

## Fitch Rates El Paso, Texas COs 'AA'; Outlook Stable

Written by Australian Business

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AUSTIN, Texas--( [BUSINESS WIRE](#) )--Fitch Ratings assigns an 'AA' rating to the following El Paso, Texas certificates of obligation (COs):

--\$68.2 million COs, series 2013.

The bonds are scheduled to sell via negotiation as early as the first week of October. Bond proceeds will be used for various public infrastructure projects and pay issuance costs.

In addition, Fitch affirms the following El Paso, TX debt:

--\$584.8 million general obligation (GO) bonds at 'AA';

--\$344.4 million COs at 'AA';

--\$60.8 million El Paso Downtown Development Corporation (DDC) special revenue bonds at 'A+'.

The Rating Outlook is Stable.

### SECURITY

The GOs and COs are secured by an ad valorem tax levied on all taxable property within the city, limited to \$2.50 per \$100 taxable assessed valuation (TAV). The COs are additionally secured by a limited \$1,000 pledge of surplus revenues from the city's waterworks and sewer system. The DDC special revenue bonds are secured by annually

appropriated lease payments made by the city from lawfully available revenue, which includes most city revenue except property taxes, to the DDC.

### KEY RATING DRIVERS

**RELATIVE FINANCIAL STABILITY:** The city has posted positive financial results in four of the last five fiscal years despite the economic downturn that has yielded slower revenue growth trends against ongoing service demands of a growing population. Management's attention to revenue fluctuations has been timely but budget balance has been slightly dependent on temporary solutions, including underfunding annual pension payments.

**ECONOMIC EXPANSION AND DIVERSIFICATION:** Much of the city's economic activity has come from its position in a key NAFTA trade corridor near Mexico's maquiladora assembly plants, as well as the presence of Fort Bliss. Recent expansion at Fort Bliss and an emerging healthcare sector somewhat offsets contractions in the manufacturing sector and credit concerns regarding historically below-average income levels and high unemployment rates.

**HIGH OVERALL DEBT BURDEN; GROWING FIXED COSTS:** Overall debt levels are high relative to market values. The pace of principal amortization is average, but is projected to slow given the city's debt issuance plans. Fitch expresses concern over the city's underfunding of annual required contributions (ARC) for the police and fire pension plans and the potential for an increase in costs associated with a growing unfunded liability from the currently adequate 70%+ funded level.

**LARGE CAPITAL PLAN:** The city's capital improvement plan (CIP) and debt issuance plans continue to grow to support the city's ongoing growth-related needs and voter-approved quality of life projects. Balancing debt issuance with tax base growth and capital needs is essential to the rating given the city's growth-related capital pressures and already above-average debt service tax rate.

**BALLPARK PROJECT NOT ESSENTIAL TO CORE OPERATIONS:** Fitch does not consider the leased asset (Ballpark) to be essential to the city's core governmental

operations, leading to a two-notch distinction between the DDC special revenue bonds and the city's limited tax bonds. However, the statutory requirement that ballpark costs are the sole eligible use of receipts of the recently voter-approved 2% increase in hotel occupancy tax (HOT), lessens Fitch's concerns about the city's incentive to make full and timely annual appropriations.

### RATING SENSITIVITIES

**ESCALATING DEBT:** Rapidly increasing debt burden without offsetting improvement in other credit areas could apply downward pressure to the rating.

### CREDIT PROFILE

### RELATIVELY STABLE FINANCIAL POSITION

The city's financial position remains stable despite some modest revenue contraction and ongoing growth-related operating and capital pressures. General fund reserves remain adequate at \$42.3 million or 13.3% of spending in fiscal 2012. This amount includes the \$16 million charter-required cash reserve, which if used must be replenished annually. Audited results for fiscal 2012 reflect a smaller \$73,000 drawdown on reserves than the previously projected \$350,000. Fitch notes that had the city fully funded its annual pension requirement, fiscal 2012 results would have been affected negatively by roughly \$5 million.

The fiscal 2013 adopted general fund budget was balanced without the use of reserves. However, two subsequent developments are projected to reduce reserves by \$4 million (1.2% of fiscal 2013 budget), resulting in a still adequate financial cushion equal to about 10.5% of projected spending. The majority of the projected drawdown (\$3 million) consists of relocation costs of city hall offices as part of the ballpark venue project which is being built on the former site of city hall.

The balance of the projected drawdown (\$1 million) is the net impact of a \$3 million

refund to the city's largest taxpayer, Western Refining Company LP. The refinery had sued the El Paso Central Appraisal District in response to a very large reappraisal of its taxable value, leading to a settlement with various taxing entities to refund all property tax levies in excess of the final taxable value. Prompt implementation of budget reductions are expected to diminish the impact by roughly \$1 million.

The budget is also based on a modest shift to the operations and maintenance property tax levy from the debt service tax rate with the use of about \$3 million in debt service reserves to maintain the total tax rate at the current \$0.65 per \$100 TAV. Although management has successfully withstood fiscal pressures in current economic conditions, the city continues to be challenged to expand its revenue stream to serve the needs of a growing population.

