Memorandum

CITY OF DALLAS

DATE October 6, 2023

TO Honorable Mayor and Members of the City Council

SUBJECT **S&P Global Ratings Assigns 'A-' and 'BBB' Ratings for Upcoming Kay Bailey Hutchison Convention Center Master Plan and Fair Park Bond Issuances**

Late yesterday, S&P Global Ratings (S&P) assigned its 'A-' credit rating and stable outlook to the upcoming City of Dallas, Texas, Special Tax Revenue Obligations (Kay Bailey Hutchison Convention Center Venue Project), Series 2023 and 'BBB' credit rating and stable outlook to the Special Tax Revenue Obligations (Fair Park Venue Project), Series 2023 (collectively, the "Bonds"). Following City Council approval on September 27, the bonds are currently scheduled to price and close ahead of the year-end deadline, as required by Texas Local Government Code Chapter 334 (the "Brimer Bill").

The bonds are a special obligation of Dallas, wherein pledged revenues securing the bonds are payable from and secured by project-financing-zone (PFZ) revenue adopted by City Council in October 2021, Chapter 351 hotel occupancy tax (HOT) revenue, and the additional two percent Brimer Bill HOT revenue approved by voters in November 2022.The 4.718 percent of the net 7 percent HOT collected within the City excludes HOT generated at the convention center hotel.

According to the S&P report, the Kay Bailey Hutchison Convention Center Venue Project 'A-' rating on the bonds reflects Dallas' "strong-to-very strong economy and favorable location in the Dallas-Fort Worth-Arlington metropolitan statistical area (MSA)," noting the PFZ area does not encompass the City's full boundary; "adequate coverage and liquidity," with projected maximum annual debt service coverage of approximately 4.8x when considering all available pledged revenue; moderate-to-high revenue volatility based on S&P's view of "historical nationwide hotel and hospitality tax trends and potential additional volatility due to the more-limited collection area for PFZ revenue;" and a "general creditworthiness, which does not limit the priority-lien rating." Additionally, the stable outlook reflects S&P's expectation that debt service coverage on the bonds will remain in excess of the additional bonds test requirement and that "pledged revenue will likely remain generally positive."

Regarding the Fair Park Venue Project 'BBB' rating, S&P states that the rating reflects Dallas' "very strong economy and favorable location within the Dallas-Fort Worth-Arlington MSA;" "weak-to-very weak coverage and liquidity" due to "projected maximum annual debt service coverage that will slightly exceed an additional bonds test" and average annual debt service; "moderate revenue volatility" based on S&P's view of "historical nationwide hotel and hospitality tax trends and no history of additional volatility at the local level outside of COVID-19;" and also the general creditworthiness of the Bonds.

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SUBJECT **S&P Global Ratings Assigns 'A-' and 'BBB' Ratings for Upcoming Kay Bailey Hutchison Convention Center Master Plan and Fair Park Bond Issuances**

Although the current ratings are capped by historical revenue trends, future ratings for the Bonds will capture the impressive rebound post-COVID and the exciting growth happening in the downtown region and the City overall. The Kay Bailey Hutchison Convention Center Venue Project and Fair Park Venue Project are highly anticipated, and we are pleased to bring the Bonds to investors and the market with the support of the S&P rating, City Council leadership, and the strength of Dallas' creditworthiness. Attached are the rating reports provided by S&P.

Please let me know if you have any questions or need additional information.

Jack Ireland
Chief Financial Officer

c:
T.C. Broadnax, City Manager
Tammy Palomino, Interim City Attorney
Mark Swann, City Auditor
Bilierae Johnson, City Secretary
Preston Robinson, Administrative Judge
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S&P Global
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Summary:

Dallas; Miscellaneous Tax

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Summary:
Dallas; Miscellaneous Tax

Credit Profile		
US$172.0 mil sr lien spl tax & rev bnds ser 2023 due 08/15/2053		
Long Term Rating	A-/Stable	New

Credit Highlights

- S&P Global Ratings assigned its 'A-' rating to Dallas' approximately $172 million series 2023 senior-lien special-tax revenue bonds, issued for Kay Bailey Hutchison Convention Center's Dallas venue project.
- The outlook is stable.

