

Los Angeles County, California

New Issue Report

Ratings

Issuer Default Rating	AA+
New Issue	
Los Angeles County Public Works Financing Authority Lease Revenue Bonds, 2019 Series E-1 and E-2	AA
Outstanding Debt	
Los Angeles County Certificates of Participation	AA
Los Angeles County Public Works Financing Authority Lease Revenue Bonds	AA
Los Angeles County Capital Asset Leasing Corporation Lease Revenue Bonds	AA
Sonnenblick-Del Rio El Monte Asset Leasing Corporation Certificates of Participation	AA
Sonnenblick-Del Rio West Los Angeles Leasing Corporation Certificates of Participation	AA
Los Angeles County Capital Leasing Corporation Lease Revenue Bonds (LAC-CAL Equipment Program)	AA
Los Angeles County Facilities, Inc. Lease Revenue Bonds (Vermont Corridor County Administration Building)	AA
Los Angeles County 2019-20 Tax and Revenue Anticipation Notes	F1+

Rating Outlook

Stable

Analysts

Alan Gibson
+1 415 732-7577
alan.gibson@fitchratings.com

Amy Laskey
+1 212 908-0568
amy.laskey@fitchratings.com

New Issue Summary

Sale Date: Negotiated sale during the week of Aug. 12, 2019.

Series: \$226,545,000 Lease Revenue Bonds, 2019 Series E-1; \$33,285,000 Lease Revenue Bonds, 2019 Series E-2.

Purpose: To refinance certain capital improvement projects, including the repayment of \$319 million of outstanding Los Angeles County Capital Asset Leasing Corporation commercial paper notes. Proceeds from the 2019 series E-2 bonds, which are being issued as qualified 501(c)(3) bonds, will specifically refinance construction costs for the parking garage at the Martin Luther King Jr. Community Hospital, a 501(c)(3) tax-exempt organization.

Security: Los Angeles County Public Works Financing Authority (the authority) lease revenue bonds are payable from Los Angeles County's (the county) facility lease rental payments to the authority and are secured by a portfolio of real estate assets pledged as collateral under a 2015 master lease between the county and the authority.

The 'AA+' Issuer Default Rating (IDR) reflects the combined strength of the county's continued solid revenue performance and prospects, strong economic underpinnings, a moderate-to-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 cyclical offset its exposure to federal and state funding decisions, Department of Health Services' (DHS) operations, and state law constraints on the county's independent ability to raise revenues.

The 'AA' rating for all of the county's rated certificates of participation (COPs) and lease revenue bonds reflects the slightly higher optionality inherent in appropriations for debt service repayment. The 'F1+' short-term rating on the 2019-20 tax and revenue anticipation notes (TRANS) corresponds to the county's IDR.

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 Ratings 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 ramps up contributions to pay down its net pension liability and significant OPEB obligations, but it is expected to remain moderate.

Long-Term Liability Burden: 'aa'

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

Rating History — IDR

Rating	Action	Outlook/ Watch	Date
AA+	Affirmed	Stable	7/30/19
AA+	Upgraded	Stable	5/31/19
AA	Upgraded	Stable	2/23/16
AA-	Affirmed	Positive	12/24/14
AA-	Assigned	Stable	6/09/11

Rating History —
Certificates of
Participation and Lease
Revenue Bonds

Rating	Action	Outlook/ Watch	Date
AA	Affirmed	Stable	7/30/19
AA	Upgraded	Stable	5/31/19
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

Rating History —
TRANS

Rating	Action	Outlook/ Watch	Date
F1+	Affirmed	—	7/30/19
F1+	Assigned	—	5/31/19

Related Research

Fitch Rates \$260MM Los Angeles County Public Works Fin Auth, CA Lease Revs 'AA'; Outlook Stable (July 2019)

Related Criteria

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

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

Short-Term Ratings Criteria (May 2019)

Operating Performance: 'aaa'

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

Rating Sensitivities

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

Credit Profile

Los Angeles 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 one-quarter of California's total economy. The county is a major 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 nine 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. However, housing price growth has slowed in the Los Angeles-Long Beach-Anaheim MSA, where the annualized rate of home price depreciation was 1.3% in the first quarter of 2019 (for more information, see Fitch's special report, "U.S. RMBS Sustainable Home Price Report, Second Quarter 2019," dated June 2019). This could be a harbinger of a future trend for the county.

