

CREDIT OPINION

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Contacts

Sarah Jensen +1.214.979.6846
Analyst
 sarah.jensen@moody's.com

Grayson Nichols +1.214.979.6851
VP-Senior Analyst
 grayson.nichols@moody's.com

CLIENT SERVICES

Americas 1-212-553-1653
 Asia Pacific 852-3551-3077
 Japan 81-3-5408-4100
 EMEA 44-20-7772-5454

Lafayette (City of) LA

Update to credit analysis

Summary

Lafayette, LA's sales tax (Aa3) credit profile is bolstered by strong coverage levels. The local economy remains relatively stable as a significant higher education and health care presence helps mitigate volatility in the oil and gas sector. The city's favorable location along two major highways provides a regional draw for the city's retail and restaurant establishments. The two sales tax pledges approved by voters, 1961 and 1985, are relatively broad and apply to most transactions. The 1985 tax excludes food and medical while the 1961 tax does not. Pledged revenues have fluctuated modestly in recent years, and collections are somewhat concentrated as the top ten taxpayers represent over 20%. The credit profile remains challenged by employment levels that have not yet rebounded to healthier levels prior to declines in the oil and gas sector.

Credit strengths

- » Strong debt service coverage
- » Relatively stable local economy with strong health care and higher education presence
- » Broad sales tax pledge with modestly improving revenues

Credit challenges

- » Moderate top taxpayer concentration
- » Recent weakness in collections and employment, likely driven in part by exposure to the oil and gas sector

Rating outlook

Moody's generally does not assign outlooks to local governments with this amount of debt outstanding.

Factors that could lead to an upgrade

- » Significant economic expansion and diversification
- » Sustained growth in pledged revenues leading to extremely strong debt service coverage

Factors that could lead to a downgrade

- » Persistent weakening of sales tax collection and significant deterioration in coverage
- » Substantial additional leveraging of pledged revenues

Key indicators

Exhibit 1

1961 tax security

Lafayette, LA

Credit Background

Pledged Revenues 1961 1% Sales and Use Tax

Legal Structure

Additional Bonds Test 1.50

Open or Closed Lien Open Lien

Debt Service Reserve Fund Requirement DSFF funded at lesser of standard 3-prong test

MADS Coverage

2017 MADS Coverage (x) 3.2x

Trend Analysis

	2013	2014	2015	2016	2017
Debt Outstanding (\$000)	185,555	174,770	162,745	150,175	126,355
Revenues (\$000)	41,997	43,949	44,474	42,795	42,997
Annual Debt Service Coverage (x)	2.4x	2.6x	2.7x	2.6x	2.9x

Source: Lafayette Consolidated Government's CAFRs, Bond Ordinances

Exhibit 2

1985 tax security

Lafayette, LA

Credit Background

Pledged Revenues 1985 1% Sales and Use Tax

Legal Structure

Additional Bonds Test 1.50

Open or Closed Lien Open Lien

Debt Service Reserve Fund Requirement DSFF funded at lesser of standard 3-prong test

MADS Coverage

2017 MADS Coverage (x) 3.3x

Trend Analysis

	2013	2014	2015	2016	2017
Debt Outstanding (\$000)	119,845	111,360	101,820	87,905	80,475
Revenues (\$000)	35,731	37,293	37,612	35,667	36,202
Annual Debt Service Coverage (x)	2.5x	2.8x	3.0x	3.0x	3.1x

The 1985 sales tax exempts food, prescriptions, and medical devices

Source: Lafayette Consolidated Government's CAFRs, Bond Ordinances

Profile

The city, along with the parish, is part of the Lafayette Consolidated Government, located in south central Louisiana, about 135 miles west of [New Orleans](#) (A3 stable) and 60 miles west of Baton Rouge ([Baton Rouge Combined City-Parish Government](#), Aa2 issuer

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rating). The city's population is estimated at a peak 125,808 as of 2016 while the parish population also reached a peak of 234,963 in 2016.

Detailed credit considerations

Tax base and nature of pledge: stable local economy despite oil and gas exposure

Ongoing development and institutional presence will provide stability for the local economy despite recent weakness in the oil and gas sector. The city benefits from its location at the intersection of two major highways which enables the city and its retailers to easily attract consumers from elsewhere in the parish and the broader region in addition to city residents. While the oil and gas sector continues to represent more than 8% of employment within the parish, ongoing development in other sectors and the city's role as a regional trade, retail, and entertainment hub are helping mitigate the recent weakness in the oil and gas sector. Over one million tourists visit the area annually, and more than 20% of the sales conducted within the parish are from visitors from outside the parish. Big box retailers have opened in recent years, and the city continues to see new small business opening up along with additional retail and restaurant development. A strong local fiber network also continues to attract new firms. Substantial health care and higher education presence also provide stability. Two of the top ten employers in the city are medical centers. Lafayette is home to the University of Louisiana-Lafayette that has an enrollment of roughly 19,000 and is the second largest university in the state.

