County of Essex

11/15/2021

PRIMARY CONTACT

Adam J Gillespie
Toronto
1-416-507-2565
adam.gillespie
@spglobal.com

SECONDARY CONTACT

Nineta Zetea
Toronto
1-416-507-2508
nineta.zetea
@spglobal.com

RESEARCH CONTRIBUTOR

Ritesh S Bagmar
CRISIL Global Analytical Center,
an S&P Global Ratings affiliate
Pune

This report does not constitute a rating action.

Credit Highlights

Overview

Credit context and assumptions	Base-case expectations
Supportive institutions and prudent financial management practices underpin creditworthiness.	Strong budgetary performance will allow for continued internal funding of the capital plan without recourse to debt.
--The county's prudent financial management will contribute to strong budgetary results.	--Extraordinary funding has helped the county mitigate the financial impacts of the pandemic.
--We believe the county's relationship with the Province of Ontario will remain well balanced and generally supportive.	--The county’s robust after-capital surpluses and pay-as-you-go capital funding strategy help minimize debt issuance.
--Recent volatility in the auto sector will hamper the recovery in employment and economic activity in the near term.	--An extremely strong liquidity position will continue to support the county’s creditworthiness.

S&P Global Ratings’ long-term issuer credit rating on the County of Essex is ‘AA+’. Extraordinary funding from the province and federal government, along with prudent spending controls, has helped Essex offset the financial impacts of the pandemic to date. Consequently, we believe that the county will continue to generate strong operating and after-capital surpluses averaging about 23% of operating revenue and 11% of total revenue, respectively. These surpluses will allow it to continue internally financing its capital plan without recourse to debt, keeping the tax-supported debt burden well below 30% of operating revenue in the next several years. In addition, the county's exceptionally strong liquidity will continue to bolster its credit profile.

Outlook

The stable outlook reflects our expectation that, in the next two years, Essex will continue its pay-as-you go strategy to finance its capital program with no recourse to debt issuance, while maintaining sound budgetary performance and robust liquidity.

Downside scenario

Although we do not believe it likely in the next two years, we could lower the rating if we came to expect a material weakening in the county's budgetary performance or financial flexibility due to, for instance, a significant downturn in economic activity in the region or a large expansion of the county's capital plan.

Upside scenario

All else equal, we could raise the ratings in the next two years if the local economy substantially strengthened, demonstrated by higher-than-expected growth and notable sector diversification; and if management's response to this growth fully met the increased complexity of the county's needs.

Rationale

Supportive institutions and prudent financial management practices underpin creditworthiness.

Essex's economy has historically focused on the manufacturing (primarily auto) and agricultural sectors and while the latter has recently grown, the former remains hampered by the global semiconductor shortage and other supply chain issues. Consequently, unemployment in the region has remained stubbornly higher than the national average through 2021. However, we believe that a large and relatively stable public-sector employment base helps to counter the concentration and volatility in the auto sector. In addition, Essex continues to focus on diversifying its economy into more service-based sectors (including tourism, agri-business, health care and social assistance, and education), which we believe will contribute to slow-but-positive medium-term growth prospects. Essex's nominal GDP per capita is close to the national level of about US$52,900, given its fairly high median household income.

Located in the southwest corner of Ontario, Essex is composed of seven lower-tier municipalities and has a population of more than 182,000. It neighbors the City of Windsor and the City of Detroit is across the Detroit River.

We believe Essex demonstrates strong financial management practices and broad political consensus on fiscal policies. Essex's council is composed of the mayors and deputy mayors of the seven lower-tier municipalities. Council members serve four-year terms and the next municipal elections will take place in October 2022. Unlike Canada's members of federal or provincial parliaments, municipal councilors do not operate under a political party system. We believe the management team has demonstrated its ability to manage revenues and expenditures appropriately under the consolidated one-year operating budgets, which are passed annually by the council, and actual variations from budget are typically moderate. The county prepares an annual asset management plan, allowing it to ensure better cost effectiveness and efficiencies for its corporate infrastructure and assets. In our opinion, financial information is sufficiently detailed and comprehensive. We also believe that debt and liquidity management is prudent and adequately risk averse.

We believe Canadian municipalities benefit from a very predictable and well-balanced local and regional government framework that has demonstrated a high degree of institutional stability. 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 and landfill closure costs) through reserve contributions.

Strong budgetary performance will allow for continued internal funding of the capital plan without recourse to debt.

We expect Essex will continue generating robust budgetary performance in our 2019-2023 base-case forecast period, supported by stable growth in the assessment base and effective spending controls. The county has received close to C$9 million in extraordinary funding from senior levels of government to help it address the financial impacts of the pandemic. This funding, along with some capital deferrals and operational savings, contributed to the county's ability to record surpluses in 2020 and 2021. Accordingly, we expect that operating balances will average 23% of operating revenue over this period while after-capital surpluses will also remain high, averaging 11% of total revenue, despite modestly higher capital expenditures.

