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Research Update:

City of Saskatoon 'AAA' Ratings Affirmed On Very Strong Economy And Exceptional Liquidity

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Overview

- We are affirming our 'AAA' long-term issuer credit and senior unsecured debt ratings on the City of Saskatoon.
- The ratings reflect our opinion of the city's very strong economy and budgetary flexibility, exceptional liquidity levels, and very low debt.
- The stable outlook reflects our expectations that, throughout the two-year outlook horizon, Saskatoon will continue benefiting from a very strong economy, and maintain exceptional liquidity, strong budgetary performance, and low debt.

Rating Action

On Jan. 17, 2017, 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.

Rationale

In the past two years, a significant decline in commodity prices has dampened Saskatoon's economic performance, resulting in negative real GDP growth and rising unemployment. Nevertheless, we believe that the city's revenue structure, with very strong budgetary flexibility, strong financial management, and very strong economy, as reflected in high nominal GDP per capita, were able to mitigate this impact.

The ratings also reflect our opinion of the city's exceptional liquidity, strong budgetary performance, and very low debt and contingent liabilities, as well as our assessment of the very predictable and well-balanced institutional framework for Canadian municipalities.

Saskatoon's economic fundamentals are very strong, in our opinion. Saskatchewan's GDP per capita averaged US\$62,800 in 2013-2015, and we estimate that the city's GDP per capita would be in line with the province's, given its stature as Saskatchewan's largest Census metropolitan area and the subsequent greater economic diversity than other areas of the province. Agriculture, the public sector, and in particular 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 Saskatoon's financial management is strong. In our view, the city's

management team is experienced and qualified to effectively enact fiscal policies, as well as effectively respond to external risks. Saskatoon demonstrates what we view as good political and managerial strength as evidenced by its very lengthy track record of passing budgets 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 Saskatoon also has very strong budgetary flexibility, which is consistent with that of its peers. In our 2015-2019 base-case forecast, we expect the city's budgetary flexibility will remain in line with historical results, with average capital expenditures that represent greater than 15% of adjusted total expenditures and modifiable revenues greater than 70% of adjusted operating revenues, on average.

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.

The city's budgetary performance has historically been stable and healthy, in our view. In our 2015-2019 base-case scenario, we expect the city will continue to generate robust operating surpluses relative to those of its peers, averaging about 18% of adjusted operating revenue. Saskatoon typically generates near-balanced results or modest deficits of less than 5% after taking into account capital revenues and expenditures, helping to maximize pay-as-you-go financing for capital projects and mitigating the need to issue additional debt. In our base-case forecast, we expect the city will generate a modest after-capital deficit, on average, from 2015-2019. Of note, Saskatoon derives some of its revenues from its land development operations. However, this introduces risks to total revenues due to the exposure to potential fluctuations in demand and the high cost of servicing land.

While we view Saskatoon's debt burden as very low, we expect that it will increase in the next two years, fueled by the city's large capital program. The city's tax-supported debt burden was about 32.3% of consolidated operating revenues in 2015 and we forecast it will remain above 30% on average through 2019. However, in our view, mitigating this increased debt burden are the large operating margins Saskatoon generates, which totaled C\$661 million in 2012-2014, and 2.8x of debt outstanding at the end of 2015. Interest expenses are what we view as low, and we expect that they will continue to represent about 1% of operating revenues, on average.

In our opinion, the city has very low contingent liabilities. We believe Saskatoon will remain contingently liable for the financing costs through the construction phase of the two public-private partnership projects (P3s) in the capital plan. One project will be in its operating phase in 2017 and the other by 2018. As a result, the costs related to both of these projects are incorporated in our analysis of the city's tax-supported debt. In addition, we deem the proposed contracts' fixed-price nature and risk transference sufficiently robust that the impact on the city's credit profile is not material. Liabilities stemming from standard future employee benefits and landfill postclosure liabilities equaled about 5% of consolidated operating revenues in 2015.

