Memorandum

CITY OF DALLAS

DATE October 8, 2021

TO Honorable Mayor and Members of the City Council

SUBJECT **Kroll Bond Rating Agency Affirms ‘AA+’ Rating and Stable Outlook for City of Dallas General Obligation Bonds - Information**

On October 4, 2021, Kroll Bond Rating Agency (KBRA) affirmed the ‘AA+’ credit rating and stable outlook for the City of Dallas, Texas Series 2020 General Obligation Bonds and Equipment Acquisition Contractual Obligations, in a statutorily required annual review. The KBRA report states that the rating affirmation reflects “the City’s sound financial profile, disciplined, forward-looking financial management practices, healthy reserves, and ample liquidity,” while the stable outlook reflects “the City’s considerable budgetary flexibility and long-term favorable outlook for economic and revenue growth.”

According to the report, KBRA continues to view the City’s “strong financial profile reflecting fiscally conservative financial management practices, solid reserves, and healthy liquidity” and the “growing economic base, robust employment expansion and declining poverty levels” as credit positives. The report also states KBRA’s view of credit challenges to the City, including elevated pension costs, “property tax levy limitation” that could have an impact on expenditures, and a “partial reliance on sales tax receipts”. KBRA also notes, “while the ultimate trajectory of recovery from the COVID-19 pandemic remains uncertain, KBRA views continued growth in property values, together with a strong recovery in FY 2021 sales tax receipts, as indicative of the City’s economic resilience.”

This affirmed rating is a positive indication of the rating agency’s view of the City’s credit profile in anticipation of upcoming General Obligation debt issuances that are currently being reviewed by KBRA for a planned November 2021 bond sale. KBRA’s upcoming review will include updated information on financial policies and the adopted FY 2022 Budget, which further reinforce the City’s strong credit profile and marketability to investors.

Attached is the published report for your review. Please let me know if you need additional information.

M. Elizabeth Reich

M. Elizabeth Reich
Chief Financial Officer

[Attachment]

c: T.C. Broadnax, City Manager
Chris Caso, City Attorney
Mark Swann, City Auditor
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M. Elizabeth (Liz) Cedillo-Pereira, Chief of Equity and Inclusion
Directors and Assistant Directors

City of Dallas, Texas

Issuer		
Affirmed	**Ratings**	**Outlook**
General Obligation Refunding and Improvement Bonds, Series 2020A	AA+	Stable
General Obligation Refunding Bonds, Taxable Series 2020B	AA+	Stable
Equipment Acquisition Contractual Obligations, Series 2020B	AA+	Stable

Methodology

- U.S. Local Government GO Methodology
- ESG Global Rating Methodology

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Rating Summary: KBRA has affirmed the long-term rating for the City of Dallas, Texas Series 2020 General Obligation Bonds and Equipment Acquisition Contractual Obligations (collectively, "the Bonds"). The affirmation reflects the City's sound financial profile, disciplined, forward-looking financial management practices, healthy reserves, and ample liquidity. As a regional hub for technology, healthcare, finance and tourism, Dallas is among the nation's top-ranked cities for economic growth, with robust employment expansion and declining poverty levels.

The Bonds are secured by a pledge of an annual ad valorem tax levied on all taxable property within the City. The State Constitution and the City Charter limit the ad valorem tax rate to $2.50 per $100 of taxable assessed valuation for all purposes, including payment of debt service. The State Attorney General will not approve debt if, based on then current taxable property values, more than $1.50 of the maximum $2.50 is required for aggregate general obligation debt service, inclusive of the bonds being proposed.

In addition, effective January 1, 2020, the Texas Property Tax Reform and Transparency Act of 2019 (SB2) caps the City's ability to grow property tax revenue (without voter approval) at 3.5% per year. Revenue to pay voter approved debt is excluded from the SB2 cap, as is revenue growth from new construction. In KBRA's view, the combination of conservative forecasting, disciplined expenditure controls and continued growth in property values support the City's ability to maintain structurally balanced operations within the more constrained property tax revenue framework imposed by SB2. While the ultimate trajectory of recovery from the COVID-19 pandemic remains uncertain, KBRA views continued growth in property values, together with a strong recovery in FY 2021 sales tax receipts, as indicative of the City's economic resilience.

The City cites the positive impact of Federal stimulus on disposable personal income and unemployment levels, both of which have almost fully rebounded from sharp pandemic-related declines, as contributing to a recovery in General Fund revenues for the fiscal year ending September 30, 2021. The City was allocated COVID-19 federal funding totaling approximately $627.3 million.

Detailed Financial Management Performance Criteria (FMPC) originally adopted by City Council in 1978, as periodically revised, provide a policy framework for fiscal decision making and are an important contributor to the City's strong governance profile. Pursuant to the FMPC, the City maintains an unassigned General Fund balance, which includes Emergency and Contingency Reserves, of at least 50 days and not more than 70 days of General Fund operating expenditures less debt service. The FY 2020 unassigned fund balance in the General Fund of $250.4 million after interfund transfers, equated to 68 days of General Fund operating expenses less debt service. However, due to rapidly growing pension and overtime costs, the City's proposed biennial FY 2022 and FY 2023 budget projects the unassigned fund balance to decline to 40 days in FY 2024 and to only 8.4 days by FY 2026 (budgetary basis). The City states that it will not allow a budget imbalance to occur, and will maintain structural balance by corrective actions, including budget reductions and/or revenue increases.

The City's sizable tax-base and strong financial position help to mitigate the burden posed by elevated pension liabilities, in KBRA's view. Pension reforms enacted in 2017 have eliminated the prospect of the Police and Fire pension plan's insolvency, increased contributions, and reduced the net pension liability. While pension costs are expected to remain elevated, overall fixed costs are affordable, especially given the City's practice of rapid direct debt amortization. In the context of its otherwise conservative fiscal controls, KBRA does not view the City's plan for pension funding, which projects a long ramp-up to full funding, as reflective of credit weakness.

The Stable Outlook reflects the City's considerable budgetary flexibility and long-term favorable outlook for economic and revenue growth. The City has proven its ability to achieve budgetary balance through operating expense reductions and without the use of reserves. Fixed costs are expected to remain moderately elevated but affordable, given recent pension reforms.

Key Credit Considerations

The rating was affirmed because of the following key credit considerations:

Credit Positives
- Strong financial profile reflecting fiscally conservative financial management practices, solid reserves, and healthy liquidity.
- Growing economic base, robust employment expansion and declining poverty levels.

