

State of Ohio

New Issue Summary

Sale Date: February 11, 2020 by competitive bid

Series: Conservation Projects GO Bonds, Series 2020A; Natural Resources GO Bonds, Series X; Coal Development GO Bonds, Series P

Purpose: Finance capital improvements

Security: General Obligation Bonds are full faith and credit obligations of the State of Ohio.

The state's 'AA+' Issuer Default Rating (IDR) and GO rating are based on its careful financial management that is reflected in maintenance of fiscal balance, the rebuilding of reserves, and low liabilities. Ohio's economy is demonstrating slow but steady growth, with recent performance more in line with, but still slightly lagging, the U.S. Sustained growth may be limited by Ohio's very slowly growing population.

Economic Resource Base: Ohio's economy is large and diverse, with distinct economic regions centered on several large urban centers. Manufacturing remains a disproportionately large sector with a concentration in more cyclically sensitive durable goods industries. Transportation equipment and related suppliers also have a strong presence. Economic growth has begun to pick up, with GDP growth and personal income trending higher, but still trailing national trends.

Key Rating Drivers

Revenue Framework: 'aa': Like most states, Ohio has an unlimited legal ability to raise operating revenues. Its revenue base is diverse and relies on broad-based income and sales taxes. Tax cuts implemented over the past several biennia have been manageable, aided by favorable economic and fiscal trends.

Expenditure Framework: 'aaa': Ohio retains ample flexibility to cut spending throughout the economic cycle. As in most states, the natural pace of spending growth is likely to be somewhat above revenue growth, requiring ongoing budget management. Carrying costs for debt and retiree benefits are below the median for states. Spending pressure in Medicaid and education appears to be well controlled.

Long-Term Liability Burden: 'aaa': Debt is typically conservatively managed and debt issuance primarily consists of GOs. On a combined basis, outstanding debt and net pension obligations are low and a below-average burden relative to other states.

Operating Performance: 'aaa': The state generally has a careful approach to financial operations and has consistently managed to achieve budgetary balance. In recent years, the state has relied more on budget reductions than revenue enhancements to balance the budget and also utilized several one-time sources during the Great Recession. The state's budget stabilization fund (BSF) has been restored after being drawn down during the recession and now totals \$2.7 billion, or over 11% of state source general revenue fund (GRF) revenues.

Ratings

Long Term Issuer Default Rating	AA+
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New Issues

\$50,000,000 Conservation Projects GO Bonds, Series 2020A	AA+
\$38,000,000 Natural Resources GO Bonds, Series X	AA+
\$8,000,000 Coal Development GO Bonds, Series P	AA+

Rating Outlook

Stable

Applicable Criteria

[Fitch Internal Liquidity Worksheet \(February 2019\)](#)

[U.S. Public Finance Tax-Supported Rating Criteria \(January 2020\)](#)

Related Research

[Fitch Rates Ohio's \\$96MM GO Bonds 'AA+'; Outlook Stable \(January 2020\)](#)

Rating Sensitivities

Ohio's IDR is sensitive to shifts in fundamental credit characteristics, including sustained economic growth that improves expectations for revenue growth. The rating is also sensitive to Ohio's ability to maintain fiscal balance in light of ongoing efforts to reduce the tax burden.

Current Developments

Tax revenues exceeded expectations in both fiscal years of the fiscal 2018-2019 biennium. Strong performance continued in fiscal 2019, with tax revenues increasing \$1 billion (4.8%) YOY and 2.9% above the revised estimate, driven by stronger than anticipated tax performance and improvement in the economy. PIT collections were very strong despite a change in withholding that lowered collections attributable to fiscal 2019. The state carried a significant fund balance into the fiscal 2020-21 biennium and maintained the budget stabilization fund at \$2.7 billion.

