FitchRatings

Public Finance
Tax-Supported
U.S.A.

San Diego County, California

New Issue Summary

Sale Date: Nov. 16, 2021, via competitive sale

Series: $49,810,000 Certificates of Participation, Series 2021

Purpose: Proceeds will be used to finance the construction of facilities at San Diego County's (the county) Youth Transition Campus.

Security: The COPs are supported by annually appropriated lease payments from the county for the use and occupancy of various leased assets, subject to abatement.

The 'AAA' Long-Term Issuer Default Rating (IDR) reflects the county's superior gap-closing capacity, strong budget management, moderate long-term liabilities and strong expenditure and revenue frameworks. Given the county's strong and growing economy and proactive budget management, Fitch Ratings expects the county to maintain its strong financial resilience throughout economic cycles.

The county's pension obligation bonds (POBs), lease revenue bonds (LRBs) and COPs are rated one notch lower at 'AA+', which is consistent with Fitch's approach for contractual obligations and appropriation-backed debt.

Economic Resource Base: San Diego County is the nation's fifth most populous county with over 3.3 million residents and 18 incorporated cities. The county's population is larger than 21 states. The core industries of its diverse economy include government, military and related defense industries, healthcare, technology, manufacturing and tourism. The county's net assessed value for tax purposes has experienced steady growth, with a 53% increase in net assessed value since 2011.

Key Rating Drivers

Revenue Framework: 'aa': Fitch expects the county's revenue growth to keep pace with U.S. economic performance due to robust gains in property tax revenues, which are offset by more moderate growth in intergovernmental revenues. The county retains authority to increase fines, fees and charges for services, but its legal ability to raise revenues is constrained by state constitutional provisions that require voter approval for tax increases.

Expenditure Framework: 'aaa': The natural pace of spending growth is likely to roughly equal revenue growth over time, reflecting strong growth in the county's general purpose revenues and good matching of revenues and expenditures related to social welfare programs funded by higher levels of government. Expenditure flexibility is solid, and fixed costs for debt service and pensions are moderate.

Long-Term Liability Burden: 'aa': Long-term liabilities for overall debt and pensions are at the low end of the moderate range relative to the county's large economic resource base.

Operating Performance: 'aaa': The county has the highest level of gap-closing capacity, reflecting strong reserve levels, limited revenue volatility and midrange inherent budget flexibility.

Rating Sensitivities

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

- Not applicable.

FACT Tools

Ratings

Long-Term Issuer Default Rating	AAA

New Issue

$49,810,000 San Diego County (Youth Transition Campus) Certificates of Participation, Series 2021	AA+

Outstanding Debt

See Outstanding Debt Details on Page 3.

Rating Outlook

Stable

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (May 2021)

Related Research

Fitch Rates San Diego County, CA's $49.8MM COPs 'AA+'; Outlook Stable (October 2021)

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

- Over the longer term, pressured financial flexibility due to slower than expected revenue growth, expenditure growth that outpaces revenues and/or sustained reductions in reserves.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	10/25/21
AAA	Revised	Stable	4/30/10
AA+	Assigned	Stable	5/31/07

Current Developments

Pandemic-Related Aid

The county received $388 million in Coronavirus Aid, Relief and Economic Security (CARES) Act funding, followed by a $648 million American Rescue Plan Act (ARPA) allocation, of which the county has received the first $324 million, with the balance expected in May 2022. In addition, the county expects to be fully reimbursed by the Federal Emergency Management Agency (FEMA) for certain emergency-related spending since March 2020. The county's framework for spending ARPA funds is focused on ongoing pandemic response, mental health and homeless services, stimulus for small businesses and other programs. Importantly, none of the ARPA funds is being used for any ongoing programs.

Fiscal Performance

The county expects to have ended fiscal 2021 with an increase to unassigned general fund balance relative to fiscal 2020, with higher than budgeted expenditures ($273.7 million) mostly due to pandemic response more than offset by higher than budgeted revenue ($492.1 million) driven by ARPA funding. The county projects ending fiscal 2021 with about $765.1 million in unassigned fund balance. The actual ending unassigned fund balance will depend in part on $193 million in expected FEMA reimbursements, some or all of which could be delayed into fiscal 2022. The unassigned fund balance generally makes up only about 30%–40% of the unrestricted (committed, assigned and unassigned) fund balance.

