

CREDIT OPINION

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Washoe (County of) NV

Update to credit analysis

Summary

[Washoe County, Nevada's](#) (Aa2 stable) strong management team and a robust balance sheet will help to offset the significant economic and financial challenges the county is facing because of the coronavirus pandemic. The state's closure of nonessential businesses, including resorts and casinos, and a halt to tourism have yielded steep revenue declines in March, April and May, and it will likely be a couple of years before the tourism and gaming economies recover fully. However, the county has excellent proactive budgeting and expense controls, as well as strong reserves and liquidity that allow it some cushion to respond to the financial shocks. The county also benefits from a very large tax base, that while still concentrated in tourism and gaming, has been diversifying over the past few years.

The combined credit effects of the coronavirus and its economic impact are unprecedented. Washoe County's tourism-based economy will be hit harder and take a longer time to recover than most economies around the country. The economic decline will negatively pressure the county's finances however we believe the county is currently well positioned to weather the stress. We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety.

Credit strengths

- » Healthy available reserves and liquidity supported by conservative management
- » Large service area and tax base that is the regional economic hub of northern Nevada

Credit challenges

- » Economy remains reliant on gaming and tourism, which have been especially hard hit by the pandemic
- » Cyclical excise taxes cause budget pressure in weak economic periods
- » Somewhat suppressed growth for property taxes, although improving, under limitations of the state's Abatement Act

Rating outlook

The stable outlook reflects our expectation that although a large use of reserves is likely in the near-term, the county's strong fiscal oversight and proactive budgeting will ensure maintenance of still solid reserve levels as the county slowly recovers economically.

Factors that could lead to an upgrade

- » Continued and sustained diversification of the county's economy
- » Stability in the local economy and increases in its tax base
- » Sustained improvement in the county's financial profile including cash and fund balance

Factors that could lead to a downgrade

- » Material weakening of the county's financial profile
- » Significant longer-term economic contraction
- » Material reduction in the county's assessed value

Key indicators

Exhibit 1

Washoe (County of) NV	2015	2016	2017	2018	2019
Economy/Tax Base					
Total Full Value (\$000)	\$37,960,810	\$41,615,621	\$44,882,850	\$47,068,286	\$49,437,372
Population	441,946	448,316	415,923	460,237	469,801
Full Value Per Capita	\$85,895	\$92,827	\$107,911	\$102,270	\$105,230
Median Family Income (% of US Median)	99.5%	100.6%	102.4%	101.5%	101.5%
Finances					
Operating Revenue (\$000)	\$423,248	\$442,581	\$453,879	\$488,454	\$507,881
Fund Balance (\$000)	\$135,439	\$131,659	\$135,261	\$148,574	\$167,107
Cash Balance (\$000)	\$147,933	\$144,818	\$148,380	\$162,375	\$184,727
Fund Balance as a % of Revenues	32.0%	29.7%	29.8%	30.4%	32.9%
Cash Balance as a % of Revenues	35.0%	32.7%	32.7%	33.2%	36.4%
Debt/Pensions					
Net Direct Debt (\$000)	\$226,270	\$153,136	\$143,544	\$135,690	\$127,691
3-Year Average of Moody's ANPL (\$000)	\$1,130,456	\$1,128,300	\$1,200,129	\$1,282,645	\$1,336,421
Net Direct Debt / Full Value (%)	0.6%	0.4%	0.3%	0.3%	0.3%
Net Direct Debt / Operating Revenues (x)	0.5x	0.3x	0.3x	0.3x	0.3x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	3.0%	2.7%	2.7%	2.7%	2.7%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	2.7x	2.5x	2.6x	2.6x	2.6x

Source: Washoe County Nevada and Moody's Investors Service

Profile

Washoe County is located in northwestern [Nevada](#) (Aa1 negative) and includes the city of [Reno](#) (A1 stable). The county is the second largest economic center of the state with just over 469,800 residents.

Detailed credit considerations

Tax base and local economy: large tax base with some tourism concentration; strong recent trend of diversification

The coronavirus pandemic and the subsequent closure of nonessential businesses will have a considerable impact on the city's local economy in the near-term though long-term prospects remain positive. The county's large tax base, while still somewhat dependent on gaming and tourism, will continue to grow and diversify over the long term given recent investment from new businesses and the

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county's place as the regional economic hub for northern Nevada. The county is home to nearly 470,000 residents or 15% of the state's population as well as a major university, the [University of Nevada Reno](#) (Aa2). Recent investment from large tech companies is diversifying the tax base and local economy and is modestly reducing the area's traditional concentration in gaming and tourism. While the recent diversification will help the county weather the impacts of the outbreak, the tourism and gaming economy has experienced skyrocketing unemployment as visitor volume slowed with the coronavirus outbreak and stopped with the governor's statewide shutdown of casinos in mid-March. Though casinos are now officially open as of June 4, they are operating at a reduced volume and with a reduced breadth of services, it remains unclear whether demand will be high given people's reluctance to travel and congregate in groups throughout the pandemic.

