S&P Global
Ratings

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Summary:
City of Thunder Bay

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Summary:

City of Thunder Bay

Issuer Credit Rating	AA/Stable/--

Key Rating Factors

Credit context and assumptions	Base-case expectations
We expect public institutions and a strong economy will continue to support the City of Thunder Bay's creditworthiness. • High income levels and a large and stabilizing public sector presence foster stability in the city's property tax base despite the negative impact from COVID-19. • We expect Thunder Bay to manage its capital program such that it maintains robust budgetary performance and debt issuance is limited. • We believe the city's relationship with the Province of Ontario will remain well-balanced and generally supportive.	Operating balances and liquidity will remain high, allowing Thunder Bay to keep debt low. • We believe that the restrictions in place to address the COVID-19 pandemic will have a modest, but manageable, impact on the city's revenues and expenditures and will be largely restricted to the current fiscal year. • We expect modest debt issuance in the next two years, which coupled with operating revenue growth and scheduled debt repayments, will result in a lower debt burden by 2022. • The city's healthy liquidity position will continue to support creditworthiness.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that, in the next two years, Thunder Bay will maintain overall sound financial results, generating modest after-capital surpluses on average, supported by prudent financial management practices and despite near-term challenges and elevated capital spending. We also expect the city will maintain a low debt burden and a robust liquidity position.

Downside scenario

We could lower the ratings over the next two years if weaker-than-expected budgetary performance and rising capital needs produced after-capital deficits consistently above 5% of total revenues, and eroded liquidity to below 1x debt service coverage.

Upside scenario

We could raise the ratings in the next two years if the city demonstrated a strong political commitment to continued stability in budget results, liquidity, and debt metrics through the implementation of more detailed long-term financial planning, with specified future capital and operating needs and related funding sources, providing greater visibility into the long-term sustainability of its financial performance.

Rationale

We believe that Thunder Bay's prudent financial management practices and cost containment efforts will help to mitigate the direct fiscal impacts stemming from the COVID-19 pandemic. We expect that the city will maintain balanced budgetary performance in the next two years, and that efforts to increase ongoing internal contributions to fund its capital program will contribute to a declining debt burden.

Thunder Bay's economy, grounded by a large public-sector presence and a supportive institutional framework, helps to mitigate broader challenges.

Thunder Bay is the center for many government services in northwestern Ontario and thus its economy is supported by large and stable public sector (health care, school boards, and municipal and provincial administration), which acts as a stabilizing force, in our view. The manufacturing, retail, and mining sectors also contribute to the local economy. While GDP per capita is not available at the local level, we believe Thunder Bay's nominal GDP per capita is generally in line with that of Canada at about US$42,000. However, we believe that a weaker demographic profile, characterized by weak population growth and a larger proportionate number of elderly residents, constrains the city's economic profile and could affect future revenue growth and expenditure needs.

In our view, Thunder Bay demonstrates adequate financial management practices and an ability to implement its strategic plan and budget. The city prepares a one-year operating budget as well as a detailed three-year capital budget with identified funding sources along with a 10-year outlook in concert with a long-term financial plan. Similar to its Canadian peers, Thunder Bay can issue debt only to finance capital expenditures, and we believe it has prudent policies to govern its debt and liquidity management.

Thunder Bay, like other Canadian municipalities, benefits 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.

High operating balances and strong liquidity will allow Thunder Bay to keep debt low.

Thunder Bay has estimated that the COVID-19 pandemic will have a net financial impact of about C$9 million in 2020. This is being driven by revenue losses from lower collection of transit fares and other various fees, penalties, and fines, as well as increased costs related to, among other items, cleaning and procurement of personal protective equipment. This estimate also includes up to C$5 million of cost containment measures that the city has identified. We believe that the fiscal impacts of the pandemic will be largely restricted to the current year, and as a result, we estimate the operating balance will decrease in 2020 before starting to recover in 2021. Despite these near-term challenges, we expect the city will continue to generate high operating surpluses, averaging almost 14% of adjusted operating revenue in our base-case scenario for 2018-2022, which will continue to facilitate its ability to internally finance its capital plan and limit the need for debt financing. We believe that capital spending in the next several years will be high, averaging about C$85 million, which could result in after-capital balances narrowing to a slim surplus of 0.4% of total revenues, on an average, in 2018-2022. Our forecast also includes the capital plan of Tbaytel, the city's wholly owned and fully consolidated telecommunications company.

We estimate the city will issue C$70 million in gross debt through 2022, some of which will help finance the expansion of Tbaytel's fiber optic network. However, given large principal payments of about C$87 million due over the same period, we expect Thunder Bay's total tax-supported debt as a proportion of consolidated operating revenues will decline to about 35% in fiscal 2022 from about 41% in 2018. In addition, the city's total debt equals less than five years of operating surpluses, representing a very low debt burden. We believe interest payments on consolidated tax-supported debt will remain at less than 2% of operating revenues. Thunder Bay's exposure to contingent liabilities is low and does not represent a material credit risk, in our opinion.

Thunder Bay's credit profile is bolstered by what we view as an exceptional liquidity position and satisfactory access to external liquidity for financing needs. We estimate that free cash will total more than C$120 million in the next 12 months, which is sufficient to cover about 3x the estimated debt service for the year.

Key Statistics

Table 1

City of Thunder Bay -- Selected Indicators

	--Year ended Dec. 31--				
(Mil. C$)	**2018**	**2019bc**	**2020bc**	**2021bc**	**2022bc**
Operating revenues	549	559	557	574	588
Operating expenditures	459	481	487	500	514
Operating balance	91	78	70	74	74
Operating balance (% of operating revenues)	16.5	13.9	12.6	12.9	12.6
Capital revenues	7	9	14	14	11
Capital expenditures	82	90	85	84	90
Balance after capital accounts	16	(4)	(0)	4	(5)
Balance after capital accounts (% of total revenues)	2.9	(0.7)	(0.1)	0.7	(0.8)
Debt repaid	29	31	32	29	26
Gross borrowings	28	28	30	21	19
Balance after borrowings	14	(6)	(3)	(4)	(12)
Direct debt (outstanding at year-end)	226	224	222	214	206
Direct debt (% of operating revenues)	41.1	40.1	39.8	37.2	35.1
Tax-supported debt (outstanding at year-end)	226	224	222	214	206
Tax-supported debt (% of consolidated operating revenues)	41.1	40.1	39.8	37.2	35.1
Interest (% of operating revenues)	1.3	1.2	1.4	1.3	1.2

Table 1

City of Thunder Bay -- Selected Indicators (cont.)					
	--Year ended Dec. 31--				
(Mil. C$)	2018	2019bc	2020bc	2021bc	2022bc
National GDP per capita (single units)	60,011	61,290	58,634	62,727	64,658

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 Thunder Bay -- Ratings Score Snapshot	
Key rating factors	**Scores**
Institutional framework	2
Economy	2
Financial management	3
Budgetary perfomance	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, April 24, 2020. Interactive version available at http://www.spratings.com/sri

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Public Finance System: Canadian Municipalities, May 12, 2020
- COVID-19 Causes More Severe Disruption For Canada's Economy, April 17, 2020

- For Canada, Below-Potential Growth Is Likely In The Near Term, Oct 7, 2019
- Guidance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- Institutional Framework Assessments For International Local And Regional Governments, July 4, 2019