The state was late in enacting the fiscal 2020-21 biennial budget as the legislature could not come to agreement on a variety of tax and policy actions. The budget, enacted 17 days after the start of the fiscal year, incorporated a reduction in income tax rates, again continuing a policy of tempering revenue with rate reductions. The budget included many of the governor's priorities, including expanding spending for education, early childhood development and battling the opioid epidemic. While the school foundation formula was not changed as proposed by the governor, the budget provided \$675 million over the biennium for targeted programs in student wellness, including mental health counseling, mentoring and other school support. Schools will receive these funds on a per capita basis. The legislature set aside \$172 million from the fiscal 2019 balance to begin the process of funding the "H2Ohio" fund for investment in water and natural resource infrastructure.

Revenues are meeting forecast through the first half of fiscal 2020, with all major revenue categories tracking close to estimate. The budget assumes modest 2.1% state revenue growth in fiscal 2020 followed by 1.7% revenue growth in fiscal 2021.

Credit Profile

The Great Recession had a widespread impact on the Ohio economy, accelerating a longstanding slump in manufacturing and weighing on the slowly growing service sector. Recent economic performance has strengthened although GDP growth and personal income continue to slightly lag the U.S. Ohio's three larger cities, and in particular its capital Columbus, are doing well with stronger population growth and ongoing successful economic development efforts.

Important employment sectors include transportation, distribution and warehousing of manufactured goods, which is facilitated by an extensive system of ports on Lake Erie, barge service on the Ohio River, and advanced air-cargo and rail infrastructure. Health care and education are growing as employment and economic sectors and relatively low non-manufacturing wages in the state have been a magnet for back-office, banking, personnel and trade operations. Service sector growth, a key source of economic expansion in other states, has been somewhat muted by Ohio's slowly growing population.

Revenue Framework

Ohio relies on a diverse set of broad-based taxes to support operations, including income and sales and use taxes. These major tax revenues are collected in the GRF with constitutional exceptions for highway-related revenues, which are directed to highway purposes, and lottery proceeds, which are directed to education.

In recent biennia, the state has pursued wide-ranging tax policy changes, shifting the source of GRF tax receipts and lowering overall receipts relative to baseline. To date, these tax policy changes have been manageable, aided by favorable economic and fiscal trends. The enacted budget for fiscal 2020-2021 continues this approach, and includes a 4% reduction in personal income tax rates. In earlier action on the transportation budget, the state increased the gas tax 10.5 cents, bringing it to 38.5 cents per gallon, alongside a slightly larger increase for diesel fuel, which will be directed toward transportation infrastructure spending.

Rating History

Rating	Action	Outlook/ Watch	Date
AA+	Affirmed	Stable	2/03/20
AA+	Revised	Stable	4/05/10
AA	Downgraded	Stable	6/10/09
AA+	Affirmed	Negative	12/15/08
AA+	Affirmed	Stable	4/13/06
AA+	Assigned		8/14/96

Ohio's 10-year historical revenue growth through 2018, adjusted for the estimated effect of policy changes, has lagged U.S. GDP growth but has grown slightly above the inflation rate. Recent performance has been stronger than is reflected in the historical trend, given the severe impact of the recession in Ohio that followed the shift in the manufacturing-based economy. Fitch anticipates the state's revenues will continue to experience some real growth going forward.

Ohio has no legal limitations on its ability to raise revenues through base broadening, rate increases, or the assessment of new taxes or fees.

Expenditure Framework

Ohio has ample flexibility within its expenditure framework. The natural pace of spending growth is likely to be in line with or marginally above its somewhat slowly growing revenue stream. Carrying costs for debt and retirement liabilities are well below the median for states.

Primary cost drivers include Medicaid and education spending. With slower growth in enrollment, Medicaid spending growth is contained and with only modest population growth, education spending pressures should be manageable. Medicaid spending was significantly below forecast levels for fiscal 2019, contributing to the state's operating surplus. Enrollment growth is expected to continue to modestly decline through most of the next biennium. The fiscal challenge of Medicaid is common to all U.S. states and the nature of the program as well as federal government rules limit the states' options in managing the pace of spending growth. Federal action to revise Medicaid's fundamental programmatic and financial structure appears less likely in the near term given divided control in Congress. As with all federal initiatives, Medicaid remains subject to regulatory changes that could affect various aspects of the program.