Despite the recent reopening, the economic damage created by the coronavirus pandemic and the governmental response has been acute and we anticipate the overall impact will be more severe for the county than many of its peers around the country. Approximately, 15% of the county's employment is in leisure and hospitality which is below the state average of 25%, but above the national average of 11%, which has driven unemployment up to 19%. We anticipate a slow recovery for the tourism and gaming industry which will leave the area with exceptionally high unemployment and reduced economic activity in the near term.

While tourism and gaming maintains a large footprint in the county, the Reno area has seen significant investment from tech companies over the last few years, including [Tesla](#) (B3 stable), [Panasonic](#) (Baa1 negative), [Switch](#) (Ba3 positive), [Apple](#) (Aa1 stable), [Alphabet](#) (Aa2 stable) and [eBay](#) (Baa1 stable). Tesla and Panasonic began producing batteries in the Gigafactory located just east of the county in Storey County. In Washoe County, large investments in manufacturing and distribution operations near the Gigafactory should continue to drive employment and housing in the Reno metro area.

The county has had a strong recovery post-recession. The county's full value (FV) grew for a seventh consecutive year, reaching a very large \$53.96 billion for 2020. Full value per capita is average, at \$115,000 (using 2020 FV), and median family income is at the national average, at 101.5% of the US for 2018. Both have been trending up following positive economic trends though a coronavirus related downturn could slow or reverse the trend.

Financial operations and reserves: recent growth in reserves and strong financial oversight will help offset severe near-term coronavirus driven revenue declines

The county's financial profile is a credit strength that will be tested over the near term because of the coronavirus pandemic. Financials improved in fiscal 2019 with available ending operating fund reserves (those designated as unassigned, assigned or committed in the general, special revenue and debt service funds plus available reserves in risk management, health benefits and equipment reserve funds) growing substantially to \$184.7 million (36.4% of revenue) from \$162.4 million (33.2%) in 2018 and \$148.4 million (32.7%) in 2017. This growth in reserves has been a conscious effort by management to rebuild reserves following the Great Recession to protect against future economic downturns.

The county's recent history of strengthening its balance sheet will help it navigate projected revenue declines in fiscal year 2020 and 2021 and an expected slow recovery of revenue. As with many local governments in Nevada, Washoe County relies on consolidated tax (Ctax) revenue (33% of general fund revenue) which is made up of formulaically distributed sales and use, government service, real property transfer, cigarette and liquor taxes. Due to the slowdown in travel, tourism and conventions and the periodic closure of casinos throughout the state, Ctax is likely to drop considerably for the fourth quarter of 2020 and remain weak in 2021 as the pandemic continues to ravage the tourism industry. As of June 4, 2020 many casinos in the state have been reopened and it remains to be seen the true impact that the shutdown and pandemic will have. County projections show a 8.5% drop in Ctax revenue in 2020 followed by a further 15.8% decline in 2021. Along with the Ctax declines the county expects the weaker economy to yield reductions in revenue across the board except property taxes which are expected to grow because of increased taxable values.

The county expects to address weaker revenue in the next two years through the use of fund balance and the deferral of capital spending and transfers. By fiscal year end 2021 the county expects to spend down unassigned general fund balance to 13.5% of expenditures. This reduction in fund balance leaves little flexibility in the general fund should revenue not rebound in fiscal year 2022. Moody's expects revenue to weaken at a greater rate with Ctax falling by a further 25% in 2021 driven by a slower than average recovery of the tourism, gaming and convention industries. This level of revenue decline will weaken county reserves further likely requiring the use of assigned balances and funds previously set-aside for capital. This weakening of other reserves would begin to put negative pressure on the county's credit profile.

Positively the county will receive approximately \$20 million from the state's allocation of CARES Act funding to address coronavirus response spending which should help address any increased spending, however these funds will not be used to address revenue declines. The county is currently evaluating the best way to use this funding which it must do before December 30, 2020. The county's ability to use these funds and other available resources and budget cuts to manage this crisis will be a significant factor in future rating reviews.

LIQUIDITY

Available liquidity grew to an even stronger 27.8% of operating revenue (\$141.2 million) as of fiscal 2019, though we anticipate liquidity will decline given expected revenue declines. The county does not use cash flow notes or other liquidity measures to support operations.

