S&P Global Ratings

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Summary:

Garland, Texas; General Obligation

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Credit Profile		
US$30.49 mil comb tax and rev certs of oblig ser 2018 due 02/15/2038		
Long Term Rating	AA+/Stable	New

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to Garland, Texas' series 2018 combination tax and revenue certificates of obligation. At the same time, S&P Global Ratings affirmed its 'AA+' long-term rating and underlying rating (SPUR) on the city's existing general obligation (GO) bonds and certificates of obligation. The outlook is stable.

The city's GO bonds and certificates of obligation constitute direct obligations of the city, payable from the proceeds of a continuing, direct annual ad valorem tax, within the limits prescribed by law, on all taxable property within its borders. The maximum allowable rate in Texas is $2.50 per $100 of assessed value (AV) for all purposes, with the portion dedicated to debt service limited to $1.50. The city's total tax rate is well below the maximum, at 70.46 cents, 31.06 cents of which is dedicated to debt service. Based on the application of our criteria, titled "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" (published Jan. 22, 2018, on RatingsDirect), we view the limited-tax GO debt pledge on par with the issuer credit rating, which is based on the city's general creditworthiness.

The series 2010 and 2015 combination tax and electric utility system revenue bonds are additionally secured by a subordinate lien on net electric utility system revenues--in an amount not to exceed $1,000. All other outstanding certificates of obligation, including the series 2018 certificates, are secured by an additional limited pledge of net revenue from the city's water and sewer system--in an amount not to exceed $1,000. Given the limited nature of the additional pledged revenues, our ratings on these obligations are based on the city's ad valorem tax pledge.

The series 2018 certificates will fund various citywide capital projects including the construction and renovation of parks and recreation facilities, vehicle and equipment purchases, drainage improvements, and street and road improvements.

The 'AA+' rating reflects our opinion of the city's:

- Adequate economy, with projected per capita effective buying income at 80.5% and market value per capita of $57,595, that is gaining advantage from access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with "strong" financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 21% of operating expenditures;

- Very strong liquidity, with total government available cash at 83.7% of total governmental fund expenditures and 5.9x governmental debt service, and access to external liquidity we consider exceptional;
- Adequate debt and contingent liability profile, with debt service carrying charges at 14.1% of expenditures and net direct debt that is 111.8% of total governmental fund revenue, as well as rapid amortization, with 79.0% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Adequate economy

We consider Garland's economy adequate. The city, with an estimated population of 236,786, is located in Collin, Dallas, and Rockwall counties in the Dallas-Fort Worth-Arlington, TX MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 80.5% of the national level and per capita market value of $57,595. Overall, the city's market value grew by 10.0% over the past year to $13.6 billion in 2018. The weight-averaged unemployment rate of the counties was 4.0% in 2016.

Garland is located 14 miles northeast of downtown Dallas. The city encompasses approximately 57 square miles, with approximately 90% of its developable area fully developed. We view the economy as stronger than what our metrics represent because of the city's diverse commercial, retail, and industrial developments that stimulate the economy, despite lower-than-average wealth and income levels. As of February 2018, the city maintained a labor force of over 120,000 with an unemployment rate of just 3.7%.

Garland has several industrial districts that have rail and motor freight transportation facilities. The top employers within the city include Kraft Foods (796 employees), US Food Service (520), Hatco (390), and L3 Communications (350). The city has several commercial projects underway that are expected to bring new jobs as well as AV growth. These include the construction of two separate data center campuses, Digital Realty and RagingWire, that will each include approximately 1 million square feet of space. The Digital Realty facility is valued at $1 billion and the RagingWire facility at $389 million for a total of approximately $1.4 billion in new valuation at build out. In 2015, Nutribiotech, a manufacturer of health and dietary supplements, built a $40 million manufacturing facility and headquarters in Garland. In 2017, the company announced a $100 million capital investment that will expand its research and development and production facilities, and create approximately 1,600 jobs over the next several years. In addition, the former Raytheon campus is under active redevelopment, which will include approximately 800,000 square feet of new commercial flex space. Manufacturing and commercial development has translated into additional residential growth, as the city has several single-family and multi-family developments that have either been recently approved or have started construction.

