FitchRatings

Public Finance
Tax-Supported
U.S.A

Garland, Texas

Ratings

Long Term Issuer Default Rating	AAA

New Issue

$22,605,000 General Obligation Refunding Bonds, Series 2019	AAA

Outstanding Debt

Combination Tax & Revenue Certificates of Obligation	AAA
General Obligation Bonds	AAA

Rating Outlook

Stable

Applicable Criteria

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

Related Research

Fitch Rates Garland, Texas' $22.6MM Series 2019 GO Refunding Bonds 'AAA'; Outlook Stable (October 2019)

Garland (TX) - ESG Navigator (May 2019)

New Issue Summary

Sale Date: On or around November 5

Series: General Obligation (GO) Refunding Bonds, Series 2019

Purpose: To refund a portion of the city's outstanding debt.

Security: The GO bonds are secured by an ad valorem tax levied on all taxable property within the city, limited to $2.50 per $100 of TAV.

The 'AAA' IDR, GO and CO bond ratings reflect the city's broad budgetary tools, supplemented by a healthy reserve position relative to an expected limited level of revenue volatility (inclusive of sales taxes). These factors combine to provide the city with a high level of operating flexibility and financial resilience throughout the economic cycle. Modest population gains and development underway or planned should maintain the city's solid pace of revenue and resource base growth. These trends should also keep the long-term liability burden in the low range. Fitch expects expenditure flexibility to remain solid, with somewhat elevated carrying costs mitigated by rapidly amortizing debt, self-support from various enterprise funds, and limited pension pressure.

Economic Resource Base: Garland is located approximately 14 miles northeast of downtown Dallas, surrounded by major transportation corridors. The city's approximately 240,000 residents are part of the large and robust Dallas-Fort Worth-Arlington (DFW) metropolitan statistical area (MSA) and benefit from economic and employment trends that continue to outpace national levels.

Current Developments: N/A

Key Rating Drivers

Revenue Framework: 'aa': General fund revenue gains should continue to outpace inflation, but trail U.S. GDP, supported by the likelihood of further development. Formula-driven utility transfers provide significant support for general fund operations and have increased notably over time. Underpinning the revenue framework assessment is the city's ample revenue-raising ability including significant available taxing margin within statutory limits.

Expenditure Framework: 'aa': Solid expenditure flexibility is derived from management's prudent budgeting practices and ability to adjust labor costs if needed. Fitch expects growth-related spending demands to be matched by revenue gains, keeping their trajectories aligned over time.

Long-Term Liability Burden: 'aaa': The long-term liability burden is low at approximately 8% of personal income and should remain in the current range despite recent passage of a large bond referendum, given rapid debt amortization and expectations for growth in population and personal income.

Operating Performance: 'aaa': The city's significant revenue-raising ability and sound expenditure control, supplemented by the strong reserve cushion relative to low expected revenue volatility, should enable the maintenance of a high level of financial flexibility during cyclical downturns.

Rating Sensitivities

Reliance on Utility Transfers: The rating is sensitive to material deterioration of utility transfers if not accompanied by the city's ability to realign spending accordingly.

Analysts

Emmanuelle Lawrence
+1 512 215-3740
emmanuelle.lawrence@fitchratings.com

Teri Wenck, CPA
+1 512 215-3742
teri.wenck@fitchratings.com

Long-Term Liability Burden: A material increase to the city's long-term liabilities without commensurate growth in the resource base could pressure the rating.

Credit Profile

The city's industrial market is one of the largest in the MSA and a diverse list of manufacturing and distribution businesses drives the local economy. Unemployment has registered below state and U.S. levels dating back to 2015.

The city's tax base remains very diverse and primarily residential despite its notable industrial/commercial base presence. Taxable assessed valuations (TAV) have generally grown at a steady, modest pace; however, over the past few years the city's tax base has experienced a sizeable uptick. From fiscals 2016 to 2019, TAV increased by 35% in total, marking three consecutive years of growth at 10% or higher. Fiscal 2020 TAV, at $16.3 billion, reflects an 8% increase over fiscal 2019 TAV. A balanced mix of new commercial and residential development coupled with appreciating values supports the recent upswing in TAV.

