FitchRatings

RATING ACTION COMMENTARY

Fitch Rates Prince William County VA Public School Auth $43MM Bonds 'AAA'; Outlook Stable

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Fitch Ratings - New York - 06 Oct 2022: Fitch Ratings has assigned a 'AAA' rating to the $43 million Virginia Public School Authority (VPSA) special obligation school financing bonds, Prince William County series 2022, to be issued by the VPSA on behalf of Prince William County, VA (county).

Proceeds of the series 2022 VPSA special obligation bonds will be used to fund various capital school improvement projects for the county. The bonds are expected to sell competitively on Oct. 25.

In addition, Fitch has affirmed the following county ratings:

--Approximately $600.9 million outstanding county VPSA special obligation bonds at 'AAA';

--Approximately $141.3 million outstanding county GO bonds at 'AAA';

--Approximately $13.6 million outstanding county refunding certificates of participation (COPs), series 2013 at 'AA+';

--Approximately $16.3 million outstanding county Industrial Development Authority (IDA) (Courts Facilities Project) facilities revenue and refunding bonds series 2016A at 'AA+';

--Approximately $46.1 million outstanding IDA facilities revenue and refunding bonds, series 2020A, 'AA+'.

--Issuer Default Rating (IDR) at 'AAA'.

The Rating Outlook is Stable.

SECURITY

The VPSA bonds are limited and special obligations of the VPSA, payable solely from payments of principal and interest to be made by the county on its local school bonds. The local school bonds are GOs of the county, for which the county has pledged its full faith and credit for payment and unlimited taxing authority. The VPSA has assigned its rights to receive all payments of principal and interest on the local school bonds to the State Treasurer acting as paying agent for the series 2022 bonds and all such payments of principal and interest on the local school bonds shall be made directly to the State Treasurer.

The outstanding IDA revenue bonds and the county's series 2013 COPs are backed by lease or basic payments equal to debt service and subject to annual appropriation by the county board.

ANALYTICAL CONCLUSION

The 'AAA' rating on the VPSA special obligation bonds reflects the county's 'AAA' IDR and GO rating, which is underpinned by the county's superior gap-closing capacity and budget flexibility, and its unlimited taxing authority. Fitch expects the county to maintain a high level of financial flexibility given its solid operating performance, healthy available fund balance, and moderate liability burden.

The 'AA+' rating on the appropriation-backed debt is one-notch below the IDR reflecting the slightly higher degree of optionality associated with appropriation payments.

Economic Resource Base

The county is located in northern Virginia, less than 25 miles southwest of Washington, D.C. The county's population reached an estimated U.S. census population of 482,204 in 2021, up 20.5% since 2010.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

The county derives the bulk of its revenues from property taxes. General fund revenue growth is expected to exceed inflation over time based on expectations for continued population growth and tax base expansion from new development and property appreciation. The county has strong control over revenues given its independent legal ability to increase property taxes without limitation.

Expenditure Framework: 'aa'

Fitch expects the natural pace of spending growth to be marginally above natural revenue growth. Moderate carrying costs and broad flexibility to manage labor-related costs afford the county solid flexibility to adjust spending.

Long-Term Liability Burden: 'aa'

The combined burden of debt and Fitch-adjusted net pension liabilities represents about 10% of personal income, at the low end of the moderate range. Fitch expects the liability burden to remain in this range as the county continues to issue debt annually to meet school and other county capital needs.

Operating Performance: 'aaa'

The county's superior budget flexibility and ample unrestricted general fund balance (equal to 15% of spending or higher dating back more than a decade) allows it to manage through economic downturns without diminishing its overall financial flexibility.

RATING SENSITIVITIES

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

--Not applicable given the 'AAA' IDR and GO rating.

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

--Slower than anticipated revenue growth sustained at a level below the rate of inflation;

--A rapid acceleration in natural pace of spending without a corresponding increase in revenue growth;

--A sustained and material erosion of the county's gap-closing capacity, resulting in a deterioration of its overall financial resilience.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

CURRENT DEVELOPMENTS

Prince William County ended fiscal 2021 with a net-operating surplus of $34.8 million, about 2.7% of general fund spending, increasing the county's unrestricted general fund balance to $255 million or nearly 20% of expenditures. The county saw positive budget variances primarily in property tax and sales tax revenues, in addition to experiencing expenditure savings.

The fiscal 2022 general fund budget of $1.4 billion was about 5% over the fiscal 2021 budget. Preliminary results show a net-operating surplus primarily due to personal property tax, sales tax, and business, professional and occupational license (BPOL) tax revenues exceeding budget expectations. The county's new cigarette tax became effective January 2022, generating $2.1 million in new revenue.

The county's $1.5 billion adopted fiscal 2023 general fund budget is about 8.7% over the fiscal 2022 budget. The budget reduces the property tax rate to $1.03 per $100 of assessed value from $1.115 and includes a $59 million, or a 9% increase in school transfers out of the general fund, in accordance with the county's revenue sharing agreement (57% schools/43% county). A full year of cigarette tax revenues is budgeted at $3 million, less than 1% of revenues. The county's recently adopted 4% meals tax, went into effect July 2022 and is budgeted to generate $24.5 million in new revenue in fiscal 2023. The cigarette tax and meals tax revenues will be shared with Prince William County Schools, following the aforementioned revenue sharing agreement. The budget includes a use of fund balance of $5.5 million for one-time purposes, less than 1% of spending. Fitch expects the county will continue to exercise strong budget management practices through current and future economic cycles and maintain reserves sufficient to retain its high gap-closing capacity.

The county received about $82.1 million in CARES Act funding and $91.4 million in ARPA funding. These amounts do not include separate allocations made to the schools. As of June 2022, the county has spent all of its CARES Act funds on various coronavirus-related costs, including premium pay for essential workers. Most of its ARPA funding has been allocated with only $8.6 million left to be assigned.

