FitchRatings

RATING ACTION COMMENTARY

Fitch Rates Henrico County, VA's $105MM GOs 'AAA'; Outlook Stable

Fri 14 Feb, 2020 - 12:40 PM ET

Fitch Ratings - New York - 14 Feb 2020: Fitch Ratings has assigned the following ratings to Henrico County, VA:

-- $50 million Economic Development Authority of Henrico County, VA revenue bonds, series 2020A (Henrico County Indoor Sports Facility Project) (Taxable) 'AA+';

--$5.83 million Economic Development Authority of Henrico County, VA revenue refunding bonds, series 2020B (Henrico County Government Project) 'AA+';

--$25.225 million general obligation (GO) refunding bonds, series 2020 'AAA'.

The proceeds of the Economic Development Authority's (EDA) series 2020A bonds will be used to finance the construction of the Henrico Sports and Convocation Center. The EDA series 2020B bonds will refund the 2009B bonds for debt service savings. These bonds are scheduled to sell on a negotiated basis Feb. 24. The proceeds of the GO refunding bonds will be used to refund the series 2010 bonds for debts service savings. The GO refunding bonds are scheduled to sell on a competitive basis March 3.

Also, Fitch has affirmed the following outstanding ratings of the county:

--Issuer Default Rating (IDR) at 'AAA';

--$568.49 million outstanding GO bonds at 'AAA';

--$6 million outstanding public facility lease revenue refunding bonds series 2009B issued by the Henrico County Economic Development Authority at 'AA+'.

The Rating Outlook is Stable.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Henrico County (VA) [General Government]	LT IDR	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
Henrico County (VA) /General Obligation - Unlimited Tax/1 LT	LT	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
Henrico County (VA) /Lease Obligations - Standard - Henrico County Governmental Projects/1 LT	LT	AA+ Rating Outlook Stable	Affirmed	AA+ Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

SECURITY

The GO bonds are general obligations of the county, and the full faith and credit of the county is irrevocably pledged. The lease revenue bonds are payable by rental payments made by the county to the EDA from any legally available source, subject to annual appropriation.

ANALYTICAL CONCLUSION

Analytical Conclusion: The 'AAA' IDR and GO ratings reflect the county's high fundamental financial flexibility and resilience to cyclical economic stress, its low liability burden and growing economic base supporting expectations for solid revenue growth absent policy action. The ratings on the lease revenue bonds are one notch below the IDR, reflecting the slightly higher degree of optionality associated with lease payments subject to appropriation.

Economic Resource Base

Henrico County surrounds the commonwealth of Virginia's capital, the city of Richmond (GO bonds AA+/Stable), on the northern side of the James River. With an estimated 2018 population of 329,261 the county's population has increased 7.3% since 2010.

KEY RATING DRIVERS

Revenue Framework: 'aa'

Fitch expects revenue growth to be above the rate of inflation going forward on the basis of the county's sound economic and demographic fundamentals. The county enjoys high revenue flexibility given the independent legal ability to increase property taxes without limitation.

Expenditure Framework: 'aa'

Fitch expects the natural pace of spending to generally track revenue growth or marginally exceed it. Moderate carrying costs and broad flexibility to manage labor-related spending support the county's superior inherent budget flexibility.

Long-Term Liability Burden: 'aaa'

The county's overall debt and pension liability burden is low. Direct debt levels account for roughly one-third of the burden and should remain stable based on limited future debt needs and the rapid pace of debt amortization. Pension liabilities are the key driver of the liability burden and have been fairly stable.

Operating Performance: 'aaa'

The county's revenue and expenditure flexibility, strong reserves and modest revenue volatility support a high level of resilience to cyclical economic pressures. The county's budget management is strong as evidenced by its recent track record of surplus results and manageable deficits during the last recession.

RATING SENSITIVITIES

SOUND CREDIT PROFILE: Sustainably lower revenue growth equal to or below the level of inflation could weaken Fitch's assessment of the county's revenue framework which may pressure the IDR, GO and revenue bonds ratings.

CREDIT PROFILE

The local employment base is substantial and diverse, representing over a quarter of the Richmond metropolitan statistical area's employment base. Two fortune 500 companies, Altria (tobacco manufacturer) and Genworth (financial services) base their headquarters in Henrico County, with the former recently expanding its corporate headquarters facility. The county is targeting investment from the data center sector due to the proximity of a new transatlantic fiber optic cable that will connect North America to Europe through Virginia. Facebook is currently constructing a 2.4 million square foot data center, which is a $1.75 billion investment with 200 full-time employees. The county's employment base has also continued to expand, keeping the unemployment rate comfortably below the nation's and in line with the commonwealth's.

Revenue Framework

The county relies mostly on property tax revenues, which were 55% of general fund revenues in fiscal 2019. Other taxes (meals and business license) and sale taxes account for almost a third of general fund revenues.