Security

We rate the series 2023 convention center bonds under our priority-lien criteria, which factors in the pledged revenue's strength and stability and Dallas' general credit quality (the obligor's creditworthiness), where the city collects and distributes taxes. Although a portion of pledged revenue is incremental revenue from certain state hotel-related sales, hotel, and beverage taxes, most pledged revenue comes from two separate citywide hotel taxes. Based on current pledged revenue projections, the percentage breakdown for each revenue source should remain relatively stable during the next several years.

The bonds are a special obligation of Dallas, payable from and secured by first-and senior-liens on pledged revenue, including project-financing-zone (PFZ) revenue, Chapter 351 hotel tax revenue, and Chapter 334 hotel tax revenue. Initially, Dallas will privately place the bonds but could sell them publicly when it refunds its debt in late 2024. The bonds will feature a five-year mandatory put. The city needs to issue against the 2% Chapter 334 "Brimer" tax by the end of calendar 2023 to leverage the new revenue stream for bond repayment.

Officials intend to use series 2023 bond proceeds to finance the initial planning and development work associated with the convention center's complete renovation and expansion. The city intends to renovate and expand the convention center as a new state-of-the-art, approximately 2.5-million-square-foot convention center featuring elevated ballrooms with terraces and Trinity River views, expanded exhibit space, and conference breakout spaces. In addition, the city intends to create a walkable neighborhood and entertainment district surrounding the convention center. During construction, those portions of the convention center not under renovation will remain open to the public.

On Oct. 13, 2021, Dallas' city council adopted an ordinance that designated a new zone, "Project Financing Zone Number One, City of Dallas, Texas" (the PFZ). It also designated the convention center as a qualified project under Section 351.1015 of Chapter 351 of the state code. The PFZ's boundaries encompass an area within a three-mile radius of the convention center's center.

As set forth in the zone ordinance, the city manager notifies the Texas Comptroller of the PFZ's designation and

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requests the comptroller deposit incremental hotel-associated revenue from within the PFZ into a suspense account for approved city uses. The incremental hotel-associated revenue includes sales taxes remitted by hotels, state hotel taxes, and mixed-beverage taxes. Dallas may use funds deposited into the suspense account to acquire, lease, construct, improve, enlarge, and equip a qualified project in the PFZ or repay bonds issued in connection with the convention center project.

Incremental revenue is the difference between current-year hotel-associated revenue collected within the PFZ and base-year hotel-associated revenue collected within the PFZ in the base year, also known as the base year amount. The PFZ expires in 30 years from the ordinance's effective date, which is currently in 2051, or at an earlier date approved by the city council as long as there are no qualified project activities outstanding.

In addition to PFZ revenue, two citywide hotel taxes, Chapter 334 and 351 hotel taxes, secure the convention center bonds. Chapter 334 authorizes Dallas to levy an additional hotel tax not to exceed 2% to fund certain venues and sporting event facilities. The electorate approved this increase in November 2022, and collections began in January 2023 to fund improvements to Fair Park and Kay Bailey Hutchison Convention Center. We understand 80% of Chapter 334 revenue secures the series 2023 convention-center hotel-tax bonds with the other 20% securing series 2023 fair park bonds issued concurrently.

Chapter 351's current provisions authorize Dallas to levy and collect a tax at any rate, not to exceed 7% of the price paid for hotel rooms within the city's corporate limits. The city currently levies the Chapter 351 hotel tax at the maximum rate of 7% with 4.718% of this dedicated to debt service for series 2021 hotel-tax-revenue bonds and the current series 2023 convention-center bonds, albeit on a subordinate basis.