The proposed fiscal 2014 budget is balanced and incorporates the reduced taxable value of Western Refining. The proposed general fund budget represents a 5.3% increase over the adopted fiscal 2013 budget and includes funding for police and fire collective bargaining agreements, the police academy, public safety vehicles, and non-departmental increases. Sales tax revenues are projected to increase by 4.4%, following 3.9% budgeted growth the year prior, which Fitch views cautiously.

### MODEST TAX BASE GROWTH

The city's \$32 billion TAV has slowed after double-digit annual TAV growth between fiscals 2005 and 2008. Growth began to slow in fiscal 2009 in line with weaker economic conditions throughout the nation. In fiscal 2011, taxable value growth was flat, but resumed 3% and 4% growth in fiscal years 2012 and 2013, respectively.

Fiscal 2014 taxable value grew negligibly by 0.3% with new construction offsetting a substantial \$460 million or 59% reduction in Western Refining's taxable value pursuant to a settlement with the El Paso Central Appraisal District. For purposes of capital planning and budgeting, the city has assumed a 1% annual growth rate through fiscal 2015, 2% growth in fiscal 2016, followed by annual 2.5% growth beginning in fiscal 2017. Fitch believes management's annual growth assumptions over the next five years are reasonable.

## HIGH DEBT BURDEN AND LARGE CAPITAL PLAN

Overall debt levels are high relative to market value at 7.4%, but are more moderate on a per capita basis at \$3,868. Given the city's plans to issue additional debt for recently voter-approved quality of life projects, as well as COs for transportation and public infrastructure projects, debt levels are projected to remain elevated in the near- to mid-term. The city's fiscal 2013-2017 debt funded CIP, which includes some of the voter-approved projects, totals \$462.7 million.

In November 2012 voters passed two propositions totaling \$473 million for quality of life projects (i.e. parks and recreation, zoo, open space, libraries, museum, and performing arts). The bond plan had a healthy 70% voter approval rate. The city's projected debt impact from issuance of the approved GO bonds is not expected to exceed \$0.05 per \$100 TAV assuming issuance over a 10-year period and the aforementioned 1%-2.5% annual tax base growth.

Fitch believes the city will be challenged to balance ongoing capital needs against an already above-average debt service tax rate, slower tax base growth in the near term, and the area's below-average socio-economic characteristics. The currently average pace of principal amortization is projected to slow in the near term as the city refinances a large bullet maturity and issues additional debt.

## ADEQUATE PENSION FUNDING LEVELS DESPITE ANNUAL UNDERFUNDING

The city maintains two, single-employer pension plans: a city employee pension fund (CEPF) and a firemen and policemen pension fund (FPPF). The city issued \$212 million in voter-authorized pension obligation bonds in 2007 and 2009 to address underfunding in the FPPF. The funded position for the combined plans is estimated at an adequate 71% as of fiscal 2012, adjusted for a 7% return on investment. The city has contributed between 97% and 100% of its ARC over the past three fiscal years for the CEPF. However, contributions were roughly 8% and 20% below the ARC for the fireman and police divisions, respectively, in fiscal 2012. Pension payments totaled about 9% of audited fiscal 2012 governmental spending, excluding capital projects, compared to 10.7% had the city paid the required amount. Fitch expresses concern over the city's underfunding and would expect a return to full funding over the near term.

Public safety employees agreed to a less generous, second-tier of pension benefits for new employees that should reduce this overall liability over time. A similarly structured program was also implemented for general city employees beginning in fiscal 2012. Carrying costs for debt service, retiree healthcare and required pension payments were moderately high at 24.9% of governmental spending, net capital expenditures.

### ECONOMIC DIVERSIFICATION

El Paso is the sixth largest city in Texas. Its current population of over 665,000 reflects ongoing growth at an average annual rate of nearly 1.5% since the 2000 census, slightly below the state's population growth rate of just over 2% for the same time period. City income levels as measured by median household income are below average, but continue to grow at a faster clip than state and national levels. Much of the city's economic activity has historically come from its position in a key NAFTA trade corridor near Mexico's maquiladora assembly plants as well as the presence of Fort Bliss, the Army's second largest installation.

The recent expansion of the military presence at Fort Bliss as a result of the Pentagon's 2005 base realignment and closure recommendations is expected to lead to roughly 10,000 additional troops from current levels by the end of 2013. Military family members are expected to total another 40,000. About two-thirds of the additional troops are expected to live off-base. The ongoing expansion of Ft. Bliss' troop strength and military facilities has boosted residential and commercial construction citywide, although the full economic impact of the expansion is still unfolding.

Government and educational entities comprise most of the top 10 civilian employers, which provide roughly 25% of the area's employment. Major additions to the city's retail, commercial and healthcare sectors brought unemployment rates down to record lows in 2007 and 2008, although they have risen notably along with the national unemployment rate. At 8.6% in July 2013, El Paso's unemployment rate remains above the state's 6.7% and the U.S. rate of 7.7%.

Additional information is available at '[www.fitchratings.com](http://www.fitchratings.com)'.

In addition to the sources of information identified in the Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, and LoanPerformance, Inc.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria'(Aug. 14, 2012);

--'U.S. Local Government Tax-Supported Rating Criteria'(Aug. 14, 2012).

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Tax-Supported Rating Criteria

[http://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=686015](http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015)

U.S. Local Government Tax-Supported Rating Criteria

[http://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=685314](http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685314)

Additional Disclosure

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