FitchRatings

Public Finance
Tax-Supported
U.S.A

Garland, Texas

Ratings

Long-Term Issuer Default Rating	AAA

New Issue

$16,745,000 Combination Tax and Revenue Certificates of Obligation, Series 2020	AAA

Outstanding Debt

Combination Tax and Electric Utility System Revenue Bonds	AAA
Combination Tax and Revenue Certificates of Obligation	AAA
General Obligation Bonds	AAA

Rating Outlook

Stable

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (March 2020)

Related Research

Fitch Rates Garland, Texas' $16.7MM Series 2020 COs 'AAA'; Outlook Stable (May 2020)

Garland (TX) [General Government] - ESG Navigator (May 2019)

New Issue Summary

Sale Date: The bonds are expected to sell competitively on or about May 19, 2020.

Series: $16,745,000 Combination Tax and Revenue Certificates of Obligation, Series 2020

Purpose: Proceeds from the new issuance are expected to finance various capital needs such as upgrades to existing facilities, the replacement of environmental waste equipment and drainage improvements.

Security: The certificates are payable by an ad valorem tax levied on all taxable property within the city of Garland, TX (the city) limited to $2.50 per $100 of taxable assessed valuation (TAV), with an additional limited pledge of surplus water and sewer system revenues not to exceed $1,000.

The 'AAA' Issuer Default Rating (IDR) and GO bond rating reflect Fitch Ratings' expectation for the city to maintain healthy financial flexibility through economic cycles, including the current downturn resulting from the coronavirus pandemic. The city's broad budgetary tools, supplemented by a healthy reserve position relative to limited historical revenue volatility, support the current rating. Fitch expects expenditure flexibility to remain solid, with somewhat elevated carrying costs mitigated by rapidly amortizing debt and self-support from various enterprises. The city's inclusion within the deep and diverse Dallas-Fort Worth MSA supports Fitch's expectation of favorable economic and revenue growth over the long term following a recovery from the current economic climate.

Economic Resource Base: Garland is located about 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) MSA and benefit from long-term economic and employment trends that have outpaced national levels for many years.

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 revenue-raising flexibility that includes a 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 its current range, notwithstanding 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 a strong reserve cushion relative to low expected revenue volatility should enable maintenance of a high level of financial flexibility during cyclical downturns.

Rating Sensitivities

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Not applicable for a 'AAA' rating.

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Factors that could, individually or collectively, lead to negative rating action/downgrade:

- A severe and prolonged slowdown in economic activity leading to materially lower revenue growth prospects, below long-term GDP trends.
- Over the near-to-medium term, increased financial pressure due to an unexpectedly sizable decline in operating revenues absent actions to adjust spending.
- Failure to realign operational spending in the event of a material deterioration of customary utility fund transfers to the general fund.

Current Developments

Sectorwide Coronavirus Implications

The ongoing coronavirus pandemic and related government containment measures worldwide create an uncertain global environment for U.S., state and local governments and related entities in the near term. While Garland's most recently available fiscal and economic data may not fully reflect impairment, material changes in revenues and expenditures are occurring across the country and likely to worsen in the coming weeks and months as economic activity suffers while public health spending increases. Fitch's ratings are forward looking in nature; as such, Fitch will monitor developments in state and local governments resulting from the pandemic as they relate to severity and duration and incorporate revised expectations for future performance and assessment of key risks.

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. The city's unemployment rate has registered below state and national levels for several years, reflecting the generally strong local and regional job market. However, given widespread business closures in response to the pandemic, Fitch expects unemployment rates to increase in the near term.

The city's tax base remains very diverse and primarily residential despite its notable industrial/commercial base presence. TAVs have generally grown at a steady, modest pace; however, in recent years Garland's tax base has experienced a sizable uptick. From fiscal years 2016–2019 TAV increased 35% in total, marking three consecutive years of TAV growth at 10% or higher. In particular, fiscal 2020 TAV, at $16.3 billion, reflects an 8% increase over fiscal 2019. A balanced mix of new commercial and residential development coupled with appreciating values support the recent TAV upswing.

While the current coronavirus-driven economic downturn yields a sizable blow to the regional economy, the long-term economic prospects for both the city and metropolitan region remain positive. Based on historical trends and the series of residential, commercial and industrial development projects that have been under way, Fitch expects tax base growth to continue.

