Moody's
INVESTORS SERVICE

Rating Action: Moody's assigns Aa1 to Ohio's G.O. Highway Bonds, Ser. X; outlook stable

06 May 2022

New York, May 06, 2022 -- Moody's Investors Service has assigned a Aa1 rating to the State of Ohio's $82.2 million General Obligation Highway Capital Improvements Bonds, Series X (Full Faith and Credit / Highway User Receipts). Moody's also maintains the Aa1 on Ohio's Issuer Rating and $9.4 billion of general obligation bonds, including $784 million of general obligation highway capital improvement bonds. The bonds are expected to price the week of May 23. The outlook on the bonds is stable.

RATINGS RATIONALE

The Aa1 general obligation rating is based on the state's strong budgetary and financial management, sound reserve levels, and affordable fixed costs associated with below-average long-term debt, pension and retiree healthcare (OPEB) liabilities. These strengths are offset by below-average economic growth, compounded by weak demographic trends.

Ohio's highway bonds are also supported by a pledge of state highway user revenues, including gasoline taxes and motor vehicle license and registration fees. Although the bonds have substantial debt service coverage by a constitutionally dedicated revenue stream, the special tax credit quality is no higher than the state's Aa1 issuer rating due to a relatively weak legal structure compared to other highly-rated special tax bonds. In addition, the bonds have insufficient legal revenue separation and economic characteristics to pierce the issuer rating.

RATING OUTLOOK

The stable outlook is based on our expectation that the state's proactive financial management, low fixed costs, fully funded rainy day fund and substantial available liquidity will continue to support satisfactory budget flexibility during the pandemic recovery period.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- Improved demographic trends, particularly in working age population growth, net migration, and age distribution, that contribute to stronger economic growth relative to peers

- Maintenance of a budget in structural surplus, together with an increase in pension contributions sufficient to "tread water"

- Development of governance tools such as consensus revenue forecasting or publicly available long-term forecasts that institutionalize current best practices, increase transparency, and ensure consistency across administrations

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Further weakening of employment, personal income or demographic trends

- Financial deterioration, including a return to budgetary structural imbalance and/or materially lower reserve levels

- Unanticipated rise in long-term liabilities and an increase in fixed-costs

LEGAL SECURITY

Ohio's general obligation highway bonds are secured by the state's full faith and credit as well as a pledge of state highway user receipts, which includes gasoline taxes and motor vehicle license and registration fees. Pledged revenues are constitutionally dedicated to state highway purposes, including debt repayment, and provide substantial coverage of maximum debt service. Bonds have been historically paid entirely from highway user receipts, and the GO backstop has not been tapped.

The highway user receipts pledge provides very strong security for the bonds, but does not surpass the state's Aa1 issuer rating. The special tax pledge has a relatively weak legal structure compared to other highly-rated special tax bonds, as well as insufficient legal separation of revenues and economic characteristics to pierce the issuer rating. The special tax legal structure is primarily established through constitutional and statutory provisions, which do not provide the same clarity and framework as a typical special tax indenture. Somewhat unclear are provisions regarding the prioritization of debt service over other transportation spending, and detail surrounding the flow of funds and the leverage constraint. In addition, these bonds do not have sufficiently strong legal and economic characteristics to exceed the issuer rating, such as a constitutional dedication that is specifically tied to debt service, and an economic base that is stronger than suggested by the issuer rating.

Despite the bonds' strong coverage, future coverage could be reduced by revenue declines, a short debt service schedule, or a change in transportation funding policy, which are not considered by a constitutional cap on issuance of GO debt for highways. GO highway bond issuance is constitutionally capped at $1.2 billion of total debt outstanding and a $220 million per-year issuance limit, under which unused portions may be added to the annual cap amount in subsequent years. Excluding the current borrowing, the state has approximately $416 million of remaining borrowing capacity. If the state issued all remaining capacity as 15-year bonds (matching the current structure), MADS coverage would decline very slightly. Additional flexibility is available due to the state's 15-year amortization policy, which is well below the constitutional authorization to amortize debt over a 30-year span.

Constitutional amendments in Ohio must be approved by a super-majority (3/5) in each legislative chamber, and then by a simple majority in a public vote. While the state has covenanted to levy and collect taxes at levels sufficient to pay debt service on the bonds, it is not prohibited from repealing or reducing the pledged revenues to sum-sufficient coverage.

Highway user receipts also pay the debt service on $122.2 million of state appropriation debt issued for 26 DOT buildings (Transportation Building Fund Capital Facilities Bonds, Series 2015A and 2018A) and annual availability payments on ODOT's 2014 public private agreement that has a max payment of $39.2 million in FY2053. In addition, in the event of an interruption in Title 23 funding, the DOT Director has covenanted to pay debt service on the state's $765 million of Major New State Infrastructure Project Revenue Bonds (GARVEEs) using other funds lawfully available. The other funds would consist of appropriations of DOT revenues from sources including state gasoline tax receipts, which would become lawfully available after GO Highway debt service is paid.

USE OF PROCEEDS

Series X proceeds will finance highway capital improvements.

PROFILE

The state of Ohio has a population of 11.7 million, located in the Midwest region of the US with 312 miles of shoreline along Lake Erie, according to NOAA. The state is the seventh-largest US state by population, and has a large, diverse economy reflected in its GDP of $615 billion (also seventh among the states).

METHODOLOGY

The principal methodology used in this rating was US States and Territories Methodology published in March 2022 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBM_1299298 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

The rating has been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

This rating is solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1288235 .

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the EU and is endorsed by Moody's Deutschland GmbH, An der Welle 5, Frankfurt am Main 60322, Germany, in accordance with Art.4 paragraph 3 of the Regulation (EC) No 1060/2009 on Credit Rating Agencies. Further information on the EU endorsement status and on the Moody's office that issued the credit rating is available on www.moodys.com.

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the UK and is endorsed by Moody's Investors Service Limited, One Canada Square, Canary Wharf, London E14 5FA under the law applicable to credit rating agencies in the UK. Further information on the UK endorsement status and on the Moody's office that issued the credit rating is available on www.moodys.com.

Please see www.moodys.com for any updates on changes to the lead rating analyst and to the Moody's legal entity that has issued the rating.

Please see the ratings tab on the issuer/entity page on www.moodys.com for additional regulatory disclosures for each credit rating.

Baye Larsen
Lead Analyst
State Ratings
Moody's Investors Service, Inc.
One Stamford Plaza
263 Tresser Boulevard
Stamford 06901
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

Emily Raimes
Additional Contact
State Ratings
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

Releasing Office:
Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
U.S.A
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.