MEMORANDUM

To: Mayor Gregory P. Kurtz
Members of Council

From: Finance Director Vernon Blaze

Date: May 22, 2020

Re: Finance Department Updates

<u>Debt</u>

Not including the $3.5 million in outstanding Ohio Public Works Commission (OPWC) loans, the City's current outstanding debt to others is broken down as follows:

Long-Term Bonds	$10.9 Million (38.5%)
Short-Term Notes (BANS)	17.4 Million (61.5%)
Total Bonds/Notes	$28.3 Million (100.0%)

Some of the $10.9 million in long-term bonds were issued in 2018, and therefore are not eligible to be refunded ("Refinanced" in lay-person's language) yet. The other portion of those $10.9 million in long-term bonds was issued in 2011. Those bonds too also aren't "callable" (when they are eligible to be refinanced/refunded) for ten years, meaning they are not eligible to be refunded/refinanced until 2021.

Therefore, the only debt that we have to make a decision on this year is the $17.375 million in short-term notes. Those have been and are one-year Bond Anticipation Notes (BANS). They are issued each year in early December and mature and are therefore due in early December of the following year.

The City has two primary options and one secondary one with those $17.375 million of BANS:

1. Primary: Continue to do what has been done in the past, and renew them for only one year.
2. Primary: Convert them from a short-term, one year maturity to a longer-term one.
3. Employ a hybrid model: Keep some in short-term BANS and convert some to long-term Bonds.

There are various advantages and disadvantages to these options.

<u>Advantages of renewing the one-year BANS for only another year</u>

- Short-term interest rates are currently lower than long-term rates
- The city sometimes has the option to pay interest only and to defer principal payments

<u>Disadvantages of renewing the one-year BANS for only another year</u>

- Short-term interest rates are quite low now, but they could increase and end up being higher in the future than the current long-term rates are
  - If that were to happen, the question asked of us then would be *"Why didn't you lock in those historically low long-term rates back in 2020?"*
- It's a small chance of happening, but when the time comes after early September to sell a new Note offering, if no buyers for the City's BANS show up to bid on the sale date (in a competitive sale), the City would somehow have to come up with a $17,375,000 check by early December

Debt, Continued

Advantages of converting the short-term BANS into longer-term Bonds

- Lock in the current historically low long-term interest rates
- Dispense with having to issue new debt each year to pay off the expiring debt, saving time and yearly financing transaction costs – Bond Counsel, Underwriters, Financial Advisors, filing fees, etc.
- Fix the City's Debt Service Costs (Principal and Interest) for as long as the Bonds are outstanding

Disadvantage of converting the short-term BANS into longer-term Bonds

- If short-term interest rates remain low for years to come, the City would end up paying more in interest by converting the short-term BANS into longer-term Bonds

Some tax and other laws have changed over the last few years. We won't get into a dissertation about those here except to say that the end-result for us here in Independence as far as these BANS are concerned is that new debt instruments (either new BANS, long-term Bonds or some hybrid combination) can be sold no earlier than 90 days prior to the maturity of existing ones.

The City's BANS mature in early December, meaning that the City can sell new replacement BANS or float a new Bond issue in early September at the earliest.

In order to complete either primary option or implement the hybrid option, we will need legislation adopted by August at the latest, even July if possible. That means we need appropriate legislation on the Agenda for either the June or the July Council Meeting.

What would "appropriate legislation" look like? Good question!

The debt market is subject to some wild swings sometimes. Last summer around late August, long-term interest rates decreased enough that they were actually lower than short-term ones. This phenomenon is called an Inverted Yield Curve. Since short-term rates are *usually* (but now always) lower than long-term ones, when that equation flips 180 degrees, the market says that interest rates have "inverted."

So that moment in time last summer would have been an ideal time for the City to convert its short-term BANS into longer-term Bonds, thereby locking in those long-term interest rates that were actually lower than short-term ones at that time.

But moments like that are fleeting and they can come and go in an instant. By later this past winter, the debt market had over-reacted once again (this time to the COVID-19 virus), especially the municipal debt market, causing borrowing rates/costs to spike up to levels not seen in years.

Fortunately the municipal debt market has already started to achieve some sense of "normalcy" again. But with the economy being what it is now, nothing can be taken for granted. The debt market conditions that exist here today going into Memorial Day Weekend can look quite differently come summer and most importantly, starting in September when the City will be eligible to sell replacement BANS or long-term Bonds.

We've been discussing this issue and decision with the legal and financial people. One option being discussed and looked into is presenting Council with both/all three options in legislative format this summer, and then making a "game-time" decision in early September as to what option to exercise (Sell replacement BANS, issue long-term Bonds, or some hybrid) based on the market conditions that exist at the time.