FitchRatings

Public Finance
Tax-Supported
U.S.A

Lynchburg, Virginia

Ratings

Long-Term Issuer Default Rating	AA+

New Issue

$49,100,000 General Obligation Public Improvement Bonds, Series 2020	AA+

Outstanding Debt

General Obligation Bonds	AA+

Rating Outlook

Stable

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (April 2018)

Related Research

Fitch Rates Lynchburg VA's $49.1MM GOs 'AA+'; Outlook Stable (December 2019)

New Issue Details

Sale Date: Jan. 15, 2020 competitively.

Series: General Obligation Public Improvement Bonds, Series 2020.

Purpose: The proceeds of the bonds will be used to finance and refinance the costs of various public improvement projects of and for Lynchburg (the city), including the refunding and redemption of the city's outstanding series 2018 bond anticipation note.

Security: The bonds are GOs of the city, payable by a pledge of its full faith, credit and unlimited taxing authority.

The 'AA+' GO rating and Issuer Default Rating (IDR) reflect the city's strong control of revenues and expenditures, as well as its strong budget management and healthy reserves. The city's long-term liability burden is manageable.

Economic Resource Base: The city of Lynchburg is located along the James River in central Virginia, roughly 50 miles east of Roanoke. The city has exhibited steady growth in population with its 2018 population of 82,126 up 8.7% since the 2010 U.S. Census, faster than the state and the nation.

Key Rating Drivers

Revenue Framework: 'aaa': Revenues have been rising at a pace below U.S. GDP growth but above the rate of inflation. The city enjoys strong revenue flexibility given its independent legal ability to increase property taxes without limitation.

Expenditure Framework: 'aa': The natural pace of spending growth is expected to remain in line with, to marginally above, revenue growth. Moderate carrying costs and broad flexibility to manage labor-related costs allow the city solid leeway to adjust spending throughout economic cycles.

Long-Term Liability Burden: 'aa': The combined burden of debt and unfunded pension liabilities is moderate at roughly 17% of personal income.

Operating Performance: 'aaa': The city's healthy financial reserves are well in excess of their target policy and, in conjunction with the city's superior ability to adjust revenues and spending, leave the city very well positioned to address cyclical revenue declines.

Rating Sensitivities

Increased Long-Term Liabilities: A material increase in the city's long-term liability burden due to additional debt issuances beyond current expectations or further increases in the city's net pension liability could pressure the rating.

Analysts

Evette Caze
+1 212 908-0376
evette.caze@fitchratings.com

Grace Wong
+1 212 908-0652
grace.wong@fitchratings.com

Credit Profile

Lynchburg's historically strong manufacturing and distribution base remains important to the local economy, although the city has expanded to become a regional hub for higher education, health services, industrial engineering and retail activity. Many of the city's longstanding taxpayers and employers continue to expand within the city. Framatome, the city's fourth largest employer and third largest taxpayer, announced it would be relocating its North American corporate headquarters to the city, increasing staff to 1,300.

Education and healthcare are the largest employment sectors in the city, which includes five higher education institutions. Growth potential for the higher education sector is promising, including at the largest institution and the city's largest employers with over 8,000 employees, Liberty University. Downtown and riverfront redevelopment activity continues to show momentum with significant public and private investment yielding new residential, arts and entertainment development. Wealth levels are below the state and national average but may be affected by the large student university population (approximately 21,776).

Revenue Framework

The city's diverse revenue stream includes a mix of property, sales and meals taxes and other nontax revenue. Property taxes are the most significant revenue source, accounting for roughly 41% of fiscal 2019 general fund revenues, followed by intergovernmental revenues at 20% and local sales and use and meals taxes each making up less than 10%.

Fitch Ratings' expectation of revenue above inflation for the city's general fund revenues is based on steady economic trends supported by increases in the taxable base and other local taxes. The city's rate-adjusted general fund revenue growth trended in line with inflation over the past decade ended fiscal 2019. The estimated fiscal 2019 assessed value is approximately $6.3 billion, which is about a 2% increase in the real property assessed value component of the tax base. The city reassesses real estate biennially. According to the 2020 budget, values are expected to increase 6%, which reflects the 2019 reassessment. Values are projected to increase 1.5% in fiscal 2021, reflecting new construction.

