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Research Update:

City of Saskatoon 'AAA' Ratings Affirmed; Outlook Remains Stable

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Table Of Contents

Overview

Rating Action

Outlook

Rationale

Key Statistics

Ratings Score Snapshot

Key Sovereign Statistics

Related Criteria

Ratings List

Research Update:

City of Saskatoon 'AAA' Ratings Affirmed; Outlook Remains Stable

Overview

- The City of Saskatoon's budgetary results have outperformed our base-case expectations in 2016, fueling strong operating balances and modest after-capital deficits.
- Although we expect that capital expenditures will be higher in the next several years, capital revenues are likely to also grow, helping mitigate the need for external debt financing.
- As a result, we are affirming our 'AAA' long-term issuer credit and senior unsecured debt ratings on the city.
- The stable outlook reflects our expectations that, throughout the next two years, Saskatoon will maintain healthy liquidity, hold its tax-supported debt below 40% of operating revenues, and post sound budget results.

Rating Action

On Jan. 24, 2018, S&P Global Ratings affirmed its 'AAA' long-term issuer credit and senior unsecured debt ratings on the City of Saskatoon, in the Province of Saskatchewan. The outlook is stable.

Outlook

The stable outlook reflects our base-case expectation that, in the next two years, Saskatoon will maintain large operating surpluses and its tax-supported debt will fall below 40% of operating levels by 2020. We also expect Saskatoon's free cash levels to remain fairly steady during the forecast period, reflecting continued prudent financial management practices.

Although we believe it unlikely in the next two years, we could lower the ratings following a sudden and large increase in capital spending not supported by capital revenues, with the resulting expansion in after-capital deficits pushing tax-supported debt above 60% of operating revenues.

Rationale

We have updated our base-case scenario for the city and extended our forecast horizon through fiscal 2020. For 2018-2020, we expect Saskatoon's creditworthiness will be largely unchanged because we believe that the city's budgetary performance will continue to be solid, debt burden will remain much

less than 60% of operating revenues, and liquidity will remain healthy. We also expect that the city will continue to benefit from a supportive institutional framework, sound financial management, and a robust economy.

A robust economy and prudent financial management continue to underpin the ratings.

We continue to view Saskatoon's economy as robust. We estimate that the city's GDP per capita would be in line with the provincial average of about US\$56,863 in 2015-2017, given its stature as Saskatchewan's largest Census metropolitan area and the subsequent greater economic diversity than other areas of the province. Saskatoon's population increased an estimated 1.9% in 2017, which is stable compared with that of 2016. Agriculture, the public sector, and the resource sector (mining and potash) are all important employers for Saskatoon, although the city does not have significant concentration in any one sector.

We believe that Saskatoon's creditworthiness reflects strong financial management. In our view, the city's management team is experienced and qualified to effectively enact fiscal policies, and effectively respond to external risks. Saskatoon demonstrates what we view as good political and managerial strength with its lengthy track record of passing budgets before the start of fiscal year and meeting goals. We also believe that management accountability is strong and financial policies are prudent. Disclosure and transparency are what we believe to be good, annual financial statements are audited and unqualified, and the city prepares robust annual operating and capital budget documents. It also prepares long-term capital and borrowing plans.

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.

Solid budgetary performance and minimal debt; albeit growing capital needs.

Saskatoon's budgetary performance has historically been solid. We expect the city's operating balances will average about 22.4% of operating revenues from 2016-2020. Also, we project the city's after-capital balances will show deficits not exceeding 5% of total revenues on average given Saskatoon's capital plan, which calls for higher capital spending in the next several years, mainly related to its aging infrastructure.

We forecast tax-supported debt will be C\$376.7 million, equal to 39.3% of operating revenues by 2020, down from an estimated 43.6% in 2017. In 2018-2020, debt repayment will exceed gross borrowings, resulting in a

declining overall tax-supported debt burden. Net change in debt over this period will be about C\$11 million. In addition, tax-supported debt is less than three years' operating surpluses, which, together with very low interest costs (1% of operating revenues on average), support our assessment of the very low debt burden. We believe Saskatoon will remain contingently liable for the financing costs through the construction phase of one of the two public-private partnership projects in the capital plan. However, because both projects will be in their respective operations phase within our rating horizon, we have included the costs related to both of these projects in our analysis of the city's tax-supported debt.

In our view, the city's liquidity is healthy. We estimate free cash and liquid assets will total C\$440 million in the next 12 months and cover more than 12x estimated debt service for the period. We expect this ratio to remain well above 100% during the forecast outlook horizon. In addition, the city benefits from strong internal cash flow generation, which boosts our assessments of its liquidity profile. We believe that Saskatoon has satisfactory access to external liquidity, given its proven ability to issue into public debt markets and the presence of a secondary market for Canadian municipal debt instruments.

