S&P Global
Ratings

RatingsDirect®

Summary:

Los Angeles County; Appropriations; General Obligation

Primary Credit Analyst:
Jennifer Hansen, San Francisco + 1 (415) 371 5035; jen.hansen@spglobal.com

Secondary Contact:
Bianca Gaytan-Burrell, Centennial + 303-721-4617; bianca.gaytan-burrell@spglobal.com

Table Of Contents

Summary:

Los Angeles County; Appropriations; General Obligation

Credit Profile		
US$250.18 mil lse rev bnds ser 2021 F due 12/01/2051		
Long Term Rating	AA+/Stable	New
US$221.475 mil lse rev rfdg bnds ser 2021 G due 12/01/2042		
Long Term Rating	AA+/Stable	New
Los Angeles Cnty ICR		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings revised its outlook to stable from negative and affirmed its 'AAA' issuer credit rating (ICR) on Los Angeles County, Calif., and its 'AA+' long-term rating and underlying rating (SPUR) on the county's existing appropriation debt. At the same time, S&P Global Ratings assigned its 'AA+' long-term rating, with a stable outlook, to the Los Angeles County Public Works Financing Authority's 2021 series F lease revenue bonds (green bonds) and 2022 series G (forward delivery).

The outlook revision reflects our view that the county has been able to weather the COVID pandemic and resulting recession without the use of reserves and in fact has been able to add to reserves due to prudent financial management and federal stimulus dollars. Although the county unemployment rate remains high, we expect it will moderate in the next year and the county will maintain very strong reserves over the near term, as it was able to build reserves instead of draw on them as originally budgeted and expected for fiscal 2021.

The 2021 series F and 2022 series G bonds are secured by semiannual lease payments made by the county to the authority. The leased assets are sufficient to support debt service on the series F and G bonds. Lease payment are payable from all available funds of the county and are subject to annual appropriation. The county is not funding a debt service reserve for the bonds; however, the debt service payments are well after the beginning of the county's fiscal year, mitigating the risk of non-appropriation due to late budget adoption. Lease payments are subject to abatement in the event of loss of, damage to, destruction of, or theft of the leased equipment, and the county covenants to maintain 24 months of rental interruption insurance to offset abatement risk. All leased assets under the master lease meet our criteria for seismic risk during the life of the obligation. The 2021 series F bonds are being issued to finance and refinance the cost of several capital improvement projects, including the MLK Behavioral Health Center, MLK Central Plant 1 and Hospital Services Building, LAC + USC Medical Center Recuperative Care Center, Olive View Campus Recuperative Care Center, Rancho Los Amigos Recuperative Care Center, and Fire Station 104 (Santa Clarita). The 2022 series G bonds will be sold as forward delivery bonds and be used to refund the series 2012 bonds in 2022.

The ICR reflects our view of the county's general creditworthiness and does not incorporate the features of any particular debt instrument.

Our issue ratings are based on our view that the county's general creditworthiness is above that of the U.S. sovereign. This reflects our view that the county would not default in a stress scenario likely to accompany a sovereign default given autonomy from sovereign intervention. We view the county as exhibiting relatively low funding interdependency with the federal government, as local taxes represent the vast majority of total governmental funds revenue. However, consistent with our view that U.S. state and local governments are moderately sensitive to country risk, we would be unlikely to set ratings on the county's obligations more than two notches above the U.S. sovereign rating.

Credit overview

The county's financial performance for fiscal 2021 and budget for fiscal 2022 have improved meaningfully since our last review in October 2020. Due to prudent management and significant ($3 billion) in federal stimulus moneys, the county's financial position was stable throughout fiscals 2020 and 2021 and is projected to remain stable in fiscal 2022. At the national level, S&P Global Economics believes that the recovery continues but may be slowing down. For more information on our view of the U.S. economy, please see our report, "Economic Outlook U.S. Q4 2021: The Rocket Is Leveling Off," published Sept. 23, 2021, on RatingsDirect. We believe that the trajectory forward is still somewhat uncertain given the delta variant of COVID-19, but 68% of county residents 12 and over are fully vaccinated and 76.3% have received at least one dose of the vaccine, rates significantly above the national averages of 55.6% and 64.5%, respectively. This has helped county residents to control the number of COVID-19 cases reported across the county during the past few months and eased some of the burden that the county's Department of Health Services (DHS) has experienced throughout the pandemic.