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's but generally above or in line with the nation's, 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%).

On a 10-year CAGR basis, total general fund revenue growth has been slightly below national GDP but has outpaced inflation. Excluding intergovernmental revenues, the 10-year CAGRs for locally controlled revenues outperform 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, which Fitch considers reasonable given recent revenue trends.

The fiscal 2020 state budget increases funding to counties for health and welfare services, in-home supportive services, homelessness aid, disaster funding, and voting systems. Such funding is expected to have a positive revenue impact on 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 onward. 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 related to 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 organized 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, has reached tentative agreement with one more, and is still in negotiations with the three over final contract wording. The settled 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 (COLAs) implemented incrementally over those three years; the 7% COLA will also apply to non-represented employees. The labor agreements contain reopeners related to a potential economic downturn. Represented employees are also covered by two fringe benefit agreements through 2021. They increase the county's contribution toward healthcare benefits while instituting a cap on the amount of unused county contributions returned to employees as taxable cash.

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 the county's expenditure flexibility will remain solid.

Long-Term Liability Burden

Overall debt of almost \$38.8 billion is a moderate-to-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 \$2.3 billion (including tobacco settlement asset-backed bonds and interest accretions) represents about 4% of the total long-term liability burden.

During the second quarter of fiscal 2021, debt plans include \$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). Longer term, the county expects that it will require long-term financing for large capital construction projects, including a new consolidated correctional treatment facility and a new Harbor-UCLA Medical Center tower. 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 determined contributions. Further increases expected will drive increased employer contributions through fiscal 2023. Using a 6% discount rate results in a Fitch-adjusted net pension liability of an estimated \$22.7 billion, reducing the asset-to-liabilities ratio to 69%.

The county's unfunded actuarial accrued OPEB liability was sizable at \$26.3 billion in fiscal 2018 (over 4% of personal income). Nonetheless, the county has 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 projects it will be able to reach full actuarially required OPEB contributions in fiscal 2028.

In addition to the county's irrevocable OPEB trust (with a May 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 6.

The county ended fiscal 2018 with a strong unrestricted general fund balance of nearly \$3.7 billion, or 20% of spending. The county projects to end fiscal 2019 with a higher 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 \$602 million, around 9% 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. 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 monies 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 monies).

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.

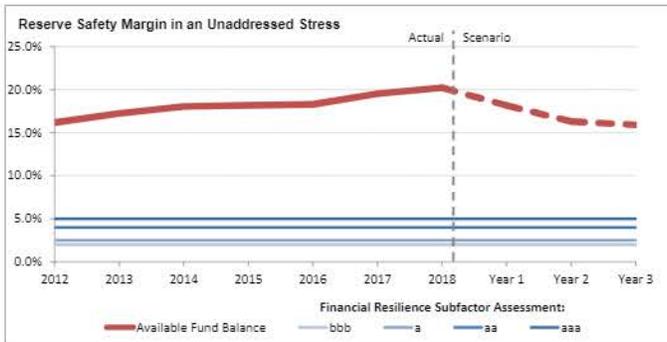
The county operates the second largest public health system in the nation. The general fund is responsible for DHS administration, online medical records, and the managed care program. State Assembly Bill 85 established a maintenance of effort funding requirement for the annual county general fund contribution 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' total budget. In addition to the NCC, other departments have transferred resources to support DHS' 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' year-end financial results continue to improve. The county projects an ending fund balance of over \$1.1 billion for fiscal 2019, compared to \$912 million at the end of fiscal 2018. Of this amount, approximately \$528 million is being set up as a long-term receivable since payments (subject to a two-year delay in approval from the federal Centers for Medicaid and Medicare Services) are not expected to be collected until September 2020. The remaining estimated \$580 million fund balance is available to fund future DHS operations, as needed. While this has resulted in the county's general fund increasing its hospital working capital loans to DHS (\$492 million projected balance for June 2019, an increase of almost \$382 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 (county 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. County officials consider that DHS is now better positioned to respond to potential future federal healthcare funding policy changes, given its stronger continuum of care, better health outcomes, and improved patient demographics.

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 healthcare reform (for example, from increased client enrollment in managed healthcare 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.

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