S&P Global Ratings

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Summary:
Washoe County, Nevada; Sales Tax

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Summary:

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Credit Profile		
Washoe Cnty sales tax rev rfdg bnds ser 2016A due 12/01/2028		
Long Term Rating	AA+/Stable	Upgraded

Rationale

S&P Global Ratings raised its long-term rating and underlying rating (SPUR) to 'AA+' from 'AA' on Washoe County, Nev.'s series 2016A sales tax revenue refunding bonds. The outlook is stable.

Credit fundamentals

The rating action reflects the application of our priority-lien tax revenue debt criteria, published Oct. 22, 2018, on RatingsDirect, which factors in both the strength and stability of the pledged revenue, as well as the general credit quality of the county, which collects pledged revenue and transfers proceeds to a bond fund maintained by the county. The priority-lien rating on the series 2016A sales tax revenue refunding bonds is limited by our view of the county's creditworthiness and is constrained from going higher unless there is an improvement in the county issuer credit rating. In our view, the pledged revenue obligations do not benefit from limited scope of operations or extraordinary expenditure flexibility of the obligated entity, while we believe pledged revenue has some exposure to operating risk.

The rating action also reflects Washoe County's strong economy and broad taxing base continue to support strong revenue collections, as the county has experienced aggregate growth in sales tax collections of 33% since 2014. Given the growth in pledged revenue recently, coverage on the sales tax improvement bonds continues to gradually improve, crossing above 7x maximum annual debt service (MADS) beginning in fiscal 2018. Given the sustained very strong coverage on the bonds and anticipated pledged revenue growth supported by ongoing development throughout the county, we anticipate these credit factors will remain strong for the foreseeable future.

Security

The bonds are secured by a 0.125% sales tax that is imposed on and collected from retailers within Washoe County. The series 2016A bonds have a first lien on revenue. We understand that, after paying debt service costs, the sales tax may only be used for flood control projects by the Truckee Meadows River Flood Management Authority (TRFMA), pursuant to a interlocal cooperative agreement (ICA) between the county and TRFMA. TRFMA's boundaries are coterminous with the county. Bond proceeds were used to refund the county's series 1998 sales tax bonds to achieve interest savings.

Key credit considerations include:

- A strong to very strong local economic population base of approximately 467,000 generating the pledged revenue, along with a tax base in the broad and diverse Reno metropolitan statistical area;
- Our view that nationwide sales taxes have historically demonstrated low volatility, in addition to our view of low

volatility at the local level; and

- Very strong MADS coverage at 7.1x, with an additional bonds test set at 2.5x.

Economic fundamentals: Strong to very strong

Washoe County is the state's second-most populous county, having roughly 467,000 residents. The county's largest cities are Reno and Sparks, so the local economy centers on tourism and gaming. However, the health care, education services, and industrial sectors have been growing. The area's leading employers are concentrated in the downtown core of Reno, the county seat. The University of Nevada-Reno, local government, and Renown Regional Medical Center are among the largest employers. Income levels are good, in our view, with median household and per capita effective buying incomes (EBIs) at 101% and 97% of the national averages, respectively. The county's employment gains have increased steadily in recent years, and the unemployment rate in 2018 was 3.8%. Management expects the area to continue to experience growth as commercial and residential development continue. Moreover, northern Nevada is seeing sizable investments from large companies like Tesla Inc. and Apple.

The Mountain region of the U.S. continues to lead the country in net migration from other states, and we expect most of these new residents to find work, with nonfarm employment growth expanding through 2021. As many of these new residents come with coastal-level buying power, we anticipate that median home price growth will proceed at more than two times the national Consumer Price Index and give developers incentive to build in a region with plenty of land. On the flip side, the forecast also points to a major slowdown in housing starts in 2019 before a rebound in 2020 and 2021. Further, we see the region's diverse portfolio of leading industries--professional services, natural resources and mining, and leisure and hospitality--and attractiveness to interstate migrants for its quality of life as helping it capture a portion of the growth that would otherwise flow to high-paying but even higher-costing metropolitan areas in the Pacific states. For more information, please see our report "Summer Should Be Smooth Sailing For U.S. State And Local Governments, But There Could Be Waves Ahead," published April 30, 2019.