The ratings reflect our view of the county's:

- Adequate economy, with access to a broad and diverse metropolitan statistical area (MSA), but a high county unemployment rate exceeding 10%;
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with balanced operating results in the general fund and an operating surplus at the total governmental fund level in fiscal 2020;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2020 of 17% of operating expenditures;
- Very strong liquidity, with total government available cash at 42.4% of total governmental fund expenditures and 20.1x governmental debt service, and access to external liquidity we consider exceptional;
- Strong debt and contingent liability profile, with debt service carrying charges at 2.1% of expenditures and net direct debt that is 7.0% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value, but a large pension and other postemployment benefit (OPEB) obligation and the lack of a plan to sufficiently address the obligation; and
- Strong institutional framework score.

Environmental, social, and governance (ESG) factors

We analyzed the county's ESG risks relative to its economy, management, financial measures, and debt-and-liability profile. Although wildfires have affected California, we do not consider fire within the county an immediate risk. The county also has elevated exposure to seismic risk; however, we believe this risk is mitigated in part by strong state building codes. Absent the implications of COVID-19, we consider the county's ESG risk to be in line with our view of the sector standard.

Stable Outlook

Downside scenario

Should the county's operations significantly deteriorate, with a weakening of both budgetary performance and flexibility, we could lower the ratings. We could also lower the ratings if the county's hospital and medical center operations deteriorate, weakening general fund performance. A weakened local economy, as demonstrated by persistently high unemployment rates above 10%, or pension and OPEB increases without corresponding increases in revenues or expenditure reductions, could also pressure the ratings.

Credit Opinion

Adequate economy

We consider the county's economy generally strong although currently experiencing reduced activity levels and high unemployment driven by social distancing and local business closures. With an estimated population of 10.1 million, Los Angeles County is in the Los Angeles-Long Beach-Anaheim, Calif., MSA, which we consider broad and diverse. The county has a projected per capita effective buying income of 96.6% of the national level and per capita market value of $174,000. However, the county's unemployment rate remains above 10% as of August 2021, but well below the 17.2% for August 2020. This remains substantially elevated when compared with the annual unemployment rate of 4.4% in 2019. During the prior recession, unemployment rose to 11.5% in 2009 and remained above 10% through 2012. We understand that the county utilizes the UCLA Anderson Forecast, which predicts that the county's unemployment rates will remain above 10% for 2021 before declining to around 9% in 2022 and about 8% in 2023.

Los Angeles is the largest county in the U.S., by population. Assessed value (AV) has grown since fiscal 2011, with a 3.7% increase for fiscal 2022. Like much of the California real estate market, home sales in the county have been very strong and overall home prices have increased significantly. The county experienced only a relatively minor dip in AV during the prior recession, a reflection of its large and mature property tax base coupled with Proposition 13 limitations on AV growth.

Similar to other large coastal areas of California, the county's housing prices and lack of affordable housing are a continuous concern. There are some indications that, although the housing market is not retracting, growth is slowing. Management indicates that some slowdown may be beneficial to the county, as more residents are able to purchase homes; additionally, a large number of homes are assessed under 1975 valuations due to Prop 13, and therefore any turnover will be beneficial to county revenue.

The county has a large and growing technology sector known as the Silicon Beach, with more than 500 technology startup companies and major employers such as Google, Yahoo!, YouTube, BuzzFeed, Facebook, Salesforce, AOL, and Electronic Arts. The county also has a very large entertainment industry with major movie studios, television networks, recording studios, video game developers, publishers, and artists.

Very strong management

We view the county's management as very strong, with strong financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

The county uses state economic data and actual historical trends in revenue forecasting and reviews expenditures and revenue against budget monthly. It prepares a five-year revenue and expenditure forecast, as well as a seven-year long-term capital plan. The county has adopted a debt management plan and a written investment policy and prepares monthly investment performance reports that it submits to the county board. The county has set a goal of building 10% of locally generated revenues in a "rainy day" and economic reserve, and has budgeted a $53.5 million deposit in fiscal 2021 that will increase the rainy day fund balance to $695.9 million. Management also has a policy of setting aside 5%-10% of its discretionary revenue for contingencies, and has set aside about 10% for the past several years.

Strong budgetary performance

Los Angeles County's budgetary performance is strong, in our opinion. The county has produced consistent surplus operating results in the general fund and across all governmental funds during the past three audited fiscal years, we anticipate that it will likely report additional surpluses in both fiscals 2021 and 2022.

