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Ratings

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Summary:

Leesburg, Virginia; General Obligation

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Credit Profile		
US$13.5 mil GO rfdg bnds due 11/17/2039		
Long Term Rating	AAA/Stable	New
Leesburg		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to Leesburg, Va.'s general obligation (GO) refunding bonds series 2020. At the same time, we affirmed our 'AAA' long-term rating on the town's GO debt outstanding. The outlook is stable.

Securing debt service on the bonds is the town's full faith and credit, including the levy and collection of ad valorem taxes that are unlimited as to rate or amount. Proceeds from the sale will refund the callable maturities of the series 2011 GO bonds for debt service savings, as well as restructure the series 2011, 2014, 2015, and 2019 GO bonds for cash-flow flexibility. Proceeds from the restructuring portion of this issue will finance the fiscal year 2021 non-callable payments on series 2011, 2014, 2015, and 2019 GO bonds, providing cash-flow flexibility for the town to cover possible fiscal year 2021 revenue shortfalls and fund the creation of a revenue stabilization reserve (RSR).

Credit overview

The rating reflects our view of the town's wealthy residential tax base favorably located within the vibrant Washington, D.C., metropolitan statistical area (MSA) that offers employment opportunities, creating housing demand and population growth. Economic growth continues to support revenue trends and budgetary balance despite increased service and expenditure requirements. Leesburg's very strong management, guided by robust policies and planning frameworks, has also supported the town's consistently strong operations.

As with most local governments, we believe challenges associated with the pandemic and a national recession could pressure Leesburg's budgets in the next one-to-two years. In line with our view of the ongoing economic contraction, we expect revenues to lag their historical performance. (For more information, see "The U.S. Economy Reboots, With Obstacles Ahead," published Sept. 24, 2020, on RatingsDirect.) Management conveyed that the town likely produced a moderate net positive result in fiscal 2020 (ended June 30) despite the challenging operating environment. The town's proactive management team is also maneuvering to create additional budgetary flexibility for the next four years in case the economic downturn becomes more severe or prolonged than we currently anticipate. Therefore, we do not expect to change the rating in the near term. Our outlook is generally for two years, but we see some risks due to the COVID-19 pandemic and U.S. recession over the next six-to-12 months.

The rating further reflects our view of the town's:

- Very strong economy, with access to a broad and diverse MSA;
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with an operating surplus in the general fund but a slight operating deficit at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 42% of operating expenditures;
- Very strong liquidity, with total government available cash at 90.8% of total governmental fund expenditures and 7.9x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 11.5% of expenditures and net direct debt that is 69.5% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 71.1% of debt scheduled to be retired in 10 years; and
- Very strong institutional framework score.

Leesburg's GO bonds are eligible to be rated above the sovereign because we believe the town 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," Nov. 19, 2013), the town predominantly derives its revenue from local sources, receiving 81% from local property, meals, and sales taxes, and it has independent taxing authority as well as independent treasury management from the federal government.

Environmental, social, and governance factors

Our rating incorporates our view regarding the health and safety risks posed by the COVID-19 pandemic and social distancing, which could affect local economic activity and finances. Absent the implications of COVID-19, we consider the town's social risks in line with those of the sector. We view its environmental and governance risks as being generally in line with those of peers.

Stable Outlook

Downside scenario

Our outlook incorporates the likelihood that a national recession and difficult funding environment could challenge Leesburg's budgets, but given current reserve levels, we believe the town's financial position will remain in line with those of similarly rated peers. However, if fund balance falls below levels we consider commensurate with the current rating, we could lower the rating.

Credit Opinion

Very strong economy

We consider Leesburg's economy very strong. The town, with a population of 53,727, is in Loudoun County in the Washington-Arlington-Alexandria MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 148% of the national level and per capita market value of $166,983. Overall, market value grew by 5.5% over the past year to $8.4 billion in 2020.

Leesburg is a wealthy bedroom community that serves the greater Washington, D.C., region's deep and diverse employment base. The town has also benefited over the past several years from growing employment opportunities within its borders, including in government contracting, medical technology, and small business entrepreneurship supported by the Mason Enterprise Center. Management reports that demand for single-family residences in Leesburg is increasingly competitive and new homes are often purchased prior to completion. Residential development remains robust in 2020, with approximately 572 single-family homes and 1,988 multifamily units in the pipeline. Similarly, commercial development has continued, with over 2.1 million square feet of commercial space in development. Additionally, Microsoft intends to construct five data centers and other administrative property in a joint land management area between Leesburg and Loudoun County, and the town will provide utility services for the development. While the project will not affect Leesburg's assessed values (AVs), we understand that a revenue-sharing agreement among Microsoft, the town, and the county will result in annual payments to the town that may start in fiscal 2023 and exceed $7 million annually by 2028.

