Los Angeles County, California

New Issue Report

Ratings

Issuer Default Rating[a]	AA+
New Issue	
2019-20 Tax and Revenue Anticipation Notes	F1+
Outstanding Debt	
Los Angeles County Certificates of Participation[b]	AA
Los Angeles County Public Works Financing Authority Lease Revenue Bonds[b]	AA
Los Angeles County Capital Asset Leasing Corporation Lease Revenue Bonds[b]	AA
Sonnenblick-Del Rio El Monte Asset Leasing Corporation Certificates of Participation[b]	AA
Sonnenblick-Del Rio West Los Angeles Leasing Corporation Certificates of Participation[b]	AA

[a]Upgraded from 'AA' on May 31, 2019.
[b]Upgraded from 'AA–' on May 31, 2019.

Rating Outlook

Stable

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New Issue Details

Sale Date: The week of June 3, 2019 via negotiation.

Series: $700,000,000 2019–20 Tax and Revenue Anticipation Notes.

Purpose: To smooth cash flow management for general fund operations during fiscal 2020.

Security: GOs of Los Angeles County (the county) payable from a first lien on unrestricted general fund revenues attributable to fiscal 2020, including requirements to set aside the first such funds received during specified time periods for note repayment.

Analytical Conclusion: Fitch Ratings' upgrade of the county's Issuer Default Rating (IDR) to 'AA+' from 'AA' reflects the combined strength of the county's continued solid revenue performance and prospects, strong economic underpinnings, moderately low long-term liability burden and highest level of gap-closing capacity. The county's demonstrated ability to cut spending, sound financial cushion and limited revenue cyclicality offset the county's exposure to federal and state funding decisions, DHS operations and state law's constraints on the county's independent ability to raise revenues.

The 'F1+' short-term rating on the notes corresponds to the county's IDR. The combination of pledged revenues and court-verified borrowable resources provides very strong debt service coverage for the notes. Full note principal and interest set-asides occur well in advance of note maturity.

The upgrade to 'AA' from 'AA–' for all of the county's rated certificates of participation and lease revenue bonds maintains the one notch distinction relative to the upgraded IDR, reflecting the slightly higher optionality inherent in appropriations for debt service repayment.

Key Rating Drivers

Revenue Framework: 'aa'

The county's revenues have demonstrated limited volatility, reflecting the size and maturity of the economy and tax base, which retains a large Proposition 13 cushion. Growth prospects for revenues are solid. The county's independent legal ability to raise revenues is limited by state law but satisfactory.

Expenditure Framework: 'aa'

The county demonstrated strong expenditure control during the Great Recession and continues to enjoy solid expenditure flexibility. Fitch expects expenditure growth to be in line with, to marginally above, future revenue growth in the absence of policy action. The portion of the budget allocated to carrying costs will increase as the county pays down its unfunded pension liability and significant other post-employment benefit (OPEB) obligations but is expected to remain moderate.

Long-Term Liability Burden: 'aa'

The county's long-term liability burden for debt and pensions is moderately low relative to total personal income. The majority of debt is issued by overlapping jurisdictions.

Operating Performance: 'aaa'

The county has demonstrated an ongoing commitment to bolster its financial cushion during the economic recovery, aided in part by the Department of Health Services's (DHS) improved financial position. The county is very well positioned to address cyclical downturns.

Rating History — IDR

Rating	Action	Outlook/ Watch	Date
AA+	Upgraded	Stable	5/31/19
AA	Affirmed	Stable	5/31/18
AA	Upgraded	Stable	2/23/16
AA–	Affirmed	Positive	12/24/14
AA–	Assigned	Stable	6/9/11

Rating History — Certificates of Participation and Lease Revenue Bonds

Rating	Action	Outlook/ Watch	Date
AA	Upgraded	Stable	5/31/19
AA–	Affirmed	Stable	5/31/18
AA–	Upgraded	Stable	2/23/16
A+	Affirmed	Positive	12/24/14
A+	Revised	Stable	4/30/10
A	Affirmed	Positive	11/5/01
A	Upgraded	—	5/23/00
A–	Downgraded	—	6/21/95
A+	Assigned	—	9/11/92

Related Research

Fitch Rates $700MM Los Angeles County, CA Notes F1+; Upgrades IDR to 'AA+'; Outlook Stable (May 2019)

Related Criteria

U.S. Public Finance Short-Term Debt Rating Criteria (November 2017)

U.S. Public Finance Tax-Supported Rating Criteria (April 2018)

Rating Sensitivities

Solid Financial Profile: The ratings are sensitive to fundamental changes in the county's financial operations and strong budget management, which Fitch does not expect.

