

CREDIT OPINION

17 March 2016

New Issue

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Harrisonburg, VA

New Issue - Moody's assigns Aa2 to Harrisonburg's (VA) \$39.8M General Obligation Public Improvement Bonds, Series 2016

Summary Rating Rationale

Moody's Investors Service has assigned a Aa2 rating to the city of Harrisonburg's (VA) \$39.8 million General Obligation Public Improvement Bonds, Series 2016. Concurrently, we have affirmed the Aa2 rating on the city's \$156 million of outstanding GO debt. The Aa2 rating reflects the city's strong local economy stabilized by the presence of James Madison University, the city's stable financial position with satisfactory reserves, and an above average, but manageable debt burden.

Credit Strengths

- » Stable and diverse tax base with institutional presence
- » Sound financial position bolstered by policies
- » Conservative approach to budgeting

Credit Challenges

- » Above average debt burden
- » Below average wealth levels

Rating Outlook

Outlooks are generally not assigned to local government credits with this amount of debt outstanding.

Factors that Could Lead to an Upgrade

- » Growth in tax base and wealth levels
- » Increase in reserve levels
- » Decreased debt burden

Factors that Could Lead to a Downgrade

- » Significant contraction in tax base
- » Decline in reserve levels

» Elevated debt burden

Key Indicators

Exhibit 1

Harrisonburg (City of) VA	2011	2012	2013	2014	2015
Economy/Tax Base					
Total Full Value (\$000)	\$ 4,324,498	\$ 4,398,795	\$ 4,339,324	\$ 4,334,809	\$ 4,352,461
Full Value Per Capita	\$ 86,391	\$ 86,485	\$ 83,245	\$ 82,392	\$ 81,368
Median Family Income (% of US Median)	85.0%	83.4%	83.4%	83.4%	83.4%
Finances					
Operating Revenue (\$000)	\$ 112,461	\$ 119,137	\$ 124,206	\$ 128,367	\$ 128,807
Fund Balance as a % of Revenues	23.8%	26.8%	25.0%	24.6%	20.9%
Cash Balance as a % of Revenues	25.7%	28.3%	26.4%	27.2%	24.6%
Debt/Pensions					
Net Direct Debt (\$000)	\$ 171,678	\$ 168,534	\$ 134,553	\$ 169,503	\$ 159,074
Net Direct Debt / Operating Revenues (x)	1.5x	1.4x	1.1x	1.3x	1.2x
Net Direct Debt / Full Value (%)	4.0%	3.8%	3.1%	3.9%	3.7%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	0.7x	1.0x	1.2x	N/A
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	1.9%	2.9%	3.6%	N/A

Source: Moody's Investors Service

Detailed Rating Considerations

Local Economy Continues to Grow; James Madison University Provides Stability

Harrisonburg's local economy will likely continue to benefit from the stabilizing presence of James Madison University and modest commercial, residential and retail development in the city. The city is the county seat of Rockingham County (Issuer rated Aa2) and is located in the Shenandoah Valley, approximately 120 miles from both Richmond (GO rated Aa2 stable) and Washington, D.C. (GO rated Aa1 stable).

Harrisonburg's economic anchor and largest employer (approximately 3,600 employees), James Madison University (JMU), is a major educational institution and part of the Commonwealth of Virginia's (GO rated Aaa stable) higher education system. Enrollment has grown to over 21,000 students, mostly located within the city limits, representing a considerable 42% of the city's 2010 estimated population. JMU continues to invest in the local economy with \$460 million in capital projects including Forbes Performing Arts Center, Bridgeforth Stadium, JMU Duke Hall, and the Port Republic Road Athletic Fields. A report compiled by JMU's Office of Institutional Research and the Virginia Employment Commission determined that, in 2009, JMU provided an economic impact of \$448 million to the economies of Harrisonburg and Rockingham County.

The city's tax base is also home to a vibrant, increasingly diverse commercial and industrial base that includes retail, auto parts, software, electronics, agribusiness and packaging product manufacturers. Tourism primarily related to the Shenandoah National Park has also driven growth in the local economy. In 2014, the City of Harrisonburg had total travel expenditures of \$112.7 million, a travel-related payroll of \$21.1 million, and 1,097 travel-related jobs.

The city's \$4.3 billion tax base continues to grow, albeit at a more moderate rate than previous years. Average annual growth since 2010 totaled 0.5%, inclusive of a 8.5% increase in 2010. Officials expect modest growth going forward. In addition to the university, the city's economy has seen ongoing industrial development, aided by the relative low cost of living and doing business in the city, as well as a variety of economic development initiatives designed to leverage the university to attract new employers. Partly due to the large student population, per capita income at \$17,080 (51.0% of VA 60.7% of US) and median family income at \$53,588 (69.8% of

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VA and 83.4% of US) remain below state and national medians. The city's unemployment, at 4.6% continues to trend lower than the state and nation.

