

CREDIT OPINION

25 March 2024


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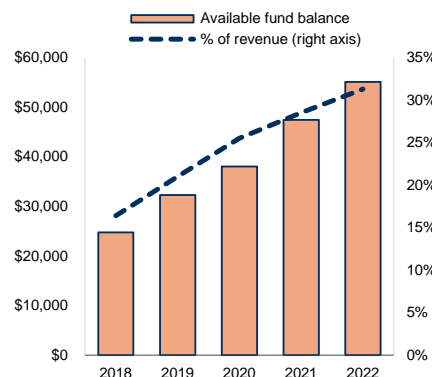
City of Allentown, PA

Update to credit analysis following upgrade to A2

Summary

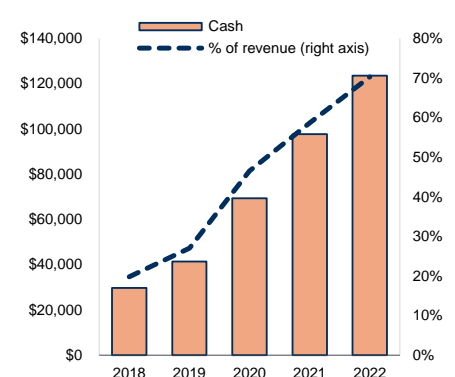
Moving on from a history of budget gimmickry, the City of Allentown (A2) has built a much more solid financial position (available fund balance was 31.3% as of 2022) amid a growing economy and revenues that continue to substantially exceed estimates. Allentown is still a low-income, high-poverty city – its adjusted median household income is just 71.2% of the US median – and its large Moody's-adjusted net pension liability remains a significant drag on its credit profile. Although Allentown may face political obstacles to increasing revenues if necessary to balance future budgets, sharp financial management will preserve a more solid financial position going forward.

Exhibit 1

Available fund balance has increased
\$ in thousands


Source: Moody's Ratings

Exhibit 2

Cash is far stronger
\$ in thousands


Source: Moody's Ratings

On March 25, we upgraded Allentown's issuer rating and general obligation ratings to A2 from A3, and removed the stable outlook on the ratings.

Credit strengths

- » Solid financial management featuring conservative budgeting and long-term planning
- » Outperformance in key tax revenues because of growing economy and expansion of large employers
- » Low debt

Credit challenges

- » Large Moody's-adjusted net pension liability
- » Low-income, high-poverty economic base
- » Political obstacles to increasing taxes

Rating outlook

Moody's does not maintain outlooks for local governments with this amount of debt outstanding.

Factors that could lead to an upgrade

- » Moderation of long-term liabilities
- » Continued improvement in resident income ratio to 80%
- » Sustained available fund balance ratio above 45% in the context of strengthened policies and stable financial management

Factors that could lead to a downgrade

- » Return to structural imbalance
- » Deterioration in available fund balance ratio below 25%
- » Reversal of recent growth and economic improvement of the city

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

Key indicators

Exhibit 3

Allentown (City of) PA

	2019	2020	2021	2022	A Medians
Economy					
Resident income ratio (%)	66.0%	67.6%	70.5%	71.2%	85.3%
Full Value (\$000)	\$4,693,181	\$4,750,763	\$5,122,164	\$5,127,830	\$765,032
Population	120,915	121,156	125,250	125,292	10,363
Full value per capita (\$)	\$38,814	\$39,212	\$40,896	\$40,927	N/A
Annual Growth in Real GDP	4.0%	-4.0%	3.6%	0.8%	4.7%
Financial Performance					
Revenue (\$000)	\$153,487	\$148,999	\$166,408	\$175,761	\$22,589
Available fund balance (\$000)	\$32,299	\$38,021	\$47,411	\$55,099	\$9,301
Net unrestricted cash (\$000)	\$41,368	\$69,333	\$97,730	\$123,582	\$13,502
Available fund balance ratio (%)	21.0%	25.5%	28.5%	31.3%	40.7%
Liquidity ratio (%)	27.0%	46.5%	58.7%	70.3%	55.3%
Leverage					
Debt (\$000)	\$95,370	\$112,088	\$106,043	\$109,462	\$18,954
Adjusted net pension liabilities (\$000)	\$328,662	\$369,094	\$345,544	\$236,367	\$28,106
Adjusted net OPEB liabilities (\$000)	\$90,409	\$89,635	\$105,260	\$102,298	\$1,627
Other long-term liabilities (\$000)	\$4,037	\$4,376	\$7,215	\$7,057	\$749
Long-term liabilities ratio (%)	337.8%	386.0%	339.0%	259.0%	272.9%
Fixed costs					
Implied debt service (\$000)	\$7,427	\$6,953	\$8,027	\$7,438	\$1,360
Pension tread water contribution (\$000)	\$12,584	\$9,006	\$7,970	N/A	\$864
OPEB contributions (\$000)	\$4,105	\$3,698	\$5,094	\$4,903	\$56
Implied cost of other long-term liabilities (\$000)	\$284	\$294	\$313	\$506	\$47
Fixed-costs ratio (%)	15.9%	13.4%	12.9%	11.8%	12.6%

