



RATING ACTION COMMENTARY

Fitch Affirms the City of Cortland, NY's IDR and WIFIA Loan at 'AA-'; Outlook Stable

Tue 23 Nov, 2021 - 3:20 PM ET

Fitch Ratings - New York - 23 Nov 2021: Fitch Ratings has affirmed the City of Cortland's Issuer Default Rating (IDR) and the outstanding Environmental Protection Agency (EPA) Water Infrastructure and Innovation Act (WIFIA) (Clinton Avenue Gateway Project) loan at 'AA-'.

The Rating Outlook is Stable.

SECURITY

The WIFIA loan is a general obligation (GO) of the city and payable from a pledge of the city's full faith and credit and taxing power, subject to a 2011 state statute limiting property tax increases to the lesser of 2% or an inflation factor (the tax cap law). This limit can be overridden annually by a 60% vote of the city common council.

ANALYTICAL CONCLUSION

The 'AA-' IDR and GO rating reflects the city's strong operating performance and moderate long-term liability burden. The city's revenue growth prospects have historically been slow, although sales tax collections are expected to show moderate increases due to state legislation that allows taxation of internet sales. Carrying costs are manageable, and the

city maintains adequate expenditure flexibility to make budget adjustments in the event of a revenue shortfall.

Economic Resource Base

The City of Cortland is located approximately 35 mile south of Syracuse and 25 miles north of Ithaca in Cortland County. Cortland's 2020 U.S. census population is 17,556 and reflects an 8.6% decline since the 2010 census. The city is home to SUNY Cortland, which has a student population of approximately 6,800. The large number of students contributes to the lower than average wealth levels and unemployment rates that exceed the state and national rates.

KEY RATING DRIVERS

Revenue Framework: 'a'

The city's revenue growth prospects are expected to remain relatively flat absent policy action. The city does maintain significant ability to independently raise revenues.

Expenditure Framework: 'a'

Expenditure growth trends are likely to be above expected revenue growth prospects without management's ongoing efforts to control spending. The city has adequate ability to make spending adjustments, and carrying costs for debt, annual pension contributions and retiree healthcare benefits are manageable.

Long-Term Liability Burden: 'aa'

Fitch expects the city's long-term liability burden for debt and pensions to remain moderate relative to the city's resource base; however, the net OPEB liability (NOL), while not an asymmetric risk, is relatively high, and if it continues to rise, could affect the assessment.

Operating Performance: 'aaa'

Fitch expects the city to manage well through the current uncertainty and future economic downturns, while maintaining a high level of financial resilience driven by strong budget management, healthy reserves, and adherence to sound fiscal policies.

RATING SENSITIVITIES

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

--A sustained improvement of the city's revenue growth prospects above the rate of inflation;

--A deceleration of the city's natural pace of spending and/or a material reduction of the city's net OPEB liability resulting in a decrease in carrying costs below 10% of governmental spending.

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

--A sustained increase in the city's liability burden above 20% of personal income;

--A material and sustained increase in the city's net-OPEB liability without a corresponding increase in annual contributions and/or growth in the city's personal income base;

--A material change in the city's budget management practices and/or a weakening of its financial resilience resulting in a deterioration of the city's overall operating performance.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure 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

In fiscal 2019, the City of Cortland realized a net operating deficit of about \$422,000 or 2% of general fund spending. General fund revenues came in less than the adopted budget, primarily due to a reduction in SUNY (State University of New York) Impact Aid funds, aid that was given to SUNY host cities like Cortland to help offset public safety costs related to SUNY campuses, which resulted in a decrease in revenues of about \$360,581 or 1.9% of general fund revenues.

General fund expenditures came in above the city's adopted budget primarily due to increased public safety spending. The city covered most of these costs through transfers in from the sewer fund and non-major governmental funds. A use of fund balance was recorded in fiscal 2019 of about \$450,387, or 2% of general fund spending, to cover the city's general fund deficit. Fiscal 2019 TAV growth remained flat at about 0.2%.

The city ended fiscal 2020 with revenues coming in ahead of budget, primarily due to increased sales tax revenues. General fund revenues are derived primarily from property taxes, which account for over 49% of revenues in 2020, followed by sales taxes at 29%. State aid normally accounts for about 12% of revenues. The majority of the city's general fund spending is driven by public safety, which accounted for 42% of 2020 expenditures, followed by employee benefits at 30%.

Year-end fiscal 2020 audited results showed a modest net operating surplus of about \$597,000, or 3% of expenditures, resulting in an increase in unrestricted general fund balance to approximately \$5 million, or about 25% of spending. Taxable assessed value growth in fiscal 2020 remains unchanged from 2019.

The city's long-term liability burden related to debt and pensions is moderate at about 12% of personal income following the issuance of the WIFIA loan. The city contributes to the state's defined benefit retirement systems including the New York State and Local Employees and the State and Local Police and Fire Retirement systems. The combined ratio of assets to liabilities as of the city's Dec. 31, 2020 audit was approximately 78%, using Fitch's investment rate of return of 6%.

Future borrowing plans are expected to be moderate; however, the city maintains a large Net-OPEB liability (NOL) of \$68.2 million, or roughly 12% of personal income, which is viewed in conjunction with the city's long-term liability burden. Annual OPEB contributions to reduce this burden have increased and continue to be made on a pay-as-you-go basis.

The \$21.2 million adopted fiscal 2021 general fund budget is balanced with no use of general fund balance, and is in line with the adopted fiscal 2020 budget. The budget includes property tax revenue growth of 2% and a large decline in sales tax revenues of about 13% primarily due to the pandemic. However, current estimates show sales tax revenues outperforming budget expectations. According to management, the city expects general fund revenues also to exceed budget. The city raised its tax rate by \$.034 to \$1.704 per \$100 assessed value (AV). The city has increased its tax rate annually for the last five years. Fiscal 2021 TAV is expected to generate 0.4% growth over fiscal 2020.

The \$22.6 million adopted fiscal 2022 general fund budget is balanced with no use of fund balance and about 3% above prior year's adopted budget. The city's fiscal 2022 property tax rate is \$1.715 per \$100 of AV, an increase of \$.011. Public safety and employee benefits remain key budget drivers.

The city's total ARPA allocation is \$2.05 million. According to management the city intends to use \$1.89 million within the next two years on community outreach, capital improvements, employee compensation, city hall upgrades and support services for city departments, keeping \$157,000 for future use.

CREDIT PROFILE

The city is the Cortland county seat and serves as a commercial hub for the surrounding residents. The area has an agricultural presence including produce and dairy farms and is home to SUNY Cortland, which serves as the city's largest employer. The university and the downtown area have expanded in recent years, which have offset some of the job losses the city experienced over the past decade. The top two tax payers are power utilities, which provides stability to the tax base. Growth in assessed values has been flat over the past five years.

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

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit

www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT ◆

RATING ◆

PRIOR ◆

Cortland (NY) [General Government]	LT IDR	AA- Rating Outlook Stable	AA- Rating Outlook Stable
	Affirmed		

Cortland (NY) /General Obligation - Limited Tax/1 LT	LT	AA- Rating Outlook Stable	Affirmed	AA- Rating Outlook Stable
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[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[U.S. Public Finance Tax-Supported Rating Criteria \(pub. 04 May 2021\) \(including rating assumption sensitivity\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

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US Public Finance Infrastructure and Project Finance North America United States
