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CREDIT OPINION
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Contacts

Natalie Claes +1.312.706.9973
Analyst
natalie.claes@moodys.com

Coley J Anderson +1.312.706.9961
AVP-Analyst
coley.anderson@moodys.com

Westerville (City of) OH

Update to credit analysis

Summary

Westerville (Aaa stable) is well positioned to absorb near-term revenue pressures that may arise from the coronavirus pandemic. The city maintains robust financial reserves and although coronavirus-related impacts will weaken income tax performance, year-to-date collections have closely matched figures from prior years. Both the income and property tax base are expected to prove resilient and are supported by above-average resident income. High leverage, which largely consists of unfunded pension liabilities, will remain a credit challenge, though this is partially offset by moderate fixed costs.

We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. We do not see any material immediate credit risks for Westerville. However, the situation surrounding coronavirus is rapidly evolving and the longer-term impact will depend on both the severity and duration of the crisis. If our view of the credit quality of the city changes, we will update our opinion at that time.

Credit strengths

» Large, wealthy tax base

» Strong financial position

Credit challenges

» Elevated pension burden

» High reliance on economically sensitive income tax receipts

Rating outlook

The stable outlook reflects our expectation that city will continue proactive and prudent fiscal management which will support the maintenance of strong operating reserves and liquidity over the next two years.

Factors that could lead to an upgrade

» Not applicable

Factors that could lead to a downgrade

» Material weakening of the property tax base or income tax receipts

» Significant narrowing of operating reserves

» Increased leverage

Key indicators

Exhibit 1

Westerville (City of) OH	2015	2016	2017	2018	2019
Economy/Tax Base					
Total Full Value ($000)	$3,006,221	$3,003,588	$3,366,011	$3,410,435	$3,484,267
Population	37,540	38,089	38,604	39,242	39,242
Full Value Per Capita	$80,080	$78,857	$87,193	$86,908	$88,789
Median Family Income (% of US Median)	155.0%	155.2%	148.7%	143.8%	143.8%
Finances					
Operating Revenue ($000)	$63,071	$65,912	$71,057	$73,145	$74,311
Fund Balance ($000)	$40,907	$39,181	$46,475	$47,534	$50,255
Cash Balance ($000)	$37,429	$39,362	$44,849	$48,865	$50,341
Fund Balance as a % of Revenues	64.9%	59.4%	65.4%	65.0%	67.6%
Cash Balance as a % of Revenues	59.3%	59.7%	63.1%	66.8%	67.7%
Debt/Pensions					
Net Direct Debt ($000)	$62,874	$51,745	$51,409	$64,235	$58,805
3-Year Average of Moody's ANPL ($000)	$177,166	$179,819	$195,510	$202,675	$219,000
Net Direct Debt / Full Value (%)	2.1%	1.7%	1.5%	1.9%	1.7%
Net Direct Debt / Operating Revenues (x)	1.0x	0.8x	0.7x	0.9x	0.8x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	5.9%	6.0%	5.8%	5.9%	6.3%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	2.8x	2.7x	2.8x	2.8x	2.9x

Sources: Moody's Investors Service, the city's audited financial statements, US Census Bureau

Profile

The City of Westerville encompasses 12.6 square miles in Franklin (Aaa stable) and Delaware (Aaa stable) Counties, approximately 15 miles northeast of Columbus (Aaa stable). It provides comprehensive municipal services, including public safety, public works and municipal utilities, to over 39,000 residents.

Detailed credit considerations

Economy and tax base: large Columbus suburb

We expect the tax base and local economy to prove resilient, supported by its location within the Columbus metropolitan area. Westerville is largely a bedroom community but also boasts a mature and strong business base. The $3.5 billion tax base has averaged 2.9% annual growth over the past five years as a result of both appreciating property values and new commercial development. A majority of new developments are located within the city's Westar Place, a 62-acre mixed-use district. Over 26,000 square feet of retail space is slated to open by year-end and Orthopedic One will be breaking ground on an $14 million, 80,000 square foot corporate headquarters and medical campus in the fall of 2020. City officials report there are approximately 16 acres remaining for development or sale within Westar Place.

The region's economy is diverse, with major employers crossing the healthcare, higher education, government and financial services sectors. Locally, the city's largest employers are JPMorgan Chase & Co. (A2 stable, 6,901 employees), Mount Carmel Health Systems (3,558 employees) and Otterbein University (Baa1 stable, 1,818 employees). Westerville continues to work in partnership with other community stakeholders to develop and execute workforce education programs and provide innovation lab and data center services to attract new businesses and support established employers. The city is home to the nation's first municipal data center, which links to its fiber-optic infrastructure and serves as a connectivity hub for local and regional businesses.

