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Ratings

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Ohio; General Obligation

Primary Credit Analyst:
Rob M Marker, Englewood + 1 (303) 721 4264; Rob.Marker@spglobal.com

Secondary Contact:
Oscar Padilla, Dallas + 1 (214) 871 1405; oscar.padilla@spglobal.com

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Credit Profile		
US$128.0 mil GO hwy cap imp bnds ser Y due 05/01/2039		
Long Term Rating	AAA/Stable	New
Ohio GO		
Long Term Rating	AAA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'AAA' long-term rating to the State of Ohio's approximately $128 million 2023 general obligation (GO) highway capital improvements bonds, series Y, and affirmed its 'AAA' rating on the state's parity debt outstanding.
- The outlook is stable.

Security

The state's highway user receipts (HURs), which the Ohio Constitution defines as any fees, excise and license taxes relating to the registration, operation, or use of vehicles on public highways or to fuels used for propelling those vehicles, secures the series Y bonds. In addition to the pledge of HURs, the bonds also have a full faith and credit pledge of Ohio, excluding net state lottery proceeds. Under our criteria, "Methodology: Rating Approach to Obligations With Multiple Revenue Streams" (published Nov. 29, 2011), we view the HURs as representing the stronger of the two security pledges, largely due to exhibited extraordinarily strong coverage levels and well-embedded constitutional provisions that limit debt issuance and prohibit diversion of these revenues to be used for the state's general operations. In addition, the Ohio Constitution restricts HURs to highway uses.

We rate the HURs under our priority-lien tax revenue debt criteria, which factors in both the strength and stability of the pledged revenues, as well as the general credit quality of the entity where taxes are distributed and/or collected (the obligor's creditworthiness or OC). The priority-lien rating for the highway capital improvement bonds is tied to the OC for the State of Ohio.

Ohio's highway capital improvement bonds are eligible to be rated above the sovereign because we believe the state can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions" (published Nov. 19, 2013), U.S. states are considered to have moderate sensitivity to country risk. State-derived revenues are the sole source of security on the bonds, and the institutional framework in the U.S. is predictable with significant state autonomy and flexibility.

Bond proceeds from the series Y issuance and other highway obligations are issued for the purpose of paying costs of construction, reconstruction, or other improvements of highways and related expenses.

Credit overview

In fiscal 2023, pledged HURs increased 1% from the previous year to $3.9 billion, which produced extraordinarily strong maximum annual debt service (MADS) coverage of 24.9x. We generally view MADS coverage greater than 4x on a forward-looking basis as extraordinarily strong. Provided current coverage levels, issuance limitations, and low revenue volatility assessment, we anticipate coverage will remain well above levels that we consider extraordinarily strong over our outlook period.

In our view, the state's constitution and bond provisions create a comprehensive framework for Ohio's highway capital improvement bonds. The Ohio Constitution (Section 5a of Article XII) prohibits the diversion of HURs to pledge as payment for debt obligations other than for payment of highway obligations, and these receipts are segregated from the state's general revenue fund, including collection and deposits into the bond service fund, without further need for legislative appropriation. Ohio has covenanted that it shall maintain statutory authority to levy, collect, and apply statewide excises, taxes, and revenue sufficient to pay debt service when due.

Key credit considerations in our assessment of the highway capital improvement bonds include:

- Very strong statewide economic fundamentals based on our view of approximately 11.8 million residents in 2022 generating the pledged revenues;
- Stability and consistent performance of Ohio's pledged revenues, which is in line with our view that nationwide gas taxes and motor vehicle registration and license fees have historically demonstrated low volatility;
- Extraordinarily strong coverage and liquidity conditions, with MADS coverage of 24.9x (based on audited fiscal 2023 pledged receipts), which we view in conjunction with the state's front-loaded debt service and rapid amortization of all highway capital improvement bonds; and
- Constitutional limitations on the amount of total debt that can be issued under the highway capital improvement bond program and provisions that separate HURs from the state's general operating funds.

Environmental, social, and governance

In our view, environmental, social, and governance (ESG) factors reflect those of the State of Ohio.

Outlook

The stable outlook mirrors the outlook on the State of Ohio and reflects our view that debt service coverage (DSC) will remain extraordinarily strong over the outlook horizon. We believe the broad-based pledge of statewide HURs supporting the highway capital improvement bond program and the historical stability of these revenues, in combination with credit strength provided by constitutional limitations for debt issuance and protections of pledged receipts, supports our expectation that credit fundamentals will remain consistent with the 'AAA' long-term rating.

Downside scenario

Although not anticipated, a negative rating action or outlook revision on the state could also lead to a negative rating action or outlook revision on these bonds. Furthermore, downward pressure on the rating could result from materially weakened pledged revenue collections that substantially diminish DSC or alterations to bond provisions that we believe weaken established legal protections.