For definitions of the metrics in the table above please refer to the [US Cities and Counties Methodology](#) or see the Glossary in the Appendix below. Metrics represented as N/A indicate the data were not available at the time of publication. The medians come from our most recently published [US Cities and Counties Median Report](#).

The real GDP annual growth metric cited above is for the Allentown-Bethlehem-Easton, PA-NJ Metropolitan Statistical Area.

Sources: US Census Bureau, Allentown (City of) PA's financial statements and Moody's Ratings, US Bureau of Economic Analysis

Profile

Allentown is the third-largest city in Pennsylvania, with a population of about 126,000.

Detailed credit considerations

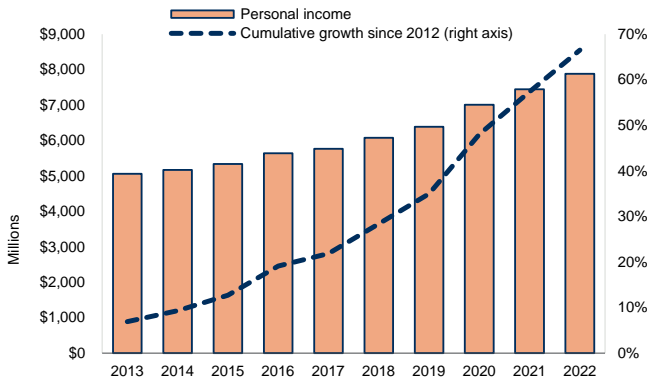
Allentown's revenue outperformance and improved fiscal management continue to drive a better financial position. Conscientious financial planning and budgetary governance, combined with growing tax revenues, will help the city preserve its stronger fiscal position going forward.

Until a few years ago, Allentown carried a structural imbalance that it routinely masked through nonrecurring maneuvers such as scoop-and-toss refundings, sale-leaseback deals to finance deficits, asset sales, and issuance of pension obligation bonds. Even with these maneuvers, the city still burned through all of its reserves by 2012, after which it executed its most significant nonrecurring maneuver: a \$211 million upfront payment in exchange for a 50-year concession on its water and sewer utility.

The cash cushion generated by that deal didn't last. The city had burned through most of that by 2018, at which point it realized it needed to change its habits. Allentown raised its property tax millage 26% in 2019 (the last time it had raised property taxes before that was 2005) and introduced an annually updated 5-year financial plan in 2020.

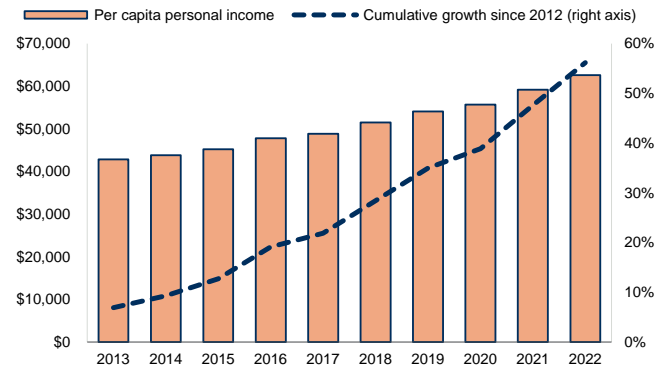
Stronger financial management helped to deliver the much-improved reserves shown in Exhibit 1 at the top of this report. Also helping was a \$57 million infusion of federal stimulus funds through the American Recovery Plan Act, as well as a pickup in economic growth that has helped to drive revenue outperformance.

