S&P Global Ratings

RatingsDirect®

Summary:

Midland County, Texas; General Obligation

Primary Credit Analyst:
Ann M Richardson, Dallas (214) 765-5878; ann.richardson@spglobal.com

Secondary Contact:
Oscar Padilla, Dallas (214) 871-1405; oscar.padilla@spglobal.com

Table Of Contents

Summary:

Midland County, Texas; General Obligation

Credit Profile		
US$15.875 mil GO rfdg bnds ser 2016 dtd 05/15/2016 due 02/15/2029		
Long Term Rating	AA+/Stable	New
Midland Cnty GO		
Long Term Rating	AA+/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' rating and stable outlook to Midland County, Texas' series 2016 general obligation (GO) refunding bonds. At the same time, Standard & Poor's affirmed its 'AA+' rating on the county's GO bonds outstanding. The outlook is stable.

The bonds are payable from an ad valorem tax levied on all taxable property within the county, within the limits prescribed by law. The maximum allowable rate in Texas is 80 cents per $100 of assessed value (AV) for all purposes, with the portion dedicated to debt service limited to 40 cents. The county's levy is well below the maximum, at 14.08 cents, 0.08 cents of which is dedicated to debt service. Despite the limitations imposed by the state levy limit law, we did not make a rating distinction for the limited-tax GO pledge given the county's flexibility under the levy limit. We understand that proceeds from the sale of the bonds will be used to refund a portion of the county's debt outstanding for interest rate savings.

The rating reflects our assessment of the following factors for the county:

- Strong economy, with projected per capita effective buying income at 124% of the national level and market value per capita of $162,643;
- Adequate management, with "standard" financial policies and practices under our financial management assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could deteriorate in the near term relative to fiscal 2014, which closed with operating surpluses in the general fund and at the total governmental fund level;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2014 of 95% of operating expenditures;
- Very strong liquidity, with total government available cash at 74.5% of total governmental fund expenditures and 24.2x governmental debt service, and access to external liquidity we consider strong;
- Very strong debt and contingent liability position, with debt service carrying charges at 3.1% of expenditures and net direct debt that is 21.6% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value and rapid amortization, with 73.5% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Strong economy

We consider Midland County's economy strong. The county has an estimated population of 136,872. The county has a projected per capita effective buying income of 124% of the national level and per capita market value of $162,643.

Overall, the county's market value grew by 4.8% over the past year to $22.3 billion in 2016. The county unemployment rate was 3.5% in 2015.

Midland County is a petrochemical-rich area that also serves as a major economic contributor to the western portion of the state. Primarily due to growth in mineral values, market value has increased by more than 70% since fiscal 2012. Despite the recent declines in oil and gas prices, market value showed gains in fiscal 2016 from the previous year. We believe the result was primarily due to increases in residential and commercial property. Preliminary values for fiscal 2017 suggest market value may fall by less than 1%, but will remain stable at about $22.3 billion. We believe the established mineral production within the Permian Basin in conjunction with the city of Midland and Midland County being a center for technology within the oil and gas sector as reasons why the county's market value will not be significantly impacted by falling oil prices over the next two years.

This mineral-related boom, however, did lead to sizable job growth and commercial/retail/residential development over the past five years. Now that fewer oil rigs are in production, much of the county's hourly labor force has moved out of the county. As a result, Midlandounty's population is estimated to have declined by about 12% in 2016 from 2015. Despite the decline in population, we do not view this as a negative credit factor as much of the hourly population was transient and the county's overall economic indicators have not shown signs of deterioration despite the loss in population. Our view of the county's economy did in fact improve as a result of countywide employment sector opportunities showing some diversification, which is likely due to the loss of hourly wage earners in the natural resources industry. Should those hourly workers return, and county's employment base become more concentrated, our view of the economy could weaken.

Adequate management

We view the county's management as adequate, with "standard" financial policies and practices under our financial management assessment methodology, indicating the finance department maintains adequate policies in some but not all key areas.

Officials routinely monitor the budget through budget-to-actual reports, and have the flexibility to make adjustments as they deem necessary. The county's use of extensive planning and analysis to devise revenue and expenditure assumptions is based on historical trend analysis and frequent conversations with the local tax assessor. The county has a goal to maintain six months' worth of operating expenditures in its general fund balance. It also maintains a formal investment policy that it reviews annually. Management reports its investment holdings quarterly to the governing body. The county lacks formalized policies in some areas, including long-term financial and capital plans and debt management.

Adequate budgetary performance

Midland County's budgetary performance is adequate in our opinion. The county had operating surpluses of 17% of expenditures in the general fund and of 9% across all governmental funds in fiscal 2014. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from 2014 results in the near term.

We adjusted for one-time capital projects and recurring general fund transfers funded through surplus funds. We recognize that given some of the revenue volatility the county has experienced in recent years, the county has been able to fund several large capital projects through an accumulation of years of general fund surpluses. As a result, we used the county's historical five-year average of capital outlay costs through unaudited 2015 to smooth data and make adjustments. Using a similar approach on unaudited data for fiscal 2015, we believe the county will once again experience a significant general fund net operating surplus in excess of 10% and more than 5% across all governmental funds. The budget for fiscal 2016 reflects about a $12 million deficit due to planned capital spending. Although we would likely adjust for capital spending in fiscal 2016, we believe that the large general fund surpluses in excess of 5% will not be achieved in fiscal 2016 given the volatile economy and loss of tax base. As a result, we believe the county should end with at least balanced operating results in fiscal 2016.