The flow of funds stipulates Dallas apply PFZ revenue toward debt service first, followed by Chapter 334 revenue and then Chapter 351 revenue, if necessary.

Credit overview

The rating reflects our view of Dallas' substantial, diverse local economy and its attraction as a national convention and tourism destination that should support growing hotel tax revenue. We, however, think that with slightly more than one-third of revenue coming from a narrower defined area, there is additional revenue-volatility and coverage risk, which we have accounted for with adjustments to our economic fundamentals and revenue-volatility assessments.

The rating also reflects projected maximum annual debt service (MADS) coverage that will exceed the additional bonds test (ABT) of 1.5x average annual debt service (AADS). Dallas plans to refund series 2023 bonds in late 2024 and issue additional debt soon after, so current MADS and annual debt service coverage (DSC), both currently exceeding 4x MADS, will likely weaken significantly during the next few years. Given ABT and plans for additional debt, we do not expect DSC will likely improve materially during the next few years unless pledged revenue grows significantly.

The rating reflects our view of Dallas':

- Strong-to-very strong economy and favorable location in the Dallas-Fort Worth-Arlington metropolitan statistical area (MSA)--The PFZ area, however, does not encompass the city's full boundary;

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- Adequate coverage and liquidity with projected MADS coverage of approximately 4.8x when considering all available pledged revenue with an ABT equal to 1.5x AADS;
- Moderate-to-high revenue volatility based on our view of historical nationwide hotel and hospitality tax trends and potential additional volatility due to the more-limited collection area for PFZ revenue; and
- General creditworthiness, which does not limit the priority-lien rating.

Environmental, social, and governance

We view environmental, social, and governance (ESG) risks as neutral in our credit analysis.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that DSC on the series 2023 convention-center bonds will likely remain in excess of the ABT of 1.5x AADS and that pledged revenue will likely remain generally positive.

Downside scenario

We could lower the rating if the DSC of MADS were to deteriorate, with Dallas sustaining the levels below the ABT, or if economic fundamentals, evidenced by income or population, were to weaken materially.

Upside scenario

Assuming all other rating factors remain stable or improve, we could raise the rating if our view of DSC were to improve to levels we consider adequate-to-strong or strong or better, even after planned additional debt.

Credit Opinion

Economic fundamentals: strong-to-very strong

We have weakened our assessment of Dallas' economic fundamentals because roughly 38% of pledged revenue comes from a defined area within a three-mile radius of downtown Dallas, including 67 hotels currently compared with more than 200 citywide. We think this presents additional risk compared with revenue collected citywide.

Dallas, with a population estimate of 1.3 million, is in Collin, Dallas, and Denton counties in the Dallas-Fort Worth-Arlington MSA, which we consider broad and diverse. Dallas is North Texas' primary business hub. The city, centrally in the U.S., is a draw for tourism and conventions. Dallas and the greater metropolitan area remain a desirable location for new businesses and corporate headquarter relocations. Dallas is home to two global 500 company headquarters and 10 Fortune 500 company headquarters. In addition, the region is home to 22 Fortune 500 companies and 45 Fortune 1000 companies. This strong economic expansion and location desirability will likely support a long-term trend of growing hotel tax revenue, both citywide and within the PFZ.

Hotels with 300 or more rooms represent a significant part of Dallas' hotel inventory; many of these hotels generate a significant portion of room-night demand from meetings and group activity, which will very likely benefit from an updated convention center. Hotel demand has significantly recovered from COVID-19 and is near pre-COVID-19 levels. During the past five years, 32 hotels with 3,701 rooms opened in the city, increasing hotel room supply by slightly more than 11%. Two additional hotels opened in 2023: the 134-room Hotel Swexan and the 141-room Home2

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Suites by Hilton Dallas Medical District Love Field. In 2023, hotels have added or are building 972 new rooms; another nearly 5,000 rooms are planned for by 2030.