Exhibit 4
10-year growth in personal income



Source: US Census Bureau

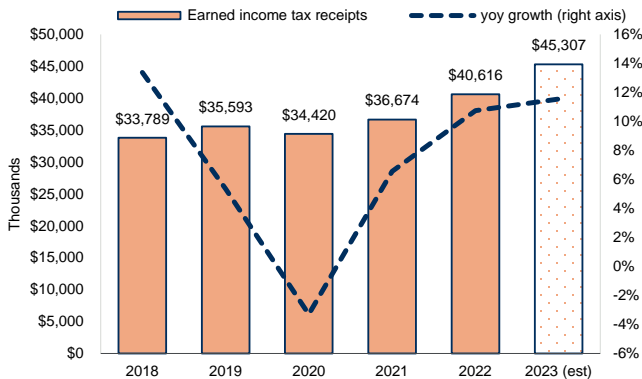
Exhibit 5
10-year growth in per capita personal income



US Census Bureau

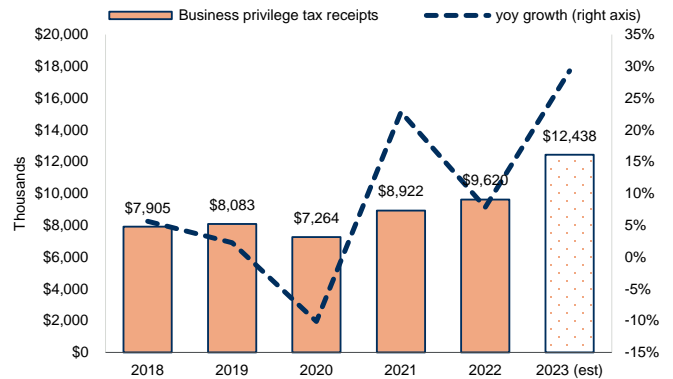
Allentown remains a low-income city with high poverty, but a trend of new development and the expansion of some major employers has helped. Lehigh Valley Hospital and St. Luke's Hospital (the city's two biggest employers) have added nearly 4,000 employees over the past decade, and a downtown revitalization district known as the Allentown Neighborhood Improvement Zone has added high-end office buildings, hotels and restaurants to the property tax rolls¹. The economic expansion and increase in incomes are visible in the performance of Allentown's earned income tax (25% of revenue) and business privilege tax (6% of revenue).

Exhibit 6
Income tax growing sharply



Source: Allentown

Exhibit 7
Business privilege tax has been climbing



Source: Allentown

The positive economic trend has combined with solid financial management to create a completely different fiscal picture from 2018. The city's 5-year financial plan in 2020 projected an available balance of \$5 million by 2024. By 2024, that projection was \$32 million. The city remains conservative in its projections; the balance is shown decreasing to \$27 million by 2028 even though tax revenues continue to exceed budgeted estimates.

Favorably, the administration has introduced and the council is considering adopting a fund balance policy that would set a minimum level at 17% of expenditures.

Allentown's leverage is moderate, mainly the result of a large Moody's-adjusted pension liability. Favorably, the city's contributions to its pension plans have increased sharply and are well above our tread water indicator (the contribution required to prevent the actuarially reported net pension liability from growing, assuming all assumptions are met). Debt is low, largely the result of the water/sewer concession deal that resulted in the defeasance of much of the city's outstanding debt at that time.

ESG considerations

Environmental

Allentown has relatively low exposure to environmental risks across all categories, including physical climate, carbon transition, water management, natural capital and pollution risks.

Social

The city's demographic profile is weak, reflecting high poverty and unemployment, and low educational attainment. Favorably, the population is growing after decades of stagnation.

Governance

Allentown's governance has shown real improvement. The city has taken steps to achieve a more structurally balanced budget and now holds solid reserves.

Rating methodology and scorecard factors

The US Cities and Counties Methodology includes a scorecard, which summarizes the rating factors generally most important to city and county credit profiles. Because the scorecard is a summary, and may not include every consideration in the credit analysis for a specific issuer, a scorecard-indicated outcome may or may not map closely to the actual rating assigned.