Revenue Framework

Operations are supported by a fairly diverse revenue base aided by formula-driven transfers to the general fund from city-owned enterprises, which accounted for about 22% of fiscal 2019 general fund revenues. Taxes generate the bulk of Garland's operating revenues. Property taxes accounted for 38% of fiscal 2019 general fund revenue, followed by 20% from sales taxes and the remainder reflecting payments in lieu of taxes/franchise fees/administrative costs from enterprises. Fitch maintains unenhanced ratings on Garland's water and sewer system revenue debt (AA/Stable) and on the city's electric utility debt (Garland Power & Light IDR: AA–/Stable).

In prior years, the pace of general fund revenue increases has exceeded inflation but trailed U.S. GDP gains. For the 10-year period ending in fiscal 2019, the rate-adjusted general fund revenue CAGR of 3.1% was below U.S. GDP but comfortably ahead of inflation. Given the current economic climate, fiscal 2020 general fund revenues will experience a decline. Based on preliminary assumptions from management, the projected general fund revenue shortfall is roughly $5 million, or 3% of budgeted operating revenues for fiscal 2020. This shortfall is primarily driven by a decline in sales tax revenues and, to a lesser extent, court revenues.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	5/8/20
AAA	Revised	Stable	4/30/10
AA+	Assigned	—	2/12/98

While the coronavirus-driven economic downturn directly impacts revenue growth, economic and revenue prospects for the city and the larger Dallas-Fort Worth-Arlington MSA remain positive over the long term.

Garland's fiscal 2020 tax rate of $0.7696 per $100 of TAV provides ample capacity below the state's statutory cap of $2.50 per $100 of TAV. However, Senate Bill 2 (SB 2), recently approved by the Texas Legislature and signed into law by the governor, makes a number of changes to local governments' property tax rate-setting processes. Most notably, SB 2 will reduce the rollback tax rate (now the "voter-approval tax rate") levy increase from 8.0% 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 SB 2 excludes new additions to tax rolls and allows for the banking of unused margin for up to three years. Remaining control over 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

Similar to many local governments, public safety is the city's largest general fund spending category, comprising nearly 51% of fiscal 2019 outlays. Public works and culture/recreation are the next largest expenditure areas.

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

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 coupled with the deferral of annual pay-as-you-go capital spending.

The city's fixed cost burden is moderately high. Carrying costs (debt service, actuarial pension payments and pay-as-you-go other post-employment benefit [OPEB] costs) totaled roughly 20% of fiscal 2019 governmental spending, which incorporates the city's policy-determined, rapid pace of principal amortization (about 80% retiring in 10 years). Debt service costs are the largest component of this metric, exceeding 12% of governmental spending in fiscal 2019.

Long-Term Liability Burden

Garland's long-term liability burden 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 debt from the electric, water and wastewater utility funds. The city's self-supporting debt has been factored into the liability assessment. More than half of the net overall long-term liability burden is attributable to overlapping entities.

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 years 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 expects to issue an additional $35 million of GO debt before the end of 2020. Fitch anticipates 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.

Garland's pension benefits are provided through the Texas Municipal Retirement System, an agent, multi-employer defined-benefit plan. Under GASB 68, the city reports a fiscal 2019 net pension liability of about $88 million, with fiduciary assets covering 91% of total pension liabilities at the plan's 6.75% investment return assumption. Using a more conservative 6% investment return assumption, the estimated asset-to-liability ratio declines to about 84%.

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 currently ample financial cushion.

The city closed fiscal 2019 with a net operating surplus of more than $800,000 and an unrestricted general fund balance of about $34 million, equal to about 17% of spending. The fiscal 2019 audit reflects better-than-budgeted results, as the city's adopted budget planned for a $2 million general fund deficit.

The city has a history of strong budgetary management as demonstrated by its favorable operating performance. Results have consistently exceeded the city's 30-day minimum unrestricted reserve policy. The city has an established practice of periodically applying reserves above the stated threshold or mid-year operating surpluses to various one-time spending priorities.