Coverage and liquidity: adequate

Our initial coverage-and-liquidity assessment is adequate and based on the ABT of 1.5x AADS because the city has substantial additional debt plans for parity debt. We have adjusted the initial score downward due to the combination of Dallas' moderate-to-high revenue volatility, adequate-to-strong initial coverage-and-liquidity assessment, and lack of a debt-service-reserve fund. With each of these considerations, we view the coverage-and-liquidity assessment as adequate.

Historical hotel tax trends have been largely positive for Dallas outside of COVID-19, experiencing steady growth due to new businesses relocating to the city and Dallas' central geographic location attracting various conventions and tourism. Using projected fiscal 2023 pledged revenue collections as if they had been collected for the entire fiscal year, MADS coverage is 4.8x with MADS occurring in 2030.

For the five years leading up to the mandatory put date, projected annual DSC ranges from 6.8x-8.6x. Based on substantial additional parity debt plans, however, we think DSC of MADS and AADS over the longer term will likely be closer to the ABT of 1.5x AADS unless pledged revenue growth were material or Dallas were to restructure debt service in a subsequent issuance. Dallas plans to refinance the bonds with a senior- and subordinate-lien structure.

Revenue volatility: moderate-to-high

We assess revenue volatility to determine the likelihood of the availability of revenue during different economic cycles. We have two levels of volatility assessment: macro and micro.

Our macro-volatility assessment begins with an assessment of the historical volatility of the economic activity taxed, including an analysis of societal, demographic, political, and other factors that could greatly affect these activities. Based on the variance of national economic activity we think most closely represents the tax base over multiple economic cycles, we use historical volatility to inform our opinion on expectations of future volatility as it relates to hotel taxes.

On a micro level, we think pledged revenue has exposure to greater revenue volatility compared to a pure citywide hotel-tax-revenue pledge because a portion of pledged revenue comes from a defined area that includes roughly 25% of the hotels within Dallas' boundaries. Although fluctuations could occur relative to economic cycles, historical trends inform our view of pledged hotel-tax collections that we consider relatively stable.

We note the material decrease in collections during 2020 and 2021 as a direct result of COVID-19 and related travel and leisure restrictions. However, hotel taxes rebounded in fiscal 2022, following sharp decreases for fiscal years 2020 and 2021.

Obligor linkage: close

In our view, Dallas does not benefit from limited operations or extraordinary expenditure flexibility. We think pledged revenue has some operating-risk exposure. Although pledged revenue will support debt service first, the flow of funds for pledged revenue allows management to use excess revenue for qualifying expenditures. We consider the hotel tax and use of revenue within Dallas' direct control, with some operating-risk exposure. Therefore, under our priority-lien

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criteria, we think there is a close relationship between the priority-lien pledge and Dallas' general creditworthiness.

Rating linkage to Dallas

We assess Dallas' general operations because we view overall creditworthiness as a key determinant of an obligor's ability to pay its obligations, including special-tax-revenue-secured bonds.

Dallas anchors the Dallas-Fort Worth-Arlington MSA, one of the nation's fastest-growing metropolitan areas. This growth supports recent taxable value increases, improving income, and growing property and sales tax revenue. However, a very weak debt-and-contingent-liability profile, particularly large unfunded pension liabilities, somewhat offsets these positive trends and credit strengths.

(For more information on Dallas' general creditworthiness, see the analysis, published March 31, 2023, on RatingsDirect.)

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.

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Summary:
Dallas; Miscellaneous Tax

Credit Profile		
US$45.9 mil sr lien spl tax rev bnds (Fair Park Venue Project) ser 2023 due 08/15/2053		
Long Term Rating	BBB/Stable	New

Credit Highlights

- S&P Global Ratings assigned its 'BBB' rating to Dallas' approximately $46 million series 2023 senior-lien special-tax revenue bonds, issued for the Fair Park venue project.
- The outlook is stable.

Security

We rate the series 2023 Fair Park bonds under our priority-lien criteria, which factors in the strength and stability of the pledged revenue and Dallas' general credit quality (the obligor's creditworthiness), where the city collects and distribute taxes.