Ohio has ample expenditure flexibility. The state has had a budget-cutting bias rather than relying on revenue increases when necessary to maintain budgetary balance, even in core spending areas. During the Great Recession, Ohio reduced distributions and phased out certain tax reimbursements to both local governments and school districts. The state's carrying cost for debt and retiree obligations is below the state median and is expected to remain low given the state's well-funded pensions and conservative debt management.

Long-Term Liability Burden

Ohio's liabilities are low and debt ratios are expected to approximate current averages. Based on 2018 data, Ohio's long-term liability burden, at 4.4% of personal income, was well under the 5.7% median for U.S. States. Including more recent issuance, the combined burden of long-term debt and net pension obligations remains low at 4.9% of 2018 personal income.

Funding of defined benefit retirement systems, which provide both for pensions and health care, has historically been considered a credit strength, with a history of annual contributions sufficient to support full actuarial prefunding of pensions and provide some support for retiree health care. Plans are cost-sharing, multi-employer with limited liabilities attributed to the state. Funding for pension benefits declined significantly with recessionary market losses, although they have since stabilized at higher levels. Changes since the recession have contributed to the improved financial sustainability of the public employees' system and the state's other major systems, as has shifting to lower discount rates and as of 2018 directing all of the system contributions to pensions from retiree health care. Despite this shift, the public employees' system maintains a relatively high level of prefunding for OPEB, just over 46% in 2018.

Operating Performance

Ohio's ability to respond to cyclical downturns reflects its ample budget flexibility and availability of reserves. During the Great Recession, Ohio's revenues suffered significant declines, exacerbated by ongoing tax reductions. The state closed the resulting budgetary gaps with both ongoing and one-time measures. Some of these measures included use of the rainy day fund, refunding debt for current year savings, unpaid employee leave, and accelerating the phase-out of tax reimbursements for schools and local governments. It is Fitch's expectation that Ohio would continue to rely primarily on expense reductions to address a future downturn and would again draw upon its now restored rainy day fund.

During times of economic recovery, Ohio rebuilds its financial flexibility including restoring its rainy day fund and reducing the use of one-time budget items. In recent biennia, tax reductions have, to some extent, absorbed the natural tax revenue growth related to overall economic expansion. A statutory increase in the rainy day funding requirement to 8.5% from 5.0% of prior year revenue provides additional capacity to address future downturns and is emblematic of the state's approach to bolstering its financial position during this period of expansion.

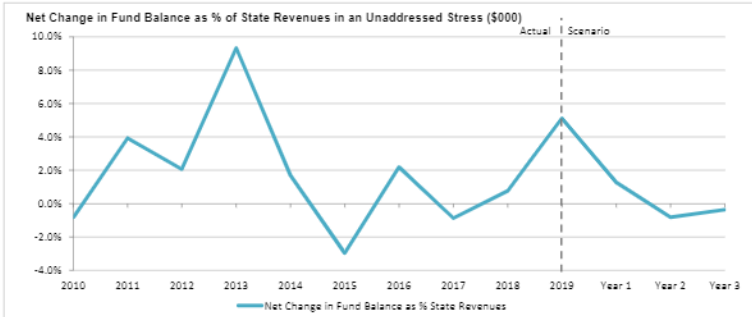
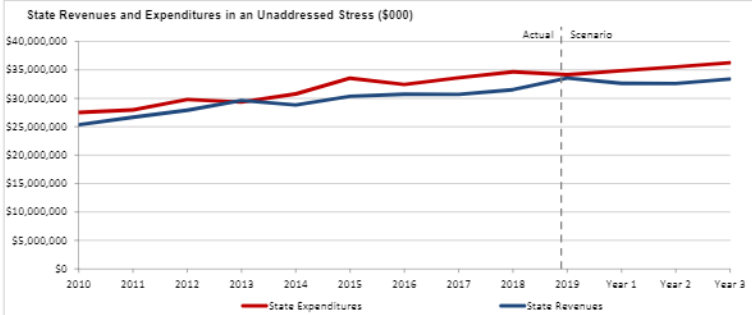
ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3' - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg

