S&P Global Ratings

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Summary:

Cuyahoga County, Ohio; Appropriations; General Obligation; Miscellaneous Tax

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Credit Profile		
US$30.6 mil econ dev rev bnds ser 2022A due 12/01/2042		
Long Term Rating	AA/Stable	New

Credit Highlights

- S&P Global Ratings assigned its 'AA' long-term rating to Cuyahoga County, Ohio's $30.6 million series 2022A economic development revenue bonds.
- At the same time, S&P Global Ratings affirmed its 'AA' long-term rating on the county's previously issued general obligation (GO) and nontax revenue debt and its 'AA-' long-term rating on the county's previously issued appropriation-secured debt.
- The outlook is stable.

Security

Certain nontax revenue secures the series 2022A bonds, but the county is legally permitted to use all available revenue to pay debt service. Given this, we rate the debt at the same level as our view of the county's general creditworthiness, as reflected by an unlimited-tax GO pledge. We believe that the county's ability to pay these obligations is closely tied to its operations, and we see no limits on the fungibility of resources available for debt service. The county will use the bond proceeds to repurpose the building formerly known as the medical mart and Global Center for Health Innovation into additional convention and meeting space. The convention center complex is owned by the county and managed by the Cuyahoga County Convention Facilities Development Corp. The county and CCCFDC will also cash-fund a portion of the project, and each intends to cover about 50% of the debt service on the bonds.

Various pledges secure Cuyahoga County's previously issued debt:

- The county's full faith and credit and an agreement to levy ad valorem property taxes within the state's 10-mill limitation secure its GO debt. We rate this debt at the same level as our view of the county's general creditworthiness.
- Lease rental payments, subject to appropriations, secure the county's series 2013 development lease revenue bonds (issued by the Cleveland-Cuyahoga County Port Authority) and series 2014 certificates of participation. We rate the obligations one notch lower than the GO rating to reflect annual appropriation risk.
- The county's guarantee of the payment of principal and interest, subject to appropriation, secures the series 2014A taxable economic development revenue bonds. Although the developer makes payments from project revenue pursuant to a loan agreement, the county annually appropriates for 100% of debt service in case of a shortfall in project revenue. We rate this one notch below the county's general creditworthiness to reflect appropriation risk.

Credit overview

Cuyahoga County is the anchor of the broad and diverse Cleveland-Elyria metropolitan statistical area, which we believe provides stability to its credit profile. Recovery in sales tax collections, ongoing expenditure management, and federal stimulus funding has helped the county maintain fiscal stability through the pandemic. While the 2022 budget is operationally balanced, we believe inflation, labor pressures, and rising recession risk could weaken budgetary performance over the outlook horizon. However, in our view, the county's very strong budgetary flexibility, including healthy reserves, mitigates potential budget pressures. In our opinion, the strength of the county's economy, management, and finances offsets its weak debt profile, which continues to be a limiting credit factor.

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

- Strong economic fundamentals, including good incomes and market values, although weaker demographics somewhat temper these;
- Structurally balanced operations, with reserves providing very strong budgetary flexibility at roughly $345 million, or 70% of expenditures (though a portion of this represents stimulus funding that will likely be spent down);
- Good financial policies and practices under our financial management assessment methodology, and strong institutional framework; and
- Weak debt and liabilities profile, including contingent debt with exposure to the sports, convention, and tourism industry, though rapid amortization somewhat offsets this.

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 that 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 stabilize population.

Outlook

The stable outlook reflects our view of Cuyahoga County's broad and diverse economy as well as its very strong budgetary flexibility and liquidity, and our expectation that the county will address challenges to maintain balanced operations, supported by its track record of very strong fiscal management. We also believe that the county's robust reserves will allow it more time and flexibility to address these challenges, and therefore we do not anticipate changing the rating over the two-year outlook horizon.

Downside scenario

In our view, the rating could come under pressure if budgetary performance weakens and if reserves were to fall below the county's 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.

Upside scenario

We could raise the rating if the county's income or wealth levels improve to levels commensurate with those of higher-rated peers, or if the county's debt and liability profile improves.

