

RatingsDirect®

Summary:

Mississippi Development Bank Jackson; Sales Tax

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US\$33.675 mil spl oblig bnds (Jackson) ser 2020 due 12/01/2030

Long Term Rating

A/Stable

New

Rating Action

S&P Global Ratings assigned its 'A' long-term rating to the Mississippi Development Bank's \$33.2 million series 2020 special obligation bonds, issued for the City of Jackson. The outlook is stable.

The bonds are payable from and secured by the proceeds of a special 1% sales tax levied on the gross proceeds of sales or gross income of certain businesses located in the city. We rate the bonds under our priority lien criteria, which factors in both the strength and stability of the pledged revenue as well as the general credit quality of the municipality where taxes are distributed and collected (the obligor's creditworthiness). Proceeds of the bonds will be used for various purposes, including for road/street improvements as well as for water/sewer and drainage projects throughout the city.

Credit overview

As Jackson is home to the state capital and a large government, higher education, and health care presence, 'its economy should provide credit stability during the coming economic recession. The stable outlook reflects our view that, given historical collections of the 1% tax providing adequate-to-strong coverage of maximum annual debt service (MADS), the city is well positioned to withstand any declines in pledged revenue associated with the COVID-19 pandemic and the ensuing economic shutdown within the city. While the impacts from the shutdown are not yet quantifiable, pledged revenue could withstand a sustained 71% decline in collections before reaching levels insufficient to fulfill pro forma debt service. Furthermore, given what we consider low revenue volatility, we do not expect pledged revenue to be sustained at significantly weaker levels. While we continue to monitor events related to COVID-19, we do not expect them to affect the city's ability to pay debt service on the bonds. Given these expectations, we do not expect to change the rating over our two-year outlook horizon.

The rating reflects our view of the city's:

- Adequate-to-weak local economy that otherwise benefits from the stabilizing influence of a strong government, health care, and higher education presence;
- Adequate coverage provided by fiscal 2019 pledged revenue, equal to 3.45x pro forma MADS; and
- Low revenue volatility on the broad-based special sales tax.

Stable Two-Year Outlook

Upside scenario

We could consider a higher rating if pledged tax collections were to remain well above the additional bonds test (ABT) for a sustained period, despite the coming economic recession.

Downside scenario

Conversely, we could consider a lower rating if the economic recession results in pledged revenue collections exhibiting extreme volatility and weaker coverage, or if the recession resulted in material deterioration of the city's economic profile.

Credit Opinion

Economic fundamentals: Adequate-to-weak

As the state's capital and largest city, Jackson serves as Mississippi's economic and cultural center. The city is also a regional educational and medical hub, with several institutes of higher education as well as multiple hospitals or medical centers located within the city, including the University of Mississippi Medical Center. We consider the strong presence of government, health care, and educational sectors as stabilizers for the city's economy. Officials estimate approximately 40% of real property within the city's jurisdictional boundaries is nontaxable, resulting in an understatement of estimated market values and, by extension, market values per capita that are characteristically very weak.

Despite these stabilizing institutions, Jackson continues to see declining population, with estimates of more than 5% decline since the 2010 Census. Furthermore, resident incomes within the city remain depressed, with per capita effective buying income equal to 60.6% of the national level. In an effort to reverse the population declines and to bring higher paying jobs, the city has implemented a number of programs to drive redevelopment, including the use of grants and other initiatives to support private investment throughout the city. Recently completed projects include a \$140 million hospital expansion that added beds and jobs, several multifamily housing developments, office renovations, and commercial expansions. While economic activity within the city remained robust before the economic slowdown from COVID-19, we will monitor the city's recovery once social distancing restrictions are lifted.

Coverage and liquidity: Adequate

Approved by a majority of voters in 2014, the city's special 1% infrastructure sales tax began collections in August 2014 and will expire on July 1, 2035. So far, collections in each full fiscal year have exceeded \$14 million annually, with the most recent year of collections, fiscal 2019, providing pledged revenue of \$14.5 million. The special sales tax can be used only for purposes approved by voters, specifically for the improvement of infrastructure within the city. While this restriction means that the city cannot use tax collections for general operating purposes, it also means that the city could be incentivized to issue additional bonds in the future to complete authorized improvements. Therefore, we have used the ABT as our baseline assessment of coverage. The bonds require that the tax revenue during the latest audited fiscal year, or any 12 consecutive months of the 18 months immediately preceding additional issuance, provide coverage of pro forma MADS equal to no less than 1.5x.

Despite using the ABT as our baseline assessment of coverage, we note that fiscal 2019 collections of \$14.5 million provide MADS coverage of 3.45x (scheduled to occur in fiscal 2022). Furthermore, we note that debt service is largely level through maturity in fiscal 2030. Providing additional liquidity, the bonds will benefit from a debt service reserve fund maintained at the least of MADS, 125% of average annual debt service, and 10% of par. While the city reports no additional near-term parity debt plans, the bonds were structured to provide the ability to issue additional debt outside of our outlook horizon (two-plus years).

Low revenue volatility

Our macro volatility assessment begins with an assessment of the historical volatility of the economic activity being taxed, and includes an analysis of societal, demographic, political, and other factors that could affect these activities. Based on the variance of national economic activity that we believe most closely represents the taxing base over multiple economic cycles, the assessment informs our opinion on expectations of volatility. To determine our view of the volatility of hospitality taxes, we used estimated sales of U.S. accommodation firms' data from the U.S. Census Bureau for the period 1993 to 2014.

On a micro level, we see no additional factors that would lead us to believe that pledged collections within the city are more or less susceptible to volatility experienced at the macro level. Although collections have varied somewhat over the five years of collections, the variations have been minimal. While the COVID-19 pandemic response is expected to result in a material deterioration of pledged revenue, we expect that the recovery will likely begin sometime late in the city's fiscal 2020.

Obligor linkage: Close

The state collects the special sales tax and remits them to the city on a monthly basis. The city then deposits one-sixth of the upcoming interest payment and one-12th of the upcoming principal payment before releasing excess funds not needed to restore the reserve fund to the city's 1% Infrastructure Tax Capital Project Fund. Given that pledged revenue flows to the city before being deposited with the trustee, we believe that pledged revenue is exposed to operating risk and that bond provisions are less restrictive with respect to revenue collection and distribution. We believe this increases the linkage between the priority lien pledge and the obligor's creditworthiness, which informs our opinion of the degree of exposure of the pledged revenue stream to operating risks of the obligor's creditworthiness.

Rating linkage to the City of Jackson

We assess the city's general operations because we view overall creditworthiness a key determinant of obligor's ability to pay all of its obligations, including bonds secured by a special tax. While the city has seen continued tax base growth over the years, the growth has largely been modest. However, the same stabilizing institutions that support the economic base of sales tax collections also benefit the city's general economic profile. Recent improvement in financial operations increased available general fund reserves to \$26.4 million, representing 24% of expenditures, in fiscal 2018. However, operating pressure as a result of billing issues for the city's utility funds has resulted in interfund borrowing and stressed enterprise fund liquidity. Favorably, a recent lawsuit settlement should provide a much needed infusion of cash to the utility funds and will repay the general fund advances. While the coming recession will reduce the city's operating revenue, we believe that the city has demonstrated the ability and willingness to adjust expenditures to ensure that its financial profile remains adequate. However, with elevated fixed costs related to debt and pension/other postemployment benefit expenses, the city may experience weaker budgetary performance over the

next one to two years.

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