Credit Challenges
- Property tax levy limitation could adversely impact expenditure flexibility.
- Partial reliance on sales tax receipts for operations exposes revenue base to economic fluctuation.
- Pension costs are expected to remain elevated.

Rating Sensitivities

▪ Ability to adapt to the new property tax limitation without significant impact on operations would be viewed positively.	+
▪ Deviation from the City's practice of conservative budgeting would increase credit risk.	-

Key Ratios	
Population Growth 2010 to 2019	
City	11.7%
State	14.8%
United States	6.1%
Top 10 Taxpayers as a % of Total Assessed Value	4.06%
Assessed Property Value 5-Yr CAGR Through FY 2021	9.2%
Unassigned General Fund Balance as % of Expenditures at FYE 2020	21.6%
Direct and Overlapping Debt as a % of Full Market Value in FY 2020	3.6%
Direct Debt Amortized Within 10 Years	75%
Fixed Costs as a % of Governmental Expenditures in FY 2020	24.2%

Rating Determinants (RD)	
1. Management Structure and Policies	AAA
2. Debt and Additional Continuing Obligations	AA
3. Financial Performance and Liquidity Position	AAA
4. Municipal Resource Base	AA+

There have been no updates to the above-mentioned rating determinants since KBRA's surveillance report published on September 30, 2020. The report incorporates a more detailed discussion of each rating determinant and includes a bankruptcy assessment.

RD 1: Management Structure and Policies

The City's strong management practices include a comprehensive budget process, a two-year balanced budget requirement, active financial monitoring, defined reserve policies, and five-year revenue and expenditure projections for the General Fund and each of the enterprise funds. Detailed Financial Management Performance Criteria (FMPC) establish a targeted unassigned General Fund balance, including Emergency and Contingency Reserves, of not less than 50 days and not more than 70 days of General Fund expenditures, less debt service. The City's fiscal year begins October 1 and ends on September 30. The FY 2021 Emergency Reserve was budgeted at $35 million which is unchanged since at least FY 2019 and is sized, in part, to withstand a 5% decline in property values. Use of the Emergency Reserve requires a super majority of City Council.

State Statutory Framework

Property Taxes

The State Constitution and the City charter limit the ad valorem tax rate to $2.50 per $100 of taxable assessed valuation for all purposes, including payment of debt service. The State Attorney General will not approve additional general obligation debt if, based on then current taxable property values, more than $1.50 of the maximum $2.50 is required for aggregate debt service, inclusive of the bonds being proposed.

In addition to the statutory cap on ad valorem tax rates, the Texas Property Tax Reform and Transparency Act of 2019 (SB2) caps the City's ability to grow property tax revenue at 3.5% without voter approval. Revenue to pay voter approved debt is excluded from the cap, as is revenue growth from new construction. The effective date of the legislation is January 1, 2020; thus FY 2021 was the first year impacted by the 3.5% cap (a cap of 8.0% was previously in place).

Pursuant to the Property Tax Code, all property is required to be reappraised at least once every three years. State law limits the appraised value to the lesser of i) market value or ii) 110% of the appraised value for the preceding tax year plus the market value of all new improvements (the 10% Homestead Cap). Additionally, the City grants an exemption of 20% of the market value of residence homesteads, as well as an additional homestead limitation, for persons 65 years of age or older or disabled.

The City has 19 active tax increment zones. Ad valorem taxes generated from approximately $18.9 billion of 2021 tax year reported certified value are dedicated to the tax increment zones and thus not pledged to general obligation debt.

Property tax collection rates are favorable, with FY 2022 property tax revenues estimated to be 98.51% of the levy.

City Sales Tax

The State sales tax rate totals 8.25%, with 6.25% being the State's share and 2% representing the local share. Pursuant to the Municipal Sales and Use Tax Act, Texas Tax Code, Ch. 321, the City levies a 1% Local Sales and Use Tax within the City (the "City Sales Tax"), with proceeds credited to the General Fund and not pledged to the payment of the Obligations. An additional 1% of the sales tax is dedicated to Dallas Area Rapid Transit (DART) (AAA/Stable), a regional transportation authority.

Debt Limits

The City has ample debt capacity. The City Charter limits bonded debt payable from ad valorem taxes to 10% of assessed property value; additionally, the FMPC limits net GO debt to 4% of market value. The City's total bonded ad valorem debt is 3.6% of full market value as of September 30, 2020.

Labor Relations

The City recently settled two large lawsuits concerning pay. In FY 2018, $62 million of GO bond proceeds and bond premium were utilized for the settlement of a lawsuit for pay of uniformed police officers. In addition, in January 2019 the courts gave final approval to a $173 million settlement announced in 2018, related to police and fire pay that date as far back as the 1980s. The City again used GO bond proceeds to settle legal claims. The FY 2021 Budget assumed a total sworn police force of 3,095 by the end of the fiscal year. The City maintained the starting pay of a police officer/firefighter at $61,367 and budgeted $4.6 million in FY 2021 for police and fire step/grade increases. For FY 2022, the starting salary of a police/firefighter was increased by 4.6% to $64,194. The forecast assumes a 3% market increase in FY 2023 and a 3% merit increase annually in FY 2024 through 2026.

ESG Management

Environmental Factors

Matters relating to climate risk are under the purview of the Chief of Equity and Inclusion, who supervises the City's Office of Environmental Quality and Sustainability (OEQS). OEQS completed development of a Comprehensive Environmental and Climate Action Plan (CECAP) which was unanimously adopted by City Council in May 2020. The CECAP identifies objectives, actions and targets in the areas of air quality, emissions reductions, transportation sustainability, water resources protection, ecosystems/green spaces, and food access. A task force has been convened to advise on implementation of the CECAP. In keeping with the CECAP plan, the City's adopted FY 2022 Budget includes a total of $3 million in investments in additional air quality monitors throughout the City, testing of solar panels on City facilities, and a solar/energy storage initiative. The City also plans to relaunch efforts to reduce heat island effects and stormwater runoff through the planting of native trees.

The City Council also adopted a Green Energy Policy in 2019 and already uses 100% renewable energy for all municipal operations. The City's Energy Program Manager is responsible for the implementation of an energy management system to monitor energy use and opportunities for energy reduction.

To ensure the adequacy of future water supply, the City is finalizing components of the 150-mile Integrated Pipeline Project, which will connect the City's water supply system to Lake Palestine, providing an additional 102 million gallons per day to the system, sufficient to meet projected demand through 2050. The City is also completing a regional water supply project with the Tarrant Regional Water District, which is expected to improve reliability of supply.

