S&P Global Ratings

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Summary:

Cuyahoga County, Ohio; Sales Tax

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Table Of Contents

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Credit Profile		
US$123.39 mil sales tax rev bnds (tax-exempt) (Ballpark Imp Proj) ser 2022A due 01/01/2037		
Long Term Rating	AAA/Stable	New
US$67.5 mil sales tax rev bnds (federally taxable) (Ballpk Imp Proj) ser 2022B due 01/01/2037		
Long Term Rating	AAA/Stable	New
US$35.265 mil sales tax rev bnds (federally taxable) (Quicken Loans Arena Proj) ser 2017B due 01/01/2035		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to Cuyahoga County, Ohio's $123.4 million series 2022A tax-exempt sales tax revenue bonds and $67.5 million series 2022B taxable sales tax revenue bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the county's previously issued sales tax revenue bonds. The outlook is stable.

The sales tax ratings reflect 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 Cuyahoga County (the obligor's creditworthiness). For more information on the county's general creditworthiness, please see our report to be published today. The 'AAA' rating on the sales tax bonds is two notches higher than the obligor's creditworthiness, reflecting our view that the pledged revenue and the flow of funds are sufficiently removed from the county's control so as to substantially mitigate operating risk.

Securing the 2022 bonds are proceeds from a 1.25% tax on all retail sales in the county and on the storage, use, or consumption in the county of tangible personal property, including automobiles. The bonds' lien on the 1.25% sales tax is on parity with the county's other sales-tax-secured bonds. One percent of the county sales tax is continuous, while the remaining 0.25% is in effect until 2027. Neither is subject to repeal. All sales tax revenue is pledged to the bonds and the debt service coverage remains very strong, in our opinion, even assuming the revenue generated from the 0.25% sales tax rate is not renewed after calendar 2027.

Proceeds of the 2022 bonds will be used to fund renovations at Progressive Field, home of the Cleveland Guardians professional baseball team. The Guardians have agreed to extend their lease on the ballpark by 15 years to 2036, corresponding with the final maturity on the bonds. The ballpark is owned by the Gateway Economic Development Corp., a nonprofit corporation overseen by the City of Cleveland and Cuyahoga County. The team will cover any cost overruns on the project.

While the bonds are legally secured only by revenue from the county's sales tax, officials plan to use other sources of revenue to repay the debt service on the bonds. The 2022A bonds are expected to be repaid with parking garage revenue, admission taxes, a general fund contribution from Cleveland, and hotel taxes and a general fund contribution from Cuyahoga County. The 2022B bonds are expected to be repaid mostly with rent payments from the Guardians. Public sources of revenue noted above will cover two-thirds of the interest costs on the 2022B bonds.

The intended sources of repayment are structured to cover 100% of debt service. Excess revenue will be used for capital repairs on the ballpark. County sales tax revenue will cover any shortfall in any of the intended repayment sources. Our rating reflects only the pledge of the county's 1.25% sales tax.

The county is also pledging tax increment revenue to its series 2015 sales tax revenue bonds, but we rate the bonds based on the pledge of sales tax revenue, which we view as the stronger pledge.

The county has also covenanted that it will fulfill any debt service shortfall on its series 2016 sales tax bonds with any legally available funds no less than two business days prior to the debt service. However, we rate the bonds based on the pledge of sales tax revenue, which we view as the stronger pledge.

The county's sales tax bonds are eligible to be rated above the sovereign because we believe the county can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions," published Nov. 19, 2013, the county has predominantly locally derived revenue sources, independent taxing authority, and independent treasury management from the federal government.

Credit overview

A pandemic-induced sales tax decline in 2020 and an increase in maximum annual debt service (MADS) with the issuance of the series 2022 bonds have caused a dilution in coverage, but coverage remains very strong. Sales tax collections dropped 10.3% in 2020 and MADS on all parity debt is increasing to $40.2 million from $25.8 million. Using only the 1% continuing portion of the sales tax, 2020 revenue of $210.7 million provides an estimated 5.2x MADS coverage. Sales tax collections have rebounded strongly in 2021 and are estimated to come in about 16% higher, which we estimate would equate to MADS coverage of about 6x. We anticipate a smaller increase in sales tax collections in 2022.

