

**Financial and Credit Rating Status Update
for the
City of Portsmouth, Virginia**

Prepared By
Davenport & Company LLC
Member NYSE • FINRA • SIPC

January 12, 2021

Davenport's Role for the City

- Davenport serves as Financial Advisor to the City in the following ways, amongst others:
 - Reports to the City Council and senior City Staff;
 - Complements City Staff with annual Budgetary Planning, Capital Planning, Financial Policy review/development and other comprehensive Financial Strategies and Planning (*i.e. Economic Development and Utility Related, amongst others*); and
 - Interacts with the National Credit Rating Agencies on behalf of the City.
- At the direction of the City, Davenport helps to determine the most cost-effective and flexible method of financing for capital projects based on the type of project, market conditions, and the projected impact of the project on the City's financial/credit standing.
- Davenport reviews the City's outstanding Debt Portfolio for potential Refinancings and alerts the City to potential savings opportunities. Davenport has served as Financial Advisor to the City on Refinancing transactions that have resulted **total savings of more than \$40 million.**
- Davenport does not:
 - Determine which projects are to be financed;
 - Underwrite any bond issue; or
 - Hold a financial interest in how a project is funded.

Credit Rating Overview

- The City maintains Credit Ratings from the three primary Rating Agencies:
 - Moody's;
 - Standard & Poor's ("S&P"); and
 - Fitch.

- Credit Ratings are important for a local government for a variety of reasons including:
 - They are a primary factor in determining the interest rate(s) the City receives when it borrows for New Money projects or to Refinance existing debt;
 - They are a barometer for the Financial and Economic health of a local government; and
 - They send a signal to potential economic development prospects about the management and economy of a local government as they determine where to locate economic development projects.

Current Credit Ratings

- Moody's Aa2, Stable Outlook (August, 2020)

- S&P AA, Stable Outlook (July, 2020)

- Fitch AA, Stable Outlook (July, 2020)

Current Credit Ratings (cont.)

	<u>Moody's</u>	<u>S&P</u>	<u>Fitch</u>		
Top Tier "Highest Possible Rating"	Aaa	AAA	AAA		
2 nd Tier "Very Strong"	Aa1	AA+	AA+	(Highest)	Considered Investment Grade
	Aa2	AA	AA	(Middle)	
	Aa3	AA-	AA-	(Lowest)	
3 rd Tier "Strong"	A1	A+	A+	(Highest)	
	A2	A	A	(Middle)	
	A3	A-	A-	(Lowest)	
4 th Tier "Adequate Capacity to Repay"	Baa1	BBB+	BBB+	(Highest)	
	Baa2	BBB	BBB	(Middle)	
	Baa3	BBB-	BBB-	(Lowest)	
5 th – 10 th Tiers "Below Investment Grade"	BB, B, CCC, CC, C, D				Below Investment Grade

Key Credit Rating Drivers

- Four elements Rating Agencies measure:
 1. Economy (*Approximately 30% of rating*)
 2. Finances / Fund Balance (*Approximately 30% of rating*)
 3. Debt and Long Term Liabilities (*Approximately 10% to 20% of rating*)
 4. Management (*Approximately 20% of rating*)

Note: Approximate weighting of each factor pertains to Moody's and S&P. Fitch does not publish a specific scorecard noting weighting by category.

Moody's Commentary, 2019

- Factors that could lead to an **upgrade**
 - » Continued ability to maintain an adequately funded pension program without budget or balance sheet deterioration
 - » Substantial increase in tax base
 - » Sustained improvement in financial performance
 - » Decreased debt burden
- Factors that could lead to a **downgrade**
 - » Inability to sustain improved funding of pension plan
 - » Reduction in reserve levels
 - » Significant increase in fixed costs and debt burden
 - » Tax base contraction or increased concentration

Source: Moody's August 1, 2019 Credit Opinion for Portsmouth

S&P Commentary, 2019

- **Outlook**

The stable outlook reflects S&P Global Ratings' opinion that Portsmouth will likely continue to maintain balanced operations and its strong finances due to its very strong management policies and practices. The area remains a vital part of the nation's defense infrastructure based on the location of key military and commercial ports. As such, we do not expect the rating to change within the outlook's two-year horizon.