The Loudoun County unemployment rate was 2.3% in 2019, and we note that Leesburg's local unemployment rate tends to fall below the county's. However, rapidly evolving economic conditions as a result of COVID-19 have affected the labor market. During the Great Recession, county unemployment peaked at 7.1%. It fell to 5.1% in September 2020 from its April 2020 high of 9.9%. Management reports that the town had been working closely with its business sectors to provide assistance where needed during the COVID-19 pandemic, and major employers have not been significantly disrupted by COVID-19. We will monitor the longer-term effects of the current downturn on the labor market and the economy overall.

Very strong management

We view the town's management as very strong, with strong financial policies and practices under our FMA methodology, indicating our view that financial practices are strong, well embedded, and likely sustainable. Highlights include:

- When formulating the budget, the town reviews five years of historical information while adhering to its five-year financial plan to update revenue and expenditures by 2% annually.
- The financial plan as well as the six-year capital improvement plan (CIP) are reviewed annually by the town council and updated to ensure that assumptions for growth are meaningful based on historical and year-to-date actual trends.
- The operating budget and CIP are intertwined to ensure that costs associated with the completion of capital projects are reflected in the revenue and expenditure forecast.
- Furthermore, management provides the council with monthly budget-to-actual reports that show trends as well as investment outcomes.
- The debt management policy identifies key affordability thresholds relative to debt service expenditures no greater than 15% of total expenditures and total debt outstanding equal to 2.5% of the town's AV. These metrics are monitored annually and reported to the council.
- An updated formal reserve policy was adopted in January 2015 and requires maintenance of the unassigned fund balance equal to 20% of general fund expenditures, a level with which the town has historically complied.

Adequate budgetary performance

Leesburg's budgetary performance is adequate, in our opinion. The town had surplus operating results in the general fund of 2.6% of expenditures, but a slight deficit result across all governmental funds of negative 1.0% in fiscal 2019, reflecting higher-than-normal capital spending. General fund operating results of the town have been stable over the last three years, with results of 2.9% in 2018 and 4.4% in 2017. Our assessment incorporates adjustments to reflect our view of operating revenues and expenses, as well our expectation for greater revenue volatility in the next one-to-two fiscal years as a result of COVID-19, the national recession, and the projected slow recovery.

The town's budget is funded primarily by three sources: property taxes (29%), other local taxes mostly consisting of meals taxes (26%), and intergovernmental revenue mostly consisting of sales taxes (26%).

Over the past five fiscal years, the town has produced consistent annual operating surpluses. Management reports that annual revenue growth commensurate with the town's economic expansion and diversification as well as careful monitoring of expenditures supported operating results. The fiscal 2019 audit included a one-time transfer from the general fund to the capital projects fund that was substantially higher than the town typically funds, which we have adjusted in our operating performance calculations. This $6.7 million transfer prefunded several pay-as-you-go capital expenditures and reflected fund balance growth over the previous three years that brought reserves significantly above the town's policy levels.

The fiscal 2020 budget was balanced and totaled approximately $60.1 million, or 2% higher than the adopted fiscal 2019 budget. Despite the generally difficult national funding environment, Leesburg projects it added approximately $180,000 to fund balance during the fiscal year while still pay-as-you-go financing nearly $2.0 million of capital projects. In April 2020, the town implemented a response to COVID-19 to address a projected $3.4 million in fiscal 2020 revenue shortfalls. The measures included hiring freezes, nonessential travel and training freezes, maintenance deferrals, capital asset replacement freezes, and canceling or closing some events or facilities. Stronger-than-anticipated sales tax and business, professional, and occupational license tax collections helped the town achieve an expected positive result for the year.

The fiscal year 2021 budget totals $62.5 million and was balanced without a real estate tax increase. The town adopted this budget at the beginning of the pandemic, and it currently projects revenue may fall approximately $5.5 million short of budgeted figures. However, the town has continued fiscal 2020 cost reductions and implemented new ones that management projects will offset the lower revenues. Given its history of conservative budgeting practices and midyear adjustments, we generally expect it will exhibit strong operating performance over the long term, although we believe revenue pressures and volatility will likely continue through fiscal 2021.

