MOODY'S
INVESTORS SERVICE

New Issue: Moody's assigns Aa1 to Newport News, VA's $53.6M GO Bonds Series 2015

Global Credit Research - 01 Dec 2015

Affirms Aa1 on $383M outstanding GO debt

NEWPORT NEWS (CITY OF) VA
Public K-12 School Districts
VA

Moody's Rating

ISSUE		**RATING**
General Obligation General Improvement and Refunding Bonds, Series of 2015		Aa1
Sale Amount	$53,630,000	
Expected Sale Date	12/14/15	
Rating Description	General Obligation	

Moody's Outlook NOO

NEW YORK, December 01, 2015 --Moody's Investors Service assigns a Aa1 rating to the City of Newport News (VA) $53.6 million General Obligation General Improvement and Refunding Bonds Series 2015. Concurrently, Moody's has affirmed the Aa1 rating on $383 million of previously issued General Obligation debt.

SUMMARY RATING RATIONALE

The Aa1 rating reflects a diversifying tax base that is expected to exhibit long-term stability, satisfactory financial operations characterized by conservative budgeting and an elevated but manageable debt position.

OUTLOOK

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

WHAT COULD MAKE THE RATING GO UP

Significant increase in reserves and financial flexibility

Improved socioeconomic indicators

WHAT COULD MAKE THE RATING GO DOWN

Reduced reserves limiting financial flexibility

Inability to fully fund NNERF ARC

Substantially increased debt burden

Erosion of tax base size, population or income levels

STRENGTHS

Stable and diversifying local economy; anchored by stable military presence

Strong financial management

Fully funded pension ARC for Newport News Employee Retirement Fund (NNERF) in FY 16

CHALLENGES

Below average demographics

Elevated debt

Exposure to federal spending cuts

RECENT DEVELOPMENTS

Recent developments are incorporated in the detailed rating rationale section.

DETAILED RATING RATIONALE

ECONOMY AND TAX BASE: ROBUST LOCAL TAXBASE BEGINS TO SEE MODEST GROWTH; DIVERSIFICATION EFFORTS CONTINUE

The $16.3 billion tax base in Newport News continues to experience modest growth following years of consecutive decline as economic development and diversification efforts continue. The U.S. Army's Joint Base Langley-Eustis and Huntington Ingalls Industries, Inc. (Senior Unsecured rated Ba1/stable) account for a large percentage of the employment base, with more than 24,000 and 22,000 employees, respectively. While the Hampton Roads area remains exposed to sequestration and federal spending cuts, the city has seen a trend of recent investment from military installations. The Joint-Base Langley Eustis has invested $408 million since 2008 and has $200 million in projects planned through 2020. Additionally, the shipyard has $1.5 billion in new investment projected over the next 5 years.

The city continues efforts to diversify its base beyond the military industry and reports over $30 million in local investment from 2010 through 2015 and 33% of its employment base designated as "high end" manufacturing. Canon Virginia recently announced its plans for a $100 million expansion in the city and Continental Automotive Systems plans to invest $152 million and create more than 500 jobs. Jefferson Labs is near completion of its $310 million upgrade and continues as a strong employer, with 1200 scientists and 700 employees on the campus. Jefferson Lab projects an additional $1 billion in investment and nearly 4,000 jobs over the next decade. A number of mixed-use residential projects are also underway in Newport News. The city's Tech Center development, a $300 million mixed-use research, retail, residential and commercial project, is nearing completion of its $160 million first phase of construction.

The city's economic development efforts have spurred significant growth in recent years, boosting assessed values by 72% over the last 10 years (2003-2013). Due to the recent economic environment, annual assessed value growth has slowed from a high of 15.4% in fiscal 2007 to declining by 2% annually over the last five years. Modest growth has returned to the base with 0.27% growth in 2015 and 1.7% in 2016. Unemployment decreased to 4.9% from a high of 8.1% in 2011. Wealth levels are below both state and national medians, with per capita income representing 75.4% and 88.7%, and median family income representing 78.9% and 92% respectively, which is typical for Virginia jurisdictions with a strong military presence outside the more wealthy Washington, D.C. region.

FINANCIAL OPERATIONS AND RESERVES: CONSERVATIVE BUDGET MANAGEMENT DRIVES SOUND FINANANCIAL PERFORMANCE

Newport News' financial position is expected to continue to remain healthy over the medium term given a strong commitment to conservative budgeting and maintaining reserves. As a result of conservative revenue projections and expenditure controls, the city has realized operating surpluses in the last 3 fiscal years. The fiscal 2014 Operating Fund surplus of $3.6 million was driven largely by strong performance of tax revenues up nearly 1% over budget. Total fund balance increased to $98.8 million or 23.5% of 2014 revenues. Available fund balance grew to $87 million, or 20.8% of revenues.

The city realized another surplus for fiscal 2015, driven primarily by conservative budgeting of expenditures which came in $3 million below budget. Revenues also outperformed budget by just under $1 million due to higher tax collection and strong performance of economically sensitive tax revenues. Growth in city revenues have remained strong through the recession with 2.3% average growth in property tax revenue since 2007 and 2.6% growth in other local revenues (sales, meals, BPOL) over the same time period.

