MOODY'S
INVESTORS SERVICE

CREDIT OPINION
13 October 2020

Rate this Research

Contacts

Coley J Anderson +1.312.706.9961
AVP-Analyst
coley.anderson@moodys.com

Eric Harper +1.312.706.9972
VP-Senior Analyst
eric.harper@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Independence (City of) OH

Update to credit analysis

Summary

The City of Independence (Aa1) is located just south of the City of Cleveland (A1 stable) in Cuyahoga County (Aa2 stable). The city maintains a sizable commercial presence that translates into a material increase in daytime population as commuters come into the city for work. The city's diverse labor market and access to employment centers throughout the metro area support resident incomes that far exceed the national median. The city reports ongoing development activity remains strong including new permit activity for residential, residential additions and commercial additions. The city is also working with a developer on a sizable 33 acre mixed use development that it expects to generate additional investment in the area over the next several years.

The city's financial profile will remain sound because of balanced operations, a resilient income tax base and substantial revenue raising flexibility. Over each of the last five audited fiscal years, the city has closed with materially sized general fund operating surpluses ranging from $400,000 to $5 million while also making large transfers out for capital improvements. The city's available reserves across its major operating funds, which consist of the general, quadrant tax increment financing and debt service funds is net of a $18.6 million receivable associated with an interfund loan that was made by the general fund to finance TIF infrastructure projects. While the loan is not likely to be repaid within the foreseeable future, the city still maintains healthy liquidity. Unaudited results for fiscal 2019 indicate a $4 million draw on reserves to defease $4 million in debt.

Income taxes are the city's primary revenue stream, accounting for a substantial 79% of fiscal 2018 operating revenue. The city has levied a 2.0% municipal income tax since 1987 and offers a full credit to residents who work and pay income tax in other municipalities. In prior years, the strong local labor market supported long-term growth in income tax receipts. Growth trends have accelerated in recent years, with a five year CAGR of 6%. Year to date income tax receipts for fiscal 2020 reflect a $500,000 improvement from fiscal 2019 and management expects to close the year with an operating surplus of at least $4 million. A relatively small portion of the city's operating revenue has been negatively impacted by the current pandemic including hotel/motel revenue which represent about 1% of total operating revenue.

The city's debt burden will moderate given a lack of additional borrowing plans while the city's pension burden will likely remain above average. City employees are members of the Ohio Public Employees Retirement System (OPERS) and the Ohio Police & Fire Pension Fund (OP&F). Ohio statute establishes a 30-year target for amortizing unfunded liabilities of all statewide cost-sharing plans. If plan actuaries determine current contribution rates and

actuarial assumptions result in an amortization period exceeding 30 years, the pension fund must submit a plan for adjusting contributions or benefits to meet the 30-year requirement.

The coronavirus outbreak is a social risk under our ESG framework, given the substantial implications for public health and safety. The pandemic is driving an unprecedented economic slowdown. We do not see any material immediate credit risks for the city given its strong liquidity and revenue raising flexibility. The situation surrounding coronavirus is rapidly evolving and the longer term impact will depend on both the severity and duration of the crisis. If our view of the credit quality of the district changes, we will update the rating and/or outlook at that time.

Credit strengths

» Solid cash position with substantial revenue raising flexibility

» Strong resident income indexes and benefit from proximity to the Cleveland MSA

» Significant increase in daytime population lends support to a stable income tax base

Credit challenges

» Substantial general fund support of tax increment financing developments

» Leverage is higher than similarly rated local governments.

Rating outlook

Outlooks are typically not assigned to local governments with this amount of debt.

Factors that could lead to an upgrade

» Material tax base expansion and further strengthening of resident income indices

» Bolstering of operating reserves and available liquidity

» Moderation of debt and pension leverage

Factors that could lead to a downgrade

» Weakening of available liquidity or available reserves

» Growth in long term leverage

» Tax base erosion or weakening of resident income indices.

Key indicators

Exhibit 1

Independence (City of) OH	2014	2015	2016	2017	2018
Economy/Tax Base					
Total Full Value ($000)	$1,303,926	$1,308,614	$1,296,719	$1,282,265	$1,312,986
Population	7,136	7,144	7,115	7,132	7,156
Full Value Per Capita	$182,725	$183,177	$182,251	$179,790	$183,480
Median Family Income (% of US Median)	137.9%	144.4%	155.6%	156.3%	165.7%
Finances					
Operating Revenue ($000)	$31,230	$34,566	$36,365	$37,940	$42,532
Fund Balance ($000)	$8,746	$8,110	$10,251	$3,651	$8,320
Cash Balance ($000)	$9,035	$10,410	$17,717	$14,989	$20,168
Fund Balance as a % of Revenues	28.0%	23.5%	28.2%	9.6%	19.6%
Cash Balance as a % of Revenues	28.9%	30.1%	48.7%	39.5%	47.4%
Debt/Pensions					
Net Direct Debt ($000)	$23,890	$21,940	$28,620	$26,600	$28,275
3-Year Average of Moody's ANPL ($000)	$58,995	$65,154	$66,648	$73,550	$78,355
Net Direct Debt / Full Value (%)	1.8%	1.7%	2.2%	2.1%	2.2%
Net Direct Debt / Operating Revenues (x)	0.8x	0.6x	0.8x	0.7x	0.7x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	4.5%	5.0%	5.1%	5.7%	6.0%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.9x	1.9x	1.8x	1.9x	1.8x

Source: Audited financial statements, US Census, Moody's Investors Service

Profile

The City of Independence is located approximately 12 miles south of downtown Cleveland. While the city is home to around 7,100 residents, its daytime population swells to nearly 21,000 because of a sizable commercial office presence that brings in commuters from throughout the Cleveland metropolitan area.