Very strong budgetary flexibility

Leesburg's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 42% of operating expenditures, or $25.4 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

The town amended its fund balance policy in January 2015 to maintain 20% of operating expenditures in the unassigned fund balance rather than 15%. Furthermore, the policy indicates that any amount over 20% could be used for one-time expenditures. The town has maintained the higher threshold, with projections for fiscal year-end 2020 showing the unassigned portion of the fund balance equal to approximately $14.5 million, or over 25% of expenditures, according to the town's calculations. In addition to the $25.4 million of assigned and unassigned fund balance at fiscal year-end 2019 that we include in our available fund balance calculations, Leesburg also held $14.3 million in committed capital projects fund balance.

The town also plans to establish a $1.4 million RSR in fiscal 2021 that it can draw on if economic and revenue conditions do not improve after this fiscal year. It intends to fund this reserve through a combination of general fund balance above its policy limit and proceeds from the current bond refunding and restructuring.

Very strong liquidity

In our opinion, Leesburg's liquidity is very strong, with total government available cash at 90.8% of total governmental fund expenditures and 7.9x governmental debt service in 2019. In our view, the town has strong access to external liquidity if necessary.

With its regular issuance of debt over the past 20 years, we believe that the town's access to external liquidity is strong and that its cash position is very strong. The town's investment portfolio consists of cash investments in the state's local government investment pools, which we do not consider aggressive and which are highly liquid to ensure that amounts are drawn when necessary to meet payment obligations.

In conjunction with a 2019 transaction, the town entered into two lines of credit with Atlantic Union Bank to provide interim financing for general capital projects ($25.5 million) and utilities fund capital projects ($32.5 million). Both agreements mature in 2024 and, on review of the events of default, do not contain payment provisions that change on certain events. The town will draw amounts from the lines of credit and will eventually refinance any amounts drawn with long-term debt. The agreements provide flexibility to finance the required funding for the projects only once construction occurs.

Strong debt and contingent liability profile

In our view, Leesburg's debt and contingent liability profile is strong. Total governmental fund debt service is 11.5% of total governmental fund expenditures, and net direct debt is 69.5% of total governmental fund revenue. Overall net debt is low at 2.5% of market value, and approximately 71.1% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

Following this transaction, the town will have about $55 million of total direct debt outstanding, including amounts retired in fiscal 2021 and excluding GO debt supported by the water and sewer fund. Its six-year CIP identifies about $232 million in future needs, only $37 million of which is expected to be financed with GO bond proceeds. The remainder of the funding will likely be derived from state and federal grants, pay-as-you-go funding, utilities (bonds and pay-as-you-go), and other governmental unit contributions (Loudoun County and the Northern Virginia Transportation Authority). Our overall net debt calculation includes the portion of overlapping Loudoun County debt attributable to Leesburg taxpayers. Given the town's expected plan of finance for these capital needs and fairly rapid amortization of principal, we believe its debt profile will remain manageable.

Pension and other postemployment benefits

- We do not view pension and other postemployment benefit (OPEB) liabilities as an immediate credit pressure because required contributions currently make up a relatively small portion of total governmental expenditures. If required contributions were to materially increase in the next few fiscal years, we believe the town's fiscal stability would not be greatly affected because of its sizable reserves.
- Pension contributions slightly exceeded our static funding metrics, which over time could improve funding levels.
- Leesburg's OPEB pre-funding mitigates risk from cost and medical claims volatility, and we expect the strong management team will make budgetary adjustments to absorb higher costs associated with contributions, if required.

As of June 30, 2019, the latest measurement, Leesburg participated in:

- The Virginia Retirement System (VRS): 89.3% funded, with a proportionate net pension liability of $11.0 million, with a current discount rate of 7.0%
- A single-employer, defined-benefit OPEB plan that provides medical coverage for retired town employees, which is 59.0% funded. The OPEB unfunded actuarial accrued liability totaled $8.9 million as of June 30, 2019

Leesburg's combined required pension and actual OPEB contributions totaled 4.7% of total governmental fund expenditures in 2019. Of that amount, 3.4% represented required contributions to pension obligations, and 1.3% represented OPEB payments. The town made its full annual required pension contribution in 2019.

Very strong institutional framework

The institutional framework score for Virginia towns is very strong.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- 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 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020