largely in line with those of similarly rated peers, in our view. The city discloses pertinent information in a transparent, easy-to-access manner and prepares robust operating and capital budgets. It implemented its first multiyear budget in 2024 with a two-year operating budget and four-year capital budget. The budget reflects the broad goals outlined in the 10-year financial plan, which contains what we view as realistic assumptions. We believe that the council will continue to put forward sizable capital plans in line with its asset management plans. Similar to Canadian peers, Sudbury can issue debt only to finance capital expenditure (capex). We believe it has prudent and conservative policies as well as a stable and well-qualified management team to govern its debt and liquidity management.

As do other Canadian municipalities, Sudbury benefits from an extremely predictable and supportive local and regional government framework that has demonstrated high institutional stability and evidence of systemic extraordinary support in times of financial distress. Most recently through the pandemic, senior levels of government provided operating and transit-related grants to municipalities, in addition to direct support to individuals and businesses. Although provincial governments mandate a significant proportion of municipal spending, they also provide operating fund transfers and impose fiscal restraint through legislative requirements to pass balanced operating budgets. Municipalities generally have the ability to match expenditures well with revenues, except for capital spending, which can be intensive. Any operating surpluses typically fund capex and future liabilities (such as postemployment obligations) through reserve contributions. Municipalities have demonstrated a track record of strong budget results and, therefore, debt burdens, on average, are low relative to those of global peers and growth over time has been modest.

A rising debt burden amid continuation of an elevated capital plan.

We believe that healthy population growth will continue to steadily increase the city's assessment base. As a result, we expect that operating revenues will remain healthy with moderate tax levies and user fee rate increases, albeit at a lower rate than in 2023 as falling interest rates moderate the historical higher-than-usual investment income. We expect operating balances will average about 14% of operating revenues in 2022-2026.

The city continues to make progress on large capital projects: a new downtown event center consisting of an arena and the cultural hub with a new central library; the Art Gallery of Sudbury; and the Sudbury Multicultural and Folk Arts Assn., in addition to material infrastructure renewal needs. Considering these projects and their timelines, we expect after-capital balances will transition to a deficit position, averaging about 5% of total revenues in 2024-2026. This includes higher-than-historical annual capital spending, of more than C$200 million on average, in the same period. Nevertheless, we also expect capex will steadily decrease after the completion of these projects.

For 2025 and 2026, we expect total debt issuance of more than C$250 million associated with these projects, as well as due to rising construction costs amid inflation-related pressures. Specifically, the city intends to issue C$135 million for the new event center and the remaining issuance relates to other projects and priority infrastructure needs. As a result, the estimated tax-supported debt will peak at C$552 million or about 67% of operating revenues by year-end 2026. We believe the debt burden will decline steadily after 2026, as we don't expect the city to issue debt beyond 2025 and 2026, in line with its stated borrowing plans. At the end of 2023, the city had C$326 million of tax-supported debt outstanding, representing about 46% of operating revenues.

We expect interest costs will remain manageable at about 1.5% of operating revenue on average in

2024-2026. We do not believe the liabilities of the city's related entities, Sudbury Airport Community Development Corp. and Greater Sudbury Utilities Inc., represent a material contingent liability risk, as we believe the likelihood of the city providing extraordinary support to them in a stress scenario is low.

Sudbury's credit profile is bolstered by what we view as an exceptional liquidity position. Although we expect cash and reserve levels will fall as the capital projects are completed in the next few years, overall liquidity should remain sufficient to cover all debt servicing requirements. We estimate total free cash in the next 12 months will be enough to cover more than 26x the estimated debt service for the period and will remain well above 100% through 2026.

Key Statistics

Table 1

City of Greater Sudbury--Selected indicators

	--Fiscal year-end Dec. 31--					
Mil. C$	**2021**	**2022**	**2023**	**2024bc**	**2025bc**	**2026bc**
Operating revenues	615	650	713	745	781	821
Operating expenditures	515	565	605	641	672	706
Operating balance	100	85	108	104	109	115
Operating balance (% of operating revenues)	16.2	13.1	15.1	14.0	14.0	14.0
Capital revenues	38	37	54	66	83	86
Capital expenditures	119	100	129	195	246	255
Balance after capital accounts	19	22	33	(25)	(54)	(54)
Balance after capital accounts (% of total revenues)	2.9	3.3	4.3	(3.1)	(6.3)	(6.0)
Debt repaid	13	9	11	11	10	13
Gross borrowings	0	103	0	0	124	135
Balance after borrowings	6	116	21	(36)	60	68
Direct debt (outstanding at year-end)	244	337	326	315	429	552
Direct debt (% of operating revenues)	39.7	51.9	45.7	42.3	55.0	67.2
Tax-supported debt (outstanding at year-end)	244	337	326	315	429	552
Tax-supported debt (% of consolidated operating revenues)	39.7	51.9	45.7	42.3	55.0	67.2
Interest (% of operating revenues)	1.1	1.5	1.4	1.4	1.3	1.9
National GDP per capita (single units)	65,825	72,249	72,127	73,304	75,035	77,376

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

Ratings Score Snapshot

Table 2

City of Greater Sudbury--Ratings score snapshot

Key rating factors	Scores
Institutional framework	1
Economy	2
Financial management	2
Budgetary performance	2
Liquidity	1
Debt burden	3
Stand-alone credit profile	aa+
Issuer credit rating	AA+

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In our "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

Sovereign Risk Indicators, July 8, 2024

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Economic Outlook Canada Q4 2024: Turning The Corner, June 24, 2024
- Institutional Framework Assessment: Canadian Municipalities Employ Flexibilities Within Fiscal Framework To Temper Cost Pressures, April 2, 2024
- Sector and Industry Variables | Criteria | Governments | Sovereigns: Sovereign Rating Methodology, March 26, 2024
- S&P Global Ratings Definitions, June 9, 2023

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed	
Greater Sudbury (City of)	
Issuer Credit Rating	AA+/Stable/--
Greater Sudbury (City of)	
Senior Unsecured	AA+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.