Credit Opinion

Broad and diverse economy, with wealth and income levels in line with the national average

Cuyahoga County is located on Lake Erie in northeastern Ohio, is the second-most-populous county in the state, and contains two townships and 57 cities and villages, the largest of which is Cleveland. 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 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. Manufacturing represents 8% of the county's employment base, while education and medical services make up the largest sector at 21%, followed by professional and business services, and transportation, trade, and utilities, each at 16%. The county is home to a diverse array of employers, including 13 corporations that rank among Fortune magazine's 1,000 largest in the U.S. We note that Sherwin-Williams Co. is building a new headquarters and research-and-development site in the county.

The 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. Public and private investment have increased, with a significant concentration in downtown Cleveland and surrounding neighborhoods. We believe that a corresponding migration of residents to the county's urban core should help counteract the county's overall population decline. The county's assessed value grew 13.1% in the 2021-2022 triennial update, reflecting a significant increase in home values, although a decrease in commercial values as a result of the pandemic partly offset this.

County unemployment was 6.3% as of June 2022. S&P Economics projects a rising risk of recession over the next year, and the county's unemployment has historically trended above national averages during recessionary periods. (For more information on S&P Global Ratings' view of the U.S. economy, see "U.S. Recession--Are We There Yet?" published Aug. 2, 2022, on RatingsDirect.)

Strong management with the use of long-term planning and a formal reserve policy

Management uses historical trend analysis and outside sources to form revenue and expenditure assumptions on a line-item basis, and the county operates on a two-year budget cycle. The county council receives detailed quarterly budget-to-actual and investment reports, and the budget can be amended as needed. The county has a comprehensive two-year budget and five-year financial projections. Officials annually update a rolling five-year capital plan that identifies funding sources and cost estimates. The county adheres to a reserve policy that requires a minimum unencumbered general fund balance equal to 25% of prior-year cash-basis expenditures. The county's investment and debt policies largely mirror state guidelines.

An election will be held in November 2022 to replace the county executive, who will retire at the end of 2022. We will monitor the turnover for any impact on the county's financial policies and practices.

The institutional framework score for Ohio counties is strong.

Very strong reserves and liquidity provide cushion against inflation, labor pressures, and rising recession risk

The county typically budgets very conservatively, resulting in positive budget variances. While the 2022 budget originally called for a $76 million use of general fund reserves, officials now project the actual draw at closer to $5 million. This projection includes more than $9 million in various one-time expenditures and, after adjusting for these, we believe the county would show an operating surplus. Many of the county's revenue sources, including sales taxes, are outperforming the budget. Sales taxes are projected to come in at $302.1 million, which would be a 3.7% increase over 2021. The county also budgets for full employment in many departments, so vacancies often lead to significantly lower expenditures. The pandemic and macroeconomic conditions have exacerbated labor shortages in the county, particularly among correction officers and social workers. As a result of the shortage in correction officers, the sheriff department's budget is trending about $12 million over budget on account of overtime costs, but savings elsewhere have offset this.

The county's 2023 budget is structured similarly to that of 2022, conservatively calling for about a $60 million use of general fund reserves. However, officials expect similar variances to those in 2022, with a closer to break-even result. While we expect the county to significantly outperform its budget, we see risk that budgetary performance could weaken relative to that of recent years given inflation and labor pressures. Although inflation has contributed to stronger sales tax collections in the short term, we believe that prolonged inflation will likely reduce consumer spending in the longer term, and therefore we see risk of sales tax revenue falling. In addition, we believe that labor shortages have contributed to the county's underspending in recent years, and therefore we think that filling these positions will likely drive up costs. We think that retention and attraction of employees could also require increasing salaries and benefits. Despite these pressures, we believe the size of general fund reserves is a credit strength, as it allows the county to absorb a large drop in revenue or cost increases without having to immediately make large expenditure reductions. Over the long term, we anticipate that the county will make the adjustments it deems necessary to maintain structural balance.