The county has kept a very low debt burden by internally funding its capital expenditures for many years and we do not expect it to issue any debt in the next two years. Accordingly, we forecast tax-supported debt to total almost C$49 million at the end of 2023, or 23% of operating revenues. Tax-supported debt consists of debt borrowed under Essex's name on behalf of its lower-tier municipalities and on behalf of Windsor. S&P Global Ratings recognizes that there is a lower credit risk associated with the debt on-lent to these self-supporting entities. The county's debt burden excluding the on-lent debt was 15% of operating revenues in 2020 and we believe that it will continue to decline in the next two years. In addition, tax-supported debt is less than five years of operating surpluses, which together with very low interest costs of less than 2% of operating revenues, supports our assessment of the very low debt burden. Essex's exposure to contingent liabilities is modest and does not represent a material credit risk, in our opinion.

The province has committed to build a new regional hospital complex, to be located in Windsor. The estimated cost is C$2 billion, for which municipalities are required to fund 10%. This would translate to almost C$100 million in funding provided by the county, and a similar contribution from Windsor. Essex anticipates that it will fund at least half of its commitment through annual tax levy contributions to a dedicated reserve, with the balance potentially being covered through debt closer to the completion of the project, which is not expected in the next five years.

Essex maintains what we consider an exceptional liquidity position through regular contributions to its reserves. We estimate that the county will hold free cash and investments of about C$200 million, or enough to cover about 30x its debt service requirements in the next 12 months' debt service. Similar to that of its domestic peers, Essex's access to external liquidity is satisfactory, in our view.

County of Essex Selected Indicators

Mil. C$	2018	2019	2020	2021bc	2022bc	2023bc
Operating revenue	170.1	185.1	195.6	198.1	205.6	213.0
Operating expenditure	130.3	143.6	145.4	152.3	159.7	167.6
Operating balance	39.8	41.5	50.3	45.8	45.9	45.5
Operating balance (% of operating revenue)	23.4	22.4	25.7	23.1	22.3	21.3
Capital revenue	9.9	14.2	9.5	10.5	10.5	10.5
Capital expenditure	34.4	30.6	31.8	35.0	35.0	35.0
Balance after capital accounts	15.2	25.1	27.9	21.3	21.4	21.0
Balance after capital accounts (% of total revenue)	8.5	12.6	13.6	10.2	9.9	9.4
Debt repaid	2.4	2.7	3.2	3.1	3.2	3.6
Gross borrowings	0.0	0.0	0.0	0.0	0.0	0.0
Balance after borrowings	12.9	22.4	24.8	18.2	18.2	17.3
Direct debt (outstanding at year-end)	64.8	62.1	58.5	55.4	52.3	48.6
Direct debt (% of operating revenue)	38.1	33.5	29.9	28.0	25.4	22.8
Tax-supported debt (outstanding at year-end)	64.8	62.1	58.5	55.4	52.3	48.6
Tax-supported debt (% of consolidated operating revenue)	38.1	33.5	29.9	28.0	25.4	22.8
Interest (% of operating revenue)	2.4	2.2	2.0	1.8	1.7	1.5
Local GDP per capita ($)	--	--	--	--	--	--

County of Essex Selected Indicators

National GDP per capita ($)	46,453.9	46,326.7	43,258.2	52,948.3	54,410.6	55,679.7

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. C$--Canadian dollar. $--U.S. dollar.

Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	2
Financial management	2
Budgetary performance	1
Liquidity	1
Debt burden	1
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 the "**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, Published Oct. 12, 2021

Related Criteria

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

Related Research

- Institutional Framework Assessments For International Local And Regional Governments, Published Oct. 6, 2021
- Economic Outlook Canada Q4 2021: Growth Delayed, Published Sept. 24, 2021
- Comparative Statistics: Risk Indicators For Canadian Local And Regional Governments, Published Sept. 1, 2021
- S&P Global Ratings Definitions, Published Jan. 5, 2021
- Public Finance System: Canadian Municipalities, Published May 12, 2020
- Guidance: Methodology For Rating Local And Regional Governments Outside Of The U.S., Published July 15, 2019

Ratings Detail (as of November 15, 2021)*

Essex (County of)	
Issuer Credit Rating	AA+/Stable/--
Senior Unsecured	AA+
Issuer Credit Ratings History	
27-Nov-2017	AA+/Stable/--
29-Nov-2013	AA/Stable/--
01-Nov-2012	AA-/Positive/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.