S&P Global Ratings

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Summary:

Mecklenburg County, North Carolina; Appropriations; General Obligation

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Table Of Contents

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Credit Profile		
US$150.0 mil GO pub imp bnds ser 2018 dtd 09/27/2018 due 03/01/2039		
Long Term Rating	AAA/Stable	New

Rationale

S&P Global Ratings assigned its 'AAA' long-term rating to Mecklenburg County, N.C.'s 2018 general obligation (GO) public improvement bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the county's existing GO debt and its 'AA+' long-term rating on the county's existing appropriation-backed obligations. The outlook is stable.

The 2018 GO bonds are secured by the county's full faith and credit, including its ability to levy ad valorem property taxes without limitation as to rate or amount. Approximately $125 million of the 2018 bond proceeds will be used to finance various capital costs for the Charlotte-Mecklenburg School System and approximately $25 million be used for parks and recreation-related capital projects. Financing for school-related projects is derived from referenda in 2013 and 2017. Following the 2018 issuance, the county will have approximately $855 million in remaining GO authorization for school-related projects associated with the 2017 referendum. Financing for parks-related projects is derived from a 2008 referendum, with $75 million in authorization remaining, though this authorization lapses in November. The county also maintains $60 million in remaining GO authorization for community college purposes.

The county's appropriation-backed obligations are rated one notch lower than the GO rating given the contingent nature of the obligations dependent on the annual appropriation of lease payments.

The county GO rating is eligible to be higher than the sovereign rating because we believe the county can maintain strong credit characteristics relative to the U.S. sovereign in a stress scenario. Under our criteria "Ratings Above the Sovereign: Corporate and Government Ratings--Methodologies and Assumptions," published Nov. 19, 2013 on RatingsDirect, the county has predominantly locally derived revenue with independent taxing authority and independent treasury management from the federal government.

The 'AAA' GO rating reflects our opinion of the county's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong management, with good financial policies and practices under our Financial Management Assessment methodology;
- Strong budgetary performance, with a slight operating deficit in the general fund but an operating surplus at the total governmental fund level in fiscal 2017;

- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 36% of operating expenditures;
- Very strong liquidity, with total government available cash at 61.3% of total governmental fund expenditures and 4.5x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 13.6% of expenditures and net direct debt that is 92.8% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value and rapid amortization, with 68.3% of debt scheduled to be retired in 10 years; and
- Very strong institutional framework score.

Very strong economy

We consider the county's economy very strong. Mecklenburg County, with an estimated population of 1.1 million, is located in the Charlotte-Concord-Gastonia MSA, which we consider broad and diverse. The county has a projected per capita effective buying income of 116% of the national level and per capita market value of $121,713. Overall, the county's market value grew by 2.6% over the past year to $129.7 billion in 2018. The county unemployment rate was 4.3% in 2017.

Mecklenburg County is located in south central North Carolina and encompasses the City of Charlotte. The Charlotte MSA has the largest regional economy between Washington, D.C., and Atlanta, and is one of the nation's leading financial centers as well as a major communications, logistics, and manufacturing center for the Southeast region. The county serves as the headquarters for a number of financial institutions, including Bank of America, and maintains core operations for U.S. Bancorp, Fifth Third Bank, and Ally Bank. The county also serves as the headquarters for several Fortune 500 companies, including Duke Energy (diversified utilities) and Nucor (metal fabrication). Furthermore, the state's labor laws and the area's high-skill labor force have made it an attractive location for international firms across a variety of industries.

The county's population has exhibited rapid growth over its recent history, mirroring growth in the Charlotte MSA by increasing by nearly 50% since the 2000 census. Given this growth and continued economic development, the county's labor force exceeds its prerecession peak by more than 30%. The county's growth has contributed to significant residential, commercial, and industrial development, and this is expected to continue. Furthermore, the county has developed a presence as a tourism destination and the tourism-related industry now is its fourth-largest employment sector. Hotel occupancy rates have increased every year since at least 2009 to 72.2%. The county's robust, structural growth has contributed to persistent growth in assessed value following the latest revaluation effective fiscal 2012. The county's next revaluation, in 2019, will take effect fiscal 2020. Officials report that the county will move to a four-year valuation cycle following the upcoming valuation.

We anticipate growth in North Carolina will remain robust as reflected in our most recent conditions forecast, published July 26, 2018. Furthermore, according to data from IHS Global Insight, the Charlotte MSA is anticipated to realize average annual employment growth of 1.7% over the next five years. Continued growth in building permits and announcements that a number of firms across a variety of sectors will expand to move into the county support continued growth prospects.

Strong management

We view the county's management as strong, with good financial policies and practices under our Financial Management Assessment methodology, indicating our view that financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis.