Management reports fiscal 2021 ended significantly better than budgeted. While the county had planned on using $197 million of reserves to help balance its budget, it ended the year increasing its reserves and adding to its rainy day reserve, which is expected to reach 10% in fiscal 2021. Management reports that sales taxes did not decrease as significantly as budgeted and concerns that DHS would become a drag on the general fund did not materialize due to federal and state funding continuing unabated. The county also received $1.1 billion in CARES Act money that supported programs to offset the significant economic losses caused by stay-at-home orders and subsequent business closures.

The county's budgets tend to be conservative, underestimating tax growth and overestimating expenditures. The adopted 2022 budget is based on the fiscal 2021 budget which had eliminated 2,556 budgeted positions but includes 315 additional positions due to some expected revenues increase. The budget is basically balanced and reduces a projected budget gap to $11 million from $50 million. Management expects that the budget gap will be closed by the end of fiscal 2022. Additionally, the budget does not include $1.9 billion of American Rescue Plan (ARP) stimulus money that will be incorporated in future budgets, as the board of supervisors is currently reviewing potential allocations of ARP. The county plans to add again to its rainy day fund in fiscal 2022. County officials generally focus on balancing ongoing revenue with ongoing expenditures, and in 2017 received voter approval for a 10-year, 25-cent dedicated sales tax to fund homelessness initiatives.

While unlikely given the current federal administration, we understand that changes to federal health care spending could pressure operations, given the size of the county's health services department. The 2022 budget does not anticipate an increase in net county cost to subsidize the DHS fund; however, a significant federal overhaul of the

Affordable Care Act (ACA) could result in a cut to state and federal support for health services, which would be a challenge for the county. Since the advent of ACA, uninsured inpatient visitors fell below 10% as compared to about 25% prior to the implementation of ACA. This risk is somewhat mitigated, by the county's buildup of reserves in the DHS fund to $987 million and expectations to further grow these in fiscal 2022. In recent years, management has restructured DHS from a hospital-based to an integrated ambulatory care system, which we believe could position the county better than many to minimize the cost of adapting to changes in health care funding.

General fund and governmental fund revenue and expenditures were adjusted to account for recurring transfers to and from the county's hospital funds. In addition, the general fund expenditures were adjusted to account for recurring transfers to the library and various debt service funds. Taxes (primarily property taxes) represented about 30% of the audited fiscal 2020 general fund revenue. The county's other major revenue streams were intergovernmental revenue from the federal government (20%) and state government (32%). Charges for services represented another 13%. Other smaller revenue sources included fines and forfeitures.

Very strong budgetary flexibility

In our view, the county's budgetary flexibility is very strong. The county was able to prudently set aside funds into reserves during the past several years, and while management had planned to use $197 million of one-time trust accounts to balance the budget in fiscal 2021, the county reports that it was able to end fiscal 2021 with another surplus. It expects reserves to increase again in fiscal 2022. According to the county's audited financial statements, it ended fiscal 2020 with $3.7 billion of reserves, equivalent to 17.3% of general fund expenditures. The county was able to add to its rainy day reserve in fiscals 2020 and 2021 and is projected to reach its 10% reserve policy in fiscal 2021.

A significant credit risk was the county DHS, which in previous years had encroached upon the general fund. Moreover, the COVID pandemic, coupled with an uncertain federal payment system, could have necessitated general fund support for the system. However, state and federal funding has continued, and DHS has increased its fund balance to over $987 million in fiscal 2021 and to a projected $1.25 billion in fiscal 2022.

Very strong liquidity

In our opinion, Los Angeles County's liquidity is very strong, with total government available cash at 42.4% of total governmental fund expenditures and 20.2x governmental debt service in 2020. In our view, the county has exceptional access to external liquidity if necessary.

Supporting our view of the county's exceptional access to liquidity is the fact that the county has issued various types of debt in the past 15 years, including lease revenue bonds, commercial paper (CP), assessment debt, and tax and revenue anticipation notes. In April 2019, the county restructured the LACCAL Lease Revenue Note Program, which consists of four separate bank letter of credit and reimbursement agreements authorizing the issuance of separate series of notes by each bank up to a maximum aggregate principal amount of $600 million. The county has $507.4 million of CP outstanding under this program.

While the state allows for what we consider permissive investments, the county's own adopted investment policy is more conservative, and its current portfolio consists primarily of investments that we consider low risk, such as U.S. Agency securities, certificates of deposit, and CP with an 'A-1' rating.

