S&P Global
Ratings

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Summary:

Harris County, Texas; CP; General Obligation

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Summary:

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Credit Profile		
US$360.0 mil GO bnds ultd tax cml pap nts ser C		
Short Term Rating	A-1+	New
US$300.0 mil GO bnds unltd tax cml pap nts ser D-2		
Short Term Rating	A-1+	New
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO bnds ultd tax cml pap nts ser C		
Short Term Rating	A-1+	Affirmed
Harris Cnty GO bnds unltd tax cml pap nts ser D-2		
Short Term Rating	A-1+	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'A-1+' short-term rating to Harris County, Texas' $360 million series C and $300 million series D-2 general obligation (GO) unlimited-tax commercial paper (CP) notes based on the application of its criteria, "General Criteria: Methodology For Linking Long-Term And Short-Term Ratings," published April 7, 2017.
- At the same time, S&P Global Ratings affirmed its 'AAA' rating on the county's GO unlimited- and limited-tax debt outstanding.
- The outlook on the 'AAA' rating is stable.

Security

The rating on the CP notes reflects our view of Harris County's strong general creditworthiness (as per the 'AAA' GO debt rating) and a pledge of unlimited ad valorem taxes levied on all taxable property within the county that secures the notes. The notes will be used to provide cash flow for near-term capital needs and the county will refinances the CP notes outstanding with long-term GO debt.

Liquidity support for the series C notes will be provided via a reimbursement agreement with Sumitomo Mitsui Banking Corp. The agreement expires on Dec. 9, 2025, and will cover $360 million of principal plus interest calculated at 10% of the full principal authorization, at the maximum note maturity of 270 days. Included in the events of default is if Fitch Ratings, Moody's, or S&P Global Ratings downgrade the county's unenhanced GO debt to below 'BBB', 'Baa2', or 'BBB', respectively, or suspended or withdrawn the rating for any credit-related reason (and such suspension or withdrawal is initiated by the respective rating agency).

Liquidity support for the series D-2 notes will be provided via a credit agreement with State Street Bank and Trust Co. The credit agreement expires on Nov. 13, 2024, and will cover $300 million of principal plus interest calculated at 10% of the full principal authorization, at the maximum note maturity of 270 days. Included in the events of default is if

Fitch Ratings, Moody's, or S&P Global Ratings downgrade the county's unenhanced GO debt to below 'A', 'A2', or 'A', respectively, or suspended or withdrawn the rating for any credit-related reason (and such suspension or withdrawal is initiated by the respective rating agency).

An unlimited ad valorem tax levied on all taxable property in Harris County secures the series C CP notes. A limited ad valorem tax, levied on all taxable property in Harris County, secures the series D-2 notes as well as GO bonds. The county has the authority to levy an ad valorem tax rate of up to 80 cents per $100 of assessed value (AV), with the portion dedicated to maintenance and operations limited to 40 cents. The current rate is 34.373 cents per $100 of AV with 30.105 cents for general fund operations and 4.268 cents for debt service.

Credit overview

Given the strength of the local economy bolstered by the city of Houston, we expect redevelopment and new construction will continue although expected recessionary pressures could dampen the pace of growth. For further information regarding S&P Global Economics' view on economic conditions, see "Economic Outlook U.S. Q4 2022: Teeter Totter," published Sept. 26, 2022, on RatingsDirect. In addition, Harris County is maintaining very strong available reserves; however, these reserves are being used as the county transitions to a different fiscal year-end to align with property tax collections. We affirmed the rating because we believe any use of reserves during this transition to a new fiscal year is based on timing of revenues and is not an indication of structural imbalance. We also recognize that the county has very strong liquidity represented by $4 billion available in total governmental funds. Although the county will issue more debt, tax base growth should mitigate the negative effect on the debt profile.

The rating further reflects our view of Harris County's:

- Access to the broad and diverse Houston metropolitan statistical area (MSA) economy;
- Standard management, with some formal policies and a strong institutional framework;
- Strong available general fund balance represented in 50% of general fund expenditures; and
- High 6.5% overall net debt, with above-average amortization.

Environmental, social, and governance (ESG)

We believe Harris County has elevated environmental risk due to its location near the Gulf coast that makes it susceptible to significant weather events, most significantly Hurricane Harvey in September 2017. In addition, the large oil and gas presence exposes the area to transition risk, which considers costs related to new regulations or the shift in employment that can occur depending on oil prices. However, the county's management team is adept at handling these environmental risks as evidenced by stable financial performance through economic and weather cycles. In our view, Harris County's governance and social factors are neutral in our credit analysis.

Outlook

The stable outlook reflects our opinion of the strong local economy, sizable reserves, and a debt profile that is made manageable by a growing tax base.