Volatility: Low

We assess the volatility of revenue in order to determine the likelihood of the availability of revenue during different economic cycles. We have two levels of volatility assessment: macro and micro.

On a macro level, we consider sales and use tax revenue to have a low historical volatility assessment, based on total retail food and service sales data from the U.S. Census Bureau over the past two decades. Our macro volatility assessment begins with an assessment of the historical volatility of the economic activity being taxed, and includes an analysis of societal, demographic, political, and other factors that could affect these activities. Nationwide retail and food service sales have historically fluctuated moderately throughout severe economic downturns and price fluctuations, as sales of nonessential goods are relatively cyclical. However, we expect overall collections will remain generally stable nationwide, given the relative inelasticity of demand for certain taxable goods and services. On a micro level, despite some declines during the recession, the county's sales tax revenue has grown for eight consecutive years by an average annual rate of 8% to $10.2 million in 2018. Sales tax collections increased $798,000 in 2018. The largest generators of taxable sales in the county, by industry, have historically been general merchandise stores, food services and drinking places, and motor vehicle and parts dealers. We understand that there is not a concentration in the top 10 taxpayers.

Coverage and liquidity: Strong

With pledged revenue totaling $10.2 million in fiscal 2018, we calculate MADS coverage at 7.1x in fiscal 2018, with MADS occurring in fiscal 2021. Since issuance in fiscal 2016, MADS coverage has increased every year as a result of continued pledged revenue growth. The county is currently unable to issue parity or subordinate debt under the ICA unless it is amended or terminated. The county asserts that there are no plans by its members to amend or terminate the ICA. The ICA may issue debt secured by pledged revenue, but only on a subordinate lien to the series 2016A refunding bonds. The county does have an outstanding series secured by pledged revenue that is subordinate to the series 2016A refunding bonds. If the ICA is amended or terminated, the county could issue debt on a parity or superior basis to the series 2016A refunding bonds if MADS coverage by pledged revenue was 2.5x in the previous year or if pledged revenue is projected to be 250% of MADS in each of the first five years immediately succeeding the issuance of such debt. We understand that management currently has no plans to issue additional debt. We expect coverage will remain strong in the near term.

Obligor linkage: Close

We believe the priority lien of pledged revenue provides some protection from operating risk; however, because the majority of pledged revenue is collected by the county and then transferred to the bond fund (managed by the county), we consider the flow of pledged revenue to be within the county's direct control. Under our criteria, this narrows the linkage between the priority-lien pledge and the obligor's creditworthiness, as we believe pledged revenue has some degree of exposure to operating risk.

Rating linkage to Washoe County

We assess Washoe County's general operations because we view overall creditworthiness as a key determinant of an obligor's ability to pay all of its obligations, including bonds secured by a special tax. The rating on the series 2016A sales tax revenue bonds is currently constrained by the county's creditworthiness. In our view, the county's creditworthiness is enhanced by the maintenance of a strong financial position, supported by what we consider strong financial management policies and practices. The county's general creditworthiness is somewhat constrained by its local economic metrics, more specifically, our calculation of market value per capita and projected per capita EBIs as a percentage of the U.S.

Outlook

The stable outlook reflects our view of the county's consistent improvement in sales tax collections and maintenance of strong coverage. As a result of continued economic improvement, pledged revenue will likely remain sufficient to provide at least strong MADS coverage. The outlook further reflects our view of the county's lack of plans to issue additional sales tax bonds. We do not expect to raise the rating in the two-year outlook horizon.

Upside scenario

Should the county's operations remain positive and the local economy strengthens further, resulting in an improvement in our view of the county's creditworthiness, we could raise the priority-lien ratings.

Downside scenario

Should pledged revenue begin a trend of decline, leading to a drop in coverage to a level we no longer consider strong, we could lower the rating.

Related Research

Criteria Guidance: Priority-Lien Tax Revenue Debt, Oct. 22, 2018