Social Factors

The City's Chief of Equity and Inclusion is appointed by the City manager and is a member of the City's executive leadership team. City Council approved the City's first Racial Equity Resolution on March 24, 2021. The City's adopted FY 2022 budget funds various policy initiatives in line with the Racial Equity Resolution. Additionally, the Budgeting for Equity initiative of the City's bond and construction management program prioritizes projects located in underserved communities.

The proposed FY 2022 budget also includes infrastructure subsidies to incentivize developers to construct additional affordable housing, and to extend water, sewer and digital infrastructure into historically underserved areas of the city. The City plans to continue to provide over $100 million in rental assistance for pandemic victims using dedicated ARPA funding, and to make a $25 million contribution to leverage public and private investment in a program to reduce and prevent homelessness, in partnership with the County and other local stakeholders. Additionally, the budget includes an increase in the minimum wage for full-time City employees from $14.00 to $15.50 per hour in FY 2022 and to $16.00 per hour in FY 2023, reinstatement of market-based pay increases for uniformed employees and merit pay for non-uniformed employees, as well as a new parental leave benefit. A tiered health benefits contribution plan designed to provide all employees with affordable health benefits is in place.

Governance Factors

The City addresses cybersecurity threats in partnership with the U.S. Department of Homeland Security and has taken proactive steps to protect and secure its information technology and infrastructure, including operational controls and authentication enhancements, among other measures.

The City self-funds employee health insurance, most tort liability exposures, and certain workers' compensation claims, and uses commercial insurance where required and to insure city property (subject to a $750 thousand deductible per loss occurrence), as well as for workers compensation losses in excess of $1.5 million per occurrence.

RD 2: Debt and Additional Continuing Obligations

While the City has successfully relied upon pay-go financing, rapid debt amortization and the careful management of other continuing obligations to maintain a moderate pace of growth in total long-term liabilities, the adequacy of pension funding remains an area of credit focus. Please see KBRA's surveillance report published on September 30, 2020 for a more detailed discussion of this rating determinant.

Overall Direct and Overlapping Debt

Direct debt consists entirely of limited tax general obligation bonds and notes, of which $2.1 billion is outstanding as of September 30, 2021. (Figure 1) This amount includes $148.8 million in outstanding general obligation commercial paper notes issued under a $350 million commercial paper program approved by the City in October 2017. The program authorization requires maintenance of credit agreements sufficient to pay all amounts payable under the program.

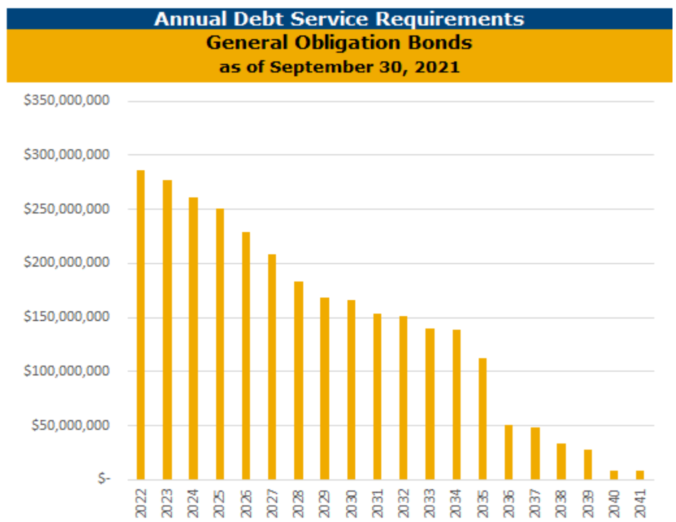
Figure 1

Direct Debt Outstanding as of September 30, 2021 (dollars in thousands)		
Direct Debt Type		9/30/2021
GO Bonds	$	1,744,760
GO Pension Bonds		201,730
Equipment Acquisition Notes		48,295
Combination Tax and Revenue Certificates of Obligation		17,065
GO Commerical Paper Notes[1]		148,756
Total Direct Debt	**$**	**2,160,606**

1. Projected outstanding as of 9/30/21
Source: City of Dallas

All outstanding long-term GO debt of the City is fixed rate. Debt service requirements are annually descending, with more than 75% of outstanding principal amortizing over the next decade. Maximum annual debt service (MADS) of $285.7 million occurs in FY 2022. (Figure 2)

Figure 2



Source: 2022 Proposed Budget. Does not include Commercial Paper Notes.

The City's overall direct and indirect debt burden is moderate at $4,715 per capita or 3.6% of the full market value of taxable property. Debt service comprised an elevated but manageable 13.6% of governmental expenditures in FY 2020. (Figure 3)

Pursuant to the City Charter, the maximum bonded indebtedness outstanding at any one time and payable from taxation is limited to 10% of assessed valuation. However, the FMPC limits net GO debt to 4% of the true market valuation of taxable property. The FMPC debt management criteria sets forth various debt metrics to ensure that the amount and term of GO and Contractual Obligation debt is in keeping with financial resources. The City expects to be in compliance with these metrics in FY 2021 and beyond.

Figure 3

City of Dallas, TX	
FY 2020 Debt Ratios	**Ratio**
Overall Direct and Indirect Debt:	
Per Capita	$4,715
As a % of Full Market Value	3.6%
Debt Amortization	
Within 10 Years	75%
Within 20 Years	100%
Debt Service as a % of Governmental Expenditures	13.6%

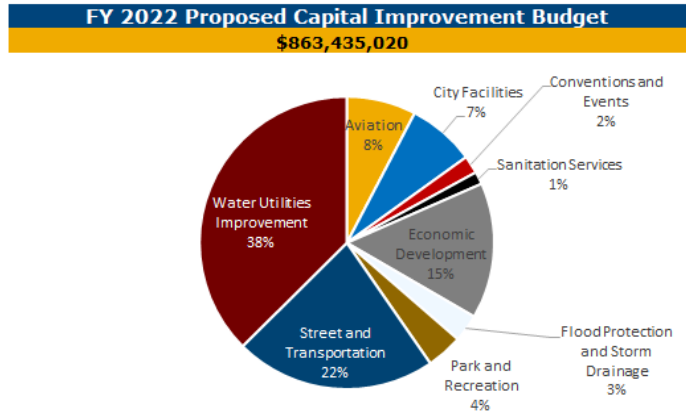
Source: City of Dallas

Capital Improvement Plan

The City maintains a comprehensive multi-year capital planning process encompassing the budget year plus two additional planned out-years. The City's proposed FY 2022 capital budget totals $863.4 million, including $445.1 million for general purpose capital improvements and $418.3 million for enterprise funds capital improvements. (Figure 4)

General purpose capital improvements address streets, parks and recreational facilities, libraries, police and fire protection facilities, cultural art facilities, flood protection and storm drainage, other City owned facilities and various economic initiatives. Enterprise fund capital improvements address water and wastewater, convention activity, airport facilities and sanitation services, and are primarily funded with revenue bonds and enterprise revenues.