There is no legal limitation on the city's ability to increase its millage or tax levy, which helps to insulate the city's revenue base against exposure to shifts in the city's tax base or economy.

Expenditure Framework

The city maintains healthy expenditure flexibility with moderate spending associated with fixed carrying costs related to debt and retiree benefits. Public safety and educational spending are the largest expenditure items for the city, each making up roughly 27% and 21%, respectively, of general fund spending. Virginia public schools are largely funded by a mix of state and local contributions. The amount of the local contribution is determined by the city council and is based on the state-determined performance standards for the school system.

Expectations for continued population growth and moderate increases in the cost of services should more or less align the pace of spending growth with revenues over time.

The city maintains a significant level of expenditure flexibility due to the favorable workforce environment that prohibits labor contracts and gives management independent control of compensation and work rules. Carrying costs associated with debt service, actuarially determined pension payments and other post-employment benefit (OPEB) actual contributions make up 15% of governmental spending. Despite the city's additional debt plans, Fitch expects expenditure flexibility to remain solid.

Long-Term Liability Burden

Long-term liabilities for debt and unfunded pensions are moderate at about 17% of personal income. The city's direct debt represents 7% of personal income and about 54% of principal amortizes within 10 years including the current issuance. The fiscal years 2020–2024 capital improvement plan totals $219.2 million for general city and school capital projects. Approximately $117 million in new money debt is projected to be issued between 2021 and 2024.

Fitch's long-term liability burden calculation includes defined benefit pension plans administered by the Virginia Retirement System (VRS) as agent plans for general employees

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AA+	Affirmed	Stable	12/24/19
AA+	Review - No Action	Stable	8/15/19
AA+	Revised	Stable	4/30/10
AA	Affirmed	Stable	5/25/04
AA	Assigned	—	1/5/93

and nonteacher employees of the component unit school system and as a cost-sharing, multiple-employer plan for teachers. The combined ratio of assets to liabilities was about 66% in fiscal 2019, when adjusted by Fitch to reflect a 6% investment rate of return assumption versus the plan's 7% rate. Systemwide funding of VRS declined over the past decade as the commonwealth set statutorily required contributions, partially used as a budget balancing measure for the state, at less than actuarially sustainable levels. The commonwealth returned to full actuarially determined employer contribution payments as of fiscal 2018, which should slow the growth in the net pension liability. Overall, the city's liability burden is on the high end of Fitch's 'aa' assessment range. Given the city's additional debt plans and pension funded status, the current 'aa' assessment and the city's overall rating may be negatively affected if the long-term liability metric increases materially above 20%.

The city offers OPEB to retirees and makes contributions on a pay-as-you-go basis. Full-time employees hired on or after July 1, 1996 are eligible to participate in the city's OPEB plan under an implicit rate subsidy. The unfunded OPEB liability as of June 30, 2019 was high at $97.4 million, or approximately 4% of personal income.

Operating Performance

The city's strong financial resilience comes from a combination of its unlimited legal authority to increase property taxes, solid expenditure flexibility and maintenance of a strong reserve cushion. A hypothetical unaddressed moderate economic decline scenario shows an operating reserve cushion that Fitch judges to be consistent with an 'aaa' financial resilience assessment. Moreover, Fitch expects that in the event of an actual revenue decline of this magnitude, the city would maintain reserves at or above its policy level (an unassigned general fund balance equal to no less than 10% of revenue) through active expenditure management. During the current fiscal year, the city increased its unassigned fund balance goal to 15% of revenues. As of fiscal year-end 2019, the unassigned fund balance was 15.4%.

Lynchburg's strong budgetary management is demonstrated by its history of favorable operating performance relative to budget and its commitment to adhere to the city’s aforementioned general fund balance policy. The city ended fiscal 2019 with a general fund operating surplus of $4 million, or 2.2% of spending. The unrestricted fund balance increased to $54.3 million, or a healthy 29% of spending.

The city's adopted fiscal 2020 general fund budget totaled $194.6 million, which is an increase of approximately $2 million, or 1.1% above the adopted fiscal 2019 budget. The budget keeps the real property tax rate stable at $1.11 per $100 of assessed value for the seventh consecutive fiscal year. The budget appropriates $3.9 million of fund balance but, given the city's history of conservative budgeting, actual results are expected to perform better than budget.