- **Upside Scenario**

If continued economic development in the area leads to improved wealth and income levels, comparable with those of its higher rated peers, while keeping all other factors constant, we could raise the rating.

- **Downside Scenario**

If the city were to significantly decrease reserves due to weak budgetary performance, without a plan to address the draws, we could lower the rating.

Source: S&P August 1, 2019 Rating Report for Portsmouth

Fitch Commentary

- **Analytical Conclusion**

The 'AA' Issuer Default Rating (IDR) and GO rating reflect Fitch Ratings' expectation that the city will maintain a high level of financial flexibility throughout economic cycles, underpinned by its healthy reserve cushion, ample revenue-raising ability and a moderate fixed-cost burden and the city's elevated long-term liability burden.

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Summary Rating Strategies (cont.)

- **Long-Term Obligations**

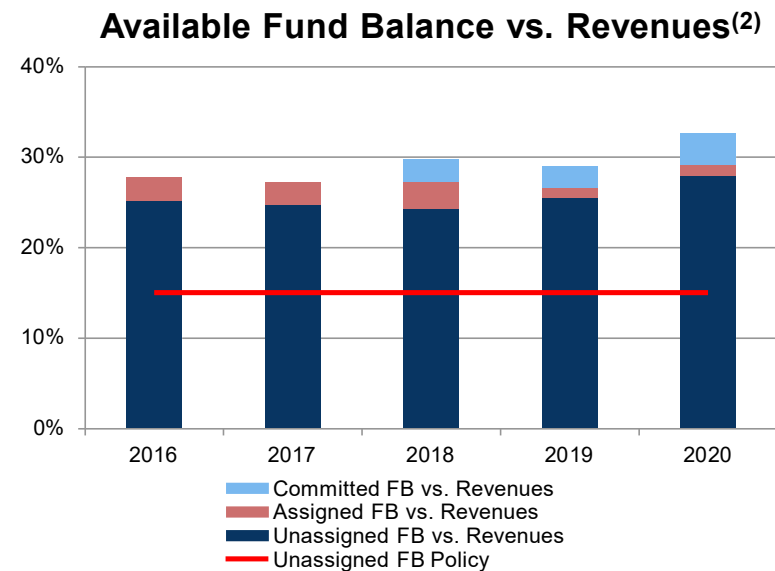
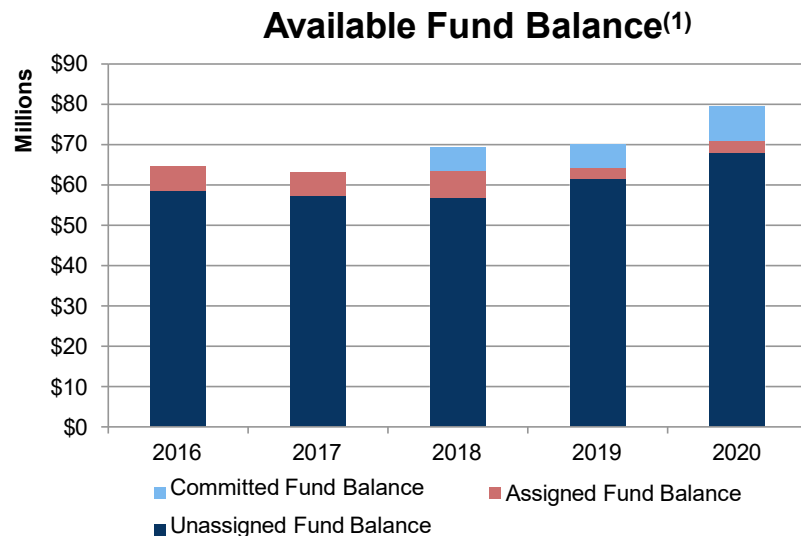
- Maintaining tax supported debt within policy limits is critical.
- Maintaining Utility Enterprise Funds that are self-supporting and not reliant on General Fund support insulates the General Fund from the long-term debt and other obligations of those funds (most notably Water/Sewer).
- Focusing on maintaining/enhancing the funded status of the City's two closed pension systems is of critical importance especially given the City's 2013 POBs.
- Continuing work to manage/limit the City's level of other long-term liabilities (OPEB, VRS obligations) is another critical factor.
- Making strategic investments in capital infrastructure helps to manage/limit the long-term cost of deferred capital maintenance.