Figure 4



Source: City of Dallas FY 2022 Proposed Budget

CIP Funding Sources

A $1.1 billion general obligation bond authorization for capital projects (the 2017 Bond Program) approved by voters in 2017 will be utilized through FY 2023. The City has spent or committed $456.9 million of this GO program budget to-date and anticipates issuing $178 million of GO debt in FY 2022 and 179.2 million in FY 2023. The City intends to continue its practice of initially funding projects with commercial paper, and subsequently refunding the CP with GO bonds.

Local Government Pension Obligation

The City participates in three single employer defined benefit pension plans. The Employees' Retirement Fund (ERF), Dallas Police and Fire System Combined Plan (DPFS Combined Plan) and the Dallas Police and Fire System Supplemental Plan (DPFS Supplemental Plan). The funding progress of the three plans, as measured by the ratio of fiduciary net position to total pension liability as of December 31, 2019, is weak at 64.6% for ERF, 43.5% for the DPFS Combined Plan, and 48.3% for the DPFS Supplemental Plan. However, the $22 million pension contribution remains manageable at 2.8% of FY 2020 full market value of taxable property, and 9.9% of governmental fund expenditures

Figure 5

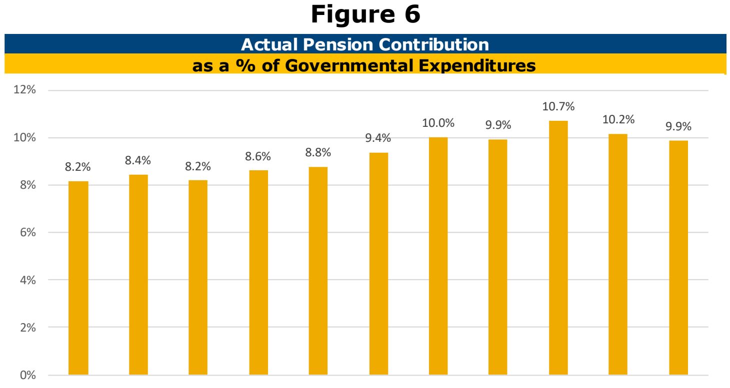
Pension Funding Status and Annual Contributions
FYE September 30 (dollars in millions)

	As of December 31, 2019 Measurement Date[1]				FY 2020		
	Total Pension Liability	Fiduciary Net Position	Net Pension Liability (NPL)	Fiduciary Net Position as a % of Total Pension Liability	Actual Contribution	Actuarially Determined Contribution (ADC)	Actual Contribution as a % of ADC
Employees' Retirement Fund (ERF)	$ 5,658.7	$ 3,658.1	$ 2,000.6	64.6%	$ 61.8	$ 92.6	66.8%
Dallas Police and Fire System Combined Plan (Combined Plan)	$ 4,732.0	$ 2,057.9	$ 2,674.1	43.5%	$ 161.9	$ 193.7	83.6%
Dallas Police and Fire System Supplemental Plan (Supplemental Plan)	$ 35.8	$ 17.3	$ 18.5	48.3%	$ 1.8	$ 1.8	100.0%
Total	**10,427**	**5,733**	**4,693**		**226**	**288**	**78.3%**

Source: CAFR

[1]As presented in FY 2020 CAFR.

Figure 6



Source: CAFRs

Employees' Retirement Fund (ERF)
The Employees' Retirement Fund (ERF) covers 16,498 members and beneficiaries as of December 31, 2019. In 2005, the City issued pension obligation bonds (POBs) for the ERF, of which roughly $127 million are outstanding as of September 30, 2021.

The City contributes 63% of the required ERF contribution, with membership contributing the remaining 37%. The City's contribution covers both POB debt service and ERF contributions. Although the total contribution is actuarially determined, contributions are adjusted to reflect provisions of City Code that (i) limit the combined employee and employer annual contribution to 36% of covered payroll, (ii) limit the annual maximum increase or decrease to 10%, and (iii) allow for adjustment of the contribution rate only if the actuarial valuation develops a rate which differs from the prior rate by more than 300 basis points. The total FY 2020 contribution was equivalent to the maximum allowed 36% of covered payroll, resulting in a contribution below the ADC. Of the City's portion of the payroll contribution, 14.20% was paid to the plan in cash and 8.48% was used to pay debt service on outstanding POBs. Because contributions fell short of the ADC, the actuarial valuation was based on a blended 5.93% discount rate. Voters approved a new benefit tier for ERF employees hired after December 31, 2016. The new tier increased the normal retirement age, thus lowering the fund's normal cost and future liabilities. The ERF includes an annual COLA based on CPI capped at 5% for members hired prior to December 31, 2016, and 3% for members hired thereafter.

Dallas Police and Fire System Combined Plan (Combined Plan)
The Dallas Police and Fire Pension System (DPFPS), a contributory defined benefit plan covering 10,402 members and beneficiaries as of December 31, 2019, experienced a funding crisis in 2015 and was expected to become insolvent in less than 10 years when the State Legislature intervened in May 2017[1]. House Bill 3158 amended State statutory provisions and created a 38-year path to 100% funding of DPFPS. HB 3158 imposes a minimum annual City contribution ranging from $165.9 million to approximately $169.6 million in each of fiscal years 2021 through 2024. Beginning in 2025, the City is expected to contribute only computation pay (hiring plan payroll), the amount of which may vary from actual payroll in 2025 and beyond[2]. Also among the reforms included in HB 3158 were a significant increase in employee contribution rates, elimination of COLAs until such time as the plan achieves a funded level of 70%, and a reduction in benefits for early retirement.

In December 2019, the DPFPS Board adopted its own funding policy which was amended in July 2020 and is reflected in the most recent actuarial valuation dated January 1, 2020[3]. The Board's provisions shorten the amortization period to a closed 25 years from 30 years, thus increasing the ADC, and require future gains or losses each year to be amortized over separate, closed 20-year periods on a level percentage of pay basis. Like the HB3158 funding policy, the Board's funding policy targets 100% funding of the actuarial accrued liability.