The bonds are a special obligation of Dallas, payable from and secured by first-and senior-liens on pledged revenue. Chapter 334 authorizes Dallas to levy an additional hotel tax not to exceed 2% to fund certain venues and sporting event facilities. The electorate approved this increase in November 2022, and collections began in January 2023 to fund improvements to Fair Park and Kay Bailey Hutchison Convention Center.

We understand 20% of the 2% hotel tax secures the series 2023 fair park bonds with the other 80% securing the city's series 2023 convention-center hotel-tax bonds issued concurrently. The bonds will be initially privately placed but may be sold publicly when they are expected to be refunded in late 2024. The bonds will feature a 5-year mandatory put. The city needs to issue against the 2% "Brimer" tax by the end of calendar 2023 to leverage the new revenue stream for bond repayment.

Officials intend to use series 2023 Fair Park bond proceeds to fund the initial work associated with several projects to upgrade Fair Park's facilities. Fair Park is a cultural and entertainment center just east of downtown Dallas.

Credit overview

The rating reflects our view of Dallas' substantial, diverse local economy and its attraction as a national convention and tourism destination that should support growing hotel tax revenue. The rating also reflects projected maximum annual debt service (MADS) coverage that will slightly exceed an additional bonds test (ABT) of 1.2x average annual debt service (AADS). The rating is currently capped at the 'BBB' category due to the coverage-and-liquidity assessment of weak-to-very weak. If the coverage-and-liquidity assessment weakens to very weak, the rating is capped at the 'BB' category. If MADS coverage decreases below 1x, we would likely revise our coverage-and-liquidity assessment to very weak.

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Dallas plans to refund series 2023 bonds in late 2024 and issue additional debt soon after, but any new-money debt will have to meet an ABT equal to 1.2x AADS. Given ABT and plans for additional debt, we do not expect debt service coverage (DSC) will likely improve materially during the next few years unless pledged revenue grows significantly.

We view revenue volatility as moderate with generally increasing trends in hotel taxes, historically outside of the unique circumstances of COVID-19 when existing hotel tax revenue decreased by more than 30%.

The rating reflects our view of Dallas':

- Very strong economy and favorable location within the Dallas-Fort Worth-Arlington metropolitan statistical area (MSA);
- Weak-to-very weak coverage and liquidity with projected MADS coverage of 1.25x and an ABT equal to 1.2x AADS;
- Moderate revenue volatility based on our view of historical nationwide hotel and hospitality tax trends and no history of additional volatility at the local level outside of COVID-19; and
- General creditworthiness, which does not limit the priority-lien rating.

Environmental, social, and governance

We view environmental, social, and governance (ESG) risks as neutral in our credit analysis.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that DSC will likely remain in excess of the ABT and that pledged revenue trends will likely remain positive.

Downside scenario

We could lower the rating if coverage of AADS decreases below the ABT of 1.2x or if our view of economic fundamentals were to weaken materially.

Upside scenario

Assuming all other rating factors remain stable or improve, we could raise the rating if MADS coverage were to improve materially, sustained at levels consistent with higher-rated peers.

Credit Opinion

Economic fundamentals: very strong

Dallas, with a population estimate of 1.3 million, is in Collin, Dallas, and Denton counties in the Dallas-Fort Worth-Arlington MSA, which we consider broad and diverse. Dallas is North Texas' primary business hub. The city, centrally in the U.S., is a draw for tourism and conventions. Dallas and the greater metropolitan area remain a desirable location for new businesses and corporate headquarter relocations. Dallas is home to two global 500 company headquarters and 10 Fortune 500 company headquarters. In addition, the region is home to 22 Fortune 500 companies and 45 Fortune 1000 companies. This strong economic expansion and location desirability will likely

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support a long-term trend of growing hotel tax revenue.