Exhibit 8

Allentown (City of) PA

	Measure	Weight	Score
Economy			
Resident income ratio	71.2%	10.0%	Baa
Full value per capita	46,278	10.0%	Baa
Economic growth metric	-1.2%	10.0%	A
Financial Performance			
Available fund balance ratio	31.3%	20.0%	Aa
Liquidity ratio	70.3%	10.0%	Aaa
Institutional Framework			
Institutional Framework	Aa	10.0%	Aa
Leverage			
Long-term liabilities ratio	259.0%	20.0%	A
Fixed-costs ratio	11.8%	10.0%	Aa
Notching factors			
No notchings applied			
Scorecard-Indicated Outcome			A1
Assigned Rating			A2

The Economic Growth metric cited above compares the five-year CAGR of real GDP for Allentown-Bethlehem-Easton, PA-NJ Metropolitan Statistical Area to the five-year CAGR of real GDP for the US

Sources: US Census Bureau, Allentown (City of) PA's financial statements and Moody's Ratings

Appendix

Exhibit 9

Key Indicators Glossary

	Definition	Typical Source*
Economy		
Resident income ratio	Median Household Income (MHI) for the city or county, adjusted for Regional Price Parity (RPP), as a % of the US MHI	MHI: US Census Bureau - American Community Survey 5-Year Estimates RPP: US Bureau of Economic Analysis
Full value	Estimated market value of taxable property in the city or county	State repositories; audited financial statements; continuing disclosures
Population	Population of the city or county	US Census Bureau - American Community Survey 5-Year Estimates
Full value per capita	Full value / population	
Economic growth metric	Five year CAGR of real GDP for Metropolitan Statistical Area or county minus the five-year CAGR of real GDP for the US	Real GDP: US Bureau of Economic Analysis
Financial performance		
Revenue	Sum of revenue from total governmental funds, operating and non-operating revenue from total business-type activities, and non-operating revenue from internal services funds, excluding transfers and one-time revenue, e.g., bond proceeds or capital contributions	Audited financial statements
Available fund balance	Sum of all fund balances that are classified as unassigned, assigned or committed in the total governmental funds, plus unrestricted current assets minus current liabilities from the city's or county's business-type activities and internal services funds	Audited financial statements
Net unrestricted cash	Sum of unrestricted cash in governmental activities, business type activities and internal services fund, net of short-term debt	Audited financial statements
Available fund balance ratio	Available fund balance (including net current assets from business-type activities and internal services funds) / Revenue	
Liquidity ratio	Net unrestricted cash / Revenue	
Leverage		
Debt	Outstanding long-term bonds and all other forms of long-term debt across the governmental and business-type activities, including debt of another entity for which it has provided a guarantee disclosed in its financial statements	Audited financial statements; official statements
Adjusted net pension liabilities (ANPL)	Total primary government's pension liabilities adjusted by Moody's to standardize the discount rate used to compute the present value of accrued benefits	Audited financial statements; Moody's Investors Service
Adjusted net OPEB liabilities (ANOL)	Total primary government's net other post-employment benefit (OPEB) liabilities adjusted by Moody's to standardize the discount rate used to compute the present value of accrued benefits	Audited financial statements; Moody's Investors Service
Other long-term liabilities (OLTL)	Miscellaneous long-term liabilities reported under the governmental and business-type activities entries	Audited financial statements
Long-term liabilities ratio	Debt + ANPL + ANOL + OLTL / Revenue	
Fixed costs		
Implied debt service	Annual cost to amortize city or county's long-term debt over 20 years with level payments	Audited financial statements; official statements; Moody's Investors Service
Pension tread water contribution	Pension contribution necessary to prevent reported unfunded pension liabilities from growing, year over year, in nominal dollars, if all actuarial assumptions are met	Audited financial statements; Moody's Investors Service
OPEB contribution	City or county's actual contribution in a given period	Audited financial statements
Implied cost of OLTL	Annual cost to amortize city or county's other long-term liabilities over 20 years with level payments	Audited financial statements; Moody's Investors Service
Fixed-costs ratio	Implied debt service + Pension tread water + OPEB contributions + Implied cost of OLTL / Revenue	

*Note: If typical data source is not available then alternative sources or proxy data may be considered. For more detailed definitions of the metrics listed above please refer to the [US City and Counties Methodology](#).

Source: Moody's Ratings

Endnotes

- 1 Taxes other than property taxes paid by these businesses don't go to the city but rather to the Allentown Neighborhood Improvement Zone Development Authority

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