CREDIT PROFILE

The county is situated within the Washington, D.C. metropolitan area. Its relative affordability compared to neighboring counties and well-educated workforce support favorable economic and demographic growth trends. Its stable economic base, rooted in government and military employment, has expanded to encompass the targeted industries of life sciences, information technology and federal government agencies and contractors. The number of data centers in the county continues to increase in and outside of Innovation Park.

The presence of the Marine Corp Base Quantico, along with the addition of the FBI Northern VA satellite office, help to attract contractors and federal agencies, but also exposes the county to changes in federal defense spending, which has been subject to volatility. The U.S. Department of Defense is the county's third-largest employer; overall, the federal government currently represents just 5% of the resident employment base.

Revenue Framework

The county primarily relies on property tax revenues, totaling 71% of general fund revenues in fiscal 2021. The next largest category was intergovernmental revenues at 13% from state and federal sources primarily for schools and other social services.

The county's 10-year general fund revenue CAGR, adjusted for real property tax rate changes, registered 4.8% in fiscal 2021. Fitch expects general fund revenue growth to moderate somewhat but trend above inflation over time given ongoing economic development as shown in solid growth in construction permits, continued home value appreciation, and a solid pipeline for new data centers. The county's taxable assessed value

(TAV) increased by 9% to about $83 billion in fiscal 2022, primarily due to the county's property reassessment, following 8% growth in fiscal 2021.

The Commonwealth of Virginia does not limit the property tax rate or levy, affording the county significant independent revenue-raising authority to help counteract cyclical budgetary stresses. The county's fiscal 2023 tax rate was reduced to $1.03 per $100 of AV from $1.115.

Expenditure Framework

The county's largest expenditure category is education, at 43% of fiscal 2021 general fund expenditures, followed by public safety at 23%. Virginia public schools are largely funded by a mix of state and local aid contributions. The amount of local contribution is determined by the county's board, and based on the state-determined performance standards for the school system, known as the required local effort (RLE). A revenue sharing agreement between the county and the component unit school district diverts 57% of general fund revenue to fund the district's budget. Importantly, the county board has the ability to adjust the agreement, if needed, supporting a solid level of overall expenditure flexibility.

Fitch expects the natural pace of spending growth to be marginally above natural revenue growth, given the county's full control over employee wages and benefits, as well as its manageable debt service and retiree benefit costs.

The county's fixed carrying cost burden is moderate, with costs for debt, pensions, and other post-employment benefits (OPEB) equaling 12% of fiscal 2021 total governmental expenditures. Debt service accounts for the majority of costs at about 8.6% and reflects an amortization rate of debt at approximately 70% of debt retired in 10 years, including this issuance. Expenditure flexibility also benefits from the state's workforce environment that provides broad legal ability to manage labor-related costs.

Long-Term Liability Burden

The county's long-term liability burden, including this issuance and the county's and component unit schools' Fitch-adjusted net pension liability, is 10.5% of residents' personal income. The county's five-year capital improvement plan from fiscal 2023-2028 of $1.2 billion (excluding school capital plans) is approximately 28.7% debt funded. Fitch expects the liability burden to remain moderate over the long term even with the issuance of this debt.

The county participates in the state-administered VRS for regular full-time employees as does the component unit school district for teachers and non-professional employees. The county also maintains a small supplemental defined benefit retirement plan for police officers, uniformed fire and rescue personnel, uniformed adult detention center staff and sheriff employees and a volunteer fire and rescue personnel length of service award program (LOSAP). On a combined basis, the net pension liability totals about 5% of personal income, largely due to the net pension liability for the teachers' plan. The combined ratio of net assets to liabilities is currently about 69% using Fitch's standard 6% investment return assumption.

The county contributes to five OPEB plans and has an unfunded OPEB liability of less than 1% of personal income. The county established an OPEB trust fund for the county and schools with assets totaling $124.3 million at the end of fiscal 2021. The county consistently funds pensions and OPEB at the aggregate actuarially determined contribution (ADC) level.

Operating Performance

The county has a superior level of inherent budget flexibility, supported by an unlimited independent revenue raising capacity and solid spending flexibility to manage through economic cycles. The county maintains a capital reserve (minimum 2% of capital projects), a revenue stabilization reserve (2% of general fund revenues), and $3 million in its economic development opportunity fund reserve as part of the committed fund balance. Additional reserves are held outside of the general fund that can be utilized with board approval, providing additional flexibility. Fitch expects the county to continue to maintain a high level of financial flexibility through the current uncertainty, with reserves remaining above the county's minimum unassigned general fund balance policy of 7.5% of general fund revenues.

The county has demonstrated its ability to reduce spending through cost control mechanisms in prior recessions by deferring most non-school capex, reducing the overall operating budget, implementing a temporary freeze on compensation increases and making a limited number of reductions-in-force, among other measures. Fitch expects the county to make similar operational changes as needed during future economic downturns and continue to update its long-term comprehensive plans and detailed forecasting reports to maintain its strong financial resilience.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means 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 Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Prince William County (VA) [General Government]	LT IDR	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
Prince William County (VA) /Appropriation Supported/1 LT	LT	AA+ Rating Outlook Stable	Affirmed	AA+ Rating Outlook Stable
Prince William County (VA) /General Obligation - Unlimited Tax/1 LT	LT	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
Prince William County (VA) /Lease Obligations - Standard/1 LT	LT	AA+ Rating Outlook Stable	Affirmed	AA+ Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

U.S. Public Finance Tax-Supported Rating Criteria (pub. 04 May 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Prince William County Industrial Development Authority	EU Endorsed, UK Endorsed

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