STANDARD & POOR'S
RATINGS SERVICES
McGRAW HILL FINANCIAL

RatingsDirect®

Ohio; Gas Tax

Primary Credit Analyst:
Eden P Perry, New York (1) 212-438-0613; eden.perry@standardandpoors.com

Secondary Contact:
Carol H Spain, Chicago (1) 312-233-7095; carol.spain@standardandpoors.com

Table Of Contents

Ohio; Gas Tax

Credit Profile		
US$250.0 mil GO hwy cap imp bnds (Ohio) ser S due 05/01/2031		
Long Term Rating	AAA/Stable	New
Ohio GO hwy cap imp bnds		
Long Term Rating	AAA/Stable	Affirmed
Ohio State Treasurer, Ohio		
Ohio		
Ohio State Treasurer (Ohio) GO hwy cap imp bnds		
Long Term Rating	AAA/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'AAA' long-term rating, and stable outlook, to Ohio's $250 million series S general obligation (GO) highway capital improvement bonds. At the same time, Standard & Poor's affirmed its 'AAA' rating, and stable outlook, on the state's parity debt outstanding.

The rating reflects our opinion of:

- The pledge of statewide highway user receipts, which are restricted for transportation purposes pursuant to the state constitution;
- Relatively consistent performance of pledged revenues over time, due in part to tax increases. Taxes and charges are levied statewide and Ohio's 2015 population is estimated at 11.6 million;
- Very strong debt service coverage levels, in our view, combined with rapid amortization of all bonds in the next 15 years;
- Constitutional limitations on the amount of debt that can be outstanding at any one time.

In addition to the pledge of highway user receipts, the bonds also have a full faith and credit pledge of Ohio (GO rating: AA+/Stable; see the full analysis published Feb. 12, 2016, on RatingsDirect). In our view, the highway user receipts represent the stronger of the two security pledges, mainly due to the very strong coverage levels. Ohio Constitution restricts highway user receipts to highway uses and they cannot be used for nonhighway obligations or uses. We understand that bond proceeds from the series S bonds will be used to fund highway capital projects.

The highway user receipts pledged to the bonds consist of motor fuel and use tax (68% of total revenues) and registration and license fees (32% of total revenues). Total fiscal 2015 pledged revenues were $2.86 billion, providing more than 22.02x coverage of maximum annual debt service, which is estimated to be $129.935 million in fiscal 2017. After this issuance, the state expects to issue about $685 million over the next five years (fiscal years 2017-2021); we expect that debt service coverage will remain very strong.

Pledged revenues have expanded by an average of 1% per year from 2008 through 2015, with some cyclicality during recession periods. Highway user receipts have declined four times since 2000: 3.8% in fiscal 2001, 3.6% in fiscal 2007, 4.9% in fiscal 2009, and 1.9% in fiscal 2012. The state attributes part of the declines in fiscal years 2007, 2009, and 2012 to a delay in recording receipts, which was partially offset by expanded collections in the next year (growth of 4.9% in fiscal 2008 and 0.35% in fiscal 2010). Despite the recorded declines, coverage has remained extremely strong, in our opinion. Pursuant to the state's constitution, revenues cannot be diverted for nonhighway purposes, which we view as a credit strength for the bonds. Ohio's motor vehicle fuel tax is 28 cents per gallon, which is in line with the average rate for all states. Ohio's tax rate is below that of most contiguous states.

The series S highway capital improvement bonds are being issued pursuant to Section 2m Article VIII of the Ohio Constitution, and are payable from all excises and taxes levied by the state relating to registration, operation, or use of vehicles and fuel taxes. Bond proceeds will be used to fund various highway capital improvements. The series S bonds are the 19th series of bonds issued under Article VIII. This constitutional amendment was approved by the electorate in November 1995 and authorizes the issuance of highway capital improvement bonds of up to $220 million per fiscal year, plus any previous fiscal year's unused authorization. No more than $1.2 billion of highway capital improvement bonds may be outstanding at any one time, and there is $758.55 million outstanding at present. Maximum maturity on the bonds cannot exceed 30 years but typically the state has amortized its bonds more rapidly. All debt (including the series S bonds) is amortized by fiscal 2031.