Credit Profile

The county covers over 4,000 square miles and includes 88 incorporated cities and 100 school districts. With a population exceeding 10 million, it is more populous than most U.S. states. The county's huge, diversified economy represents over a quarter of California's total economy.

Los Angeles County is a major economic and manufacturing center and incorporates two ports and an airport that are among the busiest in the world. Taxable AV has grown strongly in the past eight years after very small recessionary declines, reflecting the county's highly developed and mature nature and large Proposition 13 cushion. While the majority of recent growth is tied to ownership transfers of existing properties and inflation, ongoing new development and redevelopment will continue to support future tax base growth.

Despite strong economic and tax base characteristics, the unemployment rate has historically been higher than the nation's, although recently, the gap has been largely eliminated. Wealth indicators are below the state but generally above or in line with the national level, incorporating some highly urbanized and low income areas.

Revenue Framework

The majority of general fund revenues come from federal and state funding for social services (55% of total general fund revenues in fiscal 2018), although this amount can fluctuate significantly through the economic cycle due to caseloads, reimbursement timing and state budget issues. Two other key revenue sources are locally generated taxes (32%) and charges for services (10%).

Based on 10-year CAGRs, total general fund revenue growth has been slightly below national GDP but has outpaced inflation. Excluding intergovernmental revenues shows the 10-year CAGRs for locally controlled revenues outperforming national GDP growth until fiscal years 2017 and 2018 when they dipped slightly below. Fitch expects future intergovernmental revenues will be determined by federal and state policy decisions and economic performance, while locally controlled revenues will mirror future economic trends at the county level. In terms of two key locally controlled revenues, the fiscal 2020 budget assumes almost 6% property tax revenue growth and 2% sales tax revenue growth.

The proposed fiscal 2020 state budget and May revision include proposals to increase funding to counties for in-home supportive services, Medi-Cal administration, homelessness emergency aid and voting systems. Such funding would have a positive revenue impact for the county.

The county has satisfactory independent revenue-raising capacity relative to its modest historical cyclical revenue declines. However, its ability to raise revenues is constrained by state laws (in particular, Propositions 13 and 218) requiring voter approval for tax increases. Independent revenue-raising ability is largely limited to licenses, permits, fines, and charges for service.

Since 2008, voters have approved eight out of nine tax ballot measures, with support ranging from 61% to 75%. Most recently, in November 2018, voters passed Measure W with 69% support, authorizing the Los Angeles County Flood Control District to levy a special tax annually to assist in the capture of storm water and related pollution clean-up, improve water quality and provide community investment benefits. This measure, which has no sunset clause, is expected to generate approximately $300 million in new tax revenue annually for the county from fiscal 2020 onwards. Over the next five years, this will allow the county to construct an estimated $511 million in projects to address regulatory storm water and urban runoff compliance issues. The county board of supervisors is currently considering a $1.4 billion tax ballot measure in 2020 to fund critical Fire District infrastructure needs.

Expenditure Framework

The majority of fiscal 2018 general fund expenditures were on public assistance (36%), public safety (32%) and health and sanitation services (23%), which are key roles for county governments in California. Personnel costs remain the largest driver of expenditure increases. The county operates within a strong labor environment and labor has the ability to strike. Nevertheless, labor relations are productive and multiyear labor contracts have considerable flexibility.

The county has settled labor agreements with 58 of its 62 bargaining units and is close to finalizing the remaining language changes in the final four. The labor agreements are for three years (with varying expiration dates from Dec. 31, 2020 to Sept. 30, 2021) and provide for 7% cost of living adjustments implemented incrementally over those three years, which will also be received by nonrepresented employees. The labor agreements contain reopeners related to a potential economic downturn.

Represented employees are also covered by one of two fringe benefit agreements; one has been approved by the county board of supervisors and the other has reached tentative agreement. The fiscal 2020 budget absorbs $226 million in salary and benefit cost increases compared to $72 million in programmatic increases and fiscal policy changes. However, these combined cost increases are only slightly more than 1% of the combined general fund and hospital enterprise fund budgets for fiscal 2020.

