S&P Global
Ratings

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Research Update:

Norfolk County Rating Affirmed at 'AA-'; Outlook Stable

September 10, 2021

Overview

- Economic recovery in 2021 will increase as COVID-19-related restrictions ease and key industries expand.
- We expect capital spending and the debt burden will increase as the county continues to address its infrastructure needs and after-capital deficits will increase starting in 2022.
- Nevertheless, we are affirming our 'AA-' long-term issuer credit rating on the county and maintaining a stable outlook.
- The stable outlook reflects our expectation that Norfolk County will continue to generate moderately increasing operating balances that will help keep the expected tax-supported debt burden below 50% of operating revenues until 2023.

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Rating Action

On Sept. 10, 2021, S&P Global Ratings affirmed its 'AA-' long-term issuer credit rating on Norfolk County, in the Province of Ontario. The outlook is stable.

Outlook

The stable outlook reflects our expectation that in the next two years, Norfolk will post after-capital deficits averaging 0.3% of total revenues, largely due to its expanding capital plan. We also expect the county's tax-supported debt will reach 47% of operating revenues by 2023, and that Norfolk will preserve sufficient total free cash to more than cover upcoming debt service.

Downside scenario

We could lower the rating over the next two years if aggressive capital spending leads to after-capital deficits above 5% of adjusted total revenues, on average, and pushed Norfolk's tax-supported debt to more than 60% of operating revenues, or if debt service coverage were to erode to less than 100%, and we expected such a scenario to persist over the forecast horizon.

Upside scenario

We could raise the rating in the next two years if after-capital budgetary performance strengthens such that after-capital deficits are consistently below 5% of adjusted total revenues, and if strong operating revenue performance or less reliance on debt financing led to tax-supported debt falling to less than 30% of operating revenues during the forecast horizon. However, we view this scenario as unlikely.

Rationale

We expect Norfolk's economy will continue recovering in 2021 as pandemic-related restrictions ease and the county's key industries such as manufacturing and agriculture expand. The county ended 2020 in a relatively strong fiscal position as increased government transfers and prudent financial management helped more than offset pandemic-related pressures. We expect the county will continue to produce solid operating surpluses over the next few years, although this will only partially fund its sizable capital developments and aging infrastructure requirements. In our updated base-case scenario for 2021-2023, the county will issue about C$47 million for capital expenditures and we expect tax-supported debt will reach 47% of operating revenues. We expect Norfolk will continue to benefit from a supportive institutional framework. On the other hand, we believe that the county's economic profile, which reflects limited growth prospects and a less favorable socioeconomic profile, partially mitigates these strengths.

Local economy will continue to show limited growth prospects and a weaker socioeconomic profile relative to the national economy, while institutions will remain broadly supportive.

We believe that Norfolk's lower income levels, less-than-favorable population dynamics, and weaker growth prospects constrain the economy. We estimate that because of a continuing influx of retirees, those 55 and over will continue to represent more than 35% of the total estimated population of about 70,000 in 2020. The aging demographics could negatively affect the labor pool and hinder investment in Norfolk, in our view. Although several key industries such as manufacturing and agriculture have expanded over the past year, lack of sufficient labor force supply continues to affect potential growth. In addition, we consider the county's location as less favorable compared with that of peers, based on Norfolk's relative remoteness from major cities and transportation routes. Although municipal GDP data are unavailable, we estimate that Norfolk's GDP per capita is below that of Canada, which we estimate to be about US$52,900, based on the county's lower income levels.

Despite these economic limitations, we believe that Norfolk, as do other Canadian municipalities, benefits from a very predictable and well-balanced institutional 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.

We believe the management team has adequate expertise in implementing policy changes. Although there has been some recent turnover in financial management, we do not expect significant policy deviations as a result. The county presents a one-year, detailed, tax-supported operating budget. It continues to produce a one-year, rate-supported operating budget, and 10-year tax- and rate-supported detailed capital plans, with corresponding funding sources. We believe that debt and liquidity management remains prudent, with a formal investment policy and a conservative internal debt limit.

