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Summary:

Lynchburg, Virginia; General Obligation

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Credit Profile		
US$49.115 mil GO pub imp bnds ser 2020 due 08/01/2049		
Long Term Rating	AA+/Stable	New
Lynchburg GO		
Long Term Rating	AA+/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to Lynchburg, Va.'s series 2020 general obligation (GO) public improvement bonds. At the same time, we affirmed our 'AA+' rating on the city's existing GO debt. The outlook is stable.

Security and purpose

The bonds are secured by the city's full–faith-and-GO credit pledge.

We understand proceeds from this issue will be used to finance various city capital projects including the accelerated construction of the Lakeside Drive Bridge as well as permanently finance the principal balance on the 2018 line of credit, which will close this line out ahead of its June 2020 expiration.

Credit overview

The city anchors the broad four-county region where its sizable health care, education and manufacturing sectors provide employment stability. Additional economic development, both in the downtown area and elsewhere lend further stability and continue to increase the tax base. The city's historically strong financial position, which has been guided by a conservative and well-seasoned staff coupled with many formal fiscal policies further solidifies the strong rating. Currently, the city's rising debt levels and economic indicators, which are not on par with higher rated peers, preclude a higher rating at this time.

In our opinion, the rating reflects the city's:

- Adequate economy, with a local stabilizing institutional influence;
- Very strong management, with strong financial policies and practices under our Financial Management Assessment methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 37% of operating expenditures;
- Very strong liquidity, with total government available cash at 38.0% of total governmental fund expenditures and 4.1x governmental debt service, and access to external liquidity we consider strong;

- Weak debt and contingent liability position, with debt service carrying charges at 9.3% of expenditures and net direct debt that is 104.8% of total governmental fund revenue; and
- Very strong institutional framework score.

Adequate economy

We consider Lynchburg's economy adequate. The city, with an estimated population of 80,989, is located in Lynchburg (Campbell County/Lynchburg combined area). The city benefits, in our view, from a stabilizing institutional influence. The city has a projected per capita effective buying income of 72.5% of the national level and per capita market value of $82,326. Overall, the city's market value grew by 5.7% over the past year to $6.7 billion in 2020. The city's unemployment rate was 3.7% in 2018.

The city anchors the Lynchburg/Campbell County combined metropolitan statistical area (MSA) and is located in the foothills of the Blue Ridge Mountains along the James River in the center of the commonwealth. Lynchburg is the employment and retail base of a four-county region and continues to be an employment hub with a significant number (72%) of people commuting into the city for work. The city is mature, yet a healthy amount of redevelopment and expansion of existing businesses continues. Lynchburg continues to work with the Economic Development Authority (EDA) to promote future growth and redevelopment and has established several new initiatives to achieve these goals, including a local enterprise redevelopment program, the real estate rehabilitation program and the establishment of a revolving loan fund. Since 2015, the city has seen $98.6 million of investments creating 1,045 new jobs. Recent completed economic development projects have included the redevelopment of the historic Virginian Hotel, Tessy Plastics $9.2 million expansion and creating 34 new jobs, and the $30.0 million renovation of the Academy Center of the Arts in December 2018. The theatre is located in the downtown area, and serves as a magnet for continuing economic development.

The health care, retail, higher education, and manufacturing sectors anchor the employment base. Leading employers include: Liberty University (8,000+ employees), CENTRA Health (5,000+), Lynchburg city schools (1,500+), Framatome (nuclear power 1,000+) and J.Crew Outfitters (1,000+). In addition, within the city's boundaries are five higher education institutions, with Liberty University being the largest. Total enrollment accounts for almost 27% of Lynchburg's total population and, in our opinion, is a contributing factor to its lower wealth levels. Liberty University, recognized as the nation's largest private non-profit online educator, continues with its sizable campus renovation and expansion project. Construction is expected to continue into 2020, spurring additional retail development. The city's tax base continues to experience modest, yet consistent growth, increasing 11% since 2015 to $6.67 billion in 2020. We expect the tax base to continue to experience growth over the near term given the ongoing economic development occurring throughout the city.

Very strong management

We view the city's management as very strong, with strong financial policies and practices under our Financial Management Assessment methodology, indicating financial practices are strong, well embedded, and likely sustainable.

Lynchburg's fiscal and debt practices are based on a series of comprehensive policies that it adopted in 1999 and updated as necessary through a regular review process. The city uses five-year historical trend analysis, commonwealth, and federal estimates and data projections, and economic forecasts to develop its annual revenue and expenditure assumptions. Management monitors the budget through formal processes, and it tracks revenues and expenditures daily and makes quarterly reports on the results to the city council based on adopted policy. Each mid-March, the city's financial management team makes formal recommendations for budget adjustments to the city council based on budgeted numbers compared with actual results.

A five-year capital improvement program (CIP) serves as the basis for annual capital appropriations and debt financing requirements; management updates the CIP annually with identified funding sources. On an informal basis, the city maintains a five-year long-term financial forecast for revenues and expenditures and includes certain assumptions. The city adheres to comprehensive formal debt management policies in planning and addressing its capital needs, including:

- A policy that limits the city's debt service-to-budget to 10% of budgeted general expenditures,
- A limit on total debt to 4.5% of full market value,
- A principal amortization target of 60% over 10 years at the end of the five-year CIP, and
- The city's pay-as-you-go appropriations of at least 10% of the annual CIP.