Financial operations and reserves: strong financial position; exposure to economically sensitive revenue streams

Westerville maintains solid operating reserves and liquidity, which should enable the city to weather any negative economic impacts from the coronavirus. The city is highly dependent on income taxes, which accounted for 71% of general fund revenue in fiscal 2019. Across operating funds (general, fire, parks and recreation income tax, parks and recreation operating and debt service funds), income taxes comprised 52% of total revenue. While the coronavirus has stunted fiscal 2020 (year-end December 31) performance, income tax collections have proved durable, as collections through August 2020 are up roughly 1.3% compared to the prior year. Still, management assumes a 5% reduction in income tax revenue in fiscal 2020 with recovery projected over a three-year period.

The city currently levies a 2% local income tax, with 0.25% dedicated to parks and recreation. Income tax collections increased, on average, 4.2% annually between 2009 and 2019. The revenue growth has helped to sustain strong financial reserves, with the city closing fiscal 2019 with an available operating fund balance of $50.3 million or 67.6% of revenue.

City officials have amended the fiscal 2020 cash-based budget to reflect a general fund deficit of $4.8 million, inclusive of a $1.4 million transfer out for capital projects. In response, officials have Identified $10.5 million of potential expense reductions for fiscal 2020, including a hiring freeze, reductions in discretionary spending and delayed capital spending. Additionally, the city has been awarded $1.8 million of CARES Act funding for coronavirus-related expenses from Franklin County, which will offset some unforeseen costs.

Annually, between 20% and 25% of general fund income tax dollars are distributed to the general capital improvement fund to cash finance capital projects, averaging roughly 23% over the past five years. To counterbalance any near-term declines in income tax receipts, the city will be reducing transfers to the minimum 20% over the next several years. Additionally, the city has historically transferred 75% of any year-end excess unencumbered general fund balance (compared to budget) to its general capital improvement reserve which could be tapped if needed. The estimated balance is $5.5 million, however city officials have no plans to use these funds for general operations.

Liquidity

The city closed fiscal 2019 with a net cash position of $50.3 million, or a strong 67.7% of operating revenue.

Debt and pensions: above average debt and pension burdens

Fixed costs are moderate, though the debt and pension burdens will remain above average. Following an upcoming sale to finance a new public safety facility, the city's debt burden will be above-average at 2.3% of full value but more moderate when compared to operating revenue at 1.1x. The city has no plans to issue additional debt, opting to cash finance projects whenever possible.

Moody's three-year average adjusted net pension liability (ANPL) for the city is equal to a high 6% of full value and 2.8x operating revenue. Fixed costs, inclusive of debt service and pension contributions, were 15.4% of operating revenue in fiscal 2019.

Legal security

Debt service on the city's GOULT bonds is secured by its full faith and credit pledge to levy unlimited ad valorem property taxes.

The city's outstanding GOLT bonds are secured by ad valorem property taxes, subject to the State of Ohio's (Aa1 stable) statutory 10-mill limitation. Additionally, debt service on GOLT bonds carries a first budget obligation payable from all available revenue.

The city's nontax revenue bonds are special obligations of the city secured by a pledge of the city's non-tax general fund revenue, but are expected to be paid from associated project revenue and tax increment financing (TIF) proceeds.

Debt structure

All of the city's debt is fixed rate. Principal amortization is below average with 65.8% repaid within 10 years.

Debt-related derivatives

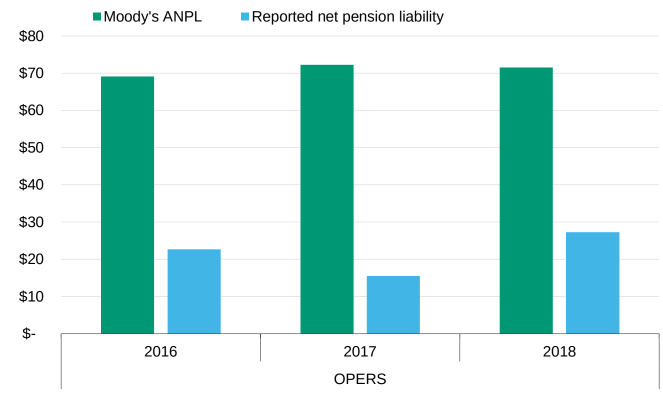
The city has no exposure to any debt-related derivatives.

Pensions and OPEB

City employees are members of the Ohio Public Employees Retirement System (OPERS) and the Ohio Police & Fire Pension Fund (OP&F). There is broad legal flexibility in Ohio to amend pension benefits, and statute establishes a 30-year target for amortizing the unfunded liabilities of all cost-sharing plans. In 2012, the 30-year target was breached and the state legislature acted by reducing benefits and increasing employee contributions. The 2012 reforms did not increase employer contributions from participating governments. As of fiscal 2018, the OPERS amortization period increased to 27 years while OP&F remained at 28 years.