The county has received $240 million in American Rescue Plan (ARP) Act funding and has allocated the entirety for revenue replacement. On a modified accrual basis, half of this was recorded as general fund revenue in fiscal 2021, leading to a large increase in the available general fund balance. The county also incurred about $24.5 million in one-time expenditures in 2021. After adjusting for this one-time revenue and these expenditures, we estimate that the general fund would have been closer to break-even. The county used about $21.1 million in ARP funding to cover personnel costs in 2021, but plans to use the majority of the remaining funding on one-time projects. We expect reserves to decrease over the next few years as the county spends the ARP funding, but we expect total available reserves to remain very strong and in compliance with the county's formal policy.

The county went to voters in 2020 to approve an increase in the health and human services (HHS) property tax levy, which has eliminated the need for a general fund subsidy to the HHS funds. The HHS funds, which represent a large component of total governmental funds, were balanced in 2021 and 2022. One of the levies will be up for renewal in 2024.

Total liquidity across all funds is also very strong, with about $1.1 billion in pooled cash and cash equivalents at the end of 2021. Management has confirmed that the county has no contingent liquidity risks from financial instruments with payment provisions that change on certain events, and we do not view the county's investment practices as risky. The majority of its investments are in highly rated U.S. government securities.

Weakening Cuyahoga County's liquidity position, in our assessment, is the county's exposure to contingent liability risk stemming from various litigation and a standby letter of credit (LOC) for debt issued by MetroHealth System, a component unit of the county.

The county is a defendant in various lawsuits, including several wrongful death lawsuits related to the jail and the county's department of children and family services. The litigation is ongoing, and while we are unable to determine the potential financial impact to the county, we do not believe a negative outcome in any of the lawsuits would materially affect overall liquidity or reserve position. We will monitor the outstanding litigation for effects on the financial position.

In 2017, MetroHealth issued $945 million in debt to finance the reconstruction of the system's hospital campus. MetroHealth is the sole obligor on the bonds (and therefore the debt is not included as direct debt of the county), though the county is serving as the counterparty for a standby LOC to fund a debt service reserve. The county can terminate the LOC if the entire notional value of the LOC (approximately $63 million) is drawn. Furthermore, the county can fund the replenishment of the debt service reserve by offsetting its annual operating subsidy to the health care system (which is a discretionary subsidy and usually in the range of $30 million to $40 million). There has been no draw on the LOC, so we do not think of it as a contingent liability that is likely to come due in the next 12 months.

Weak debt and liability profile with the potential for additional debt for new jail on the horizon

The county has about $1.4 billion in direct debt outstanding, which includes the series 2022A bonds. Several years ago, the county refinanced a large portion of its debt, resulting in significant interest cost savings, allowing it to absorb the debt service on the new bonds. Total direct debt equates to 3.6% of the county's market value, which we consider manageable at the rating. Furthermore, we consider amortization rapid, with about 71% of the county's debt scheduled to be retired in 10 years--a positive credit factor.

Existing principal payments are front-loaded, allowing budget capacity for future debt. Although the county has not formalized any debt plans, it is exploring options to build a new jail, which would include issuing debt. The maximum estimated cost of the jail is currently about $750 million, an increase given inflation. The county is also considering renovating or building a new justice center, though this project will likely occur after the jail. We could lower the rating if additional debt causes debt metrics to weaken to levels commensurate with those of lower-rated peers.

Negatively affecting our view of the county's debt profile is its exposure to speculative contingent liabilities. The county has issued substantial sales tax, nontax revenue, and appropriation debt that is supported with alternative revenue sources, and much of which was issued to support various economic development projects, including a county-owned convention center and hotel, renovations at the Rocket Mortgage FieldHouse, various residential and commercial projects, and the renovation of Progressive Field. Much of this debt is intended to be repaid with project or other alternative revenue, though the county is ultimately pledging its support if such revenue is insufficient to cover debt service. In case of shortfalls in intended repayment sources requiring ongoing general fund support and leading to operating pressures, credit impact could result.

Because of pandemic-spurred revenue shortfalls at the convention center hotel, the county had to contribute an additional $7.9 million in 2020 to support debt service and property tax payments for the hotel. However, because of a rebound in hotel activity, the county had to contribute only $4.9 million in 2021, and did not need to make a contribution in 2022.