Strong debt and contingent liability profile

In our view, Los Angeles County's debt and contingent liability profile is strong. Total governmental fund debt service is 2.1% of total governmental fund expenditures, and net direct debt is 7.0% of total governmental fund revenue. Overall net debt is low at 2.3% of market value, which is in our view a positive credit factor. Given the county's large size and rapid amortization, we do not expect that this will weaken its debt metrics.

The county does not have definitive debt plans over the next year or two, but will be doing a significant remodel of its Harbor-UCLA center, which will be a $1 billion-$2 billion project. The timing and financing of this project are somewhat uncertain, but management expects it will continue its practice of utilizing CP before issuing a long-term obligation.

Pension and OPEB liabilities:

In our opinion, a credit weakness is Los Angeles County's large pension and OPEB obligation, without a plan in place that we think will sufficiently address the obligation. Los Angeles County's combined required pension and actual OPEB contributions totaled 10.9% of total governmental fund expenditures in 2020. Of that amount, 7.2% represented required contributions to pension obligations, and 3.7% represented OPEB payments. The county made its full annual required pension contribution in 2020, which exceeded our calculation for static funding, but fell short of our calculation for minimum funding progress.

County employees participate in the Los Angeles County Employees Retirement Assn., a cost-sharing multiple-employer plan that includes six employers, including the county and the Los Angeles Superior Court. The Governmental Accounting Standards Board funded ratio is 76.4%, which we consider adequate, and is based on a discount rate of 7.00%, which is lower than the 7.25% national average but well above S&P Global Ratings' guidance for a 6.0% rate.

We expect retirement liabilities to be a growing cost pressure due largely to a high discount rate, which puts pressure on investment returns to reduce annual contributions and could add volatility and budgetary strain. The county's actuarially determined contribution (ADC) is based on a 30-year, layered, level 3.25% of payroll amortization method, which we consider very aggressive. This method creates negative amortization, which means unfunded liabilities will likely grow in the near to medium term before large deferred contributions begin to pay it down.

We believe management is addressing the rising cost of retiree benefits. The county has been prefunding an OPEB trust for the past five years, but not at full ADC levels. The plan is under 5% funded, and the county expects to fully fund its OPEB ADC by fiscal 2028, which should increase funding over time. Until the ADC is funded, costs will continue to be deferred. Management has a multiyear plan to address the county's OPEB unfunded liability, including nominal ad hoc contributions in the past as well as liability management. After negotiations regarding new employees in 2018, dependents will no longer be included in retiree health benefits, which should reduce costs significantly, although affordability is still questionable given the continuing rapid increase to health care costs.

Strong institutional framework

The institutional framework score for California counties required to submit a federal single audit is strong.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 2020 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of September 30, 2021)		
Los Angeles Cnty (dept of pub social svcs facs) (AMBAC)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
Los Angeles Cnty (Disney Concert Hall Pkg Garage)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty (Multi Cap Proj II)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty (MLK Hosp Proj)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty Cap Asset Lsg Corp, California		
Los Angeles Cnty, California		
Los Angeles Cnty Cap Asset Lsg Corp lse rev bnds (Los Angeles Cnty)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty Facs Inc, California		
Los Angeles Cnty, California		
Los Angeles Cnty Facs Inc (Los Angeles Cnty) (Vermont Corridor Cnty Admin Bldg)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty Facs Inc (Los Angeles Cnty) (Vermont Corridor Cnty Admin Bldg)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty Pub Wks Fing Auth, California		
Los Angeles Cnty, California		
Los Angeles Cnty Pub Wks Fing Auth (Los Angeles Cnty) lse rev bnds (Los Angeles Cnty) ser 2020A due 12/01/2050		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty Pub Wks Fing Auth (Los Angeles Cnty) (Master Rfdg Proj)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty Pub Wks Fing Auth (Los Angeles Cnty) (Multi Cap Proj I)		
Long Term Rating	AA+/Stable	Affirmed
Los Angeles Cnty Pub Wks Fing Auth (Los Angeles Cnty) (Multi Cap Proj I)		
Long Term Rating	AA+/Stable	Affirmed
Sonnenblick-Del Rio El Monte Asset Lse Corp, California		
Los Angeles Cnty, California		
Sonnenblick-Del Rio El Monte Asset Lse Corp (Los Angeles Cnty) (AMBAC)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.