Hotels with 300 or more rooms represent a significant part of Dallas' hotel inventory; many of these hotels generate a significant portion of room-night demand from meetings and group activity, which will very likely benefit from an updated convention center. Hotel demand has significantly recovered from COVID-19 and is near pre-COVID-19 levels. During the past five years, 32 hotels with 3,701 rooms opened in the city, increasing hotel room supply by slightly more than 11%. Two additional hotels opened in 2023: the 134-room Hotel Swexan and the 141-room Home2 Suites by Hilton Dallas Medical District Love Field. In 2023, hotels have added or are building 972 new rooms; another nearly 5,000 rooms are planned for by 2030.

Coverage and liquidity: weak-to-very weak

Our initial coverage-and-liquidity assessment is weak and based on the ABT of 1.2x AADS due to additional debt plans. We have adjusted the initial score downward due to the combination of Dallas' moderate revenue volatility, weak initial coverage-and-liquidity assessment, and lack of a typical debt-service-reserve fund funded at the least of three prongs. A springing debt-service reserve supports the bonds; however, Dallas only funds the reserve if it does not refund the bonds by February 2025. With each of these considerations, we view the coverage-and-liquidity assessment as weak-to-very weak.

Using projected fiscal 2023 collections of Chapter 334 taxes if collected for the entire fiscal year, MADS coverage is 1.25x with MADS occurring in 2037. For the five years leading up to the mandatory put date, projected annual DSC ranges from 1.25x-1.8x. We think DSC of MADS will likely remain close to the ABT of 1.2x AADS unless pledged revenue growth were material or Dallas were to restructure debt service in a subsequent issuance to where there is a material discrepancy between AADS and MADS. Historical hotel tax trends have been largely positive for Dallas outside of COVID-19, experiencing steady growth due to new businesses relocating to the city and Dallas' central geographic location attracting various conventions and tourism.

Revenue volatility: moderate

We assess revenue volatility to determine the likelihood of the availability of revenue during different economic cycles. We have two levels of volatility assessment: macro and micro.

Our macro-volatility assessment begins with an assessment of the historical volatility of the economic activity taxed, including an analysis of societal, demographic, political, and other factors that could greatly affect these activities. Based on the variance of national economic activity we think most closely represents the tax base over multiple economic cycles, we use historical volatility to inform our opinion on expectations of future volatility as it relates to hotel taxes.

On a micro level, considering stable collections, coupled with a broad base, we see no internal or external influences we think improve or weaken the macro-assessment volatility as moderate. Although fluctuations could occur relative to economic cycles, historical trends inform our view of pledged hotel-tax collections that we consider relatively stable.

We note the material decrease in collections during 2020 and 2021 as a direct result of COVID-19 and related travel and leisure restrictions. However, hotel taxes rebounded in fiscal 2022, following sharp decreases for fiscal years 2020

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and 2021.

Obligor linkage: close

In our view, Dallas does not benefit from limited operations or extraordinary expenditure flexibility. We think pledged revenue has some operating-risk exposure. Although pledged revenue will support debt service first, the flow of funds for pledged revenue allows management to use excess revenue for qualifying expenditures. We consider the hotel tax and use of revenue within Dallas' direct control, with some operating-risk exposure. Therefore, under our priority-lien criteria, we think there is a close relationship between the priority-lien pledge and Dallas' general creditworthiness.

Rating linkage to Dallas

We assess Dallas' general operations because we view overall creditworthiness as a key determinant of an obligor's ability to pay its obligations, including special-tax-revenue-secured bonds.

Dallas anchors the Dallas-Fort Worth-Arlington MSA, one of the nation's fastest-growing metropolitan areas. This growth supports recent taxable value increases, improving income, and growing property and sales tax revenue. However, a very weak debt-and-contingent-liability profile, particularly large unfunded pension liabilities, somewhat offsets these positive trends and credit strengths.

(For more information on Dallas' general creditworthiness, see the analysis, published March 31, 2023, on RatingsDirect.)

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

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