Given the large number of current members who have accrued benefits at the higher pre-HB 3158 levels and the long amortization period dictated by the funding policy contributions of HB 3158, the actuary expects that actuarial funding progress, as measured by a decline in the unfunded actuarial liability, will not occur for 20 years or more, even if all assumptions are met. The actuary's 2020 estimate projects that based on the funding policy adopted by the State in HB 3158 and the City's payroll projections, the Combined Plan will not reach full funding until 2075. This expected amortization period can vary on an annual basis (the full funding year was projected at 2057 in the 2019 valuation). The pension board is monitoring the City's payroll projections and is required to adopt further reforms, including additional funding from the City, if funding guidelines are not met by 2024.

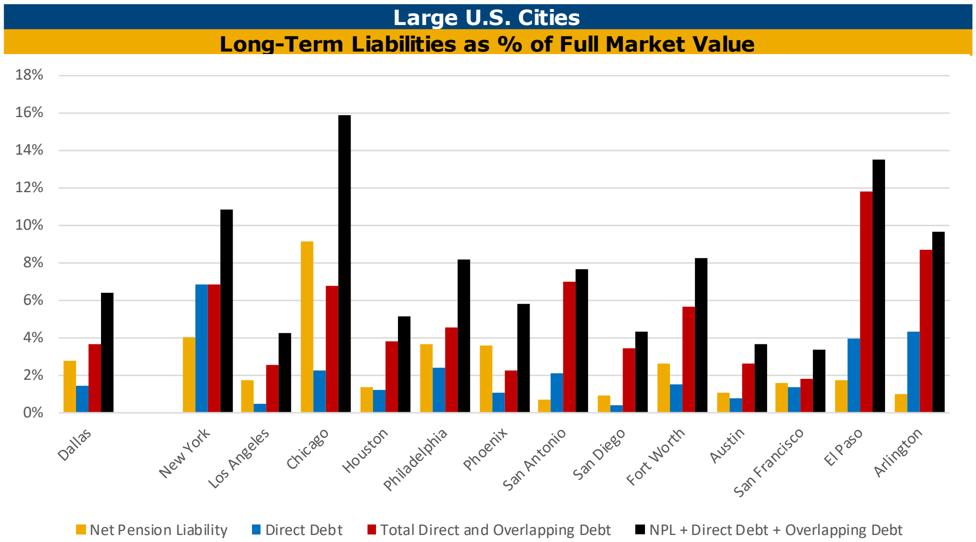
Total Pension Costs
The City's total FY 2020 pension contribution of $226 million was 78.4% of the actuarially determined contribution (ADC). While the funded position of the City's three pension plans is low, the FY 2020 net pension liability (NPL) across the three plans equates to only 2.8% of real property estimated market value and $3,570 per capita. KBRA considers these metrics to be favorable. Actual pension contributions in FY 2020 were 9.9% of governmental expenditures, down from 10.2% in FY 2019. Considering the City's favorable income and wealth levels as well as its rapidly declining debt service profile, pension obligations, while elevated, are manageable in KBRA's view.

Other Post-Employment Benefits (OPEB)
The City provides post-retirement healthcare benefits to 9,176 members as of FYE 2020. OPEB costs are moderate, and the long-term cost trajectory of the OPEB plan is contained since City-subsidized retirement healthcare benefits are only available to employees hired prior to January 1, 2010. The net OPEB liability as of September 30, 2020 was $531 million. FY 2020 benefit payments for retiree healthcare were $18.6 million, which represents a low 0.8% of governmental fund expenditures.

[1] Combined Plan provisions per State statute may only be amended by the state legislature.
[2] Differences between actual payroll and the City's hiring plan payroll in 2025 will impact when the System is projected to be fully funded. The City's plan reflects significant growth in payroll over 20 years which, if not realized, would slow actuarial funding progress.
[3] Based on plan assets as of December 31, 2019.

Fixed Costs
The City's FY 2020 fixed cost burden inclusive of pension contributions ($226 million), OPEB benefit payments ($18.6 million), and annual debt service ($310.2 million) was $554.8 million, equivalent to an elevated 24.2% of governmental expenditures. As shown below, although fixed costs comprise close to a quarter of total governmental expenditures, long-term liabilities as a percentage of full market value are in line those of many large cities across Texas and the U.S.

Figure 7



Source: CreditScope and FY 2020 CAFRs

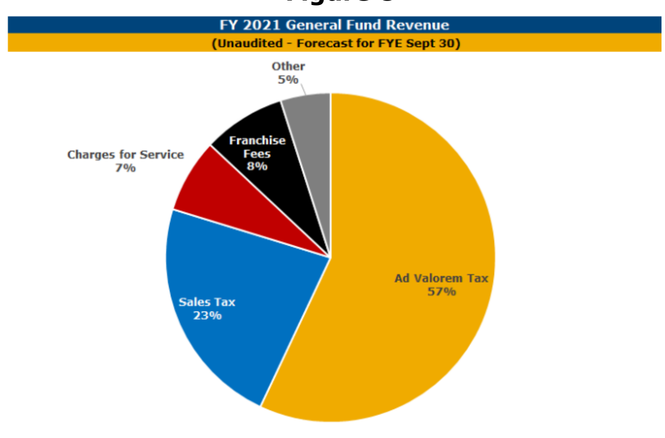
RD 3: Financial Performance and Liquidity Position

Financial operations reflect a trend of healthy operating surpluses and strong General Fund reserves with only modest sensitivity to recessionary impacts. The primary General Fund revenue sources, property taxes and sales taxes, account for 57% and 23% of forecast FY 2021 revenues, respectively. (Figure 8) In addition to the General Fund, other sizable components of governmental operations are the debt service fund, internal service fund and the water utilities fund.

The General Fund is the City's primary operating fund and the focus of KBRA's financial performance analysis. The City budgets on a cash basis of Generally Accepted Accounting Principles (GAAP) and the budget document is a complete financial plan for all City funds. The City Manager may transfer budgeted amounts within a department, while revisions altering total appropriations require City Council approval.

Property Tax
Property tax revenues support both the General Fund and the General Obligation Debt Service Fund. Strong growth in property tax values has contributed to consistent growth in ad valorem revenues despite year over year reductions in the tax rate since 2016. Of the FY 2021 ad valorem tax rate of 77.33 cents per $100 assessed value, approximately 20.75 cents is used to support debt service, with the remaining 56.58 cents used to pay for General Fund operating and maintenance costs.