The fiscal 2016 budget grew by 3.7% (2.8% net of $4.1 million in grant funds) and includes a $3 million increase in the schools transfer and a $4 million appropriation of fund balance. The budget includes conservative assumptions for sales and meals tax growth and a 2.9% increase in real estate tax revenue growth.

Liquidity

The city's liquidity position remains strong with cash increasing in fiscal 2014 to $81.6 million or 19.4% of Operating Fund revenues. The net cash position has increased 3.3% over the last five years.

DEBT AND PENSIONS: ABOVE AVERAGE DEBT POSITION WITH MANAGEABLE FUTURE CAPITAL NEEDS

The city's overall debt burden, at 2.9% is elevated, although the burden remains manageable for the city. Amortization of debt is satisfactory and exceeds the city's 60% policy with 73% of principal repaid within 10 years. Despite anticipated future issuance to fund the city's capital improvement plan (CIP), the city plans to remain in compliance with all of its debt management policies, which require total tax-supported debt service to remain under 9.5% of expenditures (7.9% in fiscal 2015), and total debt under 3% of total taxable value. The city's fiscal 2016-2020 capital improvement plan totals $337 million in expenditures of which 43% will fund street and bridge projects. Approximately, $144 million, of the capital plan is expected to be funded with additional bond issues and $143 million will be funded with grants. Given active management of the city's capital plan and satisfactory principal amortization the city's debt load is expected to increase but remain manageable.

Debt Structure

Newport News has no exposure to variable-rate demand debt and all debt amortizes over the long-term.

Debt-Related Derivatives

Newport News has no exposure to variable-rate demand debt or derivative products.

Pensions and OPEB

In 2010, the city adopted a pension reform package to not only address the low funded ratio of the Newport News Employee Retirement Fund (NNERF), but also to reduce the city's future liability. Some of the major changes to the pension plan include closing the fund to new hires and rehires for all School Board personnel and city employees, who will now be entered into the Virginia Retirement System (VRS). In addition, the city's strategy included annual incremental increases in the city's contribution with a goal of reaching the full ARC by fiscal 2017. However, the city funded 100% of the $35.4 million ARC in fiscal 2016, one year ahead of schedule. The city plans to fully fund the ARC going forward. Any failure to do so could result in negative credit pressure.

In addition to NNERF, the city, schools and airport contribute to VRS, an agent, multiple employer defined benefit pension plan administered by the Commonwealth. The city contributed 100% of the ARC for both plans. The city's combined adjusted net pension liability (ANPL), under Moody's methodology for adjusting reported pension data, is $1 billion, or an above average 2.29 times operating revenues. The three year average of the city's ANPL to Operating Revenues is an above average 2.32 times, while the three-year average of ANPL to full value is also an above average 6.31%. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities.

The city also provides Other Post- Employment Benefits (OPEB) to city and school employees. In fiscal 2014 the city contributed 86% of its annual OPEB costs (up from 64% in 2013) and 98% of the schools OPEB costs. Overall, fixed costs including annual pension, OPEB and debt service expenditures summed to a slightly elevated 29% of fiscal 2014 expenditures, however the ratio drops to 17% when accounting for obligations paid by user fees, outside funds and other outside resources. Going forward, if the city is not able to maintain its solid reserve levels due to these increasing long-term obligations, negative credit pressure is possible.

MANAGEMENT AND GOVERNANCE

Newport News' strong financial position is supported by a history of conservative budgeting. Continued adherence to financial policies and a commitment to multi-year financial forecasting will position the city favorably for strong operations.

Virginia cities have an institutional framework score of "Aaa" or very strong. Cities rely on property taxes to support operations, providing for high revenue raising flexibility as property taxes are unlimited. Expenditures, which are primarily for education, are predictable and counties have the ability to reduce expenditures if necessary.

KEY STATISTICS

-2015 Full valuation: $16.3 billion

-2015 Full value per capita: $89,193

-Median family income as a % of US: 92%

-Fiscal 2014 Available Operating Fund balance: 20.8% of revenues

-Five-year Dollar Change in Operating Fund balance as a percent of revenues: -1.54%

-Fiscal 2014 Net Operating cash balance: 19.4% of revenues

-Five-year Change in Cash Balance as a percent of revenues: 3.32%

-Institutional Framework: Aaa

-Operating History (Five-year average of operating revenues/operating expenditures): 1.00x times

-Net Direct Debt / Full Value: 2.9%

-Net Direct Debt / Operating Revenues: 1.10 times

-Three-year Average of Moody's ANPL/Full Value: 6.31%

-Three year Average of Moody's ANPL/Operating Revenues: 2.32 times

OBLIGOR PROFILE

Newport News is located in the Hampton Roads MSA. The city is home to a number of stabilizing military institutions and has a population of 182,965.

LEGAL SECURITY

Debt service is secured by the city's unlimited general obligation tax pledge.

USE OF PROCEEDS

The 2015 new money bonds will finance various city-wide CIP projects including solid waste, storm water and waste water system improvements and other items. The $4.7 M refunding bonds will advance refund the series 2006 EDA bonds for an expected net present value savings of 9.9% without extending debt maturity.

PRINCIPAL METHODOLOGY

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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