The stable outlook reflects our expectation that sales tax collections will remain sufficient and produce very strong debt service coverage. We do not anticipate changing the ratings during the two-year outlook timeframe unless the county were to issue substantial additional debt, further diluting coverage. The county is exploring options to build a new jail, which we believe would likely involve the issuance of debt, so we will monitor this for impact on the credit.

Furthermore, under our criteria, there is a link between the attributes of the priority lien pledge and the obligor's creditworthiness. Thus, in some cases movement in the obligor's creditworthiness could dictate or limit movement in the priority lien rating. In our view, the county has sufficient budgetary flexibility to mitigate pressures over the next two years. At the end of fiscal 2020, the county's available general fund balance was $253 million, or 53% of operating expenditures. The county has also been approved to receive a total of $240 million in American Rescue Plan Act funding, which we believe provides additional budget flexibility.

The 'AAA' rating also reflects our view of the county's:

- Role as the anchor for the broad and diverse Cleveland-Elyria metropolitan statistical area, which provides resiliency to the sales tax base, though historical population decline somewhat tempers this;

- Sales tax revenue activity that has historically demonstrated low volatility over a long-term horizon; and
- Very strong MADS coverage and good legal provisions, including the direct transfer of pledged revenue from the state tax commissioner to the bond trustee and a 3x MADS historical additional bonds test.

Environmental, social, and governance

We consider social risks in line with the sector. Although the county has experienced historical population decline, this has moderated in recent years and we believe that the county's status as the anchor for a more stable broad and diverse economy largely mitigates this risk.

The county jail has been in the spotlight for several years after eight inmates died in 2018, and the U.S. Marshals Service released a report finding "inhumane" conditions at the jail, including overcrowding and inadequate medical care. The state attorney general took over the investigation in early 2019, and this has led to various indictments, including of the former jail director. The county has taken action to address the issues at the jail, and operations at the facility have improved, but uncertainty remains about the potential impact of lawsuits related to the jail, and therefore we consider governance risks elevated.

The county's location on the shores of Lake Erie poses some coastal erosion risk, but the county has a long-term lakefront plan that we believe will mitigate erosion, so we consider environmental risks neutral within our credit analysis. Overall, we view the county's access to the Great Lakes, the largest freshwater resource in the world, as a potential environmental natural capital opportunity, as it could attract business investment and potentially stabilize population trends.

Stable Outlook

Downside scenario

We could lower the rating if sales tax revenue declines or the county issues substantial additional debt to the extent that we no longer expect coverage to remain well above 4x, which we consider extraordinary strong under our criteria. We could also lower the ratings if general creditworthiness deteriorates. In our view, the rating could come under pressure if budgetary performance weakens and reserves were to fall below the policy-mandated level without an adequate plan to replenish them. We could also lower the rating if intended repayment sources for supporting certain debt were to fall short of projections, requiring ongoing general fund support, or if the county were to issue significant additional debt.

Credit Opinion

Economic fundamentals: Strong-to-very-strong

Cuyahoga County serves an estimated 2020 population of 1.3 million in northeastern Ohio, on Lake Erie and anchored by Cleveland, which we consider a broad and diverse economy. The city is a regional financial, health care, and services center that provides a wide variety of jobs to county residents. The county's population has been declining, although the decline appears to be moderating, with the 2020 U.S. census showing only a 1.2% drop over the past decade. We do not view the population decline as a significant credit weakness, given that the county anchors a larger and more stable metropolitan region.

The county's per capita effective buying income is 96% of the national level. County per capita retail sales were 95.6% of the U.S. level in 2020. Leading sales taxpayer information is not available, but given the size of the county we do not view concentration as an issue. The average unemployment rate for the county in 2020 was 10.2%, elevated because of the pandemic, but as of October 2021 had fallen to 4.1%. The county's economy has diversified away from manufacturing, and its largest employers are predominantly medical, governmental, and service-oriented, the largest being the Cleveland Clinic Health System (44,665 employees). Cuyahoga County has codified economic development as a priority and has supported various projects to add and retain jobs and support housing in Cleveland and throughout the county in recent years.

Coverage and liquidity: Very strong

An additional bonds test on the county's other parity sales tax debt--defined as one-half of the aggregate continuing county sales tax receipts (1%) during the prior 24 consecutive months prior to the sale of additional bonds, which is greater than 300% of the debt service charges on all bonds payable during any bond year--covers the bonds. Based on calendar years 2020 and 2021, the continuing sales tax amount calculated for the past 24 months is $223.1 million and the coverage for all series of bonds is more than 5.5x in any debt service payment year.