Manageable pension and other postemployment benefit (OPEB) liabilities

Pension and OPEB costs are manageable for the county, although pension cost escalation is likely given plan assumptions and methods. OPEB costs are not a credit pressure and unlikely to become so in the near term.

Cuyahoga County participated in the following plans as of June 30, 2020:

- Ohio Public Employees' Retirement System, 93.0% funded using a 6.9% discount rate, with a proportionate share plan's net pension liability of $239.8 million
- State Teachers Retirement System of Ohio: 87.8% funded, with a proportionate share of the plan's net pension liability of $2.4 million

We do not view OPEB liabilities under these plans as significant source of credit pressure.

We expect long-term pension/OPEB costs could face volatility as a result of aggressive assumptions and amortization methods designed to defer contributions. Pension reforms in the past, as well as recent OPEB reforms, help mitigate the risk of cost escalation. For more information on our view of these plans, see "Pension Spotlight: Ohio," published Jan. 7, 2021.

Cuyahoga County Key Credit Metrics

	Most recent	Historical information		
		2021	2020	2019
Strong economy				
Projected per capita EBI as % of U.S.	97			
Market value per capita ($)	81,101			

Cuyahoga County Key Credit Metrics (cont.)				
	Most recent	Historical information		
		2021	2020	2019
Population		1,226,182	1,236,826	1,242,100
County unemployment rate (%)		6.5		
Market value ($000s)	99,444,471	87,925,137	87,280,603	
Ten largest taxpayers as % of taxable value	5.6			
Adequate budgetary performance				
Operating fund result as % of expenditures		(0.8)	(3.3)	3.7
Total governmental funds result as % of expenditures		3.8	2.8	(2.4)
Very strong budgetary flexibility				
Available reserves as % of operating expenditures		70.5	52.8	40.8
Total available reserves ($000s)		344,650	252,642	194,567
Very strong liquidity				
Total government cash as % of governmental funds expenditures		82	69	51
Total government cash as % of governmental funds debt service		785	640	452
Strong management				
Financial management assessment	Good			
Weak debt and long-term liabilities				
Debt service as % of governmental funds expenditures		10.5	10.8	11.4
Net direct debt as % of governmental funds revenue	97			
Overall net debt as % of market value	3.6			
Direct debt 10-year amortization (%)	71			
Required pension contribution as % of governmental funds expenditures		4.2		
OPEB actual contribution as % of governmental funds expenditures		0		
Strong institutional framework				

Note: Data points and ratios may reflect analytical adjustments. EBI--Effective buying income. OPEB--Other postemployment benefits.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019
- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of September 22, 2022)

Ratings Detail (As Of September 22, 2022) (cont.)		
Cuyahoga Cnty econ dev rev rfdg bnds (Shaker Sq Proj) ser 2010D dtd 09/03/2010 due 06/01/2011-2020 12/01/2010-2020 2025 2030		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty misc tax		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty taxable economic dev rev rfdg bnds		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty taxable economic dev rev rfdg bnds		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty taxable economic dev rev rfdg bnds		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty taxable econ dev rev bnds (Flats East Dev LLC Proj)		
Long Term Rating	AA-/Stable	Affirmed
Cuyahoga Cnty GO		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty GO (ltd tax) cap imp bnds		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty GO (ltd tax) taxable cap imp rfdg bnds (federally taxable) (Sports Fac Imp Proj) ser 2019B due 12/01/2027		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty APPROP		
Long Term Rating	AA/Stable	Affirmed
Cuyahoga Cnty APPROP		
Long Term Rating	AA/Stable	Affirmed
Cleveland-Cuyahoga Cnty Port Auth, Ohio		
Cuyahoga Cnty, Ohio		
Cleveland-Cuyahoga Cnty Port Auth (Cuyahoga Cnty) lse		
Long Term Rating	AA-/Stable	Affirmed
Cleveland-Cuyahoga Cnty Port Auth (Cuyahoga Cnty) APPROP		
Long Term Rating	AA-/Stable	Affirmed