Figure 8



Source: City of Dallas, TX.

The City's FY 2021 supplemental taxable assessed value[4] grew 6.35% from the prior year, to $149.1 billion, and continued to increase by 4.56% for FY 2022. The City forecasts future year property value growth to moderate to 3.5%, reflecting an expected reduction in the rate of growth of reappraisals and new construction, as well as the impact of the Texas Property Tax Reform and Transparency Act of 2019 (SB2). SB2 caps the City's ability to grow property tax revenue at 3.5% unless approved by voters. Revenue to pay voter approved debt is excluded from the cap, as is revenue growth from new construction. SB2 became effective January 1, 2020 (impacting FY 2021). In FY 2020 the levy increase for existing properties was 3.7%. Had SB2 been in effect for FY 2020, approximately $2.8 million in expenditure reductions would have been required to balance the budget.

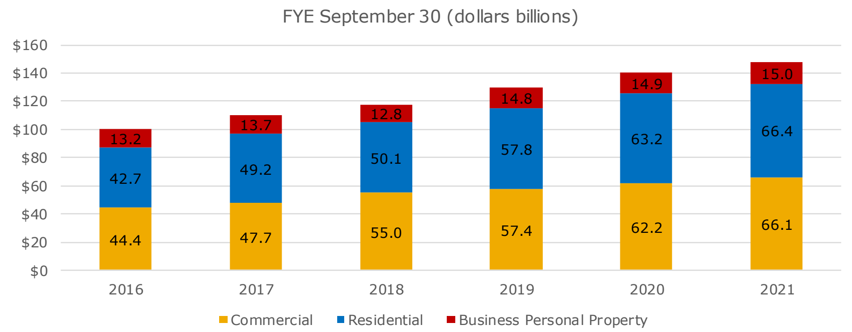
[4] FY 2021 supplemental values reflect values after resolution of disputes.

Property values in the City's 19 active Tax Increment Financing Zones (TIRZ) have increased dramatically in recent years. As of August 2021, over 47,000 new residential units were completed, under construction or planned, and more than 20 million square feet of commercial space has been built or redeveloped in the various TIRZ.

Figure 9

City of Dallas, TX

Taxable Assessed Valuation by Category



Source: City of Dallas

<u>City Sales Tax</u>

The 1% City Sales Tax is collected by the State and remitted monthly. It does not apply to motor vehicle sales or motor fuel sales, which somewhat tempers the inherent volatility of the revenue stream. Following a moderate 11% peak to trough decline during the Great Recession, sales tax revenues increased at a CAGR of 4.8% from FY 2011 through 2019.

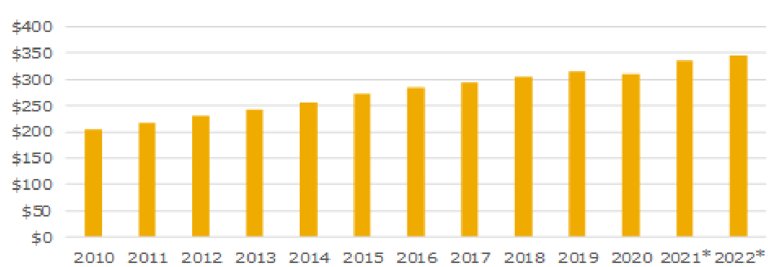
The pandemic caused sales tax revenues to decline sharply during the second half of FY 2020. Full FY 2020 sales tax revenues of $310.7 million were down 0.87% versus $313.5 million recorded in FY 2019. With the reopening of the local economy, sales taxes have recovered more quickly than anticipated. July 2021 monthly sales tax receipts (most recent available) are up 26% from July 2020. Cumulative sales tax receipts over the 12-month period from July 2020 to July 2021 have increased by a robust 9.5%, reflecting rebounding economic conditions. The City amended its budget for FY 2021 sales tax revenue from $296.3 million to $305.1 million during the mid-year appropriation process. Currently projected FY 2021 sales tax revenues of $336 million exceed the amended budget by approximately 10% and are 7.2% above FY 2019 (pre-pandemic) sales tax revenues. The City has budgeted a further 2.5% increase in sales tax revenues for FY 2022 reflecting expectations for continued growth tempered by lower disposable personal income and inflationary pressures.

Although the pandemic illustrated the volatility of sales tax and other economically sensitive revenues of the City, KBRA views the combination of conservative forecasting, disciplined budget practices, sound reserves and continued growth in property values as supportive of the City's ability to maintain structurally balanced operations within the more constrained property tax revenue framework imposed by SB2.

Figure 10

City of Dallas, TX

City Sales Tax Revenue FYE September 30 ($ millions)



Source: City of Dallas

*Projected

FY 2020 Audited Financial Results

Despite pandemic-related impacts on FY 2020 sales taxes, franchise fees, alcoholic beverage taxes, and other economically sensitive revenues, increases in ad valorem tax and operating grants allowed the City to maintain a trend of exceptional growth in reserves (15.4% CAGR in ending General Fund balance from FY 2016 through FY 2020).

Moreover, unassigned General Fund balance levels have consistently met or exceeded the City's policy. As of FYE 2020, unassigned General Fund balance grew to a very strong $250.4 million after interfund transfers, or 68 days of General Fund operating expenses less debt service, exceeding the FMPC's 40-day minimum in FY 2020. The minimum fund balance requirement was increased to at least 50 days but not more than 70 days of General Fund operating expenditures less debt service on June 9, 2021. FY2020 General Fund revenues grew 1.3% YoY, relative to 0.4% expenditure growth, thus increasing the operating surplus versus the prior year.

