



RATING ACTION COMMENTARY

Fitch Rates Harris County, TX's LT CP Notes, Series A-1 'AAA'; Outlook Stable

Mon 28 Aug, 2023 - 12:12 PM ET

Fitch Ratings - Austin - 28 Aug 2023: Fitch Ratings has assigned a 'AAA' rating to bank notes associated with Harris County, TX's limited tax (LT) commercial paper (CP) notes, series A-1.

Fitch has also affirmed its 'AAA' on the following Harris County, TX obligations:

--Issuer Default Rating (IDR);

--\$899.6 million limited tax bonds;

--\$796.2 million unlimited tax bonds;

--\$151.3 million toll road unlimited tax bonds;

--\$1.019 billion Harris County Flood Control District limited tax bonds

--\$317.3 million Harris County Flood Control District contract tax revenue bonds;

The Rating Outlook is Stable.

RATING ACTIONS

| ENTITY / DEBT ↕ | RATING ↕ | | | PRIOR ↕ |
|--|----------|---------------------------|----------|---------------------------|
| Harris County (TX) [General Government] | LT IDR | AAA Rating Outlook Stable | Affirmed | AAA Rating Outlook Stable |
| Harris County (TX) /General Obligation - Limited Tax/1 LT | LT | AAA Rating Outlook Stable | Affirmed | AAA Rating Outlook Stable |
| Harris County (TX) /General Obligation - Unlimited Tax/1 LT | LT | AAA Rating Outlook Stable | Affirmed | AAA Rating Outlook Stable |
| Harris County Flood Control District (TX) /General Obligation - Limited Tax/1 LT | LT | AAA Rating Outlook Stable | Affirmed | AAA Rating Outlook Stable |

| | | | | |
|---|----|---------------------------|----------|---------------------------|
| Harris County Flood Control District (TX) /Limited Ad Valorem Tax Revenues/1 LT | LT | AAA Rating Outlook Stable | Affirmed | AAA Rating Outlook Stable |
|---|----|---------------------------|----------|---------------------------|

[VIEW ADDITIONAL RATING DETAILS](#)

The A-1 bank note rating is being assigned in connection with the execution of a liquidity agreement with State Street Bank and Trust Company, to be effective Sept. 13, 2023, which provides support for the series A-1 notes. Based on a review of the terms governing bank bonds specified in the agreement, it is Fitch's opinion that the incremental risk associated with bank bonds does not have a material effect on the long-term credit quality of the county.

SECURITY

The LT CP notes (and associated bank bonds) and LT bonds are payable from an annual property tax levy limited to \$0.80 per \$100 assessed valuation (AV) for operations and debt service. The unlimited tax bonds are payable from an unlimited annual property tax levy. The Harris County Flood Control District (the district) limited tax bonds are payable from an annual property tax levy limited to \$0.30 per \$100 AV for operations and debt service. The district's contract tax revenue bonds are payable from payments received from the county pursuant to a flood control projects contract. The county's obligation to make the payments is backed by a pledge of its tax levy, limited to \$0.80 per \$100 AV.

ANALYTICAL CONCLUSION

The county's 'AAA' IDR reflects its ample gap-closing capacity and prospects for maintaining structural balance through economic cycles given superior inherent budget flexibility supplemented by large reserves, a moderate long-term liability burden and robust economic base and growth prospects.

Economic Resource Base

With a 2022 population totaling nearly 4.8 million, Harris County is the largest county in Texas and the third largest in the nation, encompassing all but a small portion of the city of Houston. Expansion of the health care, biomedical research, aerospace, port, and petrochemical industries over the past several decades has reduced the historically strong reliance on the energy exploration sector.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

A long-term healthy pace of revenue growth is likely to continue as cyclical contraction within the energy sector is balanced against continued expansion of the county's diverse economy. The county's overall revenue-raising ability remains high relative to modest historical revenue volatility.

Expenditure Framework: 'aa'

The county's solid expenditure flexibility is aided by strong workforce controls, pay-go capital spending, and lack of collective bargaining agreements with any of its personnel. Fitch expects growth-related spending demands to be matched by revenue gains, keeping their trajectories in line with one another.

Long-Term Liability Burden: 'aa'

At an estimated 13% of resident personal income, the county's long-term liability burden is moderate and Fitch expects it to remain so, driven primarily by overlapping debt. Future growth-related debt and capital needs should

stay aligned with likely further robust population and economic gains. The county consistently funds its pension at actuarially determined levels and the net pension liability is modest relative to the resource base.