Satisfactory Reserves Despite One-Time Capital Use in Fiscal 2015

Because of conservative budgeting practices, the city's financial position is likely to remain stable with sound reserve levels through the medium term. Most recently, the city ended fiscal 2015 with a \$5 million decline in General Fund balance, driven largely by a \$2.4 million transfer to the capital projects fund. Additionally, the city transferred \$2.7 million to the Sanitation Enterprise Fund to offset a landfill closure contractual liability and \$800,000 to schools for construction projects. Following a 6 cent property tax increase and strong collections, the city realized additional property tax revenue of \$3.9 million. Economically sensitive revenues performed favorable to budget as well.

Officials are projecting a 3.8% growth in sales tax revenue for fiscal 2016. This assumption is reasonable given that in fiscal 2015 sales tax increased 4.8% over fiscal 2014. The city ended with an unassigned General Fund balance of \$24.2 million, or a still strong 25% of General Fund revenues), which is well above the city's policy to maintain 18%.

The city's primary revenue source is property taxes (38.7%), followed by other local taxes (37.8%) representing an elevated dependency on economically sensitive revenues. The exposure to a somewhat economically volatile revenue source is mitigated by the city's conservative approach to budgeting for these revenues.

The fiscal 2016 budget totals \$102.1 million and includes a \$750,000 appropriation of fund balance for one-time payment to the Harrisonburg-Rockingham Emergency Communications Center for a radio communications upgrade project. The budget includes a funding increase for Harrisonburg Public Schools and public safety. Based on preliminary revenue and expenditure estimates, the city is expected to have structurally balanced operations in fiscal 2016.

LIQUIDITY

Despite a decline from fiscal 2014 to fiscal 2015, the city's cash position remains healthy. Cash totaled \$25.4 million in fiscal 2015 down from \$29.1 million in fiscal 2014, representing a still satisfactory 26.3% of revenues.

Above-Average Debt Burden to Remain Manageable

The city's debt profile is expected to remain manageable given anticipated modest growth in the city's tax base despite plans for additional borrowing. The city's overall debt burden is an above average 4.3% of full valuation when compared to the state (2.7%) and national (1.1%) medians for similarly rated entities, but remains well within the city's policy of 6%. The city maintains a five-year (2016-2020) \$302 million Capital Improvement Plan (CIP), which includes school-related capital project for the first time in the city's capital planning process, representing nearly 60% of projects. Debt service represented a moderate 9.2% of operating expenditures in fiscal 2015 which is well below the city's policy of 15%.

DEBT STRUCTURE

Amortization is slightly below average with 68% of principal retired within 10 years.

DEBT-RELATED DERIVATIVES

Harrisonburg has no exposure to variable-rate debt or derivative agreements.

PENSIONS AND OPEB

The city and the city school board participate in the Virginia Retirement System a multi-employer defined benefit pension plan run by the Commonwealth of Virginia. The city's combined adjusted net pension liability, under Moody's methodology for adjusting reported pension data, is \$176.2 million, or approximately an above-average 1.37 times operating revenues. Moody's uses the adjusted net pension liability to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities. We determined the city's share of liability for the state-run plans in proportion to its contributions to the plans. Fixed costs including annual pension, OPEB and debt service expenditures summed to a moderate 15.6% of expenditures.

Harrisonburg Benefits from Strong Management Team and Comprehensive Policies

Harrisonburg has strong management including monthly budget reporting and sound policies covering fund balance and reserves, debt, asset maintenance, and capital planning. Virginia cities have an institutional framework score of "Aaa," or very strong. City revenues are

highly predictable as the majority come from property taxes. Revenue raising ability is high because cities have the ability to increase property tax rates annually, without limit. Expenditures, which are primarily for educational costs, are highly predictable and cities have a strong legal ability to reduce costs quickly if needed given a modest fixed cost burden and no collective bargaining units.

Legal Security

The bonds are secured by the city's general obligation unlimited tax pledge.

Use of Proceeds

The 2016 GO Bonds will fund construction of new elementary school and pre-k facility, an HVAC system at the school, road improvements, pedestrian and bike trails.

Obligor Profile

The City of Harrisonburg is located in the geographic center of the Shenandoah Valley of Virginia. Home to James Madison University which has a student population of 21,000. The city has a population of 53,491.

Methodology

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

Ratings

Exhibit 2

Harrisonburg (City of) VA

Issue	Rating
General Obligation Public Improvement Bonds, Series 2016	Aa2
Rating Type	Underlying LT
Sale Amount	\$39,815,000
Expected Sale Date	04/04/2016
Rating Description	General Obligation

Source: Moody's Investors Service

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REPORT NUMBER 1020128

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