The county's fiscal 2022 budget assumes a 3% gain in property tax revenue and a 5% gain in total revenue compared to third quarter estimates for fiscal 2021. The budget appropriations include about $209 million to support one-time projects, including some capital. In addition, the budget appropriates $157 million of ongoing revenue for one-time purposes to facilitate ongoing budget balance given some uncertainty about the strength of the economic recovery and the cessation of federal stimulus.

As of the end of fiscal 2020 (last available audit), the general fund's unrestricted fund balance (committed, assigned and unassigned) totaled $1.7 billion, or 38% of expenditures and transfers out. While the county may draw on its unrestricted fund balance, Fitch expects the county to maintain a 'aaa' financial resilience assessment given its strong starting position, as well as other efforts to balance its revenues and expenditures over time.

Credit Profile

The county's population growth rate has been modestly below average, rising 6.6% between 2010 and 2020 compared to 7.4% nationally. Prior to the pandemic, employment levels had increased steadily since 2010, while unemployment rates had fallen below 4%. Employment is weighted modestly above average in government, leisure and hospitality and professional and businesses services compared to national employment trends, reflecting the large military presence in the county and the strong tourism foundation given its coastal location.

According to Fitch's Oct. 19, 2021 "U.S. Metro Labor Markets Tracker," the San Diego-Carlsbad MSA was 44th out of 53 large metros in terms of jobs recovered between April 2020 and August 2021. The county's unemployment rate was still above the national average in August at 5.8%, compared with 4.1% nationally. As in other MSAs, the leisure and hospitality sector was the most heavily impacted by the pandemic and has been slower to recover.

The county assessor made temporary downward adjustments to some commercial values (primarily hotels, restaurants and shopping centers), resulting in a loss of $2.9 billion in fiscal 2022 taxable assessed value (TAV), which was more than offset by new properties and increased values from ownership changes. There was a net gain of $20.3 billion in TAV (3.4% over fiscal 2021 TAV). Home prices increased 12% in 2020, and the county expects around a 4% gain in TAV in fiscal 2023.

Revenue Framework

Intergovernmental revenues accounted for about 57% of total general fund revenues in fiscal 2020. Intergovernmental funding largely represents state and federal support for mandated health and human services programs managed by the county, including transfer payments. Property taxes provide the bulk of general purpose revenues, which fund the county's discretionary budget. Taxes accounted for 30% of general fund revenues in fiscal 2020.

Fitch expects revenue growth to closely track U.S. economic growth. Trends in total general fund revenues are heavily influenced by the county's receipt of intergovernmental revenues, which are largely determined by caseload trends, as well as state and federal service mandates. While intergovernmental revenues vary over time, these program revenues match related expenditure obligations well, and the county's disciplined practice of not backfilling cuts in social programs has allowed it to maintain fiscal balance even as state and federal funding have changed over time.

The 10-year CAGR of total revenues through fiscal 2020 had exceeded inflation and GDP growth over time. Fitch expects revenue growth to continue to exceed GDP given continuing population and property value growth.

Locally generated tax revenues fund the county's general purpose budget and are driven by its strong property tax base and population growth. TAV growth (which drives the county's property tax revenues) rose 4.6% annually on average for the decade through fiscal 2022.

Like other California local governments, the county's independent legal ability to raise revenues is limited by state constitutional provisions requiring voter approval for tax increases. The county retains the ability to set fees and service charges at sufficient levels to recover costs, and it updates such items regularly as part of its annual budget process.

Expenditure Framework

Health and human services spending represents about half of total general fund expenditures, and public safety accounted for less than 40% of spending in fiscal 2020. While transfer payments form a large part of the health and human services budget, compensation costs predominate in the general fund budget. The county does not own a public safety net hospital; therefore, it does not face the same degree of healthcare spending pressures that other large urban counties must manage.

Based on current spending practices, Fitch expects the natural pace of expenditure growth to track revenue growth in the absence of policy action. The assessment reflects the matching of social services spending to underlying funding and strong tax revenue growth that is expected to keep pace with rising salary and benefit costs within the general fund budget. The county is at the end of five-year labor contracts (expiring at the end of fiscal 2022 and fiscal 2023) with the vast majority of its employees. Annual salary increases range between 1% and 3%, and the current agreements include a new retirement tier with modestly lower retirement benefits, which will reduce retirement costs over the very long term as more employees are hired into the new tier and employees from other retirement tiers retire.