In our opinion, the city has minimal contingent liabilities. Liabilities stemming from standard future employee benefits and landfill postclosure liabilities equaled about 5.9% of consolidated operating revenues in 2016.

Saskatoon's high degree of budgetary flexibility supports the city's financial performance. High modifiable revenues, primarily from taxes, fees, and user charges, typically account for more than 85% of operating revenues. We expect these to remain at similar levels. We also project capital expenditures to average close to 30% of total expenditures for 2016-2020.

Key Statistics

Table 1

City of Saskatoon -- Financial Statistics							
	--Fiscal year ended Dec. 31--						
	2014	2015	2016	2017bc	2018bc	2019bc	2020bc
Operating revenues	802.6	814.8	800.2	829.4	869.6	912.3	957.6
Operating expenditures	557.7	618.4	582.3	635.8	677.0	725.2	777.1
Operating balance	244.9	196.4	217.8	193.6	192.6	187.1	180.5
Operating balance (% of operating revenues)	30.5	24.1	27.2	23.3	22.2	20.5	18.9
Capital revenues	66.6	131.1	92.2	67.1	62.6	130.1	154.3
Capital expenditures	306.5	330.3	274.7	261.9	295.4	323.0	322.3
Balance after capital accounts	5.0	(2.9)	35.4	(1.2)	(40.2)	(5.8)	12.5
Balance after capital accounts (% of total revenues)	0.6	(0.3)	4.0	(0.1)	(4.3)	(0.6)	1.1

Table 1

City of Saskatoon -- Financial Statistics (cont.)							
	--Fiscal year ended Dec. 31--						
	2014	2015	2016	2017bc	2018bc	2019bc	2020bc
Debt repaid	21.4	25.1	24.0	24.7	29.0	32.8	30.8
Gross borrowings	25.0	15.0	0.0	0.0	61.8	10.3	9.3
Balance after borrowings	8.6	(12.9)	11.4	(25.9)	(7.3)	(28.4)	(9.0)
Modifiable revenues (% of operating revenues)	76.7	80.1	84.7	86.2	86.8	87.5	88.1
Capital expenditures (% of total expenditures)	35.5	34.8	32.1	29.2	30.4	30.8	29.3
Direct debt (outstanding at year-end)	238.1	228.1	204.0	179.4	215.8	198.5	182.5
Direct debt (% of operating revenues)	29.7	28.0	25.5	21.6	24.8	21.8	19.1
Tax-supported debt (outstanding at year-end)	238.1	263.1	318.8	361.4	420.8	398.2	376.7
Tax-supported debt (% of consolidated operating revenues)	29.7	32.3	39.8	43.6	48.4	43.7	39.3
Interest (% of operating revenues)	0.9	1.3	1.5	0.8	0.7	0.8	0.7
National GDP per capita (single units)	55,807	55,430	55,910	58,407	60,167	61,735	63,474

Note: 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. Base case reflects S&P Global Ratings' expectations of the most likely scenario. Downside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with a downgrade. Upside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with an upgrade. bc--Base case.

Ratings Score Snapshot

Table 2

City of Saskatoon -- Ratings Score Snapshot	
Key rating factor	Assessment
Institutional Framework	Very predictable and well-balanced
Economy	Very strong
Financial Management	Strong
Budgetary Flexibility	Very strong
Budgetary Performance	Strong
Liquidity	Exceptional
Debt Burden	Very low
Contingent Liabilities	Very low

Note: S&P Global Ratings' ratings on local and regional governments are based on eight main rating factors listed in the table above. Section A of S&P Global Ratings' "Methodology For Rating Non-U.S. Local And Regional Governments," published on June 30, 2014, summarizes how the eight factors are combined to derive the foreign currency rating on the government.

Key Sovereign Statistics

Sovereign Risk Indicators, Dec. 14, 2017. Interactive version available at <http://www.spratings.com/sri>

Related Criteria

- Criteria - Governments - International Public Finance: Methodology For Rating Non-U.S. Local And Regional Governments, June 30, 2014
- Criteria - Governments - International Public Finance: Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments And Related Entities And For Rating Their Commercial Paper Programs, Oct. 15, 2009
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Governments - International Public Finance: Methodology And Assumptions: The Impact Of PPP Projects On International Local And Regional Governments: Refined Accounting Treatment, Dec. 15, 2008

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

Saskatoon (City of)

Issuer Credit Rating	AAA/Stable/--
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.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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