Figure 11

General Fund Summary Statement of Income and Balance Sheet FYE September 30 (Audited GAAP Basis) (dollars in thousands)	2016	2017	2018	2019	2020
Statement of Income					
Revenues					
Ad Valorem Tax	534,289	578,032	611,133	677,607	728,339
Sales Tax	285,669	295,361	307,149	320,413	314,385
Franchise Fees	135,098	138,998	146,209	135,697	120,944
Services to Others	109,736	126,498	122,924	109,491	102,021
Other	56,347	53,972	58,063	67,600	61,586
Total Revenues	1,121,139	1,192,861	1,245,478	1,310,808	1,327,275
Expenditures					
Public Safety	688,943	712,990	736,879	774,182	792,917
General Government	101,376	121,279	144,161	167,958	150,372
Culture and Recreation	128,089	136,984	143,813	141,594	132,749
Other	204,302	188,791	210,790	196,919	209,401
Total Expenditures	1,122,710	1,160,044	1,235,643	1,280,653	1,285,439
Excess (Deficiency) of Revenues Over (Under) Expenditures	(1,571)	32,817	9,835	30,155	41,836
Other Financing Sources (Uses)	6,432	11,316	11,255	10,745	5,641
Net Change in Fund Balance	**4,861**	**44,133**	**21,090**	**40,900**	**47,477**
Beginning Fund Balance	200,102	191,031	235,164	256,254	297,154
Restatement	(13,932)	-	-	-	-
Beginning Fund Balance After Restatement	186,170	191,031	235,164	256,254	297,154
Ending Fund Balance	**191,031**	**235,164**	**256,254**	**297,154**	**344,631**
Balance Sheet					
Assets					
Cash and Cash Equivalents	177,790	203,452	216,346	277,654	328,272
Receivables	113,905	142,490	142,466	119,530	128,026
Other	14,731	15,514	16,384	30,643	32,930
Total Assets	306,426	361,456	375,196	427,827	489,228
Liabilities					
Accrued Payroll	20,250	21,273	23,633	28,339	8,569
Accounts Payable	31,811	35,339	32,985	35,684	35,215
Other	22,112	20,648	12,680	13,416	44,083
Total Liabilities	74,173	77,260	69,298	77,439	87,867
Deferred Inflows of Resources (Unavailable Revenue)	41,222	49,032	49,644	53,234	56,730
Fund Balance					
Nonspendable	10,659	11,143	11,227	13,385	15,385
Restricted	9,593	12,061	10,244	11,185	8,724
Committed	1,250	1,250	1,250	1,250	2,000
Assigned	15,836	38,963	20,727	37,109	41,071
Unassigned	153,693	171,747	212,806	234,225	277,451
Total Fund Balance	**191,031**	**235,164**	**256,254**	**297,154**	**344,631**
Unassigned Fund Balance as a % of Expenditures	13.7%	14.8%	17.2%	18.3%	21.6%

Source: CAFRs

Liquidity Position

The City maintains ample liquidity as evidenced by consistent growth in year-end fund balance. The FY 2020 governmental funds cash position was $733 million, equating to a very strong 117 days cash on hand, with an additional $130 million of pooled cash and cash equivalents held in Internal Service Funds.

FY 2021 Operations and Forecasted Results

FY 2021 General Fund revenues rebounded more rapidly than anticipated. Forecast (unaudited) FY 2021 General Fund revenues of $1.5 billion are $31.9 million or 2.2% above budget, due primarily to stronger than anticipated property tax and sales tax receipts. The City forecasts FY 2021 General Fund expenditures of $1.5 billion, in line with budgetary expectations. The City projects an ending FY 2021 General Fund balance of $272.1 million, approximately 15% above the FY 2021 amended budget ending fund balance level.

FY 2022 and FY 2023 Budget Overview

The City Manager's proposed FY 2022 and FY 2023 biennial budget was submitted to City Council on August 10, 2021. The adopted $1.5 billion FY 2022 General Fund budget, up 6.2% from the FY 2021 amended budget, contemplates a $48.1 million or 4.1% increase in property tax revenues (despite a sixth consecutive annual decrease in the tax rate). Of this increment, approximately 52% is tax revenue to be raised from new property additions to the tax roll in FY 2021. The budget also projects a 13% increase in sales tax revenues over the amended FY 2021 budget (up 2.5% versus FY 2021 actuals).

The FY 2022 and FY 2023 budgets anticipate maintenance of the unassigned General Fund balance, which includes the Emergency and Contingency Reserves and residual reserves, at $272.1 million, or between 62 and 65 DCOH. While the budget projects a structural imbalance of $87 million in FY 2024 and a decline in the General Fund balance to $40.9 million (8.4 DCOH) by FY 2026 primarily as a result of increasing personnel costs, the City states that it will not allow a budget imbalance to occur, and will maintain structural balance by corrective actions, including budget reductions and/or revenue increases.

Reflecting legislative and community priorities made more tenable through the receipt of $355.4 million in ARPA funding, the proposed FY 2022 and FY 20233 biennial budget prioritizes the advancement of economic development, environment and sustainability, housing and homelessness solutions, public safety, culture and quality of life, transportation, infrastructure, and workforce, education and equity initiatives.

RD 4: Municipal Resource Base

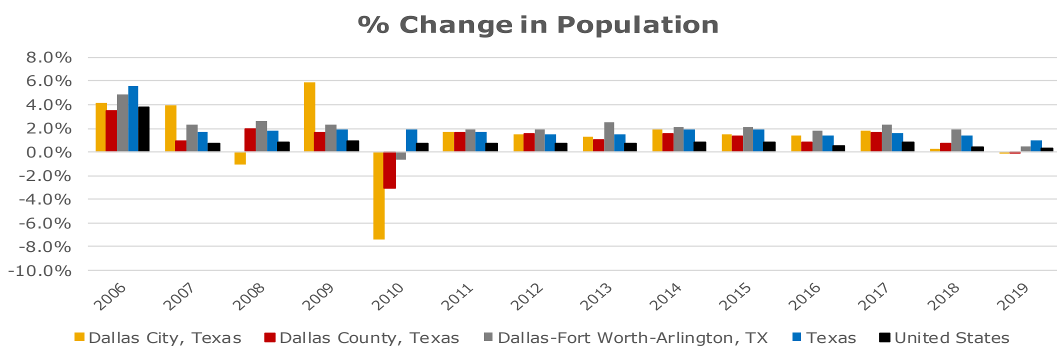
Incorporated in 1856, Dallas is approximately 378 square miles in area and is the county seat of the County of Dallas. The City, which is spread across four counties (Dallas, Collin, Denton and Rockwall) is the primary economic driver in the Dallas-Fort Worth-Arlington metropolitan statistical area (MSA), which is the fourth largest MSA in the nation behind the New York, Los Angeles, and Chicago.

The City is served by Dallas/Fort Worth International Airport ("DFW") (AA/Stable), which ranked 4th among commercial service airports in enplanements in 2019, before the COVID-19 pandemic, behind Hartsfield-Jackson Atlanta International, Los Angeles International, and Chicago O'Hare International (A+/Stable). In addition to DFW, Dallas Love Field and Dallas Executive Airport provide service to the City. The City is also a hub for rail service with lines to Chicago, Los Angeles, and San Antonio.