- **Management**

- Continued focus on maintaining compliance with financial policy guidelines demonstrates a focus on responsible long-term financial management.

General Fund Balance vs. Policy

- The City's General Fund Balance has historically been solid and in compliance with the adopted Financial Policy Guidelines.
- The solid Fund Balance levels have been a counterbalance to other City credit challenges (i.e. pension funding and debt levels).



(1) Available Fund Balance consists of Assigned, Committed, and Unassigned Fund Balance.

(2) For purposes of calculating Fund Balance Policy, Revenues consist of General Fund Revenues and Transfers In to the General Fund.

Source: Annual audited financial reports.

2021 General Obligation Public Improvement and Refunding Bonds

- The City has identified the need to obtain approximately \$45 million of debt funding in support of the City's previously adopted multi-year Capital Improvements Program for the General Government.
- In addition, Davenport identified the opportunity to refinance approximately \$56 million of existing debt for debt service savings purposes (i.e. reduce the interest cost without any extension of debt maturity).
- These two needs will be combined into a single issuance that is planned to be sold in the next 60 days in order to take advantage of the historically low interest rate environment.
- Additional detail will be provided to City Council in advance of the planned public hearing in mid-February.
- A time-schedule is included on the following page.

Next Steps

- January 12, 2021
 - Davenport presents the Financial and Credit Rating Status Update to City Council.
- Balance of January, 2021
 - City Staff, Davenport, and Bond Counsel (McGuireWoods) prepare materials for the upcoming sale of the 2021 General Obligation Refunding and New Money Bonds (the “2021 GO Bonds”).
- Week of February 15
 - Conference calls with National Credit Rating Agencies.
- February 16, 2021
 - **Regular Meeting of City Council**
 - City Council holds a Public Hearing authorizing the issuance of the 2021 GO Bonds.
- By February 26
 - Receive updated credit ratings.
- Week of March 1
 - Sell the 2021 GO Bonds.
- By March 31
 - Close on 2021 GO Bonds.

Note: The 2021 GO Bonds will be issued to fund previously approved capital projects for the General Government (i.e. not utility enterprise supported). Staff and Davenport are also actively reviewing the multi-year capital funding plan for the Utility Enterprise Funds and will report back to City Council during the first quarter of the calendar year with an update on the Utility Enterprise Funds.

Appendix – Credit Rating History

Credit Rating History

General Obligation Credit Rating History						
Date	Moody's		Standard & Poor's		Fitch Ratings	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
February 1971	A	--	--	--	--	--
October 1975	A1	--	--	--	--	--
January 1987	A1	--	AA-	--	--	--
February 1994	A1	--	AA-	Stable	--	--
May 1995	A	--	AA-	Stable	--	--
September 1997	A3	--	AA-	Stable	--	--
December 1997	A3	--	AA-	Stable	A+	--
May 2000	A3	--	AA-	Stable	AA-	--
April 2001	A1	Stable	AA-	Stable	AA-	--
June 2001	A1	Stable	AA-	Stable	AA-	Stable
December 2003	A1	Stable	AA-	Stable	AA-	Negative
October 2005	A1	Stable	AA-	Stable	AA-	Negative
July 2006	A1	Stable	AA-	Stable	AA-	Stable
March 2009	A1	Stable	AA-	Negative	AA-	Stable
February 2010	A1	Stable	AA-	Stable	AA-	Stable
May 2010	Aa2	Stable	AA-	Stable	AA	Stable
November 2010	Aa2	Stable	AA	Stable	AA	Stable
June 2011	Aa2	Stable	AA	Stable	AA	Stable
March 2012	Aa2	Stable	AA	Stable	AA	Stable
December 2012	Aa2	Stable	AA	Stable	AA	Stable
May 2013	Aa2	Negative	AA	Stable	AA	Stable
March 2015	Aa2	Stable	AA	Stable	AA	Stable
March 2016	Aa2	Stable	AA	Stable	AA	Stable
December 2017	Aa2	Stable	AA	Stable	AA	Stable
June 2019	Aa2	Stable	AA	Stable	AA	Stable
August 2019	Aa2	Stable	AA	Stable	AA	Stable
Current	Aa2	Stable	AA	Stable	AA	Stable

Green denotes upgrade/recalibration or positive outlook revision

Red denotes downgrade or negative outlook revision

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