Garland's tax base continues to experience healthy growth spurred by industrial, commercial, and residential development. Taxable AV increased by an average of 7.66% per year since fiscal 2014. In aggregate, the tax base expanded by $3.5 billion or 34% between fiscal years 2014 and 2018. Preliminary data from the Dallas County Appraisal District suggest that tax base growth for fiscal 2019 will be in line with the level of growth experienced in recent fiscal years. The tax base is very diverse, with the top 10 taxpayers comprising 5% of AV. Although we expect development activities in the city to continue, we do not expect to see a material change in the economic metrics over the next two years.

Very strong management

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

Highlights include management's use of formal historical trend analysis to derive revenue and expenditure budget assumptions. The city can amend the budget, as necessary, throughout the year with city council approval. Management provides quarterly reports on budget-to-actual results to the council. In addition, the city's formal five-year financial plan--publicly published and updated at least annually--includes projections for all major operating funds. Furthermore, the city maintains a five-year capital investment plan with identified cost estimates and funding sources that management updates annually.

The city's formal local investment management policy complies with the Texas Public Funds Investment Act, and the city provides quarterly reports to the council on holdings and earnings. The formal debt management policy includes basic policies such as an overall net debt limitation at 5% of AV. The formal reserve policy calls for the maintenance of 30 days' operating expenditures for the general fund and 45 days for water, sewer, and electric funds.

Strong budgetary performance

Garland's budgetary performance is strong in our opinion. The city had operating surpluses of 4.7% of expenditures in the general fund and of 9.3% across all governmental funds in fiscal 2017.

In our calculations, we have adjusted the city's revenues and expenditures to treat recurring transfers as either revenues or expenditures, and subtracted significant one-time expenditures funded through cash on-hand or debt proceeds. Garland's total governmental funds revenue base is diverse; leading sources include property taxes (42%), sales taxes (14%), charges for services (12.5%), and intergovernmental revenues (7%). Each of these revenue sources has demonstrated stable and steady growth in the past three fiscal years.

Garland has a history of conservative budgeting highlighted by better-than-budgeted final results. Despite budgeting to use fund balance in each of the past four years, the city managed to increase fund balance as a result of expenditure savings and strong-than-expected revenue growth. This trend continued in fiscal 2017 when the city reported a positive net change in fund balance of $8.1 million, despite projecting to draw down its general fund balance by approximately $3.8 million in the final amended budget. The city reported considerable expenditure savings related to capital projects that were not completed during the year and were, therefore, rolled into the fiscal 2018 budget. The city intends to use the surplus reported in fiscal 2017 and additional positive budgetary variances to fund one-time expenditures in the fiscal 2018 budget. Given the use of excess fund balance and the one-time nature of the expenditures being funded, we do not expect our opinion of the city's budgetary performance to weaken despite plans to reduce fund balance below fiscal 2017 levels. Over the medium term, we expect the city to maintain at least balanced operating performance.

The fiscal 2018 amended budget projects a fund balance drawdown of approximately $14.4 million. The reduction in fund balance is tied to one-time expenditures including $7.6 million of streets project rollovers from fiscal 2017, a $4.6 million land purchase, and $2.2 million of additional one-time capital spending. Currently revenues are tracking ahead of budget by $500,000 and expenditures are within budget. Year-end projections forecast a final use of fund balance of only $6.5 million, which is primarily due to expenditure savings from capital projects not expected to be completed during the current fiscal year.

Very strong budgetary flexibility

Garland's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 21% of operating expenditures, or $34.4 million. Over the past five years, Garland's available fund balance has exceeded 15% of expenditures and the city's formal fund balance policy. In fiscal 2018, the city expects one-time expenditures including the purchase of land and expenditure rollovers from the fiscal 2017 budget to reduce available fund balance back to historical levels. Officials are projecting to end fiscal 2018 with an available fund balance of $28.8 million, or a projected 16% of expenditures, which we still consider very strong. We anticipate that fund balance will continue to be maintained in the range of 16%-18% of expenditures. Therefore, we expect that the city will maintain its very strong budgetary flexibility over the next two years.