Credit Opinion

Economic fundamentals: very strong

With a population of approximately 11.8 million as of 2022 and effective buying incomes at 92% of the U.S., the taxing-base-supporting pledged revenues is very strong. Population growth has historically generally trailed the U.S., increasing a modest 1.6% between 2012-2022 compared with a 6.0% increase nationally. While we anticipate population growth rates will remain modest (S&P Global Market Intelligence projects 0.47% growth from 2023-2026), the spread has remained narrow over the past decade. On a one-, five-, and 10-year basis, Ohio's compound annual population growth rate has trailed the U.S. by 45, 37, and 43 basis points, respectively.

Ohio's expansive economy is likely to remain supportive of our very strong assessment, particularly provided recent large-scale economic development announcements, including from Intel, Honda, First Solar, Ultium Cells, and others. Also, Ohio has a track record of attracting business development through both its favorable business tax climate and JobsOhio, the state-authorized nonprofit economic development corporation, which should continue to support relatively stable economic fundamentals.

Revenue volatility: low

Historically, HURs pledged to the bonds consist primarily of motor fuel and use taxes (approximately 71% of the fiscal year 2023 total HURs), while registration and license fees comprise the remainder. We consider gas tax revenues to have a low historical volatility assessment based on our view of the relative inelasticity of demand for motor fuel. Nationwide gasoline sales have historically fluctuated less than the total consumption of goods and services, even during severe economic downturns. However, should permanent technological or social trends emerge that disrupt or weaken gasoline consumption or changing fuel economy standards cause a shift in market dynamics over the long term, we could modify our view of revenue volatility.

Effective July 1, 2019, the state raised its motor vehicle fuel tax by 10.5 cents per gallon to the current rate of 38.5 cents per gallon and its diesel fuel tax by 19 cents to 47.0 cents per gallon. With this increase, we still view Ohio's motor fuel and diesel tax rates as comparable with those of most bordering states. At the same time, the state enacted an additional annual registration fee of $200 for plug-in electric motor vehicles and $100 for hybrid motor vehicles, effective Jan. 1, 2020. As secular adoption of electric and hybrid vehicles widens, we believe the state could identify changes in its revenue composition, and the legislature could continue to enact changes to registration fees in future biennia to preserve the stability of HURs. Despite occasional legislative proposals to suspend motor fuel taxes or registration fees, the executive branch expressed the importance of these revenues for highway improvements and road safety.

Between 2006-2023, HUR collections have, on average, increased 2.7% annually, with the most recent decline (-0.1%) occurring in fiscal 2016 and the most significant decline occurring in 2009 (-4.7%).

Coverage and liquidity: very strong

Consistent with historical trends, coverage and liquidity remain very strong. HURs fiscal 2023 of $3.9 billion produced MADS coverage of 24.9x (with MADS occurring in 2023), and we anticipate coverage will remain extraordinarily strong provided growing pledged revenue trends and a debt service schedule with declining debt service requirements from 2025 through maturity in 2039.

While there is no additional bonds test (ABT) for these obligations, we believe the lack of an ABT mitigates the state's constitutional protections of user receipts and limitations on debt issuance. The state's constitution limits total principal outstanding to $1.2 billion. It also prohibits annual issuance of more than $220 million in principal (plus the principal amount of highway obligations that in any previous fiscal years could have been, but were not issued, within the $220 million fiscal year limit). After the debt service payment, excess HURs flow to specific operations permitted under state law, including administrative costs of levying these taxes, construction, and maintenance of highway infrastructure, traffic enforcement, and hospitalization of indigent persons injured in motor vehicle accidents on public highways.

Obligor linkage: close

Although we consider the constitutional dedication of HURs for transportation-related projects positively, the collection and distribution of pledged revenue by the state present a degree of operating risk, and we, therefore, view the linkage between the priority lien pledge and Ohio as close under our priority lien criteria.

The Ohio Constitution and regulations established by law allow for continuous appropriation of HURs to the highway capital improvement bond service fund pledged to the bonds. Sufficient amounts shall be set aside before any other distributions are made to pay debt service due each year. The distribution of these receipts is not subject to biennial appropriation by the state legislature. Management reports that HURs are never co-mingled with the state's general revenue fund (GRF), and the state collects the pledged revenues and deposits them into dedicated funds. In addition, debt service for highway capital improvement bonds is included in the state's transportation budget rather than its GRF budget.

Rating linkage to Ohio

We assess Ohio's general operations because we view its overall creditworthiness as a key determinant of the obligor's ability to pay all its obligations. Ohio's 'AA+' GO rating reflects the state's strong government framework, supported by significant flexibility to adjust funding levels, a high degree of disbursement autonomy, and balanced budget requirements that preclude it from ending the year with an operating deficit. Prudent financial and budgetary management practices, a moderate debt burden, and adequate pension funding discipline further support the rating.

Furthermore, we expect Ohio will demonstrate an ongoing commitment to limiting its pension and other postemployment benefits (OPEB) liabilities, while also adhering to its longstanding 5% constitutional debt service limit, both of which support a predictable fixed-cost profile and support to our view of the state's long-term credit stability. We consider the state's debt levels to be moderate, with rapid amortization and a conservatively managed capital and debt program. Ohio has also implemented significant pension reform changes in recent years and made steady progress in funding OPEB.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

- 2022 Update Of Institutional Framework For U.S. Local Governments