Fitch expects new projects and further expansion of the existing non-residential base will support continued economic and TAV growth. New residential development that includes various mixed-use and multi-family projects is also occurring. In spite of this new residential development, management has indicated signs of a cooling Dallas housing market and is preparing for TAV in future years to grow at a slower pace. Fitch has identified the Dallas-Fort Worth area housing market as being among the most overvalued in the U.S. For more information, see U.S. RMBS Sustainable Home Price Report: Third Quarter 2019 dated September 2019.

Revenue Framework

Operations are supported by a fairly diverse revenue base, aided by formula-driven transfers to the general fund from the city-owned enterprises, which accounted for about 19% of fiscal 2018 general fund revenues. Taxes generate the bulk of the city's operating revenues. Property taxes accounted for 37% of fiscal 2018 general fund revenue and sales taxes another 21%. Payments in lieu of taxes/franchise fees/administrative costs from enterprises account for the remainder of general fund tax revenue. Fitch maintains unenhanced ratings on Garland's water and sewer system revenue debt (AA/Stable) as well as the city's electric utility debt (GP&L IDR AA-/Stable).

Fitch believes revenue growth will be solid, in line with historical performance. The city's commercial, industrial, and manufacturing base developed in part due to the city's strategic location in the Dallas-Fort Worth metroplex and access to major ground transportation routes. Ongoing investment and new development planned and underway that expands this base should drive further economic expansion.

Garland's fiscal 2020 tax rate of $0.7696 per $100 of TAV includes a maintenance and operations rate of $0.3940 and debt service rate of $0.3756. The current tax rate is well below the constitutional and city charter cap of $2.50. However, the Texas legislature recently approved and the governor signed into law Senate Bill 2 (SB2), which makes a number of changes to local governments' property tax rate setting process. Most notably, SB2 will reduce the rollback tax rate (now the 'voter approval tax rate') levy increase from 8% to 3.5% for most local taxing units and require a ratification election (replacing the current petition process) if any local taxing unit exceeds its voter approval rate. The tax rate limitation in SB2 excludes new additions to tax rolls and allows for banking of unused margin for up to three years. Remaining control over the property tax rate plus other local revenues such as fines, fees and charges for services is sufficient to generate still ample revenue-raising flexibility relative to Fitch's assessment of expected modest revenue volatility in a typical downturn. The revenue cap does not apply to debt service tax levies.

Expenditure Framework

Public safety is the city's largest general fund spending category, comprising nearly 52% of fiscal 2018 outlays. Public works and culture and recreation are the next largest expenditure areas.

Fitch expects future spending will generally track or marginally exceed the anticipated solid revenue growth, continuing a trend of moderate, steady investments in personnel and capital.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	10/28/19
AAA	Revised	Stable	4/30/10
AA+	Affirmed	Stable	4/13/04
AA+	Assigned		2/12/98

Expenditure flexibility is aided by the city's lack of contracts with employee groups. Management exhibited its flexibility regarding labor costs and headcount during the last recession when it responded to weaker revenue performance. Spending adjustments included a combination of salary and position reductions/freezes in addition to deferral of annual pay-go capital spending.

The city's fixed cost burden is moderately high. Carrying costs (debt service, actuarial pension payments, and pay-go OPEB costs) totaled roughly 20% of fiscal 2018 governmental spending, which incorporates the city's policy-determined, rapid pace of principal amortization (about 80% retired in 10 years). Debt service costs are the largest component of this metric, exceeding 12% of governmental spending in fiscal 2018.

Long-Term Liability Burden

Garland's long-term liability remains low at about 8% of personal income. The city's long-term liability burden reflects a large portion of its direct debt as self-supporting from the electric, water, and wastewater utility funds. Following this refunding, the amount of GO debt supported by the city's utility funds will be notably less. More than half of the net overall long-term liability burden is attributable to overlapping entities, with net direct debt at more than 2% of personal income and the Fitch-adjusted net pension liability (NPL) less than 1%.

On May 4, 2019 voters approved a $423.7 million GO bond program. According to management, the bonds will be issued over the next seven to 10 years to finance various public improvements, including, street replacement, quality of life enhancements, public safety upgrades and storm drainage improvements. According to management, the city anticipates issuing roughly $50 million of the GO debt in 2020. Fitch anticipates that economic growth will keep the city's long-term liability burden in the low range (equal to or less than 10% of personal income) over the next several years.