While the population trends have been strong, employment trends in the region have weakened since 2014, as indicated by a shrinking labor force and declining number of jobs. The estimated population as of 2016 is 125,808, up 4.3% from the last census. As of August 2018, the city's unemployment rate was 5.3% which was comparable to the state (5.5%) but higher than the nation (3.9%) for the same period. Positively, since August 2017, the labor force and number employed did modestly increase by 1.6% and 1.9% respectively. Despite this improvement, the labor force still remains 9% lower than it was in 2014. The trend is similar across the broader parish as well. Lower employment levels can challenge sales tax collections. Resident wealth levels are consistent with national levels and are likely somewhat depressed given the large university presence. As of the 2016 American Community Survey per capita income and median family income are 101.9% and 97.2% of national levels, respectively.

The nature of the sales tax pledge is broad, and the taxes were approved in perpetuity. The 1961 sales tax is a 1% sales and use tax levied on all retail sales including food, medicine, and medical devices. The 1961 pledge is a bit broader than the city's 1985 sales tax which excludes food and medical purchases, which has provided a bit more stability in the 1961 pledged revenue stream. Collections are moderately concentrated as the top ten sales taxpayers account for approximately 23.5% of the city's sales tax collections.

Debt service coverage and revenue metrics: strong coverage supported by modestly improving revenues

Coverage levels will remain healthy, reflecting a relatively stable revenue base and descending debt service. Over the last twenty years, the city's 1961 and 1985 1% sales and use tax revenues have generally seen moderate annual growth with a few exceptions. In 2006, the city's pledged revenue collections for both the 1961 and 1985 taxes spiked significantly (approximately 19% over the prior year), largely due to the influx of population from the New Orleans area and points south following Hurricane Katrina. During the national recession, collections fell 4.4% in 2009 but stabilized in 2010 for the broader 1961 pledge. By contrast, the more narrow 1985 tax pledged revenues fell 5% in 2009 and 1% in 2010 before returning to growth in 2011. Most recently, weakness in the oil and gas sector driving weaker employment trends resulted in a 3.8% decline in fiscal 2016 for the 1961 tax and 5.2% decline in the 1985 tax. Both taxes recovered a portion of that decline in fiscal 2017 but remain the peak in fiscal 2015. Despite the recent fluctuations, coverage levels remain strong. The \$43 million of 1961 revenues collected in fiscal 2017 provide a solid 3.15 times coverage of maximum annual debt service (MADS) set to occur in 2022. Likewise, the 1985 collections in fiscal 2017 provide a healthy 3.26 times MADS coverage with MADS to occur in 2020.

Through the first eleven months of fiscal 2018, sales tax revenues have softened slightly, with a 0.5% year-over-year decline in the 1961 revenues and 0.9% decline in the 1985 collections. The city has budgeted for flat collections in fiscal 2018 and 2019 and 2% annual growth for fiscals 2020-2022. The average annual growth over the past five years is 1.2% for the 1961 tax and 1% for the 1985 tax.

LIQUIDITY

As of fiscal 2017, the 1961 sales tax sinking fund had a liquidity position of \$7.1 million and the 1961 reserve fund liquidity position of \$11.6 million. For the 1985 tax, the sinking fund had cash of \$4.1 million and the reserve fund held \$8.8 million.

Debt and legal covenants: manageable debt profile supported by adequate legal provisions

Leverage on the 1961 and 1985 sales taxes will remain manageable despite future issuance plans. Following the 2018 refunding issuances for both liens, the city has \$115.2 million in outstanding principal secured by the 1961 sales tax and \$71.3 million outstanding secured by the 1985 tax. The city has a projected \$70 million in future borrowing incorporated into the city's bond issuance plans over the next five years, which will be manageable given the descending debt service schedule. Future issuance could occur as early as the first quarter of 2019. The city manages its debt profile to maintain at least 2 times coverage on outstanding debt.

Legal provisions for the bonds are the same for both the 1961 tax and 1985 tax. Provisions include an additional bonds test (ABT) of 1.50 times MADS for succeeding fiscal years including any additional debt to be issued. A debt service reserve is also required to be funded at the lesser of (i) 10% of the original principal proceeds from the bonds, any outstanding parity bonds, and any issue of additional parity bonds, (ii) MADS, or (iii) 125% of the average aggregate amount of principal installments and interest becoming due in any fiscal year. The reserve fund is cash funded for both liens. As approved by voters, of the excess revenues from both pledges that remain following debt service, the city may use up to 35% for general purposes.

DEBT STRUCTURE

All parity debt under both pledges is fixed rate and amortizes over the long term. Annual debt service for the 1961 tax peaks at \$13.7 million in fiscal 2022 before descending through maturity in 2038. For the 1985 tax, annual debt service peaks at \$11.1 million in fiscal 2020 and then descends through maturity in 2034.

DEBT-RELATED DERIVATIVES

There are no swap or interest rate derivative agreements associated with these pledges.

Management and governance: consolidated government

The Governing Authority of the Lafayette City-Parish Consolidated Government is the Council, consisting of nine members elected from nine single member districts. The Charter further provides that the Mayor President succeeds to all powers of the Mayor of the City.

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