The pace of spending growth absent policy actions is likely to be in line with, to marginally above, revenue growth patterns given high-needs communities within the county. Fitch expects the county will continue to control expenditures aggressively.

Although Fitch expects that debt, pension and OPEB carrying costs will grow as a percentage of general fund spending, due to planned debt issuances, rising pension contributions, and increased retiree healthcare benefit prefunding, it also expects that the county's expenditure flexibility will remain solid.

Long-Term Liability Burden

Overall debt of almost $39 billion is a moderately low burden on county taxpayers' resources. The majority is debt issued by overlapping jurisdictions outside of the county's control, approximately 59% of the total long-term debt and pension liability burden. This portion could grow significantly. By themselves, school and community college districts located within the county have $19.4 billion in unissued bond authorizations.

By contrast, net direct county debt of about $2.4 billion, including tobacco settlement asset-backed bonds and interest accretions, represents about 4% of the total long-term liability burden. This figure includes an imminent issuance, during first-quarter fiscal 2020 of approximately $350 million of long-term lease revenue bonds to refinance commercial paper note financing of completed construction projects.

Future debt plans include, during second-quarter fiscal 2021, $425 million of long-term lease revenue bonds to finance the county's contribution toward the $650 million Los Angeles County

Museum of Art (LACMA) project to construct a new building for its permanent collection ($125 million will repay commercial paper issued by the county; the balance of $300 million will be repaid by LACMA's private fundraising campaign, with the county acting as the debt backstop). By fiscal 2024, the county is considering issuing around $883 million in lease revenue bonds to take out initial short-term funding for construction of a new consolidated correctional treatment facility. Even if all proposed debt was issued immediately, the county's long-term liability burden would remain moderate.

Adjusted pension liabilities represent about 37% of the total long-term liability burden. The Los Angeles County Employees Retirement Association (LACERA) reported a $10.8 billion net pension liability at June 30, 2017 (a funded ratio of 82%, assuming a 7.25% discount rate). This net pension liability represented an almost 6% increase over the previous year despite the county consistently funding LACERA's actuarially required contributions. Further increases are expected that will drive increased employer contributions through fiscal 2023. Using a 6% discount rate results in a Fitch-adjusted increase in the county's net pension liability to an estimated $22.7 billion, reducing the asset-to-liabilities ratio to 69%.

The county's unfunded actuarial accrued OPEB liability is sizable at $26.3 billion in fiscal 2018 (over 4% of personal income). The county does have the ability to reduce it. The county enacted OPEB reforms in 2015, which are reflected in the fiscal 2018 report liability number, and is increasing its annual contributions, funded in part by maximizing subvention revenues from other governments. The county's new fringe benefit agreements with its bargaining units do not include any OPEB policy changes. The county is budgeting $246 million in pre-funding contributions to its OPEB trust fund in fiscal 2020. This is the fifth year of a multiyear plan to incrementally increase the prefunding of retiree healthcare benefits. The county is projecting that it will be able to reach full actuarially required OPEB contributions by fiscal 2028.

In addition to the county's irrevocable OPEB trust, with a March 31, 2019 balance of $1.1 billion, LACERA has an almost $116 million reserve for annual healthcare premium fluctuations.

Operating Performance

The county has prioritized maintenance of strong general fund balances and continued strengthening of its reserves during the economic recovery, in the face of increasing employee remuneration costs. For details, see Scenario Analysis, page 7.

The county ended fiscal 2018 with a strong unrestricted general fund balance of nearly $3.7 billion, or 20% of spending. While the county is currently projecting to end fiscal 2019 with a lower unrestricted general fund balance of nearly $3.2 billion, it typically outperforms its May projections and in fact expects to add to the unrestricted general fund balance. Although the fiscal 2020 general fund budget is balanced using a $1.5 billion fund balance drawdown, in practice the county again expects to increase its general fund balance at year end.

The rainy day fund (part of the unrestricted general fund balance) has a current balance of $525 million, around 8% of ongoing discretionary revenues (excluding federal and state pass-through funding). The goal is to reach 10%, which the county expects to achieve in fiscal 2022 through a further $117 million in contributions over the next three fiscal years. The county has also budgeted 10% of new discretionary revenues for contingency appropriations in fiscal 2020.