Fitch expects long-term revenue growth to trend above the level of inflation. The 10-year compound average growth rate of 2% through fiscal 2019, which is above inflation, is not adjusted for reductions in the machinery and tools, aircraft or data center personal property tax rates, or the implementation of a meals tax in fiscal 2015 that has generated over $28.6 million in new revenue on average annually (in comparison to more than $815 million in general fund revenue in fiscal 2019). Given notable tax base growth and a robust pipeline of economic activity, Fitch expects future revenue growth to trend above inflation. The fiscal 2019 taxable assessed value (TAV) was $46 billion or 6.3% above the prior year, and the estimated fiscal 2020 TAV is $47.6 billion or a 4% annual increase.

Fitch's revenue framework assessment is also supported by high revenue raising ability provided by the unlimited property tax rate and levy. The real property tax rate has not been increased in 41 years and is viewed by Fitch as regionally competitive.

Expenditure Framework

The county's largest expenditure is education at roughly 35% of general fund expenditures, followed by public safety at about 30%. Virginia public schools are largely funded by a mix of state and local aid contributions, the latter being subject to satisfaction of state determined performance standards for the school system rather than enrollment.

Fitch expects the natural pace of spending growth to remain generally in line with, to marginally above revenue growth given steady population and manageable education spending needs.

Fixed carrying costs associated with debt service, actuarially determined pension payments and other post-employment benefits (OPEB) actual payments consumed 11% of fiscal 2019 governmental spending. The county has broad discretion over the terms of employee wages and benefits given the absence of collective bargaining. Fitch believes the county's pay-go capital spending, including a $69 million transfer (approximately 8% of fiscal 2019 spending) to the capital projects fund in fiscal 2019, provides additional flexibility, which is a much higher transfer than in prior years.

Long-Term Liability Burden

Overall net debt plus the county's Fitch-adjusted net pension liability (NPL) is low at approximately 7% of resident personal income. The adjusted NPL makes up the majority of the liability. The county's fiscal 2020-2024 $1.15 billion general government and schools capital improvement plan incorporates the remaining authorization from the 2016 $419.8 million voter-approved bond resolution to fund school, parks, library, fire station and road projects. Approximately $674 million of the plan is unfunded while $315.2 million of the plan is debt funded from the 2016 authorization. The remainder of the plan ($162 million) is funded with general fund revenues including meals tax revenues. Given the currently low debt burden and rapid principal amortization (71% in 10 years following the current refunding), the overall debt burden is expected to remain low notwithstanding the potential for additional new money issuance.

The current issuance will fund the construction of a sports and convocation facility, which will spur redevelopment of the former Virginia Center Commons Mall site to a mixed-use development. The facility will be used for youth athletics, student convocations, and hosting tournaments and other private events. The complex will be operated by a private management company and is expected to be operational by the summer of 2022.

The county participates in the statewide Virginia Retirement System (VRS), an agent multiple-employer defined benefit pension plan. All county employees, including county school board and non-professional employees participate in VRS. As of the June 30, 2018 measurement date, aggregate fiduciary assets covered approximately 71% of total pension liabilities when adjusted by the Fitch standard 6% rate of return assumption (VRS's reported asset to liability ratio is 80% at its 7% return assumption). The Fitch-adjusted aggregate NPL is over approximately $956 million or about 4% of personal income.

The county provides limited OPEB and the outstanding net liability is minimal relative to personal income. The aggregate net OPEB liability is approximately $85 million or less than a half of 1% of personal income.

Operating Performance

Given the county's superior inherent budget flexibility in the form of control over revenues and spending, Fitch expects the county to manage through economic downturns while maintaining a high level of fundamental financial flexibility. Reserves are expected to remain above the county's 15% target throughout the economic cycle. The general fund recorded a modest $115,586 operating surplus in fiscal 2019, inclusive of the $69 million transfer out to the capital projects fund. The unrestricted general fund balance of $265.5 million in fiscal 2019 was a high 32.6% of general fund spending. The county also reported a balance of $280.7 million in the capital reserve fund that will be used over time to fund the capital improvement plan but could be used for general fund purposes if needed.

The county proved its financial resilience and strong budget management through the most recent recession by instituting a hiring freeze, offering a retirement incentive, refunding debt and making department budget reductions among other measures. Fitch expects the county to make similar operational changes as needed during a future economic downturn.

The fiscal 2020 adopted general fund budget of $782 million is a 5.4% increase over the fiscal 2019 budget. While the budget keeps the real property tax rate stable for another year, $30 million of the general fund balance has been appropriated. The budget rewards eligible general government and schools employees with a 3% merit-based salary increase, funds a variety of public safety initiatives and the largest increase to the school budget since fiscal 2007. Given the county history of conservative budgeting, Fitch expects operating performance relative to budget to be positive.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

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 Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

FITCH RATINGS ANALYSTS

Evette Caze
Director
Primary Rating Analyst
+1 212 908 0376
Fitch Ratings, Inc.
33 Whitehall Street New York 10004

Grace Wong
Director
Secondary Rating Analyst
+1 212 908 0652

Michael Rinaldi
Senior Director
Committee Chairperson
+1 212 908 0833

MEDIA CONTACTS

Sandro Scenga
New York
+1 212 908 0278
sandro.scenga@thefitchgroup.com

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

U.S. Public Finance Tax-Supported Rating Criteria – Effective January 10, 2020 to March 27, 2020 (pub. 10 Jan 2020)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

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