Ohio, State of (OH)

Scenario Analysis



Analyst Interpretation of Scenario Results:

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Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(2.7%)	(0.1%)	2.5%

Revenues, Expenditures, and Net Change in Fund Balance	Actuals										Scenario Output		
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Year 1	Year 2	Year 3
Expenditures													
Total Expenditures	49,495,495	51,255,563	51,177,175	50,876,071	53,690,264	58,064,992	58,708,554	59,869,809	60,956,137	60,966,546	62,185,877	63,429,594	64,698,186
% Change in Total Expenditures	1.0%	3.6%	(0.2%)	(0.6%)	5.5%	8.1%	1.1%	2.0%	1.8%	0.0%	2.0%	2.0%	2.0%
State Expenditures	27,525,951	27,954,118	29,781,323	29,338,970	30,769,509	33,531,021	32,426,854	33,611,309	34,661,565	34,152,614	34,835,666	35,532,380	36,243,027
% Change in State Expenditures	(8.5%)	1.6%	6.5%	(1.5%)	4.9%	9.0%	(3.3%)	3.7%	3.1%	(1.5%)	2.0%	2.0%	2.0%
Revenues													
Total Revenues	47,301,545	49,977,434	49,297,817	51,164,075	51,738,478	54,880,042	56,989,243	56,959,027	57,815,314	60,384,156	60,000,611	60,501,904	61,858,663
% Change in Total Revenues	5.7%	5.7%	(1.4%)	3.8%	1.1%	6.1%	3.8%	(0.1%)	1.5%	4.4%	(0.6%)	0.8%	2.2%
Federal Revenues	21,969,544	23,301,445	21,395,652	21,537,101	22,920,755	24,533,971	26,281,700	26,258,500	26,294,572	26,813,932	27,350,211	27,697,215	28,455,159
% Change in Federal Revenues	16.2%	6.1%	(8.2%)	0.7%	6.4%	7.0%	7.1%	(0.1%)	0.1%	2.0%	2.0%	2.0%	2.0%
State Revenues	25,332,001	26,675,989	27,901,965	29,626,974	28,817,723	30,346,071	30,707,543	30,700,527	31,520,742	33,570,224	32,650,400	32,604,689	33,403,504
% Change in State Revenues	(1.9%)	5.3%	4.6%	6.2%	(2.7%)	5.3%	1.2%	(0.0%)	2.7%	6.5%	(2.7%)	(0.1%)	2.5%
Excess of Revenues Over Expenditures	(2,193,950)	(1,278,129)	(1,879,358)	288,004	(1,951,786)	(3,184,950)	(1,719,311)	(2,910,782)	(3,140,823)	(582,390)	(2,185,266)	(2,927,690)	(2,839,523)
Total Other Financing Sources	1,984,605	2,326,274	2,457,660	1,010,348	2,440,585	2,284,308	2,393,066	2,643,785	3,383,641	2,299,661	2,600,892	2,664,209	2,718,438
Net Change in Fund Balance	(209,345)	1,048,145	578,302	2,761,858	488,799	(900,642)	673,755	(266,997)	242,818	1,717,271	415,626	(263,481)	(121,085)
% Total Expenditures	(0.4%)	2.0%	1.1%	5.4%	0.9%	(1.6%)	1.1%	(0.4%)	0.4%	2.8%	0.7%	(0.4%)	(0.2%)
% State Expenditures	(0.8%)	3.7%	1.9%	9.4%	1.6%	(2.7%)	2.1%	(0.8%)	0.7%	5.0%	1.2%	(0.7%)	(0.3%)
% Total Revenues	(0.4%)	2.1%	1.2%	5.4%	0.9%	(1.6%)	1.2%	(0.5%)	0.4%	2.8%	0.7%	(0.4%)	(0.2%)
% State Revenues	(0.8%)	3.9%	2.1%	9.3%	1.7%	(3.0%)	2.2%	(0.9%)	0.8%	5.1%	1.3%	(0.8%)	(0.4%)

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. For further details, please see Fitch's US Tax-Supported Rating Criteria.

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