Operating Performance: 'aaa'

The combination of the county's solid expenditure flexibility and ample revenue-raising authority, as well as its record of ample reserve funding, should enable maintenance of the highest level of financial flexibility through economic cycles.

RATING SENSITIVITIES

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

--Not applicable given the current 'AAA' rating.

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

--Economic contraction that negatively affects key county revenues, particularly property tax upon which the county is heavily reliant, and materially erodes the county's gap-closing capacity;

--Although unlikely, a sustained increase in the long-term liability burden near or above 20% of personal income due to substantially larger debt issuance than expected or large declines in the county's resource base.

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

The county has maintained its very strong financial position through the pandemic recovery. The fiscal 2022 audit posted an unrestricted fund balance of approximately \$1.4 billion or 48% of spending despite a net general fund deficit of approximately \$191 million (6.5% of spending) due primarily to coronavirus-related expenditures funded from the county's public improvement contingency (PIC) fund. Reported as part of the general fund group, the PIC fund received property tax revenues from a dedicated property tax levy in fiscal years 2007-2020.

Local property taxes, which accounted for 82% of general fund revenues in fiscal 2022, were not affected by the pandemic and continued to grow despite various COVID-related payment deadline extensions. The county does not collect sales taxes. Overall stability in its primary revenue stream largely allowed county management to avoid implementing cost saving measures, such as mid-year budget cuts or hiring freezes.

The county received \$426 million in federal Coronavirus Aid, Relief, and Economic Security Act funds in fiscal 2021 which were recorded outside the general fund. Harris County was also allocated a total of \$916 million in American Rescue Plan Act (ARPA) aid which is also recorded outside of the general fund. The county's allocation of these funds is focused on the areas of health, housing, and job creation. A portion of the ARPA funds has been allocated for

initiatives to reduce the large criminal case backlog (\$20 million) and public health payroll and other eligible expenses (\$30 million) as allowed under the revenue replacement provision of the act.

Fiscal Year End Change

Effective fiscal 2023, the county commissioners court changed the fiscal year end from Feb. 28 to Sept. 30 in order to better align the annual budget process with the property assessment cycle. To transition to the new fiscal year, the county approved a budget for a seven-month period from March 1, 2022 through Sept. 30, 2022, designated as short fiscal year 2022. Concurrently, the county also approved a planning budget for fiscal 2023.

The short fiscal year 2022 fell between the fiscal 2022 and fiscal 2023 collection cycles, so the budget for short fiscal year 2022 relied primarily on the county's large reserves for county operations and debt service costs. As a result, the audit for short fiscal year 2022 posted a large net general fund deficit of \$1.2 billion, reducing the unrestricted fund balance to \$416 million or 21% of spending. Prior fiscal years ended concurrently with the peak collection of property tax revenues in January and February supporting very high reported fund balances. Fitch anticipates future fund balances will generally remain at or above the lower but still ample level with balanced fiscal operations.

The fiscal 2023 budget is balanced, includes \$59 million in pay-go capital outlays, and was adopted at a no new revenue O&M tax rate (for existing properties). Based on the county auditor's third quarter projection, the cash-basis ending balance is projected to approximate \$357 million or 16% of spending, modestly above the beginning cash balance of \$347 million. Concurrent with the approval of the fiscal 2023 budget, the county established a new policy regarding the PIC fund (now renamed the contingency fund) that establishes a fund balance target equal to 12.5% of the auditor's estimated general fund revenue for each fiscal year. As part of the general fund, cash and investments within the contingency fund currently total \$190 million, below the 12.5% target of \$323 million, although the county expects to exceed its target upon the receipt of \$260 million in FEMA reimbursements.

The proposed fiscal 2024 budget is balanced and based on preliminary certified AV of \$657 billion, an increase of 12.3% over the prior year. The proposed budget increases the property tax levy on existing properties slightly below the 3.5% levy cap allowed by state law and also includes use of the county's unused O&M increment, totaling \$0.01759 per \$100 AV. As a result, O&M tax revenue is projected to increase by \$217 million or 12.6% over the prior year. To compensate for the lack of a COLA in fiscal 2023, the proposed budget includes COLA's of 7% for civilians and non-deputy law enforcement and 4% for deputies. The budget also includes \$20 million in supplemental funding to increase jail staffing in response to rising jail population plus \$37 million for outsourcing inmates to other county detention centers.