In addition, we believe that Midland County is prone to performance volatility due to cyclical revenues. General fund revenues increased by nearly 40% from fiscal 2010-2014, or to about $81.2 million from $49.0 million. The county's general fund revenues did show a slight decline, based on unaudited data, in 2015 from 2014. Although the decline was only about 1.5%, sales tax alone has accounted for more than 50% of general fund revenue over the past three years. Budgeted sales tax for fiscal 2016 is about $11 million less than unaudited sales tax collections in 2015. Consequently, we view Midland County's revenue to be volatile, and could cause some budgetary pressure in the future.

Very strong budgetary flexibility

Midland County's budgetary flexibility is very strong, in our view, with a high available fund balance in fiscal 2014 of 95% of operating expenditures, or $65.0 million. We expect the available fund balance to remain above 75% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

The county's available fund balance has been maintained at levels above 75% of operating expenditures over the past three audited years, and we anticipate it will again in fiscal 2015. Based on the draft audit for fiscal 2015, we believe the county will increase its available fund balance to about $68.3 million, or about 99.8% of adjusted operating expenditures. The budget for fiscal 2016 does reflect about a $12 million drawdown from fund balance due to nonrecurring capital projects, which could weaken reserves to about 75% of expenditures. Management has, however, proven its ability to exceed budgeted expectations, even before the recent mineral boom. Furthermore, we note that management is in the process of crafting its fiscal 2017 budget, and has no plans to further reduce the fund balance through capital spending. Management may in fact look to reduce some operating costs to offset projected revenue declines. As a result, we do not anticipate Midland County's budgetary flexibility to weaken nor do we believe reserves will fall below 75% of expenditures within the next two years.

Very strong liquidity

In our opinion, Midland County's liquidity is very strong, with total government available cash at 74.5% of total governmental fund expenditures and 24.2x governmental debt service in 2014. In our view, the county has strong access to external liquidity if necessary.

We adjusted cash to account for certificates of deposit and investments with a weighted average-maturity of less than one year. This strong access to external liquidity is demonstrated by the county's access to the market in the past two decades. Midland County has issued primarily GO-backed bonds over the past 20 years. It has historically had what we consider very strong cash balances and, we do not believe its liquidity position will materially worsen over the next two years despite a planned capital spenddown in fiscal 2016. Currently, all of Midland County's investments comply with Texas statutes and the county's internal investment policy. At year-end fiscal 2014, the majority of the county's investments were held in state investment pools and highly rated municipal investments. Given the portfolio diversification, we do not consider the county's investments to be aggressive. The county has no privately placed bank agreements that could lead to acceleration of debt payments.

Very strong debt and contingent liability profile

In our view, Midland County's debt and contingent liability profile is very strong. Total governmental fund debt service is 3.1% of total governmental fund expenditures, and net direct debt is 21.6% of total governmental fund revenue. Overall net debt is low at 2.6% of market value, and 73.5% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

The county has no plans to issue debt within the next two years. Even if there were a significant downturn in market value within the next two years, causing the county's overall net debt to rise above 3% of market value, we do not expect the county's debt profile to weaken.

Midland County's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 5.8% of total governmental fund expenditures in 2015. Of that amount, 4.6% represented required contributions to pension obligations, and 1.3% represented OPEB payments. The county made its full annual required pension contribution in 2015.

Midland County participates in the Texas County and District Retirement System (TCDRS), which is administered by the State of Texas. The county's required pension contribution is its actuarially determined contribution, which is calculated at the state level, based on an actuary study. Using updated reporting standards in accordance with Governmental Accounting Standards Board (GASB) Statement No. 68, the county's net pension liability was measured as of Dec. 31, 2014, and was $11.3 million. The TCDRS plan maintained a funded level of 91.3%, using the plan's fiduciary net position as a percent of the total pension liability. For additional details on GASB 67 and 68, see our report "Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria," published Sept. 2, 2015, on RatingsDirect. The county also contributes to an OPEB plan, which is funded on a pay-as-you-go basis.

Strong institutional framework

The institutional framework score is strong.

Outlook

The stable outlook reflects our opinion that we will not change the rating over the two-year outlook horizon. The outlook further reflects our view of the county's very strong reserves and demonstrated ability to balance its operations despite our expectation that there could be some revenue volatility. In addition, the outlook reflects our opinion that Midland County's economy could fluctuate in the future with employment sector concentration, but its key economic indicators, namely market value per capita and effective buying economy, will remain what we consider to be strong.

Upside scenario

A higher rating would likely follow a significant expansion and diversification of the economic base, coupled with the adoption and demonstrable on-going practice of several key management policies.

Downside scenario

We could lower the rating if reserves were to fall to levels below 75% of operating expenditures and the economy showed signs of weakening, or if there were significant budgetary pressures caused by revenue volatility that reduced reserves below management's informal goal.

Related Criteria And Research

Related Criteria

- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- USPF Criteria: Local Government GO Ratings Methodology And Assumptions, Sept. 12, 2013
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: Limited-Tax GO Debt, Jan. 10, 2002

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- 2015 Update Of Institutional Framework For U.S. Local Governments