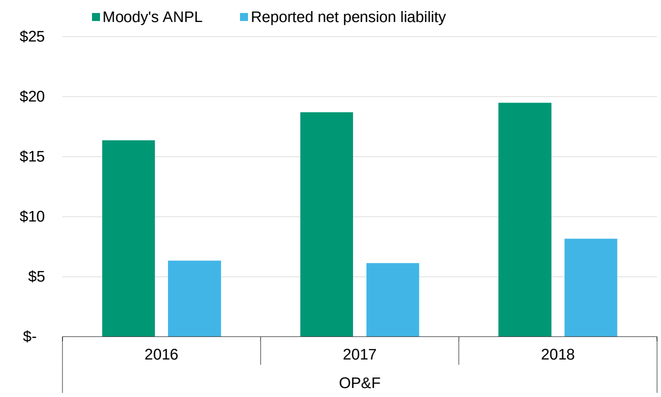
Moody's ANPL for OPERS declined by 1% in 2018 because of an increase in the market-based interest rate from the prior year, although the decline would have been larger had the plan not experienced negative investment returns. On a reported basis, the net pension liability increased by 75% due primarily to OPERS lowering the discount rate to 7.2% from 7.5% and weak investment performance. In fiscal 2018, the ANPL for OP&F increased 4% and reported net pension liabilities increased 33%, both because of weak investment performance.

Exhibit 2
Slight decline in 2018 OPERS ANPL
($ billions)



Sources: OPERS, Moody's Investors Service

Exhibit 3
Increasing ANPL trend for OP&F
($ billions)



Sources: OP&F, Moody's Investors Service

Pension contributions to OPERS and OP&F were 113% and 91%, respectively, of tread water[1] in fiscal 2018. Contributions to the plans, which are set by the state based on a percentage of payroll, have historically been below tread water. The combined ANPL is likely to grow based on current contribution practices for the plans.

ESG considerations

Environmental

According to data from Moody's affiliate, Four Twenty Seven, Franklin County has relatively high exposure to water stress and extreme rainfall events compared to counties nationally. Extreme weather events are typically accompanied by state and federal assistance, which mitigates environmental risk. We also expect the city's strong planning and financial resources will enable it to navigate any environmental challenges.

Social

Social considerations that factor into the city's credit into the city's credit profile include its demographic and socioeconomic characteristics. The city is a wealthy community closely tied to the broader Columbus metropolitan area, which should sustain its strong resident incomes and economic base. The population has grown roughly 8.6% since the 2010 census and median family income is estimated at 143.8% of the national level. As of July 2020, Westerville's unemployment rate was 7.0%, well below both the state (9.1%) and nation (10.5%). The current rates are elevated given the surge in unemployment claims related to coronavirus.

Governance

Westerville's strong fund balance policies and multi-year financial planning allow the city to respond to fluctuations in income taxes while addressing local capital needs. City policy mandates a general fund balance of no less than 50% of operating expenditures. Though not a formal policy, the city has also historically transferred 75% of any year-end excess unencumbered balance (compared to budget) to its general capital improvement reserve.

The city is governed by a seven-member Council elected to staggered four-year terms. The council appoints the City Manager, who serves as the city's chief executive and administrative officer. The Mayor is elected by the City Council and is the city's ceremonial and titular chief executive.

Ohio cities have an Institutional Framework score of "A", which is moderate. The sector's major revenue source, income tax, is subject to a 1.0% cap that can be overridden with voter approval only. Increases in property taxes also generally require voter approval. Revenues and expenditures tend to be predictable.

Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

The difference between the Scorecard Outcome and the Assigned Rating reflects the city's strong fiscal management which has supported the maintenance of robust reserves. The city also maintains significant liquidity outside of governmental funds.

Exhibit 4

Westerville (City of) OH

Scorecard Factors and Subfactors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$3,484,267	Aa
Full Value Per Capita	$88,789	Aa
Median Family Income (% of US Median)	143.8%	Aa
Finances (30%)		
Fund Balance as a % of Revenues	67.6%	Aaa
5-Year Dollar Change in Fund Balance as % of Revenues	14.7%	Aa
Cash Balance as a % of Revenues	67.7%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	14.2%	Aa
Management (20%)		
Institutional Framework	A	A
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	1.0x	Baa
Notching Factors:[2]		
Unusually Strong or Weak Budgetary Management and Planning		Up
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	2.3%	A
Net Direct Debt / Operating Revenues (x)	1.1x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	6.0%	Baa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	2.8x	A
	Scorecard-Indicated Outcome	Aa2
	Assigned Rating	Aaa

[1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.
Sources: Moody's Investors Service, the city's audited financial statements, US Census Bureau

Endnotes

1 Our "tread water" indicator measures the annual contribution required to prevent reported net pension liabilities from growing, given the entity's actuarial assumptions. An annual government contribution that treads water equals the sum of employer service cost and interest on the reported net pension liability at the start of the fiscal year.

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