

Research Update:

Regional Municipality of Peel 'AAA' Ratings Affirmed; Outlook Remains Stable

September 19, 2024

Overview

- The Regional Municipality of Peel's strong economy and prudent financial management will continue to support healthy and stable operating results.
- That said, we expect the region's elevated capital expenditures (capex) to result in high after-capital deficits over the next two years and increased reliance on debt.
- S&P Global Ratings affirmed its 'AAA' long-term issuer credit and senior unsecured debt ratings on the region.
- The stable outlook reflects our expectation that the weakening in after-capital performance will be temporary, operating results will remain very strong, and the projected increase in the debt burden will not exceed our base case.

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Rating Action

On Sept. 19, 2024, S&P Global Ratings affirmed its 'AAA' long-term issuer credit rating on the Regional Municipality of Peel. The outlook remains stable.

Outlook

The stable outlook reflects our expectation that the region's growing tax base, very strong operating surpluses, robust financial management, and exceptional liquidity will continue to benefit Peel's credit profile. We expect the large capital plan and lower-than-expected development charges (DC) revenue to fund capital works will result in after-capital deficits of about 6% of total revenues in the next two years. We also expect the debt burden, excluding debt on lent to the region's lower-tier municipalities, will increase to more than 60% of operating revenues in 2026.

Downside scenario

We could lower the ratings in the next two years if the region's capital needs stay elevated and result in after-capital deficits greater than 5% of total revenue on a sustained basis, and a higher-than-expected tax-supported debt burden.

Rationale

The ratings reflect our view of Peel's diverse and wealthy economy, with a growing tax base that supports the region's very strong operating balances of about 16% of operating revenues on average, over the forecast horizon. However, Peel's large capital plan and lower-than-expected DC revenue will result in higher after-capital deficits and an increasing debt burden to fund capital needs. That said, as the region makes progress on its priority capital projects, the after-capital balances will improve steadily after 2026. We believe its prudent financial management and extremely strong liquidity will help Peel navigate through the potential changes to the service delivery model as part of Ontario's regional government review.

Strong financial management practices and a resilient economy bolster the ratings.

After Bill 185 confirmed that the region will not be dissolved, the region is still awaiting the outcome of the transition board's recommendations to the province on service delivery. In our opinion, Peel's strong financial management policies and practices will support very strong credit quality through the changes in legislation, if any. The region has a track record of planning and managing for change. Although it experienced elevated turnover in key staff and administrative functions, in turn increasing management and execution risk, its experienced management team and robust policies mitigate that risk.

The region's diverse economy is supported by growing immigration and benefits from proximity to and integration with the Greater Toronto Area (GTA), despite slow economic activity. Peel contains the local municipalities of Brampton and Mississauga, as well as the Town of Caledon. It hosts an extensive transportation network, including Canada's largest airport, two national rail lines, and some of the nation's largest highways, which fully integrates it with the GTA's large employment base and allows good access to other markets. Although Peel's population is expanding, growth in the labor force outpaced the rate of employment, leading to a high unemployment rate of 8.5% as of June 30, 2024, higher than the provincial and national averages. Nevertheless, as the economy recovers with projected continued working age immigration, we expect key job market indicators will improve.

As do other Canadian municipalities, Peel 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 capital expenditures 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.

An elevated capital plan will pressure budgetary performance and lead to greater reliance on debt.

We believe that healthy population growth will continue to steadily expand the region's assessment base. As well, the region continues to implement higher-than-historical net increases in tax levies to support the growing population. As a result, we expect operating balances will remain very strong, averaging about 16% of operating revenues in 2022-2026.

To support the rising service needs, the region's capital plan remains elevated in 2024-2026, averaging more than C\$1 billion annually. Future capex primarily relates to state-of-good repair (SOGR) and investment in the Peel Regional Police and housing-related infrastructure projects in response to the province's accelerated housing targets. In addition, we expect collection of DC revenues will remain subdued in the next two years due to slower-than-expected development activity. As a result, we expect after-capital deficits to increase, averaging about 6% of total revenues in 2024-2026. We expect the deficits after-capital accounts will improve outside the outlook horizon as current projects reach completion. The region has robust cash reserve balances available to finance a portion of the future SOGR capital needs. This mitigates the rise in after-capital deficits over the next two years, in our view.

We expect the region's reliance on debt will increase to fund the growth capital plan, while SOGR needs will be funded by the existing reserves. Peel intends to issue more than C\$2 billion debt in 2024-2026, including debt on behalf of lower-tier municipalities. As a result, tax-supported debt, which includes both the region's debt as well as debt on-lent to the lower-tier municipalities, will increase to about 84% of operating revenues in 2026. Excluding on-lent debt, we expect the region's debt burden to rise above 60% of operating revenues in 2026. Although we expect interest costs will increase, we believe they will remain manageable at about 3% of operating revenues on average in 2023-2025.

In our view, Peel's liquidity is a key credit strength. We estimate total free cash in the next 12 months will be enough to cover more than 12x the estimated debt service for the period. We expect this ratio will remain well above 100% during the outlook horizon. Supporting the liquidity position is the region's strong access to capital markets and domestic bank financing. As of Dec. 31, 2023, available cash and investments totaled C\$3.2 billion.

Key Statistics

Table 1

Regional Municipality of Peel -- Selected indicators

(Mil. C\$)	--Year ended Dec. 31--					
	2021	2022	2023	2024bc	2025bc	2026bc
Operating revenues	2,678	2,706	3,051	3,286	3,481	3,685
Operating expenditures	2,225	2,304	2,546	2,729	2,917	3,110
Operating balance	453	402	505	557	565	575
Operating balance (% of operating revenues)	16.9	14.9	16.5	17.0	16.2	15.6

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Table 1

Regional Municipality of Peel -- Selected indicators (cont.)

(Mil. C\$)	--Year ended Dec. 31--					
	2021	2022	2023	2024bc	2025bc	2026bc
Capital revenues	331	395	103	300	440	450
Capital expenditures	453	591	745	993	1,307	1,263
Balance after capital accounts	332	206	(137)	(136)	(302)	(238)
Balance after capital accounts (% of total revenues)	11.0	6.7	(4.3)	(3.8)	(7.7)	(5.8)
Debt repaid	230	115	129	125	149	326
Gross borrowings	248	73	0	455	832	826
Balance after borrowings	350	164	(266)	194	381	262
Direct debt (outstanding at year-end)	1,618	1,578	1,451	1,779	2,453	3,090
Direct debt (% of operating revenues)	60.4	58.3	47.6	54.1	70.5	83.9
Tax-supported debt (outstanding at year-end)	1,618	1,578	1,451	1,779	2,453	3,090
Tax-supported debt (% of consolidated operating revenues)	60.4	58.3	47.6	54.1	70.5	83.9
Interest (% of operating revenues)	2.6	2.7	2.4	2.8	3.8	4.7
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

Regional Municipality of Peel--Ratings score snapshot

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

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 Q3 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

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Ratings Affirmed

Peel (Regional Municipality of)

Issuer Credit Rating AAA/Stable/--

Peel (Regional Municipality of)

Senior Unsecured AAA

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.

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