The county's expenditure flexibility is solid. Fixed costs for debt service and retiree benefits are moderate at about 14% of governmental expenditures in fiscal 2020. The county's longstanding practices of funding capital needs from current resources and other post-employment benefits (OPEB) at actuarial levels provide ready sources of additional flexibility should the county need to reduce expenditures to address a budgetary imbalance. The county's labor framework is manageable and typical for California, with management retaining the right to impose terms in the rare instances where labor negotiations reach an impasse. Most of the county's multiyear labor contracts expire at the end of fiscal 2022, with the Deputy Sheriff's contract extending through the end of fiscal 2023.

Long-Term Liability Burden

Long-term liabilities, including net pension liabilities (NPLs) and overall debt, are at the low end of the moderate range relative to the county's resource base at approximately 11% of personal income. Debt issuances of overlapping jurisdictions account for about two thirds of total liabilities, and direct debt makes up less than 6%.

Outstanding Debt

San Diego County (2012 Cedar and Kettner Development Project) Certificates of Participation	AA+
San Diego County (Cedar and Kettner Development) Refunding Certificates of Participation (Taxable)	AA+
San Diego County (County Administration Center Waterfront Park) Refunding Certificates of Participation	AA+
San Diego County (Edgemoor and RCS Refunding) Certificates of Participation	AA+
San Diego County (Justice Facilities Refunding) Certificates of Participation	AA+
San Diego County Pension Obligation (Current Interest) Bonds	AA+
San Diego County Pension Obligation Bonds	AA+
San Diego County Pension Obligation Bonds (Taxable)	AA+
San Diego Regional Building Authority (County Operations Center) Lease Revenue Refunding Bonds	AA+

NPLs are the county's largest direct liability, accounting for slightly more than a quarter of the total long-term liability burden. The county's 2020 NPL equaled about $6.0 billion when adjusted to a standard 6% return rate assumption. While pension liabilities are significant, the county has worked to address the issue in recent years, having made additional pension payments beyond actuarial requirements, prepaying a significant amount of POB debt service and setting aside in restricted general fund balance about $300 million for future payments. Pursuant to the county's charter, once funds such as these have been appropriated, they may not be used for any other purpose.

The county has also been increasing ongoing contributions to the plan by funding more than the actuarially determined contribution and as a result of the reduced rate of return assumption made in recent years (from 7.5% in fiscal 2015 to 7.0% in fiscal 2019). The county closed its OPEB plan to new entrants in 2007, and its unfunded liability was very modest at $106 million at the end of fiscal 2020, equal to 0.1% of personal income. The county has been fully funding its OPEB actuarially determined contribution of about $18 million for several years.

Operating Performance

The Fitch Analytical Stress Test (FAST) scenario analysis tool relates the county's historical general fund revenue volatility to GDP to support the assessment of operating performance under Fitch's criteria. FAST is not a forecast (actual revenue declines will vary from FAST) but it provides a relative sense of revenue risk exposure across Fitch's local government portfolio. The county's FAST revenue volatility is moderate relative to Fitch's U.S. local government sector, which is indicative of the county's stable revenue structure.

Fitch expects the county to maintain the highest degree of fundamental financial flexibility throughout economic cycles. This expectation reflects the county's strong reserve position, solid expenditure flexibility, satisfactory revenue-raising capacity and thorough and conservative budget planning and reserve policies. The county's unrestricted general fund balance equaled $1.7 billion, or 38% of spending, at the end of fiscal 2020. The county has a strong track record of making ongoing budget adjustments as needed to maintain or restore budgetary balance. The county only drew on reserves modestly in one year during the Great Recession and, during the current recession, Fitch expects the county to reduce expenditures and use a moderate amount of reserves while maintaining its reserve safety margin consistent with the 'aaa' resilience assessment.

Budget management is also quite strong. The county has built up reserves significantly during the current economic expansion with regular additions to its already healthy reserves. It makes actuarially determined pension and OPEB contributions, and it is actively working to reduce accrued liabilities.