Debt and pensions: manageable debt burden; pension contributions below "tread water" so liabilities will rise

The county's debt is manageable with portions of its GOLT debt supported by revenue streams other than general revenue. Post-issuance, the county will have approximately \$217.8 in outstanding GOLT bonds with approximately \$34.3 million of those being self-supported by other revenue streams. Net of self-supported debt, the county's debt burden is a modest debt burden of 0.4% of full value and 0.4 times operating revenue. We anticipate the county's debt burden will remain modest going forward.

DEBT STRUCTURE

Most of the county's debt is fixed rate, GOLT debt with various additionally pledged revenue with the exception of Flood Control Bonds, Series 2006. The variable interest rate on the flood control bonds is equal to the sum of BMA (Bond Market Association) Swap Rate plus 0.70%. The approximately \$15.4 million of remaining principal had an interest rate of 2.527% which will be reset May 1, 2021.

The county also has outstanding sales tax bonds that are paid from a 0.125% countywide sales tax dedicated for infrastructure. The bonds maintain a strong 2.5 times additional bonds test and no debt service reserve which is seen as a weakness. The bonds maintain strong coverage at well over 7.0 times and are expected to maintain high coverage despite projected revenue declines.

DEBT-RELATED DERIVATIVES

The county is not exposed to debt-related derivatives.

PENSIONS AND OPEB

The county's pension liabilities are a credit weakness and will likely grow. Its pension is with the Nevada Public Employee Retirement System (PERS), a cost sharing, multiple-employer defined benefit plan. The county's share of the contribution to the plan in 2019 was \$29.2 million, a moderate 5.7% of operating fund revenue. However, the county's share of pension contributions were \$8.1 million short of Moody's calculation of what is necessary to prevent the county's pension liabilities from growing under plan assumptions, including the amount needed to cover normal costs and the interest on the unfunded liabilities. This "tread water gap" is moderate at 1.6% of the county's operating revenue.

The county's three-year adjusted net pension liability (ANPL) is high at 2.8% of full value and 2.63 times operating revenue based on an adjusted net pension liability of \$1.3 billion. The difference between this and the county's reported unfunded liability of \$414.6 million primarily reflects our use of a 4.14% discount rate compared to the plan's use of a 7.50% discount rate. This adjustment is made to improve comparability of reported pension liabilities among different issuers.

The county also provides other post-employment benefits (OPEB) of health insurance coverage to eligible retirees from various employee groups through several programs. Annual OPEB contributions in 2019 totaled \$24.9 million, or 4.9% of operating funds revenue. The county's adjusted net OPEB obligation at the end of 2019 was calculated at \$407.7 million. Given conservative return assumptions for the plan's assets, Moody's views the city's annual and overall OPEB liability as manageable.

ESG considerations

Environmental

Environmental considerations are not material credit drivers of the city's credit profile

Social

Social considerations are incorporated in our evaluation of the county's credit profile, including wealth and income levels, regional economic drivers and other factors. The rapid and widening spread of the coronavirus outbreak has led to spikes in unemployment and presents public health and safety risks.

Governance

Nevada counties have an institutional framework score of "Aa," or strong. Revenue are moderately predictable. State-shared excise taxes ("consolidated taxes"), the largest revenue source, are distributed under a long-standing legislative formula and are economically sensitive. Property taxes are subject to overlapping tax rate restrictions and abatement limits but may be adjusted by management. However, the property tax caps of up to 3% or 8%, by class, still allow for moderate revenue-raising ability. Expenditures primarily consist of personnel costs, which are highly predictable. Management has a moderate ability to make spending adjustments despite an active union presence.

The county's management team is strong and operating performance benefits from conservative stewardship. Management also strategically reduced available reserves in the recent recession and annual deficits transitioned to surpluses. The county has exhibited a strong ability to manage through crises which should help it navigate the coronavirus pandemic and subsequent economic fallout.

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

Washoe (County of) NV		
Scorecard Factors	Measure	Score
Economy/Tax Base (30%)^[1]		
Tax Base Size: Full Value (in 000s)	\$53,957,591	Aaa
Full Value Per Capita	\$115,048	Aa
Median Family Income (% of US Median)	101.5%	Aa
Notching Factors:^[2]		
Economic Concentration		Down
Finances (30%)		
Fund Balance as a % of Revenues	32.9%	Aaa
5-Year Dollar Change in Fund Balance as % of Revenues	8.8%	A
Cash Balance as a % of Revenues	36.4%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	9.8%	A
Notching Factors:^[2]		
Unusually volatile revenue structure		Down
Management (20%)		
Institutional Framework	Aa	Aa
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures (x)	1.0x	A
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	0.4%	Aaa
Net Direct Debt / Operating Revenues (x)	0.4x	Aa
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	2.5%	A
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	2.6x	A
	Scorecard-Indicated Outcome	Aa2
	Assigned Rating	Aa2

[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.

Source: US Census Bureau and Moody's Investors Service

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