Liquidity

Saskatoon's exceptional liquidity bolsters its credit profile, in our opinion. In our base-case scenario, we estimate free cash and liquid assets to average about C\$362 million in 2017 and to cover more than 13x the projected debt service for 2017. In our opinion, the city's internal cash flow generation is robust, with operating balances before interest representing more than 5x debt service. In addition, 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. We believe that the city will maintain exceptional liquidity levels to meet debt service requirements.

Outlook

The stable outlook reflects our base-case expectations that, in the next two years, Saskatoon will continue to benefit from a very strong economy and maintain exceptional liquidity. We further expect the city's debt burden to increase moderately to about 40% of consolidated operating revenue and for high operating margins to continue mitigating it.

Although we view it as unlikely in the medium term, we could lower the ratings if the city's capital program were to increase significantly and remain high, putting pressure on budgetary performance and debt.

Key Statistics

Table 1

City of Saskatoon -- Economic Statistics						
	--Year ended Dec. 31--					
	2011	2012	2013	2014	2015	2016bc
Population	234,200	239,000	248,700	257,300	262,900	268,849
Population growth (%)	N.M.	2.0	4.1	3.5	2.2	2.3
GDP per capita (local currency) (single units)	N/A	N/A	N/A	N/A	N/A	N/A

Table 1

City of Saskatoon -- Economic Statistics (cont.)						
	--Year ended Dec. 31--					
	2011	2012	2013	2014	2015	2016bc
Real GDP growth (%)	6.3	4.7	6.7	4.6	(0.4)	(0.1)
Unemployment rate (%)	8.6	5.5	4.3	4.1	5.8	6.9

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. Sources typically include national statistical offices.

Table 2

City of Saskatoon -- Financial Statistics							
	--Year ended Dec. 31--						
(Mil. C\$)	2013	2014	2015	2016bc	2017bc	2018bc	2019bc
Operating revenues	765	803	815	852	891	929	969
Operating expenditures	545	558	618	674	723	780	841
Operating balance	220	245	196	178	168	149	129
Operating balance (% of operating revenues)	28.7	30.5	24.1	20.8	18.9	16.1	13.3
Capital revenues	102	67	131	73	79	87	108
Capital expenditures	380	307	330	240	262	288	356
Balance after capital accounts	(58)	5	(3)	11	(14)	(52)	(119)
Balance after capital accounts (% of total revenues)	(6.7)	0.6	(0.3)	1.2	(1.4)	(5.1)	(11.1)
Debt repaid	23	21	25	24	25	32	30
Net budget loans	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Balance after debt repayment and onlending	(81)	(16)	(28)	(13)	(38)	(84)	(149)
Balance after debt repayment and onlending (% of total revenues)	(9.3)	(1.9)	(3.0)	(1.4)	(4.0)	(8.3)	(13.8)
Gross borrowings	60	25	14	0	89	9	18
Balance after borrowings	(21)	9	(14)	(13)	50	(75)	(132)
Operating revenue growth (%)	0.7	4.9	1.5	4.6	4.6	4.2	4.4
Operating expenditure growth (%)	10.1	2.3	10.9	9.1	7.2	7.9	7.8
Modifiable revenues (% of operating revenues)	74.4	76.7	80.1	81.0	81.8	82.6	83.3
Capital expenditures (% of total expenditures)	41.0	35.5	34.8	26.2	26.6	27.0	29.7
Direct debt (outstanding at year-end)	235	238	228	204	268	245	233
Direct debt (% of operating revenues)	30.7	29.7	28.0	24.0	30.1	26.4	24.0
Tax-supported debt (% of consolidated operating revenues)	30.7	29.7	32.3	37.4	50.5	51.7	47.6
Interest (% of operating revenues)	0.8	0.9	1.3	0.9	0.7	1.0	0.9
Debt service (% of operating revenues)	3.7	3.6	4.4	3.7	3.5	4.4	4.0

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.

Ratings Score Snapshot

Table 3

City of Saskatoon -- Rating Score Snapshot	
Key Rating Factors	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

*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 government's foreign currency rating.

Key Sovereign Statistics

Sovereign Risk Indicators, Dec. 14, 2016

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

Ratings List

Ratings Affirmed

Saskatoon (City of)

Issuer Credit Rating	AAA/Stable/--
Senior Unsecured	AAA

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