Fitch Rates Olathe (KS) GO Bonds 'AA+' & GO Notes 'F1+'; Outlook Stable

Mon 08 Jun, 2020 - 2:04 PM ET

Fitch Ratings - New York - 08 Jun 2020: Fitch Ratings has assigned ratings to the following Olathe (KS) obligations:

-- $75.6 million general obligation (GO) temporary notes, series 2020-A 'F1+';

-- $32.2 million GO improvement bonds, series 233 'AA+'.

The bonds and notes are being issued to finance a portion of the costs of certain public improvements and to refund certain general obligation bonds. They are scheduled to sell on June 16.

Fitch has also affirmed the following ratings for Olathe:

-- Issuer Default Rating (IDR) at 'AA+';

-- Approximately $174 million in outstanding GO bonds at 'AA+';

-- Approximately $54 million GO temporary notes, series 2019-A at 'F1+'.

The Rating Outlook on the bonds is Stable.

SECURITY

The bonds and notes carry the city's unlimited tax general obligation pledge.

ANALYTICAL CONCLUSION

The 'AA+' rating reflects Fitch's expectation that the city will maintain a superior level of fundamental financial flexibility in an economic downturn, including solid flexibility to control both revenues and expenditures. The rating also reflects a low long-term liability burden. The 'F1+' rating on the notes corresponds to the long-term rating.

ECONOMIC RESOURCE BASE

Olathe is a suburban community located approximately 20 miles southwest of Kansas City, KS and is the seat of Johnson County. The city's population has doubled since 1990, and it presently stands at approximately 140,000. City management anticipates a slow return to consumer confidence this year, despite the opening of the State and Johnson County being underway. Management will continue this approach for the 2021 budget.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

Fitch expects that the city's revenue growth absent policy actions will continue at a rate in line with national GDP. Fitch expects that the city will maintain substantial independent legal ability to raise operating revenues even after the implementation of the tax lid.
Expenditure Framework: 'aa'

The natural pace of expenditure growth should be in line with that of revenue growth, and the city has solid control over its main expenditure items.

Long-Term Liability Burden: 'aaa'

Long-term liabilities are low at around 10% of personal income. Fitch expects the metric to remain at around this level.

Operating Performance: 'aaa'

The rating assumes that the city will continue to maintain reserves at a level consistent with a 'aaa' financial resilience assessment during the current economic downturn. The city has maintained high reserves throughout the recent economic recovery.

Rating Sensitivities

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-- A sustained decline in carrying costs;

-- A sustained, materially lower long-term liability metric, which Fitch does not anticipate.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-- A reduction in revenue growth expectations;

-- An increase in long-term liabilities such that the long-term liability metric becomes inconsistent with the 'aaa' assessment.
BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Public Finance issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

CURRENT DEVELOPMENTS

The coronavirus and related government containment measures worldwide creates an uncertain global environment for U.S. state and local governments and related entities in the near term. While the city’s most recently available fiscal and economic data may not fully reflect impairment, material changes in revenues and expenditures are occurring across the country and likely to worsen in the coming weeks and months as economic activity suffers and public health spending increases. Fitch’s ratings are forward looking in nature, and Fitch will monitor developments in state and local governments as a result of the virus outbreak as it relates to severity and duration, and incorporate revised expectations for future performance and assessment of key risks.

In its baseline scenario, Fitch assumes sharp economic contractions hit major economies in 1H20 at a speed and depth that is unprecedented since World War II. Recovery begins from 3Q20 onward as the health crisis subsides after a short but severe global recession. GDP remains below its 4Q19 level through most of 2021. The downside scenario depicts a significantly larger fall in GDP with a slow recovery beginning after 2021. Additional details, including key assumptions and implications of the baseline scenario and a downside scenario, are described in the full report at https://www.fitchratings.com/site/re/10120570.
Due to the coronavirus pandemic, the city projects that it will see revenue declines across its various revenue streams of almost 13% from fiscal 2018 actuals, in line with the Fitch Analytical Stress Test (FAST) baseline stress scenario results. However, through a combination of expenditure reductions and a use of available reserves that would leave the reserve safety margin well above the 'aaa' level, Fitch expects that the city will be able to manage through the baseline stress scenario while maintaining strong levels of gap-closing capacity.

CREDIT PROFILE

The city benefits from its proximity to the Kansas City metropolitan statistical area (MSA) in addition to its own vibrant and expanding commercial/industrial sector, anchored by several national companies. Economic indices are favorable and unemployment is low. Large employers include Farmers Insurance and Garmin, which are expanding their operations in the city. Assessed value growth has been strong, increasing by between 6% and 9% each year from 2014 through 2019.

REVENUE FRAMEWORK

The city’s revenue growth should remain strong given the diverse tax base and revenue stream. Sales tax comprised over 50% of 2018 general fund revenue while property tax revenue made up around 20%. Fitch believes exemptions in the statewide property tax lid law will enable the city to continue to increase revenues at a substantial level if necessary.