Population

The City is the 3rd largest city in the State of Texas (AAA/Stable) and 9th largest in the nation with a population of 1.3 million. Population growth in Dallas (11.7% since 2010) has significantly outpaced the nation but modestly lags the State. The City's growing employment base has fueled both domestic and international migration with foreign-born residents making up 24.8% of the City's population in 2019.

Figure 12



	2010	2019	Δ 2010 to 2019	10 Year CAGR (2019)
Dallas City, Texas	1,202,797	1,343,565	11.7%	0.33%
Dallas County, Texas	2,377,351	2,635,516	10.9%	0.73%
Dallas-Fort Worth-Arlington, TX	6,402,922	7,573,136	18.3%	1.62%
Texas	25,257,114	28,995,881	14.8%	1.58%
United States	309,349,689	328,239,523	6.1%	0.67%

Source: U.S Census

Per capita income of $36,288 is above the statewide average (112.5% of the State) reflecting the City's ability to attract higher wage jobs. With 48 colleges and universities in the Dallas MSA, educational attainment in the City surpasses the nation and state. The City's poverty rate of 17.5% is elevated relative to the state (at 13.6%) but has materially declined from 23.6% in 2010, which is a notable positive trend relative to other large cities.

Tax Base and Demographic Data

The City's taxable value has exhibited strong growth over the years, increasing by a 9.2% 5-Year CAGR to $155.9 billion in 2021. The City's tax base per capita is very strong at approximately $119,549. The top 10 taxpayers represent 4.06% of FY 2021 taxable assessed value, which KBRA views as diverse (Figure 13). Tax base concentration has declined from FY 2010, when the top ten taxpayers represented 5.28% of taxable assessed value. Property tax collections have historically been high, averaging over 98% annually since 2015. In FY 2020, the property tax collection rate was 98.2%.

Figure 13

City of Dallas Ten Largest Taxpayers			
Company	**Business**	**FY 2020-2021 Taxable AV ($000)**	**% of Taxable AV**
Oncor Electric Delivery co.	Electric Utility	$ 1,039,140	0.74%
Northpark Land Partners	Developer	$ 740,206	0.53%
Texas Instruments, Inc.	Electronics Mfg.	$ 707,863	0.50%
Southwest Airlines	Air Transportation	$ 653,943	0.47%
FM Village Fixed Rate LLC	Developer	$ 565,934	0.40%
AT&T Corporation	Telephone Utility	$ 550,322	0.39%
Atmos Energy	Gas Utility	$ 383,822	0.27%
Equinix LLC	Technology	$ 374,138	0.27%
Teachers Insurance	Insurance	$ 353,658	0.25%
Walmart Stores, Inc.	Retailer	$ 343,318	0.24%
Total		**$5,712,344**	**4.06%**

Source: City of Dallas 2020 Disclosure Tables

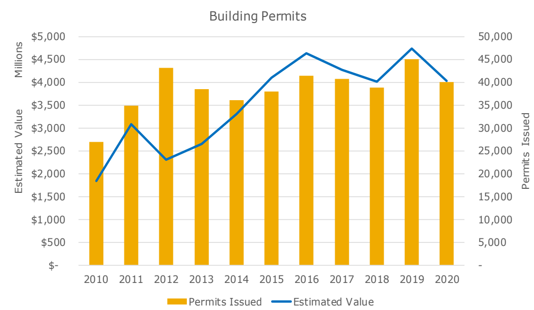
Economic Development Activities

The City has seen substantial commercial and residential development over the years as its population has grown. Since 2010, the number of building permits issued in the City has increased at a compounded annual growth rate of 4%, while the estimated value of new construction has increased by 8.1% to over $4.0 billion. The onset of the pandemic in 2020, however, negatively impacted new construction values and building permits issued which both declined from the previous year by 14.9% and 11%, respectively.

Employment

Since the Great Recession and prior to the incidence of the COVID-19 pandemic, City employment exhibited continuous growth. The City is the headquarters of nine Fortune 500 companies, including AT&T, Energy Transfer, Southwest Airlines and Texas Instruments. Despite pandemic-related declines in tourism related employment within the MSA, overall City employment as of July 2021 represents 101.5% of 2019 pre-pandemic levels, demonstrating significant resiliency, particularly compared to the State and nation, for which employment levels remain 1.5% and 2.5%, respectively, below pre-pandemic levels.

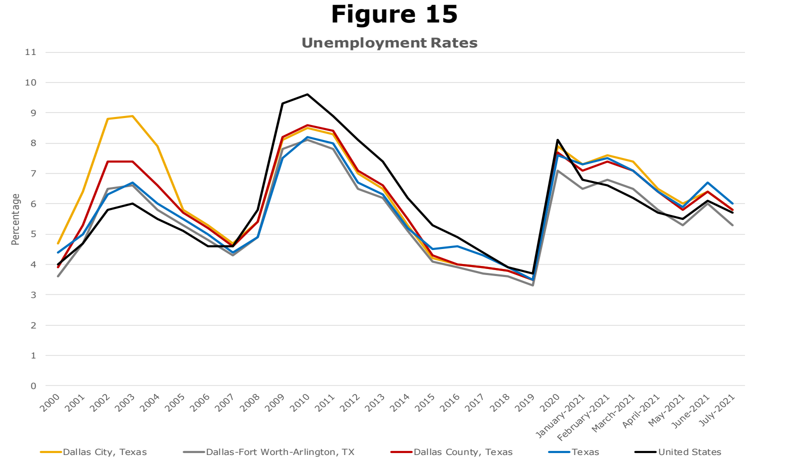
Figure 14



Source: City of Dallas Building Inspection Division

The City's unemployment rate declined each year from 2010 through 2019 and trended below that of the State from 2015 through 2019. As was the case in many urban areas, the onset of the pandemic in March 2020 caused the City's unemployment rate to surge from 3.5% in 2019 to 7.9% in 2020. As of July 2021, however, the City's unemployment rate of 5.8% is again below that of the State's at 6.0% and just slightly above the U.S. average of 5.7% (Figure 15).

Figure 15



	Dallas City, Texas	Dallas County, Texas	Dallas-Fort Worth-Arlington, TX	Texas	United States
July 2021	5.8	5.8	5.3	6.0	5.7
June 2021	6.4	6.4	6.0	6.7	6.1
Great Recession Peak	8.5	8.6	8.1	8.2	9.6
Point Δ Since Great Recession Peak	-2.7	-2.8	-2.8	-2.2	-3.9

Source: U.S Bureau of Labor Statistics