Downside scenario

We could consider a negative rating action if budgetary performance deteriorates significantly, resulting in a reduction of available fund balance to levels that are no longer comparable with those of peers. A material weakening of key economic indicators could also pressure the rating.

Credit Opinion

Substantial local economy centered around the energy sector but experiencing ongoing economic development and rising property values

Harris County serves over 20 cities including the city of Houston, which is the primary anchor for the MSA. Consistent growth in Houston and in the greater region and state, along with rebounded oil prices and steady appreciation of existing properties, have supported growth in total market value. Expansions in higher education and health care are contributing to economic stability and employment growth across the region. The top 10 taxpayers represent the area's dependency of the energy sector since they include a power plant, oil and gas companies, and chemical plants. Population growth is spurring an ongoing need for housing and officials noted that Houston has led the nation in the number of new apartment units during 2022. The Port of Houston is the No. 1 port in the U.S. for waterborne tonnage and is undergoing a $1 billion expansion to accommodate more activity. ExxonMobil Corp. is moving its headquarters from the Dallas MSA to the greater Houston MSA sometime in 2023. In addition, space and technology companies are locating within the county and Texas Medical Center is expanding. We anticipate the Houston economy will remain strong, despite recessionary pressures, because of its access to affordable housing, employment opportunities, and solid pattern of growth.

Standard financial practices with some formal policies

Harris County provides monthly budget-to-actual reports to the county commissioners and investments are reported on a quarterly basis and are guided by a formal investment policy. The formal debt policy provides guidelines for the use of short-term debt, minimum net present value savings to achieve when refunding debt, and amortization. Capital needs are identified by departments for inclusion in the budget or to be addressed by bond proceeds but a long-term capital plan is not formally adopted and updated each year. Harris County is currently looking to develop a 10-year long-term financial forecast. Emergency funds are available as per the county's policy that created the public improvement contingency fund and established it to have a target balance equal to 12.5% of the auditor's estimated new general fund revenue for each fiscal year. The institutional framework score for Texas counties is strong.

Very strong reserves despite use of fund balance in 2022 and a change in fiscal year dates, with stability expected for fiscal 2023

We have adjusted for recurring transfers into the general fund from the proprietary funds, as well as adjusted for one-time expenditures and transfers funded through debt proceeds and surplus cash.

Harris County recently changed its fiscal year-end to Sept. 30, from Feb. 28, to better align with the property tax cycle. This change means that a short fiscal year occurred between March 1, 2022, and Sept. 30, 2022. Because property taxes are due Feb. 1, a majority of these collections fell outside the short fiscal year reporting period; therefore, the general fund is relying on reserves for cash flow needs. The short fiscal year budget assumed that the starting available general fund balance would decrease from more than $1 billion to $602 million, which would be approximately 46% of budgeted expenditures. We have affirmed the rating despite a large use of reserves in 2022 because we believe the use of reserves is due to the change in the fiscal year and not an indication of structural imbalance. Property taxes collected in February 2023 should be able to contribute to the available general fund balance during the full 12-month fiscal year. Should Harris County draw down reserves to a level that is no longer consistent with the 'AAA' rating, we could consider a lower rating.

The fiscal 2023 adopted budget was balanced with $2.2 billion in revenues and expenditures. The commissioners court voted for "no new revenue" tax rates; however, increasing AVs will generate an increase in property tax revenue.

For the fiscal year that ended Feb. 28, 2022, the general fund finished with a $45 million net operating deficit that was primarily driven by higher-than-expected expenditures related to COVID-19 health and safety measures and approximately $300 million is expected from s Federal Emergency Management Agency reimbursement during the current 2023 fiscal year. The general fund available unassigned balance totaled $1.3 billion, which was approximately 50% of general fund expenditures.

The county's primary general fund revenue consists of property taxes (82%) and charges for services (11%). Property tax collections remain strong, with annual collections exceeding 98% for the past 10 years.

Harris County has been allocated $915.5 million in American Rescue Plan Act funds, which will be used for health programs, housing, jobs, and education, as well as to alleviate the county's court backlog.

The county does not have any contingent liabilities that expose it to liquidity risk. Harris County entered interest rate swaps with Citibank N.A. and JP Morgan Chase & Co. relating to toll road senior-lien revenue refunding bonds series 2007B; however, the toll road has ample liquidity to cover the swaps, which had a negative fair value of $19.6 million each as of Feb. 28, 2022.

High debt burden, with continued issuances anticipated

Harris County has approximately $1.8 billion in direct debt outstanding and has $2.4 billion in authorized unissued bonds, including $1.7 billion for a flood control district and $499 million for roads. On Nov. 8, 2022, voters approved three bond propositions totaling $1.2 billion, with $900 million for roads, drainage, and transportation related programs; $200 million for parks and trails; and $100 million for public safety facilities. The debt will be issued over the next several years depending on tax base growth and the effect on the tax rate.