Very strong liquidity

In our opinion, Garland's liquidity is very strong, with total government available cash at 83.7% of total governmental fund expenditures and 5.9x governmental debt service in 2017. In our view, the city has exceptional access to external liquidity if necessary.

The city's exceptional access to external liquidity is demonstrated through its access to the market over the past 15 years. Garland has frequently issued bonds over the past two decades, including both fixed- and variable-rate GO bonds; commercial paper notes; and electric, water, and sewer revenue bonds.

It has historically had what we consider very strong cash balances and, given management's demonstrated ability to maintain balanced operations, we do not believe its cash position will worsen. All of Garland's investments comply with Texas statutes and the city's internal investment policy. As of Feb. 28, 2018, the city held investments in U.S. treasury coupon securities, federal agency coupon securities, certificates of deposit, and investment pools, which we do not consider aggressive. Garland does not have any contingent liabilities that could lead to unexpected liquidity deterioration from very strong levels.

Adequate debt and contingent liability profile

In our view, Garland's debt and contingent liability profile is adequate. Total governmental fund debt service is 14.1% of total governmental fund expenditures, and net direct debt is 111.8% of total governmental fund revenue. Approximately 79.0% of the direct debt is scheduled to be repaid within 10 years, which is in our view a positive credit factor.

Our ratios have been adjusted to reflect the portion of tax-backed GO bonds and certificates of obligation supported by the city's enterprise funds. Garland has $110.4 million of authorized but unissued GO bonds remaining. Officials are planning to issue between $30 million and $40 million in certificates of obligation annually over the next four years. In addition, the city expects to issue tax notes annually in an amount between $3 million to $8 million over the next five years. Given rapid debt amortization, we do not believe current debt plans will have a material impact on the city's debt profile.

Garland's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 9.2% of total governmental fund expenditures in 2017. Of that amount, 7.0% represented required contributions to pension obligations, and 2.1% represented OPEB payments. The city made its full annual required pension contribution in 2017.

Garland participates in the Texas Municipal Retirement System, an agent multiemployer public employee retirement system. It is required to contribute at an actuarially determined rate, and has historically contributed in excess of the annual required cost. The city's net pension liability measured $57,452,759 as of Dec. 31, 2016. The plan maintained a funded level of 93.66%, using the plan's fiduciary net position as a percentage of the total pension liability.

The city also provides health care benefits to retirees, which it pays for on a pay-as-you-go basis. As of the latest valuation date (Oct. 1, 2016), the unfunded actuarial liability for OPEB was $63.3 million. In the fiscal 2018 adopted budget, Garland approved a long-term funding strategy for OPEB including annual contributions from the general fund and the utility funds to an OPEB Trust Fund. The annual utility fund transfer, which the city had been making for four years, is approximately $750,000, and the initial contribution from the general fund will be $500,000, which will be increased by $85,000 per year until the annual general fund contribution reaches $1.5 million.

Given the current funded status of the city's pension plan and established strategies to manage future retirement costs, we do not believe pension and OPEB liabilities present material risk to the city's debt and contingent liability profile.

Strong institutional framework

The institutional framework score for Texas municipalities is strong.

Outlook

The stable outlook reflects our opinion of Garland's consistent financial performance and expanding local economy, supported by very strong management. We do not expect to change the rating during the next two years because we believe that Garland will likely maintain very strong reserves and strong budgetary performance and continue to benefit from participation in the broad and diverse Dallas-Fort Worth MSA.

Upside scenario

Improvement in the city's debt profile and wealth and income indicators relative to those of higher rated peers could result in a higher rating, all else equal.

Downside scenario

If reserves were to decline to levels we consider just strong or adequate, triggered by increased fixed costs and weakened budgetary performance, we could lower the rating.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- 2017 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of May 16, 2018)		
Garland GO		
Long Term Rating	AA+/Stable	Affirmed
Garland GO		
Long Term Rating	AA+/Stable	Affirmed
Garland GO		
Long Term Rating	AA+/Stable	Affirmed
Garland GO		
Long Term Rating	AA+/Stable	Affirmed
Garland GO		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.