Following the Great Recession, the county's sales tax revenue grew at an annual average of 6.1% from 2009 to 2016. In 2016 to 2018, sales tax revenue fell by 6.7% as the state phased out the ability to apply sales and use taxes to services provided by Medicaid managed care organizations. Collections saw a 12.6% rebound in 2019 to $293.6 million (on an audited basis). When the pandemic hit in early 2020, officials projected that sales tax revenue would fall 20% in 2020. However, the county outperformed these projections, and actual collections came in only 10.3% lower at $263.4 million. Of this, approximately $210.7 million represents revenue from the continuing 1% tax.

Using 1.25% sales tax revenue of $263.4 million in 2020, MADS of $40.2 million (including all sales tax bonds) occurring in 2031 results in coverage of 6.6x. Annual debt service gradually ramps up through 2026, is relatively level through 2031, then drops off slightly until final maturity in 2038. Assuming just the 1% sales tax revenue ($210.7 million) is used after 2027, MADS coverage drops to 5.2x, which we still consider very strong. When the 2017 sales tax revenue bonds (the most recent parity debt) were issued, MADS coverage was about 9x (using the 1% tax). Although coverage has fallen, under our criteria, coverage of more than 4x is still considered extraordinary strong. We also expect coverage to improve in 2021. Estimates show a 16% rebound in sales tax collections, and we project that MADS coverage using the 1% sales tax should be closer to 6x. The county is also budgeting for 2% increase in 2022, which we believe is a reasonable assumption given economic conditions.

Although officials have not formally identified any additional debt plans, we are aware that the county plans to build a new jail, which we believe will likely involve the issuance of additional debt, potentially secured by sales tax revenue. The maximum estimated cost of the jail is about $550 million, though the actual cost may be lower. In the future, if we no longer expect coverage to remain well above 4x,whether as a result of additional debt or a drop in revenue, the rating could come under pressure.

Volatility: Low

General sales taxes in Ohio are economically sensitive, though we consider overall volatility and elasticity comparatively limited. Furthermore, locally derived sales tax collections tend to remain in line with broader macroeconomic variables and do not exhibit materially greater volatility than do general-use sales taxes across the state or nationally.

Obligor linkage: Mitigated

We consider the flow of pledged revenue substantially removed from the county's direct control. Pursuant to resolutions and the trust agreement, the state tax commissioner deposits sales tax revenue monthly into the trustee-held sales tax revenue fund. We consider this a strength, as it isolates the sales tax revenue to ensure timely bondholder payments. The trustee will deposit 25% of the amount that will be sufficient to pay interest on the bonds due in the next interest payment date and 10% of the amount sufficient to pay principal due on the next principal date. As a result, sufficient money will be on hand in the sales tax bond fund two months prior to debt service due dates for payment on the bonds. To the extent that the aforementioned intended repayment sources for the 2022 bonds are sufficient for debt service, the excess sales tax revenue will be remitted to the county. If the intended repayment sources are not deposited with the trustee in a timely manner, then the county will be reimbursed with the project revenue at a later date. The series 2022 bonds will not have a debt service reserve.

Rating linkage to Cuyahoga County

We assess Cuyahoga 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 special tax revenue. Proactive expenditure reductions and federal stimulus funding have helped the county weather the pandemic without financial deterioration. The county expects to report operating surpluses in 2021 and 2022. In our view, the county also benefits from a very healthy reserve position. Therefore, we expect fiscal stability over the next two years. The strength of the county's economy, finances, and management offset its weaker debt profile.

Related Research

- Criteria Guidance: Priority-Lien Tax Revenue Debt, Oct. 22, 2018
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

Ratings Detail (As Of January 6, 2022)		
Cuyahoga Cnty sales tax rev bnds (pub square proj) ser 2015A due 12/01/2033		
Long Term Rating	AAA/Stable	Affirmed
Cuyahoga Cnty sales tax rev bnds (pub square proj) ser 2015A due 12/01/2033		
Long Term Rating	AAA/Stable	Affirmed
Cuyahoga Cnty SALESTAX		
Long Term Rating	AAA/Stable	Affirmed

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