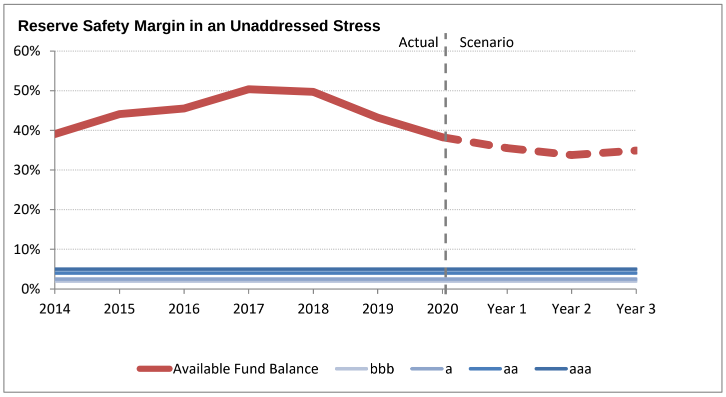
ESG Considerations

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, due to either 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.

San Diego County (CA)

Scenario Analysis

Ver 48



Analyst Interpretation of Scenario Results

The FAST scenario analysis tool, which relates the county's historical general fund revenue volatility to GDP to support the assessment of operating performance under Fitch's criteria. FAST is not a forecast (actual revenue declines will vary from FAST), but it provides a relative sense of revenue risk exposure across Fitch's local government portfolio. The county's FAST revenue volatility is moderate relative to Fitch's U.S. local government sector, which is indicative of the county's stable revenue structure.

The county has a strong track record of making ongoing budget adjustments as needed to maintain or restore budgetary balance, and Fitch expects the county to reduce expenditures and use a moderate amount of reserves while maintaining its reserve safety margin consistent with the 'aaa' resilience assessment.

Scenario Parameters:			Year 1	Year 2	Year 3
GDP Assumption (% Change)			(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)			2.0%	2.0%	2.0%
Revenue Output (% Change)	*Min Y1 Stress:* **-1%**	*Case Used:* **Moderate**	(1.0%)	3.0%	5.0%
Inherent Budget Flexibility				Midrange	

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2014	2015	2016	2017	2018	2019	2020	Year 1	Year 2	Year 3
Total Revenues	3,442,685	3,513,002	3,600,031	3,523,189	3,759,736	3,897,406	4,304,496	4,261,451	4,388,606	4,606,227
% Change in Revenues	-	2.0%	2.5%	(2.1%)	6.7%	3.7%	10.4%	(1.0%)	3.0%	5.0%
Total Expenditures	3,443,562	3,486,256	3,607,213	3,509,323	3,732,466	3,870,667	4,298,362	4,384,329	4,472,016	4,561,456
% Change in Expenditures	-	1.2%	3.5%	(2.7%)	6.4%	3.7%	11.0%	2.0%	2.0%	2.0%
Transfers In and Other Sources	272,657	282,503	296,852	301,128	352,061	311,769	308,428	305,344	314,455	330,048
Transfers Out and Other Uses	199,824	153,653	171,752	178,754	219,588	222,301	270,454	275,863	281,380	287,008
Net Transfers	72,833	128,850	125,100	122,374	132,473	89,468	37,974	29,481	33,074	43,040
Bond Proceeds and Other One-Time Uses	-	-	-	-	-	-	-	-	-	-
Net Operating Surplus/(Deficit) After Transfers	71,956	155,596	117,918	136,240	159,743	116,207	44,108	(93,398)	(50,336)	87,811
Net Operating Surplus/(Deficit) (% of Expend. and Transfers Out)	2.0%	4.3%	3.1%	3.7%	4.0%	2.8%	1.0%	(2.0%)	(1.1%)	1.8%
Unrestricted/Unreserved Fund Balance (General Fund)	1,422,848	1,605,703	1,720,420	1,857,815	1,964,598	1,768,317	1,748,991	1,655,593	1,605,258	1,693,069
Other Available Funds (GF + Non-GF)	-	-	-	-	-	-	-	-	-	-
Combined Available Funds Balance (GF + Other Available Funds)	1,422,848	1,605,703	1,720,420	1,857,815	1,964,598	1,768,317	1,748,991	1,655,593	1,605,258	1,693,069
Combined Available Fund Bal. (% of Expend. and Transfers Out)	39.1%	44.1%	45.5%	50.4%	49.7%	43.2%	38.3%	35.5%	33.8%	34.9%

Reserve Safety Margins	Inherent Budget Flexibility				
Moderate	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	16.0%	8.0%	5.0%	3.0%	2.0%
Reserve Safety Margin (aa)	12.0%	6.0%	4.0%	2.5%	2.0%
Reserve Safety Margin (a)	8.0%	4.0%	2.5%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.0%	2.0%	2.0%	2.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's scenario analysis assumes the GDP and expenditure growth sequence shown in the 'Scenario Parameters' section. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

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