We expect sizable capital spending will lead to larger after-capital deficits and more debt issuance during the forecast horizon.

Although 2020 presented increased budgetary pressures, the county was able to end the year in a relatively strong position due to increases in tax revenues, government transfers, and its cost-containment strategies. This is reflected in our revised base-case scenario for 2019-2023, where we expect operating balances to average 20% of adjusted operating revenues and after-capital deficits to decrease to 0.3% of adjusted total revenues, on average. However, given the county's capital replenishment and infrastructure requirements, it expects to spend about C$190 million in capital expenditures from 2021-2023, which we estimate will lead to larger after-capital deficits starting in 2022.

We estimate debt will continue rising as Norfolk proceeds with its capital plan. We expect additional borrowings of about C$47 million in 2021-2023, bringing tax-supported debt to about 47% of operating revenues by 2023. We believe that interest payments will remain very modest, at less than 2% of operating revenues for 2021-2023. At the same time, in our opinion, the county has minimal contingent liabilities. Liabilities stemming from retirement-related benefits and landfill post-closure costs equaled about 14% of consolidated operating revenues in 2020.

In our view, the county's liquidity is solid. By our estimates, total free cash is about C$40.4 million and covers about 3.9x estimated debt service over the next 12 months. We expect this ratio will remain above 100% during the forecast outlook horizon. Similar to that of its domestic peers, Norfolk's access to external liquidity is satisfactory, in our view.

Key Statistics

Table 1

Norfolk County -- Selected Indicators

	--Fiscal year ended Dec. 31--					
(Mil. C$)	**2018**	**2019**	**2020**	**2021bc**	**2022bc**	**2023bc**
Operating revenues	173	178	197	200	207	215
Operating expenditures	149	156	151	157	162	168
Operating balance	23	22	46	43	45	47
Operating balance (% of operating revenues)	13.5	12.4	23.4	21.4	21.7	22.0
Capital revenues	10	10	16	19	9	9
Capital expenditures	37	40	40	54	68	68
Balance after capital accounts	(3)	(7)	22	8	(14)	(11)
Balance after capital accounts (% of total revenues)	(1.5)	(3.9)	10.3	3.5	(6.3)	(5.0)

Table 1

Norfolk County -- Selected Indicators (cont.)

	--Fiscal year ended Dec. 31--					
(Mil. C$)	**2018**	**2019**	**2020**	**2021bc**	**2022bc**	**2023bc**
Debt repaid	6	5	7	7	7	8
Gross borrowings	0	27	21	0	21	26
Balance after borrowings	(8)	14	37	1	1	7
Direct debt (outstanding at year-end)	54	76	82	69	84	102
Direct debt (% of operating revenues)	31.4	42.6	41.6	34.6	40.3	47.1
Tax-supported debt (outstanding at year-end)	54	76	82	69	84	102
Tax-supported debt (% of consolidated operating revenues)	31.4	42.6	41.6	34.6	40.3	47.1
Interest (% of operating revenues)	1.3	1.1	1.3	1.1	1.1	1.3
National GDP per capita (single units)	60,196	61,466	58,016	65,195	67,992	69,683

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

Norfolk County -- Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	3
Financial management	3
Budgetary performance	2
Liquidity	1
Debt burden	2
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, July 12, 2021. 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

- Risk Indicators For Canadian Local And Regional Governments, Sept. 1, 2021
- Credit Conditions North America: Q3 2021: Looking Ahead, It's Looking Up, June 29, 2021
- Economic Outlook Canada Q3 2021: Growth Setback In The Spring Will Give Way to Summer Boom, June 25, 2021
- Prudent Financial Management And A Strong Institutional Framework Are Helping Canadian Municipalities Negotiate The Impact of COVID-19, Nov. 30, 2020
- Guidance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019

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	
Norfolk County	
Issuer Credit Rating	AA-/Stable/--

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