SUB-SOVEREIGN

MOODY'S
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CREDIT OPINION

15 May 2019

Update

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RATINGS

Vancouver, City of

Domicile	British Columbia, Canada
Long Term Rating	Aaa
Type	Senior Unsecured - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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City of Vancouver (Canada)

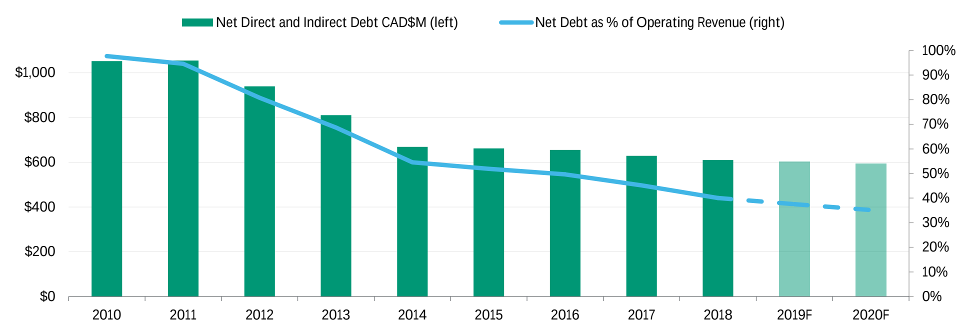
Update following affirmation of Aaa rating

Summary

The credit profile of the City of Vancouver (Aaa stable) reflects high levels of liquidity and a strong local economy that supports access to a broad tax base. The city's credit profile also benefits from strong debt affordability and solid governance and financial management practices enabling consistent, positive fiscal outcomes. These positives are balanced against rising infrastructure needs from a growing population and persistent housing affordability challenges despite recent housing initiatives. Vancouver also benefits from a high likelihood that the Province of British Columbia (Aaa stable) would provide extraordinary support if the city faced acute liquidity stress.

Exhibit 1

Debt continues to decline, supporting strong debt affordability



Source: Moody's, City of Vancouver

Credit strengths

- » Strong economic growth supported by economic diversity
- » Positive operating results backed by stable revenue sources
- » High levels of liquidity and affordable debt burden
- » Strong governance and supportive institutional framework

Credit challenges

- » Housing affordability pressures which persist despite recent policy actions
- » Continued pressure on capital spending from population growth and infrastructure initiatives

Rating outlook

The outlook is stable, reflecting continued strong debt affordability, and our view that the city will be able to maintain positive operating results.

Factors that could lead to a downgrade

A sustained period of fiscal losses, a significant increase in the city's debt burden beyond projected levels, or a permanent reduction in the city's liquidity sources would result in downward pressure on the rating.

Key indicators

Exhibit 2

City of Vancouver

as at 12/31	2013	2014	2015	2016	2017	2018	2019F
Net Direct Debt/Operating Revenue (%)	68.6	54.5	51.9	49.6	45.2	40.0	37.5
Gross Operating Balance/Operating Revenue (%)	30.3	29.3	28.7	27.6	28.4	31.2	31.5
Cash Financing Surplus (Requirement)/Total Revenue (%)	5.6	10.4	12.3	4.1	5.8	10.8	7.2
Interest Payments/Operating Revenue (%)	3.3	2.9	2.7	2.8	2.8	2.4	2.2
Debt Service/Total Revenue (%)	4.3	4.0	3.3	2.4	9.2	2.3	8.0
Capital Spending/Total Expenditures (%)	19.7	17.2	16.6	26.1	20.2	14.8	19.0
Self-Financing Ratio	1.3	1.7	1.9	1.2	1.4	1.9	1.9

Source: Moody's, City of Vancouver financial statements

Detailed credit considerations

On 9 May 2019 we affirmed the city's Aaa rating with a stable outlook, reflecting high levels of liquidity, a strong local economy and strong debt affordability.

The credit profile of Vancouver, as expressed in its Aaa stable rating, reflects a baseline credit assessment (BCA) of aaa for the city and the likelihood of extraordinary support coming from the Province of British Columbia in the event that the municipality faced acute liquidity stress.

Baseline credit assessment

Strong economic growth supported by economic diversity

The population of the city of Vancouver has seen consistent growth in recent years, rising to around 673,000 (2.6 million for the metropolitan area) at year-end 2018 driven to a large extent by immigration. The city serves as a major trade, transportation and service centre and is home to Canada's largest and busiest port, the Port Metro Vancouver.

Vancouver's economy is diversified and benefits from its position as a gateway to the Pacific and access to Asian markets. The economy has expanded at a solid pace in recent years, supported by strong performances in the resource, services, technology and construction sectors. Despite recent measures to curb speculative demand and some softening in the real estate sector in 2018, the construction sector remains strong. Its strength is fuelled by robust residential real estate construction in support of increasing housing demand, which over the last few years exceeded housing supply.