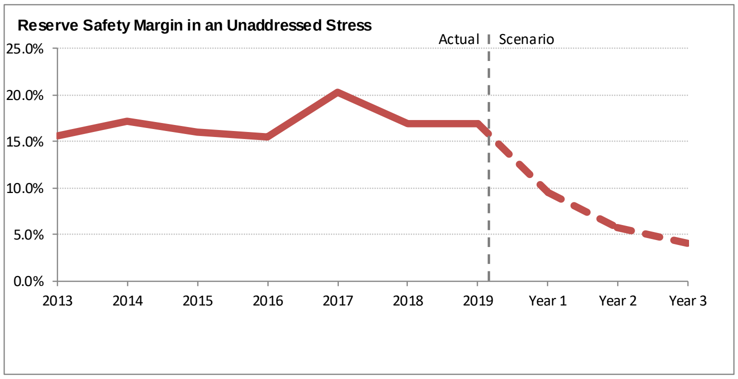
Similar to the previous year, the adopted fiscal 2020 budget reflected expectations of a $2 million general fund deficit. While the city has historically posted better-than-budgeted results by fiscal year end given the coronavirus pandemic and subsequent economic slowdown, management currently expects expenditures to outpace revenues by about $3.7 million. This shortfall encompasses a projected $5 million loss in general fund revenues and $1.3 million in immediate expenditure cuts. City representatives have confirmed that the budget is being closely monitored, with additional adjustments to be made as needed. Representatives have also confirmed that the fiscal 2021 budget will maintain the 30-day minimum unrestricted reserve policy. Even amid the currently stressed economic environment, Fitch expects the city to continue managing its resources prudently to maintain a strong financial cushion.

ESG Considerations

The highest level of environmental, social and governance (ESG) credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, due to either 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.

Garland (TX)

Scenario Analysis



Analyst Interpretation of Scenario Results:

The city closed fiscal 2019 with a net operating surplus of more than $800,000 and an unrestricted general fund balance of about $34 million, which equals 17% of spending. The fiscal 2019 audit reflects better-than-budgeted results, as the city adopted budget indicating a $2 million general fund deficit.

Even with an assumed 5% decline in operating revenues for 'Year 1' of Fitch's Scenario Analysis output, the city has a solid reserve cushion. Moreover, it is important to note that the decline in operating revenues captured in the scenario output is driven by a Fitch-assumed decline in U.S. GDP and historical revenue volatility. Historically, the city has experienced relatively low volatility in comparison to U.S. GDP.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(3.3%)	3.8%	2.0%
Expenditure Assumption (% Change)	0.0%	2.0%	2.0%
Revenue Output (% Change)	(7.9%)	6.3%	4.1%
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	112,670	114,929	119,597	132,698	138,522	144,275	153,569	141,499	150,392	156,523
% Change in Revenues	-	2.0%	4.1%	11.0%	4.4%	4.2%	6.4%	(7.9%)	6.3%	4.1%
Total Expenditures	143,450	146,693	153,453	166,838	167,153	182,617	197,962	197,962	201,922	205,960
% Change in Expenditures	-	2.3%	4.6%	8.7%	0.2%	9.3%	8.4%	0.0%	2.0%	2.0%
Transfers In and Other Sources	34,878	35,504	35,914	37,772	39,504	45,471	47,872	44,110	46,882	48,793
Transfers Out and Other Uses	1,898	2,274	2,043	2,327	2,724	7,394	2,591	2,591	2,643	2,696
Net Transfers	32,980	33,230	33,871	35,445	36,780	38,076	45,281	41,519	44,239	46,098
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	2,200	1,466	15	1,304	8,149	(265)	888	(14,945)	(7,291)	(3,339)
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	1.5%	1.0%	0.0%	0.8%	4.8%	(0.1%)	0.4%	(7.5%)	(3.6%)	(1.6%)
Unrestricted/Unreserved Fund Balance (General Fund)	22,733	25,594	24,924	26,198	34,436	32,271	34,020	19,075	11,785	8,445
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	22,733	25,594	24,924	26,198	34,436	32,271	34,020	19,075	11,785	8,445
Combined Available Fund Bal. (% of Expend. and Transfers Out)	15.6%	17.2%	16.0%	15.5%	20.3%	17.0%	17.0%	9.5%	5.8%	4.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -3.3% GDP decline in the first year, followed by 3.8% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 0.0% rate in Year 1, and a 2.0% rate of inflation in Years 2 and 3. 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.