CREDIT PROFILE

The Houston MSA is home to several thousand energy companies, ranging from large multi-national concerns to numerous mid-sized-to-smaller exploration, construction, engineering and service companies. The county's employment base has recovered from the effects of the oil price shock in the second quarter of 2020 which led to widespread layoffs in the manufacturing, construction/mining, and leisure/hospitality sectors. The county's unemployment rate has returned to pre-pandemic levels, totaling 4.5% in June 2023, modestly above state and national averages.

Similar to pre-pandemic trends, professional and business services are expected to be one of the MSA's leading growth sectors. The trade and transportation sector is projected to benefit from additional activity at the Port of Houston due to the fast-growing export market for U.S. oil, natural gas, and chemicals. The port is ranked first in the U.S. in foreign waterborne commerce and second in total tonnage.

The current price of West Texas Intermediate (WTI) oil per barrel (\$78) has benefited the county's energy sector and approximates Fitch's projection of \$81 in 2023. Additional details are described in the report entitled, "North American Energy (Oil & Gas) Outlook in 2023" published Dec. 8, 2022 on www.fitchratings.com.

Continued in-migration and natural population growth will serve to buoy the county's housing market and taxable values over the medium term. The county experienced a nearly 17% population gain in 2010-2022, the majority of which occurred in the unincorporated areas. Fitch expects the MSA's strong population growth trend to continue, aiding in the stabilization of the housing market during energy sector downturns. Per Zillow, the median home value totals \$279,401, nearly flat over the 12-month period ending July 2023.

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

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

FITCH RATINGS ANALYSTS

Jose Acosta

Senior Director

Primary Rating Analyst

+1 512 215 3726

jose.acosta@fitchratings.com

Fitch Ratings, Inc.

2600 Via Fortuna, Suite 330 Austin, TX 78746

Lauren Wynn

Director

Secondary Rating Analyst

+1 512 215 3738

lauren.wynn@fitchratings.com

Eric Kim

Senior Director

Committee Chairperson

+1 212 908 0241

eric.kim@fitchratings.com

MEDIA CONTACTS

Sandro Scenga

New York

+1 212 908 0278

sandro.scenga@thefitchgroup.com

Additional information is available on www.fitchratings.com**PARTICIPATION STATUS**

The rated entity (and/or its agents) or, in the case of structured finance, one or more of the transaction parties participated in the rating process except that the following issuer(s), if any, did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure.

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)

ADDITIONAL DISCLOSURES

[Dodd-Frank Rating Information Disclosure Form](#)

[Solicitation Status](#)

[Endorsement Policy](#)

ENDORSEMENT STATUS

Harris County (TX)

EU Endorsed, UK Endorsed

DISCLAIMER & DISCLOSURES

All Fitch Ratings (Fitch) credit ratings are subject to certain limitations and disclaimers. Please read these limitations and disclaimers by following this link: <https://www.fitchratings.com/understandingcreditratings>. In addition, the following <https://www.fitchratings.com/rating-definitions-document> details Fitch's rating definitions for each rating scale and rating categories, including definitions relating to default. ESMA and the FCA are required to publish historical default rates in a central repository in accordance with Articles 11(2) of Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 and The Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019 respectively.

Published ratings, criteria, and methodologies are available from this site at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance, and other relevant policies and procedures are also available from the Code of Conduct section of this site. Directors and shareholders' relevant interests are available at <https://www.fitchratings.com/site/regulatory>. Fitch may have provided another permissible or ancillary service to the rated entity or its related third parties. Details of permissible or ancillary service(s) for which the lead analyst is based in an ESMA- or FCA-registered Fitch Ratings company (or branch of such a company) can be found on the entity summary page for this issuer on the Fitch Ratings website.

In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings

information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001. Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

dv01, a Fitch Solutions company, and an affiliate of Fitch Ratings, may from time to time serve as loan data agent on certain structured finance transactions rated by Fitch Ratings.

Copyright © 2023 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved.

[READ LESS](#)

SOLICITATION STATUS

The ratings above were solicited and assigned or maintained by Fitch at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

ENDORSEMENT POLICY

Fitch's international credit ratings produced outside the EU or the UK, as the case may be, are endorsed for use by regulated entities within the EU or the UK, respectively, for regulatory purposes, pursuant to the terms of the EU CRA Regulation or the UK Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019, as the case may be. Fitch's approach to endorsement in the EU and the UK can be found on Fitch's [Regulatory Affairs](#) page on Fitch's website. The endorsement status of international credit ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.