The county has identified a $2.6 billion backlog in deferred maintenance and building systems replacement projects. To begin whittling that down, the county is implementing a five-year, $750 million plan to address its highest priority projects, drawing upon existing funds in its committed general fund balance and its commercial paper program. The county also has committed moneys available to begin addressing its $350 million information technology replacement and modernization needs over the next five years and implementation of a $337 million new voting system (the cost of which will be partially offset by federal and state moneys).

The county's Title IV-E waiver, related to federal funding of foster children services, is due to expire on Sept. 30, 2019, which would result in a $213 million per year funding reduction. The county is lobbying for a two-year extension until a new federal "Families First Preservation Act" program is implemented. If that does not happen, the county will look at service provision alternatives and bridge-funding options.

The county operates the second largest public health system in the nation. The general fund is responsible for DHS administration, online medical records and the managed care program. State Assembly Bill 85 established a maintenance of effort funding requirement for the annual county general fund contribution to DHS, with 1% increases annually. On this basis, the net county contribution (NCC) has been stable, increasing 1% annually since fiscal 2015.

In fiscal years 2019 and 2020, county officials report that the NCC represented around 5% of DHS's total budget. In addition to the NCC, other departments have transferred resources to support DHS's absorption of correctional health services, the county board of supervisors has provided new funding for strategic initiatives, and the state has increased pass-through funding for mental health programs. Consequently, gross county contribution increases in recent years have been driven primarily by policy decisions, rather than DHS budgetary pressures.

DHS's year-end financial results continue to improve. The county is projecting an ending fund balance of approximately $1.1 billion for fiscal 2019, compared to $912 million at the end of fiscal 2018. DHS anticipates using some of this fund balance in fiscal 2020 until three new revenue programs are fully operational in fiscal 2021, subject to final approval by the Centers for Medicare and Medicaid Services. While this has resulted in the general fund increasing its hospital working capital loans to DHS ($456 million projected balance for June 2019, an increase of almost $347 million compared to June 2018), they remain well below the high of almost $1.1 billion in June 2011.

DHS continues to benefit from a number of external and internal reforms, most notably the Affordable Care Act (ACA) and an improved payor mix (district officials report a 7% uninsured rate in fiscal 2018, compared to a pre-ACA rate of 25%), the 'Medi-Cal 2020' extension for California public hospitals through Dec. 31, 2020, healthcare service and electronic system integration, infrastructure investments, and departmental reorganization. DHS considers itself better placed to respond to potential future federal healthcare funding policy changes, given its stronger continuum of care, better health outcomes and improved patient demographics.

Notes Finance Cash Flow Needs

Note proceeds will be used to smooth cash flow management for general fund operations during fiscal 2020. The county expects all three note set-asides to occur in months with positive net ending balances, thereby allowing sufficient coverage of between 2.5x and 8.1x solely on the basis of each month's projected net ending balance, without drawing upon $4.4 billion to $7.0 billion in projected borrowable funds at those set-aside dates. Including projected borrowable funds increases coverage to between 17.9x and 65.3x. The repayment deposit structure sets aside 100% of principal and interest two months in advance of note maturity. Based on the previous 11 fiscal years, the county consistently outperforms its projected year-end cash balances.

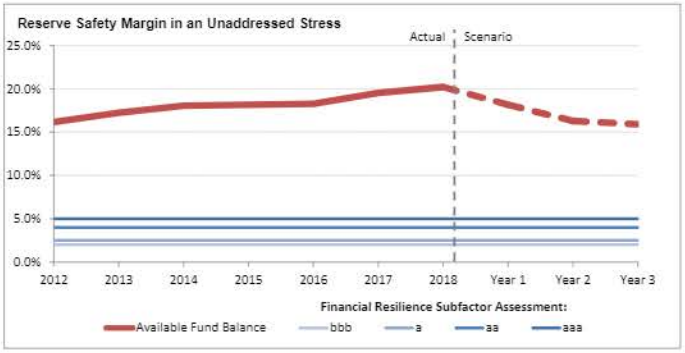
Related Ratings

As noted above, Fitch has upgraded to 'AA' from 'AA–' the following outstanding ratings, each of which is linked to the county's IDR:

- $1.6 billion Los Angeles County Public Works Financing Authority lease revenue bonds (multiple capital projects), 2010 series A (tax-exempt) and series B (Build America Bonds); lease revenue bonds (multiple capital projects II), series 2012; lease revenue bonds (multiple capital projects), series 2015A; lease revenue bonds (master refunding project), series 2015B (tax-exempt) and 2015C (federally taxable); and lease revenue bonds, 2016 series D;
- $55 million county COPs, series 1993 Disney Parking Project and 2012 refunding COPs (Disney Concert Hall Parking Garage);
- $58 million Sonnenblick-Del Rio El Monte Asset Leasing Corporation senior COPs, series 1999 (Department of Public Social Services Facility) and series 2001 (Department of Public Social Services Facility - Phase II);
- $28 million Sonnenblick-Del Rio West Los Angeles Asset Leasing Corporation senior COPs, series 2000 (Department of Public Social Services Facility);
- $13 million Los Angeles County Capital Leasing Corporation lease revenue bonds (LAC-CAL equipment program), series 2017A;
- $302 million lease revenue bonds, series 2018A (Vermont Corridor County Administration Building) (tax-exempt) and series 2018B (Vermont Corridor County Administration Building) (federally taxable).

Los Angeles County (CA)

Scenario Analysis



Analyst Interpretation of Scenario Results:

The county has prioritized maintenance of strong general fund balances and continued strengthening of its reserves during the economic recovery, in the face of increasing employee remuneration costs. During the great recession, the county demonstrated notable gap-closing ability despite state-imposed constraints on its revenue-raising ability. It received additional revenue through federal stimulus funds and health care reform (for example, from increased client enrollment in managed health care under the Affordable Care Act). On the expenditure side, the county relied on employee attrition, unfilled vacancies, departmental curtailments, efficiency initiatives, 0% COLAs for four to five years (depending on the bargaining unit), and use of reserves and capital funds. The county maintains a notable amount of expenditure control due to moderate carrying costs and labor contracts with considerable flexibility.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(1.0%)	2.1%	3.5%
Inherent Budget Flexibility		Midrange	

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2012	2013	2014	2015	2016	2017	2018	Year 1	Year 2	Year 3
Total Revenues	13,825,979	14,606,938	15,208,018	15,454,733	16,190,186	17,081,934	17,726,265	17,549,002	17,921,392	18,549,716
% Change in Revenues	-	5.6%	4.1%	1.6%	4.8%	5.5%	3.8%	(1.0%)	2.1%	3.5%
Total Expenditures	13,619,386	14,013,588	14,790,147	15,237,807	15,863,407	16,573,050	17,531,885	17,882,523	18,240,173	18,604,977
% Change in Expenditures	-	2.9%	5.5%	3.0%	4.1%	4.5%	5.8%	2.0%	2.0%	2.0%
Transfers In and Other Sources	484,995	508,087	468,614	393,023	374,195	438,769	734,228	726,886	742,310	768,336
Transfers Out and Other Uses	772,080	863,738	663,327	522,934	506,555	680,922	684,390	698,078	712,039	726,280
Net Transfers	(287,085)	(355,651)	(194,713)	(129,911)	(132,360)	(242,153)	49,838	28,808	30,271	42,055
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	(80,492)	237,699	223,158	87,015	194,419	266,731	244,218	(304,712)	(288,510)	(13,205)
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	(0.6%)	1.6%	1.4%	0.6%	1.2%	1.5%	1.3%	(1.6%)	(1.5%)	(0.1%)
Unrestricted/Unreserved Fund Balance (General Fund)	2,327,239	2,566,028	2,790,224	2,861,745	2,991,807	3,368,535	3,680,895	3,376,183	3,087,672	3,074,468
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	2,327,239	2,566,028	2,790,224	2,861,745	2,991,807	3,368,535	3,680,895	3,376,183	3,087,672	3,074,468
Combined Available Fund Bal. (% of Expend. and Transfers Out)	16.2%	17.2%	18.1%	18.2%	18.3%	19.5%	20.2%	18.2%	16.3%	15.9%

Reserve Safety Margins	Inherent Budget Flexibility				
	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	16.0%	8.0%	5.0%	3.0%	2.0%
Reserve Safety Margin (aa)	12.0%	6.0%	4.0%	2.5%	2.0%
Reserve Safety Margin (a)	8.0%	4.0%	2.5%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.0%	2.0%	2.0%	2.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

The ratings above were solicited and assigned or maintained at the request of the rated entity/Issuer or a related third party. Any exceptions follow below.