General fund revenue grew at an average of 3.3% annually from 2008 to 2018, including 5.6% in 2018. Fitch expects ongoing economic development and assessed value expansion will lead to continued revenue growth in line with GDP growth.

The city should continue to have a substantial level of control over revenue increases despite the implementation of the tax lid for the fiscal 2018 budget, which limits property tax growth to the CPI. Exemptions to the lid include growth in public
safety and debt service expenditures. The city also maintains some ability to adjust other locally controlled revenues. Fitch believes the exemptions to the tax lid give the city a solid degree of independent legal ability to raise revenues.

**EXPENDITURE FRAMEWORK**

The city's main expenditure items include public safety, general government and public works (55%, 25% and 12% of general fund expenditures, respectively, in 2018).

Fitch expects that the natural growth rate of expenditures will be in line with or marginally above the strong natural growth rate of revenue.

The city has a solid degree of flexibility in its main expenditure items. Carrying costs were 21% of government expenditures in 2018, with the majority of the carrying costs for rapidly amortizing debt. In addition, the city has no labor contracts, so there is ample flexibility to control headcount. Fitch expects the level of carrying costs to decline given the declining debt service schedule.

**LONG-TERM LIABILITY BURDEN**

Olathe's long-term liabilities are at the high end of the low category, with the combined, Fitch-adjusted net pension liability and overall debt as a percentage of personal income at around 10%. Fitch expects that city personal income may grow at a faster rate than long-term liability growth. The city has moderate debt plans over the next two years and a fast amortization schedule. Fitch expects that the long-term liability burden as a percentage of personal income will remain relatively close to 10% over the next several years, as new debt replaces the debt rolling off while the pension burden increases and the resource base grows.

The city participates in two components of the cost-sharing, multiple-employer Kansas Public Employees Retirement System covering general employees and
uniformed workers. As of the measurement date in Olathe's most recent audit, both components show a ratio of assets to liabilities of 69%. As adjusted by Fitch to reflect a 6% discount rate instead of the elevated 7.75% rate used by the plan, that ratio falls to 55%.

OPERATING PERFORMANCE

Fitch expects that the city will continue to exhibit a superior level of gap-closing capacity through the current downturn given its high degree of inherent budget flexibility and strong available reserves. The city's reserve levels, which are far above the level Fitch believes is needed to offset a revenue decline in a moderate downturn scenario, enhance the high inherent budget flexibility in the current baseline stress scenario. The city's available general fund reserve levels in 2018 were 29% of general fund expenditures. Management reports that the city added to reserves in 2019.

The city has maintained a high level of available reserves through the course of the expansion that followed the great recession. Current available reserve levels are above both the city's formal policy of maintaining at least 15% of revenues in the general fund and in line with its target of 30% of revenues.

Management has updated its revenue forecast given stay-at-home orders to anticipate a revenue decline of $12.3 million across the city's sales, property and franchise taxes, and its fines and fees revenue. The city's forecast is in line with the baseline stress scenario as modeled by FAST. Given these potential revenue declines, the city has made several expenditure reductions, including a hiring freeze, a two-week unpaid furlough for all employees (except firefighters and police officers), a cap on purchases, deferring some expenditures and transferring expenditures to other funds, where possible. While management anticipates that it may need to utilize some reserves to balance operations, Fitch believes that management has been proactive in identifying revenue shortfalls and reducing expenditures in anticipation of the declines. City management has stated that it still expects to have available reserves in line with its target of 30% of revenue at the end of 2020.
In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

<table>
<thead>
<tr>
<th>ENTITY/DEBT</th>
<th>RATING</th>
</tr>
</thead>
<tbody>
<tr>
<td>Olathe (KS) [General Government]</td>
<td>LT AA+ Rating Outlook Stable Affirmed</td>
</tr>
<tr>
<td></td>
<td>IDR</td>
</tr>
<tr>
<td>Olathe (KS) /General Obligation - Unlimited Tax/1 LT</td>
<td>LT AA+ Rating Outlook Stable Affirmed</td>
</tr>
<tr>
<td>Olathe (KS) /General Obligation - Unlimited Tax/1 ST</td>
<td>ST F1+ Affirmed</td>
</tr>
</tbody>
</table>

VIEW ADDITIONAL RATING DETAILS

FITCH RATINGS ANALYSTS

Endorsement Policy

ENDORSEMENT STATUS

Olathe (KS)  
EU Endorsed

DISCLAIMER

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS. IN ADDITION, THE FOLLOWING HTTPS://WWW.FITCHRATINGS.COM/RATING-DEFINITIONS-DOCUMENT DETAILS FITCH'S RATING DEFINITIONS FOR EACH RATING SCALE AND RATING CATEGORIES, INCLUDING DEFINITIONS RELATING TO DEFAULT. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH RATINGS WEBSITE.

READ LESS

COPYRIGHT

Copyright © 2020 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the
extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch’s factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be
changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001.

Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see https://www.fitchratings.com/site/regulatory), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

SOLICITATION STATUS

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.
ENDORSEMENT POLICY

Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the EU Regulatory Disclosures page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.