Detailed credit considerations

Legal security

The city's GOLT bonds are secured by the pledge and authorization to levy a property tax within the State of Ohio's (Aa1 stable) statutory 10 mill limitation. The bonds also carry a full faith and credit pledge.

ESG considerations

Environmental

According to data from Moody's affiliate, Four Twenty Seven, Cuyahoga County has relatively high exposure to extreme rainfall. This risk is somewhat mitigated by the city's healthy liquidity and proactive capital planning. The county is currently working with underlying communities to identify potential issues and mitigate future damage.

Social

Social considerations that factor into the city's credit into the city's credit profile include its demographic and socioeconomic characteristics. The city is a wealthy community closely tied to the broader Cleveland metro area. The population has remained stable over the last two decades and median family income is estimated at 167% of the national median. At 11.6% as of August 2020, the county's unemployment rate was higher than state and national levels of 8.8% and 8.5%. The current rates are elevated given the surge in unemployment claims related to coronavirus.

Governance

Ohio cities have an Institutional Framework score of "A," which is moderate. The sector's major revenue source, income tax, is subject to a 1.0% cap that can be overridden with voter approval only. Increases in property taxes also generally require voter approval. Revenue and expenditures tend to be predictable. The City of Independence Charter allows City Council to increase the income tax rate to a level equivalent to that of the City of Cleveland's without voter approval. In 2017, Cleveland's income tax rate was raised to 2.5% from 2.0%. While city management does not intend to increase its income tax rate (which is currently at 2.0%) at this time, the added flexibility enhances the city's revenue raising ability should future income tax collections weaken. Moving the rate to 2.5% would generate an additional $10 million in annual operating revenue.

Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 2

Independence (City of) OH

Scorecard Factors and Subfactors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$1,383,899	A
Full Value Per Capita	$193,390	Aaa
Median Family Income (% of US Median)	165.7%	Aaa
Notching Factors:[2]		
Regional Economic Center		Up
Finances (30%)		
Fund Balance as a % of Revenues	19.6%	Aa
5-Year Dollar Change in Fund Balance as % of Revenues	-7.7%	Baa
Cash Balance as a % of Revenues	47.4%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	20.0%	Aa
Notching Factors:[2]		
Other Scorecard Adjustment Related to Finances: punative operating history from capital transfers, material revenue raising flexibility		Up
Management (20%)		
Institutional Framework	A	A
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	0.9x	B & Below
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	2.1%	A
Net Direct Debt / Operating Revenues (x)	0.7x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	5.7%	Baa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.8x	A
	Scorecard-Indicated Outcome	Aa2
	Assigned Rating	Aa1

[1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.
Sources: US Census Bureau, Moody's Investors Service

Source: Audited financial statements; US Census; Moody's Investors Service

REPORT NUMBER 1248913

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Moody's
INVESTORS SERVICE

Council Meeting Report
Vernon Blaze – Finance Director
Tuesday, October 13, 2020

The City currently has $17.375 million in one-year notes that mature in December. The City's options are to either re-issue one-year notes, or bond these notes out by issuing a longer-term instrument (a bond), where the interest rate would be fixed for a longer period of time than just one year.

After much discussion and consultation, the majority of Council and the Administration decided to pursue the long-term bond option since tax-free municipal borrowing rates reached all-time, historic lows back in early August. The conclusion reached was that if there ever was a time to lock in low interest rates, when they are at/near all-time historic lows would be that time.

The City intends to use cash to pay off $2.125 million of the current $17.375 one-year notes when they mature, resulting in a bond issue of $15.25 million.

To prepare to issue those bonds as soon as late October, the City had to obtain a rating from one of the national credit rating agencies. Having had a past relationship with Moody's, it was decided to have Moody's once again rate the City and its debt.

A lot of demographic, economic and financial data was prepared and resulted in the compilation of a comprehensive Preliminary Official Statement (POS). The POS and Moody's credit rating will both be used by investment managers when submitting bids (interest rates) on the upcoming bond issue.

Moody's has 21 different credit rating categories – ten of them in the Investment Grade category and 11 in the Speculative Grade category. I am happy to report that of those 21 credit rating categories, Independence was awarded the second highest rating possible – Aa1 – and obviously in the Investment Grade category. Moody's summary description of an Aa1 rating is "High quality, very low credit risk."

A credit rating that high does not happen by accident. It takes consistent, concerted and collaborative efforts by the Mayor and administrative team, members of Council and the Finance Team to comprehensively ensure that the City's financial management results in ratings such as the one received. My heartfelt "thanks" goes out to everyone involved in this process this year and those involved for a lot longer than just this year – your dedication and service to the City does not go unnoticed.

I have been asked what it would take for Independence to obtain the highest credit rating possible. The bar for that rating is quite high. In addition to the above-noted $15+ million bond, the City also has over $10 million in other outstanding long-term bonds, and also owes itself over $20 million now (due to cash being advanced from the General Fund to various TIF Funds that should ultimately be paid back to the General Fund).

That totals over $45 million of liabilities that are formally recognized by the auditors on the City's Balance Sheet (A financial statement lists what is owned and subtracts off from that what is owed). That total liabilities level of over $45 million would have to be significantly reduced for Independence to be able to achieve the highest credit rating possible.