No immediate pressures expected from pension and other postemployment benefit liabilities

We do not view pension and other postemployment benefit (OPEB) liabilities as an immediate source of credit pressure for Harris County, as required contributions make up a small portion of total governmental expenditures, and they are not expected to materially increase in the next few years, particularly given the plan's funded status. As a result, we do not expect a material increase in pension contributions that could affect the county's fiscal stability.

Harris County participated in the following plan as of Dec. 31, 2021 (the latest measurement date):

- The Texas County and District Retirement System, which is over funded, with a $253 million net pension asset. Actuarial assumptions include a discount rate of 7.6%, which we consider aggressive, representing market risk and resulting contribution volatility if the plan fails to meet its assumed investment targets. Contributions are likely to grow, given the level percent-of-payroll funding method (and high at 4.7%), as opposed to level-dollar contributions, which would result in consistent payments.

The county also provides health care benefits to retirees, paying for them on a pay-as-you-go basis. As of Feb. 28, 2022, Harris County's OPEB liability totaled $3.9 billion. Although this is a large liability, the county's operating budget is sizable and contributions are on a pay-as-you-go basis.

Ratings above the sovereign

Harris County's GO bonds are eligible to be rated above the sovereign because we believe the county can maintain better credit characteristics than the U.S. in a stress scenario. (See "Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions," published Nov. 19, 2013.) Under our criteria, U.S. local governments are considered moderately sensitive to country risk. The county's GO pledge is the primary source of security on the debt; this severely limits the possibility of negative sovereign intervention in the payment of the debt or in the operations of the county. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy, independent treasury management, and no history of government intervention. Harris County has considerable financial flexibility, as demonstrated by the very high fund general balance as a percent of expenditures as well as by very strong liquidity.

Harris County, Texas--Key Credit Metrics

	Most recent	Historical information		
		2022	2021	2020
Very strong economy				
Projected per capita EBI % of U.S.	88.3			
Market value per capita ($)		107,129.4		
Population (no.)			4,798,048	4,787,379
County unemployment rate(%)			6.5	
Market value ($000)		514,012,192	504,850,540	482,200,998
Ten largest taxpayers % of taxable value	3.9			
Weak budgetary performance				
Operating fund result % of expenditures		(1.7)	17.9	7.8
Total governmental fund result % of expenditures		(6.2)	0.7	5.8
Very strong budgetary flexibility				
Available reserves % of operating expenditures		50.8	58.1	65.0
Total available reserves ($000)		1,354,037	1,407,072	1,504,457
Very strong liquidity				
Total government cash % of governmental fund expenditures		104.9	104.2	135.9
Total government cash % of governmental fund debt service		1,587.4	1,205.6	1,182.2
Adequate management				
Financial Management Assessment	Standard			
Adequate debt & long-term liabilities				
Debt service % of governmental fund expenditures		6.6	8.6	11.5
Net direct debt % of governmental fund revenue	93.9			
Overall net debt % of market value	6.5			

Harris County, Texas--Key Credit Metrics (cont.)				
	Most recent	Historical information		
		2022	2021	2020
Direct debt 10-year amortization (%)	57.4			
Required pension contribution % of governmental fund expenditures		4.8		
OPEB actual contribution % of governmental fund expenditures		1.7		
Strong institutional framework				

EBI--Effective buying income. OPEB--Other postemployment benefits. Data points and ratios may reflect analytical adjustments.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022
- 2022 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of November 16, 2022)		
Harris Cnty go comm paper nts ser C dtd 01/20/1998 due 01/01/2028		
Short Term Rating	A-1+	Affirmed
Harris Cnty GO		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Harris Cnty GO disaster recovery comm paper nts ser J-1 due 05/19/2030		
Short Term Rating	A-1+	Affirmed
Harris Cnty GO sub ln (AGM)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed

Ratings Detail (As Of November 16, 2022) (cont.)		
Harris Cnty GO unltd tax commercial paper nts ser C due 01/10/2022		
Short Term Rating	A-1+	Affirmed
Harris Cnty GO CP		
Short Term Rating	A-1+	Affirmed
Harris Cnty GO CP		
Short Term Rating	A-1+	Affirmed
Harris Cnty GO CP		
Short Term Rating	A-1+	Affirmed
Harris Cnty GO CP		
Short Term Rating	A-1+	Affirmed
Harris Cnty Flood Cntl Dist, Texas		
Harris Cnty, Texas		
Harris Cnty Flood Cntl Dist (Harris Cnty) GO		
Long Term Rating	AAA/Stable	Affirmed

Many issues are enhanced by bond insurance.