



RATING ACTION COMMENTARY

Fitch Upgrades Vestavia Hills, AL's GO Warrants and IDR to 'AAA'; Outlook Stable

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Fitch Ratings - New York - 25 Jan 2024: Fitch Ratings has upgraded the following ratings for Vestavia Hills, AL:

--City's Issuer Default Rating (IDR) to 'AAA' from 'AA+';

--Approximately \$85 million outstanding GO warrants to 'AAA' from 'AA+'.

The Rating Outlook is Stable.

RATING ACTIONS

ENTITY / DEBT ↕	RATING ↕	PRIOR ↕
Vestavia Hills (AL) [General Government]	LT IDR AAA Rating Outlook Stable Upgrade	AA+ Rating Outlook Stable
Vestavia Hills (AL) /General Obligation - Limited Tax/1 LT	LT AAA Rating Outlook Stable Upgrade	AA+ Rating Outlook Stable

[VIEW ADDITIONAL RATING DETAILS](#)

SECURITY

The warrants are general obligations of the city payable from all lawfully available revenues and funds, and secured by an irrevocable pledge of the full faith and credit of the city on an equal and proportionate basis of payment with all present and future general obligation indebtedness of the city, and subject to the prior payment of the necessary and reasonable expenses of operating the city.

ANALYTICAL CONCLUSION

The one-notch upgrade to 'AAA' of the ratings on the city's GO warrants and the IDR reflects Fitch's expectations for continued strong revenue growth supporting future budgets and maintenance of healthy reserves through economic cycles based on historical trends. The rating also reflects the city's low long-term liability burden with no current plans for additional debt and its broad revenue and spending flexibility.

Economic Resource Base

Vestavia Hills is an affluent residential community with a 2022 estimated population of 38,292, which is up 12.5% since the 2010 US Census. The city is located approximately three miles south of downtown Birmingham ('AA-' IDR), with the majority of the city falling within Jefferson County ('AA-' IDR) with parts reaching out into Shelby County.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

Growth prospects for revenues are strong and have improved with the city's ongoing economic development. The city has no independent ability to raise property taxes, but flexibility in sales tax and other locally generated revenues such as business licenses and fees provide a greater ability to offset expected revenue declines in a moderate economic downturn.

Expenditure Framework: 'aa'

Expenditure needs are expected to grow marginally above revenue growth based on typical spending needs. The state's flexible work force environment provides the city significant control over personnel costs. Fixed costs are manageable and largely devoted to debt service.

Long-Term Liability Burden: 'aaa'

The city's liability burden associated with direct and overlapping debt and Fitch adjusted net pension liabilities is low at 6% of residents' personal income. Direct city and overlapping debt of the city board of education and Jefferson County are the primary drivers of the liability. The city has no future debt plans as it plans to use state grants and pay-as-you go funding to support capital and transportation related needs.

Operating Performance: 'aaa'

Fitch expects the city to display a high level of financial resilience during economic downturns given its relatively stable revenue history, sizable reserves, and superior level of overall budgetary flexibility in the form of its revenue raising ability and solid expenditure flexibility.

RATING SENSITIVITIES

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

--Not applicable as the ratings are at Fitch's highest rating level.

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

--Material and prolonged deviation in the city's financial management and operating practices could pressure the rating;

--Although not expected, an increase in the long-term liability burden to a level that exceeds 10% of personal income;

--A sustained decline in unrestricted general fund reserves to a level closer to 10% of spending and/or inconsistent with a 'aaa' assessment and expectations for a slow recovery.

CURRENT DEVELOPMENTS

Vestavia Hills operating performance has improved as robust economic conditions the past four fiscal years have improved revenue performance leading to an increase in unrestricted reserves to very strong levels. A combination of population and tax base growth, a 1% increase in the sales tax rate effective June 2018, and taxation of online sales beginning in 2021, has supported growth in sales tax revenues and ad valorem tax revenues. Business licenses fees, which reflect sales activity, have also experienced growth coming out of the pandemic. The presence of four Publix supermarkets and a Walmart provided stability to

sales tax revenues during the pandemic because grocery sales, including food purchases, are not exempt from sales tax in Alabama.

The city has experienced surplus operations the past five fiscal years through fiscal 2022 (ended Sept. 30) with unrestricted reserve balances improving to \$24.8 million (44% of spending) from \$14 million in fiscal 2018 (35% of spending). It has historically maintained strong reserve levels, which have exceeded 30% since fiscal 2010. Results reflect positive revenue variances associated with sales taxes and do not include the \$9 million of general fund transfers out to support its capital project funds. Sales and use taxes accounted for 42% of general fund revenues followed by property tax revenues at 27%.

Included in the city's unrestricted reserve balance is \$15.4 million of committed funds for economic stabilization in case of an emergency, slightly exceeding its target goal of 25% of prior year spending and transfers out. American Rescue Plan Act (ARPA) funds have been used to support capital-related projects, and none have been utilized for general fund operating purposes.

Management is projecting another net operating surplus for the general fund of over \$3 million for fiscal end 2023 leading to further improvement of reserves and reflective of positive revenue variances compared to budget.

The fiscal 2024 general fund budget of \$66.4 million reflects a 11.5% increase in revenues compared to the fiscal 2023 budget. The budget increase is primarily associated with larger than usual increases in salaries for public safety and other employees to support retainage and meet market-based levels to remain competitive. Sales tax and property tax revenues are budgeted in line with fiscal 2023 actuals; however, management is projecting these revenues to exceed budget. Property values have experienced double-digit growth the last several years but according to management appear to be stabilizing, which Fitch considers reasonable considering the increase in mortgage rates and high, but improving, levels of inflation.

CREDIT PROFILE

Vestavia residents benefit from the proximity to the city of Birmingham's deep, diverse and stable employment base built around the education and health service sectors. Vestavia's workforce is highly educated, with income levels more than double the Alabama median and well above the national level. The city's unemployment rate is well below both the state and nation.

The city's tax base is diverse and growing with median home values more than double that of the county and state. Fitch expects future tax base and population levels to grow due to economic projects underway, including The Bray development of Liberty Park, a multi-year project and the largest part of the city's master development plan. The project includes approximately 1,800 new multi and single-family residential units and a 100-acre town center with retail outlets, a hotel, and medical and office space. Construction has begun on this phase of the development.

The Bray will also include the headquarters of Medical Properties Trust, a real estate investment company that specializes in health care facilities. The facility is under construction and expected to be completed December 2025. This new development should also drive new sales tax growth, which will help absorb the likely increase in spending for services associated with such projects.

Total carrying costs for debt service, required pension contributions and other post-employment benefits (OPEB) contributions were 16.6% of total governmental fund spending for fiscal 2022. Carrying costs are primarily devoted to debt service for GO warrants and short-term fleet and equipment leases. Overall carrying costs are expected to remain stable given an absence of additional borrowing plans. The city's workers are restricted by state law from organizing, which Fitch believes contributes to a high degree of control over personnel costs.

Fitch believes the city's superior level of budgetary flexibility combined with strong available general fund balance reserves provides the highest gap-closing capacity to manage through economic downturns. The city's conservative formal reserve policy requires a targeted goal of 25% of prior year spending as committed for emergency purposes. Fitch expects management will continue to budget conservatively and scrutinize future discretionary spending, helping to mitigate declines in the city's unrestricted reserve fund balance and maintain its high level of financial resilience.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit

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APPLICABLE CRITERIA

[U.S. Public Finance Tax-Supported Rating Criteria \(pub. 04 May 2021\) \(including rating assumption sensitivity\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

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Vestavia Hills (AL)

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