The metro Vancouver region is expected to see strong real GDP growth with a projected growth rate averaging 2.3% during 2019-2022, although this growth will be slower than the robust growth that averaged 2.7% during 2015-2018 due to tightening lending conditions and a slowing housing market. Vancouver's unemployment rate continued its downward trend to 4.3% in 2018, trending below the provincial and national averages. We anticipate that the unemployment rate will remain at current low levels over the next 2-3 years.

Positive operating results backed by stable revenue sources

Vancouver consistently posts strong operating results supported by a stable share of property taxes (55% of 2018 operating revenue) and user fees (18% of operating revenue) and we expect that this composition will remain consistent over the next few years. Gross operating surplus was 31.2% of operating revenue in 2018 and averaged 29.0% for the period 2014-2018, as revenue growth continued to exceed expenditure growth. Going forward, we expect operating revenue growth primarily from rising property taxes, user fees, and development fees, while operating expense growth will reflect expenses related to a rapidly growing metropolitan region, including wages and fixed costs, utilities costs and other costs related to maintaining city services. In our view the city will be able to maintain positive operating margins over the next 2-3 years supported by predictable property taxes and user fees.

Vancouver's budgetary flexibility is somewhat constrained by the fact that it needs to manage property tax increases in conjunction with other taxing authorities including the Province of British Columbia (for school taxes), TransLink (the region's public transit authority), as well as regional authorities of Metro Vancouver. The city could face fiscal pressures if expenditures outpaced revenue growth, however Vancouver's ability to maintain strong fiscal results is supported by prudent fiscal management and strong cash flow generation. The city also maintains sizeable reserves, including the CAD5.7 billion (assessed value) Property Endowment Fund.

High levels of liquidity and affordable debt burden

Vancouver's liquidity profile is very strong and the city's liquidity position has continued to improve over the last nine years. Cash and investments (net of sinking funds) covered approximately 3.1x outstanding debt and 1.5x operating expense in 2018. Despite ongoing pressure on liquidity from governmental services and infrastructure investments in the capital plan, we expect that the city's liquidity profile will remain robust with a comfortable net cash position over the next 12-24 months.

Net direct and indirect debt measured 40% of operating revenue in 2018 and continued to improve each year since 2009. The city will finance ongoing debt maturities from its sinking fund reserves, which represented 45% of total debt in 2018, which we consider a very strong level (39% in 2017). The city also includes safeguards against excessive debt, including setting an internal limit on its annual tax-supported debt servicing payments to 10% of operating expenses (the city expects this ratio to be below the limit over the next 6 years). New debt issuances, estimated at approximately CAD125 million in each of the next four years, will be used primarily to maintain and renew the city's critical infrastructure and public amenities in state of good repair. While this puts modest pressure on debt and liquidity metrics going forward, we anticipate that the city's debt burden will remain manageable given sizeable debt maturities that will be repaid from reserves. Debt affordability is supported by a continued low interest rates environment, although we anticipate a steady rise in interest rates over the next few years. Interest payments relative to operating revenue remained low at 2.4% in 2018.

The Moody's-adjusted net debt balance includes the city's debentures net of sinking funds (CAD611 million in 2018), and excludes the debt of Metro Vancouver (CAD2 billion in 2018). The city, which is a member of but does not borrow through Metro Vancouver, has contingent liability through a joint and several guarantee for the debt of Metro Vancouver which borrows on behalf of its member area municipalities (except Vancouver).

With the exception of utility projects (water, sewer and neighbourhood energy), authority to borrow for capital projects requires electorate approval and is sought via plebiscite held concurrently with civic elections. In addition to multi-year financial planning, management has historically adhered to conservative debt and investment management policies, limiting the city's exposure to market-related risks and helping to ensure relatively smooth debt servicing costs.

Strong governance and supportive institutional framework

Vancouver's operating results are supported by strong governance and prudent financial management practices including comprehensive, transparent and timely financial reporting. The city uses a long-term financial planning framework, including a 10-year Capital Strategic Outlook, a 4-year Capital Plan, and a 5-year Financial Plan which help identify anticipated pressures upfront.

The institutional framework governing municipalities in British Columbia is mature and highly developed. The division of roles and responsibilities between the province and municipalities is clearly articulated. Historically, changes to the institutional framework have occurred at a measured, evolutionary pace, following discussions between both parties.

Vancouver's credit profile also benefits from the stability inherent in the provincial institutional framework. Provincial legislation dictates a high degree of oversight, including limits on debt burdens, while policy flexibility, on both the revenue and expenditure sides, helps Vancouver manage pressures as they arise.

Housing affordability pressures which persist despite recent policy actions

Housing prices in Vancouver experienced rapid historical growth due to a strong regional economy, consistent demand from a rising population and certain speculative activity, and limited supply of housing stock. These pressures resulted in an escalation of living costs, potentially limiting employers' ability to attract workers and therefore impact economic activity. In addition, the city faces expenditure pressures from social services since it needs to allocate significant capital resources to increase affordable housing supply and improve vacancy rates.