Ohio's gas tax bonds are eligible to be rated above the sovereign because we believe the state can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect), U.S. states are considered to have moderate sensitivity to country risk. State-derived revenues are the sole source of security on the bonds, and the institutional framework in the U.S. is predictable with significant state autonomy and flexibility.

Outlook

The stable outlook reflects Standard & Poor's view that the broad pledge of statewide highway user receipts supporting the bond program has been stable over time. We believe that the bond provisions governing the issuance of additional debt will ensure that extremely strong debt service coverage levels will continue. Given both of these factors, we do not expect a lower rating during the two-year outlook horizon. However, if pledged revenues fell to a level that negatively impacted the debt service coverage this could put downward pressure on the rating.

Economy

The U.S. Census Bureau's July 2015 population estimate for Ohio is 11.6 million, making Ohio the seventh-most populous state in the nation. About half of the state's residents reside in the Cleveland, Cincinnati, and Columbus metropolitan statistical areas. Ohio's population over the past decade was relatively weak, averaging only 0.16% growth annually, well below the U.S average of 1.0%. The state is made up of a larger dependent population than the nation at 61.9% for the state versus 60.2% for the nation, according to data from the U.S. Census Bureau's American Community Survey for 2014. Outmigration is consistent, particularly among young professionals aged 20-34, and is most prevalent in communities with a strong manufacturing presence such as Cleveland, Dayton, and Toledo.

However, Ohio's economy continues to expand, and although the expansion has been slow compared with previous post-recession phases, the state's unemployment rate significantly improved in 2015. Ohio's 2013 unemployment rate was 7.5%, just above the U.S. rate, but dropped to 4.9% as of February 2016, which is still better than the U.S. rate.

Ohio's manufacturing sector remains a strength in the state's economy, chiefly due to Ohio's heavy presence in the auto industry, after suffering significantly in the Great Recession. However, IHS Global Insight Inc. projects a slight dip in manufacturing sector employment--0.2% average annual employment growth from 2015 to 2016. It also projects overall average annual job growth to be 1.2% in 2016 (a slight decline from 1.3% in 2015) and an average of 0.73% annually from 2017 to 2019, which would be below the projected national level. In our view, Ohio's manufacturing sector will remain a significant component in the state's economy, but in our view the sector's long-term performance is still not clear.

State Enacted 2016-17 Biennium Budget

The enacted 2016-2017 biennium budget is balanced with what we view as minimal reliance on one-time revenue sources. The total biennium appropriations are approximately $71.2 billion and are based on expected total general revenue fund (GRF) biennial revenues of $71.3 billion. The enacted budget continues the implementation of significant tax reform as part of the state's goal of making Ohio more competitive in attracting jobs and investments and to help small businesses. The tax reforms included small business tax relief and personal income tax reduction, which are partially offset with an increase to the cigarette tax and the restriction of the retirement income tax credit to certain levels, as well as increased allocation of certain taxes to the GRF. The budget also increased funding of kindergarten to grade 12 education, higher education, and Medicaid. The fiscal 2016 budget anticipates an increase of total sources by 10.8% primarily due to an increase in federal grants. Total sources are projected to rise by 4.6% by fiscal 2017.

Appropriations in fiscal 2016 are budgeted at $34.9 billion or a 13.1% increase over fiscal 2015, with Medicaid being the largest driver of the increase. According to the state, this is due to the shift of federal Group 8-related appropriations and reimbursements to the GRF. State-share appropriations increase by a more moderate 5.3% from fiscal 2015. The fiscal 2017 budget shows a 4.2% total increase; again, the state share growth is more modest at 3.5% from fiscal 2016. Ohio has budgeted a modest drawdown of about $110 million in the GRF over the biennium. The GRF ending balance is budgeted to close at $503 million in fiscal 2016 and $439 million in fiscal 2017; the balances exceed the state's statutory 0.5% ending GRF requirement. Along with the substantial reserves in the budget stabilization fund, the ending fund balance of $439 million in fiscal 2017 is more than adequate in our view.

Related Criteria And Research

Related Criteria

- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: State Ratings Methodology, Jan. 3, 2011

- USPF Criteria: Special Tax Bonds, June 13, 2007
- USPF Criteria: Methodology: Rating Approach To Obligations With Multiple Revenue Streams, Nov. 29, 2011
- Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions, Nov. 19, 2013