The city has its own investment policy that it reviews annually with its financial advisor. Reports are made and shared with the city manager and city council on a quarterly basis. The city recently adjusted and strengthened (Dec. 10, 2019) its long-adopted reserve policy, which calls for the maintenance of undesignated general fund balance equal to a minimum of 10% of General Fund revenues with a goal of 15% as the city strives to grow incrementally each year subject to revenues available.

Strong budgetary performance

Lynchburg's budgetary performance is strong in our opinion. The city had operating surpluses of 2.2% of expenditures in the general fund and of 5.5% across all governmental funds in fiscal 2019.

Lynchburg's budgetary performance has been strong overall, in our view, benefitting from conservative budgeting practices and several formal fiscal policies. These practices have allowed for the generation of surpluses over the past three fiscal years, which have in turn, increased reserves; keeping them at very strong levels.

Fiscal 2019 closed with a $4.0 million surplus, net of transfers. The city has a stable revenue stream with little exposure to volatile revenues. Property taxes accounted for 46% of general fund revenues, rising to over 72% when all local taxes, such as sales and use, meals, and business licenses are included. Property tax rates have remained unchanged since 2013; standing at $1.11/per $100 with a collection rate averaging over 99% over the past five years.

The fiscal 2020 budget totals $194.6 million and includes the use of $3.9 million of reserves; half of what was budgeted for in the fiscal 2019 budget. The property tax rate of $1.11#?#$100 remains unchanged. Management reports revenues and expenditures are tracking on target with budget; projecting fiscal 2020 to close, at least, on a break-even basis.

Given the city's strong fiscal operations coupled with projections for, at least, break-even operations in the near term, we do not expect the city's budgetary performance to weaken over the next several years.

Very strong budgetary flexibility

Lynchburg's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 37% of operating expenditures, or $69.3 million. The available fund balance includes $38.4 million (20.6% of expenditures) in the general fund and $30.9 million (17% of expenditures) that is outside the general fund but legally available for operations.

Audited fiscal 2019 general fund reserves were $38.4 million or 20.6% of expenditures after adjusting for transfers. In addition, when reserves outside the general fund are included, specifically the committed portion of the general, city capital and school capital project funds, levels rise to $69.3 million or 37.1% of expenditures. These reserve levels are well above the city's formal policy of 10% (rising to 15%). With, at least, break-even projections for fiscal 2020, we do not expect the city's budgetary flexibility fund to deteriorate over the near term.

Very strong liquidity

In our opinion, Lynchburg's liquidity is very strong, with total government available cash at 38.0% of total governmental fund expenditures and 4.1x governmental debt service in 2019.

In our opinion, the city has strong access to external liquidity, as it has issued GO debt frequently over the past 20 years. The obligor has contingent liquidity risk exposures that we consider manageable at the current rating level. The exposures come from $12.0 million of debt sold directly to various bank facilities, previously done in 2012, 2013, and 2015. There are no acceleration provisions and the city maintains sufficient liquidity. In addition, the city does not hold any investments we deem aggressive.

Weak debt and contingent liability profile

In our view, Lynchburg's debt and contingent liability profile is weak. Total governmental fund debt service is 9.3% of total governmental fund expenditures, and net direct debt is 104.8% of total governmental fund revenue.

Factoring in this issue, the city has a total of $228 million of net direct debt, much of which is for school-related needs. Over the years, the city has instituted a 'Just in Time' funding approach which calls for the use of a two to three year line of credit to fund, in a timely manner, the city's capital needs. This issue will repay the remaining amount of the existing 2018 line of credit prior to its expiration in June 2020. With the success of this funding approach, the city plans to continue using this model to finance ongoing projects. The city anticipates entering into a new Line of Credit in March-April 2020 as part of the next phase of its capital improvement program. The city plans to issue additional debt of about $30.5 million some time in fiscal 2023.

Lynchburg's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 5.2% of total governmental fund expenditures in 2019. The city made its full annual required pension contribution in 2019.

Pension and other postemployment benefits

We do not view pension and OPEB liabilities as an immediate source of credit pressure for Lynchburg. Although OPEB liabilities are paid on a pay-as-you-go basis, the low cost and liability is unlikely to lead to credit pressure in the near term.

Lynchburg participates in the following plans:

- Virginia Retirement System retirement plan: 74% funded, with a proportionate net pension liability of $97.3 million; and
- A single-employer, defined-benefit health care plan covering eligible retirees and spouses, with an OPEB liability of about $84.1 million.

Very strong institutional framework

The institutional framework score is very strong.

Outlook

The stable outlook reflects our view of Lynchburg's consistent financial performance and stable economy, which is supported by very strong budget flexibility, liquidity, and management. The growing area economy, which serves as an anchor for the region, lends stability to the rating. As such, we do not expect to revise the rating over our two-year outlook horizon because we believe the city will maintain its very strong financial position and manage its debt burden.

Upside scenario

In our opinion, if the city were to experience significant improvements in overall economic indicators, and have them maintained, and its debt and liability positon were to improve, while all other factor averages being held constant, we might raise the rating.

Downside scenario

Conversely, if budgetary performance or debt and contingent liability were to decline, placing fiscal pressure on the city, or economic indicators were to erode, we might lower the rating.

Related Research

- U.S. State And Local Government Credit Conditions Forecast, Oct. 29, 2019
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019