City employees participate in the Texas Municipal Retirement System (TMRS), a state-wide, joint contributory, hybrid defined benefit pension plan. Under GASB 68 and using a 6.75% investment return assumption, the city has reported in its fiscal 2018 audit that there is NPL, with fiduciary assets covering 100% of total pension liabilities. Using Fitch's standard 6.0% investment return assumption, the NPL is $83.8 million and the ratio of assets to liabilities is still strong at 92%.

Operating Performance

Fitch expects Garland to demonstrate a high level of financial resilience during an economic downturn, consistent with past performance. The 'aaa' resilience assessment is informed by the city's revenue raising capabilities, solid expenditure flexibility and its currently ample financial cushion.

The city has a history of strong budgetary management as demonstrated by its favorable operating performance. Results have consistently exceeded to the city's 30-day minimum unrestricted reserve policy. Management continues an established practice of periodically applying reserves above the stated threshold or mid-year operating surpluses to various one-time spending priorities. Based on the adopted budget for fiscal 2020, which began on October 1, general fund expenditures outpace revenues by a bit more than $2 million. The city has historically posted better-than-budgeted results by fiscal year-end. Fitch expects the city to continue managing its resources prudently to maintain a strong financial cushion.

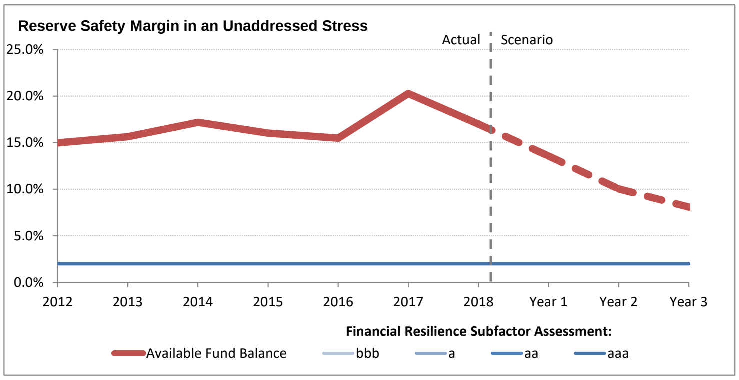
ESG Considerations

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 our ESG Relevance Scores, visit https://www.fitchratings.com/esg.

Garland (TX)

Scenario Analysis



Analyst Interpretation of Scenario Results:

The city closed fiscal 2018 with an unrestricted general fund balance of roughly $32 million, which accounts for 17% of operating expenditures and transfers out. The fiscal 2019 adopted budget reflects a general fund drawdown of about $2 million, for one-time capital expenditures. However, based on unaudited year-end results provided by management, the city expects to produce at least break-even results.

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%)	1.8%	3.6%
Inherent Budget Flexibility		Superior	

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2012	2013	2014	2015	2016	2017	2018	Year 1	Year 2	Year 3
Total Revenues	111,083	112,670	114,929	119,597	132,698	138,522	144,275	142,832	145,400	150,613
% Change in Revenues	-	1.4%	2.0%	4.1%	11.0%	4.4%	4.2%	(1.0%)	1.8%	3.6%
Total Expenditures	140,427	143,450	146,693	153,453	166,838	167,153	182,617	186,269	189,994	193,794
% Change in Expenditures	-	2.2%	2.3%	4.6%	8.7%	0.2%	9.3%	2.0%	2.0%	2.0%
Transfers In and Other Sources	33,891	34,878	35,504	35,914	37,772	39,504	45,471	45,016	45,825	47,468
Transfers Out and Other Uses	1,858	1,898	2,274	2,043	2,327	2,724	7,394	7,542	7,693	7,847
Net Transfers	32,033	32,980	33,230	33,871	35,445	36,780	38,076	37,474	38,132	39,621
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	2,689	2,200	1,466	15	1,304	8,149	(265)	(5,963)	(6,461)	(3,560)
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	1.9%	1.5%	1.0%	0.0%	0.8%	4.8%	(0.1%)	(3.1%)	(3.3%)	(1.8%)
Unrestricted/Unreserved Fund Balance (General Fund)	21,305	22,733	25,594	24,924	26,198	34,436	32,271	26,309	19,847	16,287
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	21,305	22,733	25,594	24,924	26,198	34,436	32,271	26,309	19,847	16,287
Combined Available Fund Bal. (% of Expend. and Transfers Out)	15.0%	15.6%	17.2%	16.0%	15.5%	20.3%	17.0%	13.6%	10.0%	8.1%

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.