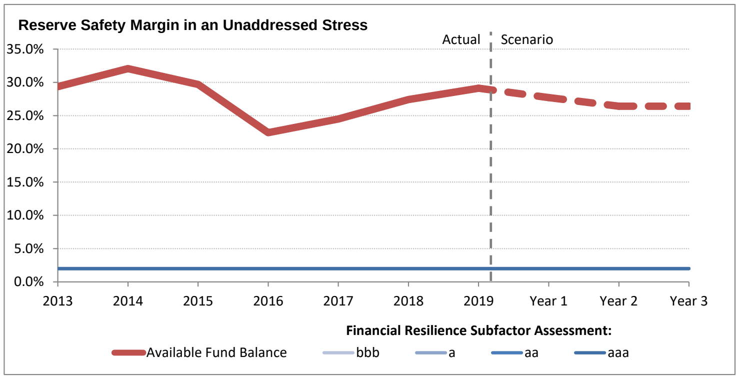
ESG Considerations

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.

Lynchburg (VA)

Scenario Analysis



Analyst Interpretation of Scenario Results:

The city's strong financial resilience comes from a combination of its unlimited legal authority to increase property taxes, solid expenditure flexibility, and maintenance of a strong reserve cushion. A hypothetical unaddressed moderate economic decline scenario shows an operating reserve cushion that Fitch judges to be consistent with an 'aaa' financial resilience assessment. Moreover, Fitch expects that in the event of an actual revenue decline of this magnitude the city would maintain reserves at or above its policy level (an unassigned general fund balance equal to no less than 10% of revenue) through active expenditure management. During the current fiscal year, the city increased its unassigned fund balance goal to 15% of revenues. As of fiscal year-end 2019, the unassigned fund balance was 15.4%.

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)	(1.0%)	2.1%	3.3%
Inherent Budget Flexibility		Superior	

Revenues, Expenditures, and Fund Balance				Actuals					Scenario Output	
	2013	2014	2015	2016	2017	2018	2019	Year 1	Year 2	Year 3
Total Revenues	169,308	173,619	176,616	180,853	184,021	186,819	190,091	188,190	192,092	198,471
% Change in Revenues	-	2.5%	1.7%	2.4%	1.8%	1.5%	1.8%	(1.0%)	2.1%	3.3%
Total Expenditures	158,463	158,787	167,290	175,666	178,740	177,528	179,440	183,029	186,689	190,423
% Change in Expenditures	-	0.2%	5.4%	5.0%	1.7%	(0.7%)	1.1%	2.0%	2.0%	2.0%
Transfers In and Other Sources	4,148	62	23,561	8,603	1,585	17,278	644	637	651	672
Transfers Out and Other Uses	13,982	10,162	34,021	23,840	4,871	7,116	7,243	7,388	7,536	7,687
Net Transfers	(9,834)	(10,100)	(10,461)	(15,237)	(3,286)	10,162	(6,599)	(6,751)	(6,885)	(7,014)
Bond Proceeds and Other One-Time Uses	4,130	-	22,648	8,066	-	2,160	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	1,011	4,732	(1,135)	(10,050)	1,996	19,453	4,052	(1,589)	(1,483)	1,034
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	0.6%	2.8%	(0.6%)	(5.2%)	1.1%	10.7%	2.2%	(0.8%)	(0.8%)	0.5%
Unrestricted/Unreserved Fund Balance (General Fund)	49,414	54,146	53,011	42,962	44,957	50,008	54,369	52,780	51,297	52,331
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	49,414	54,146	53,011	42,962	44,957	50,008	54,369	52,780	51,297	52,331
Combined Available Fund Bal. (% of Expend. and Transfers Out)	29.4%	32.0%	29.7%	22.4%	24.5%	27.4%	29.1%	27.7%	26.4%	26.4%

Reserve Safety Margins			Inherent Budget Flexibility		
	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	16.0%	8.0%	5.0%	3.0%	2.0%
Reserve Safety Margin (aa)	12.0%	6.0%	4.0%	2.5%	2.0%
Reserve Safety Margin (a)	8.0%	4.0%	2.5%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.0%	2.0%	2.0%	2.0%	2.0%

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. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

The ratings above were solicited and assigned or maintained at the request of the rated entity/Issuer or a related third party. Any exceptions follow below.