A number of federal, provincial and municipal policy actions have been implemented between 2016 and 2018 to temper the persistent rise in housing prices. These measures included tighter federal mortgage eligibility rules, and the implementation of measures including a property transfer tax on purchases by foreign residents, a tax on vacant and secondary homes, and a luxury home surtax. The city implemented its own measures with the empty homes tax and new short-term rental regulations. While these measures resulted in a softening in the increase of home prices, prices remain above the national averages and affordability continues to be a significant concern for the city. For 2019, Vancouver allocated CAD78 million in capital funding (including CAD30 million in new projects) to improve affordability and increase housing supply. Over the four-year period of the 2019-2022 Capital Plan, the city earmarked CAD540 million for affordable housing initiatives. The city's operating expenditures also include CAD8 million related to housing affordability. Although the majority of funding will come from development contributions, these initiatives continue to put pressure on the city's expenditures.

In response to its housing affordability challenges, City Council approved the creation of the Vancouver Affordable Housing Endowment Fund in 2018, with the goal of transferring CAD2 billion in non-market housing assets from its capital and property endowment funds. The city expects that it will be able to better manage its stock of affordable housing assets under the new consolidated fund.

Nevertheless, the city's revenue profile remains relatively sheltered from fluctuations in home prices. This is because the city has flexibility to adjust property tax (mill) rates annually to reflect changes in property assessments in order to ensure fairly stable property tax revenues in a changing real estate price environment. Therefore, property tax revenues tend not to fluctuate with short-term volatility in home prices.

Continued pressure on capital spending from population growth and infrastructure initiatives

Anticipated population growth over the next few years will continue to place pressure on the existing transportation and utilities infrastructure in Vancouver, and will necessitate both property tax and utility rate increases. For 2019, City Council approved a property tax increase of 4.15%. The tax increase supports both the city's maintenance and new initiatives, including funding its CAD563 million 2019 capital expenditure budget (this amount is significantly higher than the restated CAD444 million 2018 capital budget, due to significant increases in the city's priority areas to maintain or renew its ageing infrastructure and improve housing affordability). In April 2019, Council also approved a 1% tax shift from certain non-residential to residential properties for 2019, with an additional 1% to be phased in over the following two years. Utility rates are expected to increase a combined 8.7% in 2019 (7.9% in 2018) in order to keep pace with the growing cost of providing utility services in Vancouver.

A significant portion of the city's capital spending supports green infrastructure projects. Vancouver implemented the 'Greenest City Action Plan' in 2011 to become the 'world's greenest city' by 2020, with three priority areas in carbon, waste and ecosystems. The plan was complemented by the 'Renewable City Action Plan', approved in 2017, which aims to derive the city's energy from 100% renewable sources by 2050.

The 2019 capital budget represents the first year of the city's new CAD2.8 billion, 2019-2022 capital plan. The capital plan is financed through a combination of pay-as-you-go financing from development contributions, city contributions, capital reserves and debt financing. Although the projected debt financing will result in modest pressures on Vancouver's debt to operating revenue ratio, the debt burden will remain affordable and continues to position the city well in its rating category compared with other Aaa-rated Canadian municipalities.

Extraordinary support considerations

Moody's assigns a high likelihood of extraordinary support from the Province of British Columbia (Aaa stable), reflecting our assessment of risk to the province's reputation as a regulator of municipalities and incentive for the provincial government to minimize the risk of potential disruptions to capital markets if Vancouver or any other municipality were allowed to default.

Rating methodology and scorecard factors

The assigned BCA of aaa is one notch above the scorecard-indicated outcome of aa1. The scorecard-indicated outcome of aa1 reflects (i) an idiosyncratic risk score of 2 (presented below) on a 1 to 9 scale, where 1 represents the strongest relative credit quality and 9 the weakest; and (ii) a systemic risk score of Aaa, as reflected in the sovereign bond rating for the Government of Canada (Aaa stable).

For details about our rating approach, please refer to Rating Methodology: Regional and Local Governments, 16 January 2018.

Exhibit 3

City of Vancouver

Baseline Credit Assessment	Score	Value	Sub-factor Weighting	Sub-factor Total	Factor Weighting	Total
Scorecard						
Factor 1: Economic Fundamentals						
Economic strength	5	100.46	70%	3.8	20%	0.76
Economic volatility	1		30%			
Factor 2: Institutional Framework						
Legislative background	1		50%	1	20%	0.20
Financial flexibility	1		50%			
Factor 3: Financial Performance and Debt Profile						
Gross operating balance / operating revenues (%)	1	29.89	12.5%	2.25	30%	0.68
Interest payments / operating revenues (%)	3	2.57	12.5%			
Liquidity	1		25.0%			
Net direct and indirect debt / operating revenues (%)	3	40.00	25.0%			
Short-term direct debt / total direct debt (%)	3	11.90	25.0%			
Factor 4: Governance and Management - MAX						
Risk controls and financial management	1			1	30%	0.30
Investment and debt management	1					
Transparency and disclosure	1					
Idiosyncratic Risk Assessment						**1.94(2)**
Systemic Risk Assessment						**Aaa**
Suggested BCA						**aa1**

Source: Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
VANCOUVER, CITY OF	
Outlook	Stable
Senior Unsecured -Dom Curr	Aaa

Source: Moody's Investors Service

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