S&P Global
Ratings

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Summary:

County of Essex

Primary Credit Analyst:
Hamzah Saeed, Toronto; hamzah.saeed@spglobal.com

Secondary Contact:
Nineta Zetea, Toronto + 1 (416) 507 2508; nineta.zetea@spglobal.com

Research Contributor:
Ekta Bhayani, CRISIL Global Analytical Center, an S&P affiliate, Mumbai

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Summary:

County of Essex

Issuer Credit Rating	AA+/Stable/--

Key Rating Factors

Credit context and assumptions	Base-case expectations
Supportive institutions and prudent financial management practices will support the County of Essex's creditworthiness. • Stable economic profile will provide consistency in the county's property tax base despite the negative impact of COVID-19. • The county's prudent financial management will continue to allow it to post strong operating balances. • We believe the county's relationship with the Province of Ontario will remain well-balanced and generally supportive.	Strong budgetary performance will assist in keeping reliance on debt low. • Essex will continue to generate strong operating margins despite the near-term impact of the pandemic on the county's fiscal position. • A track record of robust after-capital surpluses will help minimize debt issuance. • The county's extremely strong liquidity position will continue to support its creditworthiness.

Outlook

The stable outlook reflects our expectation that, in the next two years, Essex will efficiently use its pay-as-you go strategy to finance its growing capital program with no recourse to debt issuance, while maintaining sound budgetary performance and robust liquidity despite the fiscal pressures arising from the pandemic, which we believe will be temporary. It also reflects our belief that local economic growth will be gradual, and the current council's priorities will continue reflecting a balanced fiscal environment.

Downside scenario

Although we do not expect it, further weakening of economic activity, due to, for instance, loss of major employers or demographic trends, could lead to lower-than-expected tax revenue collections. This, combined with the county's difficulty in scaling back capital projects or enacting offsetting property tax increases, could further erode Essex's financial performance. Under this scenario, we could lower the ratings in recognition of the county's weakened budget flexibility.

Upside scenario

All else equal, we could raise the ratings in the next two years if the local economy substantially strengthened, supported 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

As the global spread of COVID-19 continues, we believe Essex will not be immune to the expected deterioration in economic activity and increased budgetary stresses in 2020. Although the impact of the pandemic will depend on the rate of spread and duration, we believe that Essex's prudent financial management and cost-containment efforts will help generate robust operating balances and mitigate the direct fiscal impacts stemming from the pandemic. At the same time, we expect the county's strong budgetary performance will continue to support its capital expenditures through its pay-as-you-go strategy and mitigate the need to issue debt; this, in turn, will help preserve the county's exceptionally strong liquidity.

Supportive institutions and prudent financial management practices will support creditworthiness. We believe Essex's nominal GDP per capita is close to the national level of about US$ 42,000, in 2019, given its fairly high median household income. Essex's local economy was relatively stable in 2019, with an unemployment rate near 6%, higher property assessment values, and steady construction activity, as reflected in the value of building permits and housing starts. We expect these trends will continue once the negative-but-temporary impacts of COVID-19 on the local economy subside. The economy has historically focused on the manufacturing (primarily auto) and agricultural sectors; it also includes large public-sector employers. Essex is increasing its efforts to diversify its economy into service-based sectors (including tourism, agri-business, health care and social assistance, and education), which we believe could contribute to slow-but-positive medium-term growth prospects. Nevertheless, we estimate that the auto sector, which tends to be volatile, still accounts for almost 20% of the county's employment.

Located in the southwest corner of Ontario, Essex is composed of seven lower-tier municipalities and has a population of more than 181,000. 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; members serve four-year terms. Unlike Canada's members of federal or provincial parliaments, municipal councilors do not operate under a political party system. We believe the management team is well qualified and largely stable; it has demonstrated its ability to find cost efficiencies to adhere to the council's fiscal decisions. The county produces consolidated one-year operating budgets and actual variations from budget are moderate. It 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.

Like other Canadian municipalities, Essex benefits from a very predictable and well-balanced local and regional government framework that has demonstrated high 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.

Strong budgetary performance will assist in keeping reliance on debt low. Essex continues to effectively control spending. We expect its budgetary performance will remain superior in our 2018-2022 base-case forecast period, with sound operating balances averaging over 23% of operating revenues. In addition, by our estimate, despite a planned increase in capital spending in the medium term, after-capital surpluses will be close to 8% of total operating revenues, on average. We expect the county will continue addressing its capital needs at a faster pace in the near future. With the construction of the new hospital the county could be required to increase rates more, and we believe it has the ability to do so. The new health system's cost is an estimated C$2 billion, for which municipalities are required to fund 10%. This would translate to almost C$100 million funding provided by the county, and a similar contribution from Windsor. Although the construction timing has not been finalized, Essex's preliminary funding strategy includes an upfront commitment of C$50 million, funded via annual levies for 10 years, as well as commitment transfers, with the balance potentially being covered through debt issuance.

We estimate that the tax-supported debt will decrease to below 30% of total consolidated operating revenues in the next two years, as the county funds its capital plan primarily with internal resources. Tax-supported debt outstanding includes debt borrowed under Essex's name on behalf of its lower-tier municipalities and on behalf of Windsor. Because the county has no debt planned in the next two years, we expect these items to total about C$56 million at the end of 2021, or about 28% of consolidated operating revenues. S&P Global Ratings recognizes that there is a lower credit risk associated with the debt on-lent to these self-supporting entities. The overall debt burden (excluding the on-lent debt) is 15.3% of consolidated 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 (about 2% of operating revenues, on average, for 2019-2021), 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.

In addition to the low debt burden, Essex has an exceptional and stable liquidity position. We estimate free cash balances and investments will be about C$207 million in the next 12 months. This should cover about 30x next 12 months' debt service. Similar to that of its domestic peers, Essex's access to external liquidity is satisfactory, in our view.

Key Statistics

Table 1

County of Essex Selected Indicators

	--Fiscal year--					
(Mil. C$)	**2017**	**2018**	**2019**	**2020bc**	**2021bc**	**2022bc**
Operating revenues	161	170	185	191	202	208
Operating expenditures	126	130	144	149	154	159
Operating balance	35	40	42	42	48	50
Operating balance (% of operating revenues)	21.7	23.4	22.4	22.0	23.7	23.9
Capital revenues	7	10	14	11	11	11
Capital expenditures	35	34	31	43	43	44
Balance after capital accounts	7	15	25	10	15	17
Balance after capital accounts (% of total revenues)	4.3	8.5	12.6	5.0	7.2	7.6
Debt repaid	2	2	3	3	3	3

Table 1

County of Essex Selected Indicators (cont.)						
	--Fiscal year--					
(Mil. C$)	**2017**	**2018**	**2019**	**2020bc**	**2021bc**	**2022bc**
Gross borrowings	0	0	0	0	0	0
Balance after borrowings	5	13	22	7	12	14
Direct debt (outstanding at year-end)	67	65	62	59	56	53
Direct debt (% of operating revenues)	41.8	38.1	33.5	30.8	27.7	25.3
Tax-supported debt (outstanding at year-end)	67	65	62	59	56	53
Tax-supported debt (% of consolidated operating revenues)	41.8	38.1	33.5	30.8	27.7	25.3
Interest (% of operating revenues)	2.6	2.4	2.1	2.0	1.8	1.6
National GDP per capita (single units)	58,591	60,011	61,291	57,698	61,644	63,541

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. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful.

Ratings Score Snapshot

Table 2

County of Essex--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, Oct. 12, 2020. An interactive version is 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

- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- 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
- Public Finance System Overview: Canadian Municipalities, May 12, 2020