Key practices include:

- Conservative and comprehensive budget development processes that incorporate performance-based and service-level considerations, which have contributed to strong financial performance;
- Monthly reporting of budget-to-actual performance to the county board;
- Maintenance of a comprehensive capital improvement program that, although not rolling, is regularly reviewed and incorporated into budgeting and planning processes;
- A formal investment and banking policy that entails the monthly reporting of investment earnings and holdings;
- A formally adopted debt management policy that includes a number of targets beyond statutes to which the county must adhere; and
- A formally adopted fund balance policy that stipulates the combined total general fund and debt service fund balance will exceed 28% of general fund revenue.

Per the fund balance policy, funds in excess of 28% of actual general fund revenue can be appropriated to the capital, technology, and fleet reserves with a cap equivalent to property tax revenue generated from 2.25 cents. Should the balance fall below 28%, the policy requires that the balance be replenished within two years unless the board decides to extend the replenishment period to three years.

Strong budgetary performance

Mecklenburg County's budgetary performance is strong, in our opinion. The county had slight deficit operating results in the general fund of 0.8% of expenditures but a surplus result across all governmental funds of 1.8% in fiscal 2017.

Historically, the county's budgetary performance in its general fund and debt service fund (DSF) has been positive, allowing it to accumulate a substantial fund balance. In our view, the county's conservative budgeting practices, which limit the use of reserves to pay-as-you-go capital and other nonrecurring expenditure funding, have contributed to its positive results. Our assessment of operating performance combines the county's general fund and DSF given that the debt service fund carries a dedicated property tax levy and is considered a major operating fund. Additionally, the county's fund balance policy addresses the combined general and debt service funds.

We adjust our assessment of results in the combined general fund and DSF to include transfers out for regular capital outlays and ongoing transfers related to funding for the county's five-year deferred maintenance plan. Our assessment of results across total governmental funds reflects an adjustment for expenditures financed from debt proceeds. The deferred maintenance plan lays out $150 million in deferred projects to be financed over five years from current resources. Despite the continued funding of the deferred maintenance plan and pay-as-you-go capital spending, officials estimate a surplus of nearly $50 million for fiscal 2018 across both funds, primarily as a result of positive expenditure variances from unfilled vacancies and lower-than-budgeted debt service as a result of the 2017 refunding bonds It is our opinion that the county maintains a healthy revenue mix, with property taxes as the largest budgeted revenue source, equal to 63.3% of combined general fund and DSF revenue, followed by sales taxes at 14.1%.

The 2019 budget includes a 0.75-cent property tax rate increase, bringing the rate to 82.32 cents. The increase is largely targeted to expand to the county's pre-kindergarten education programs. The budget also includes the use of $57.9 million in reserves, slightly higher than the amounts appropriated in prior years in its ongoing effort to finance capital projects from reserves. We note that the county maintains a track record of achieving positive budgetary variances, partly mitigating the magnitude of appropriated fund balance in its budgets. While the 2019 budget includes planned but relatively large appropriations for capital and deferred maintenance, we anticipate budgetary performance will remain strong-to-adequate.

Very strong budgetary flexibility

Mecklenburg County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 36% of operating expenditures, or $553.3 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

Our calculation of the county's available fund balance includes committed and unassigned balances in the general fund and the committed portion of the DSF. We then take our calculated available fund balance position of $553.3 million as a percentage of combined general fund and DSF expenditures and transfers. Despite the planned use of general fund balance for fiscal 2019, we anticipate that the county's available fund balance will remain near or above 30% given its track record of positive performance relative to budgets.

Very strong liquidity

In our opinion, Mecklenburg County's liquidity is very strong, with total government available cash at 61.3% of total governmental fund expenditures and 4.5x governmental debt service in 2017. In our view, the county has strong access to external liquidity if necessary given the variety of debt obligations issued over the past 15 years. The county has significantly reduced its contingent liquidity risk in the past several years, exiting its swap agreements and reducing its variable-rate debt portfolio. Furthermore, the county eliminated its exposure to variable-rate debt and privately placed debt in 2017. The county's operating investments are held in high-quality U.S. government agency securities, commercial paper, and the state cash and investment pool. Given the county's conservative budgeting practices and strong financial oversight, we anticipate its liquidity position will remain very strong.

Strong debt and contingent liability profile

In our view, Mecklenburg County's debt and contingent liability profile is strong. Total governmental fund debt service is 13.6% of total governmental fund expenditures, and net direct debt is 92.8% of total governmental fund revenue. Overall net debt is low at 2.2% of market value, and approximately 68.3% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

The county has realized a strong debt position and has built a relatively high debt capacity as a result of constrained borrowing and rapid amortization over the past several years. With the capacity, the county plans to issue around $100 million to $200 million in each of the next several fiscal years. Following the 2018 issuance, the county will issue amounts under is 2018 GO referendum as financing needs arise. Given the county's rapid amortization, we anticipate debt service costs will remain manageable as new debt is issued. Depending on the timing of the new debt relative to the current amortization schedule, our opinion of the county's debt and liability profile may change to adequate, though we would not anticipate this as having a near- or medium-term impact on the county's overall credit quality.

Mecklenburg County's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 2.5% of total governmental fund expenditures in 2017, with 1.2% representing required contributions to pension obligations and 1.3% representing OPEB payments. The county met its annual required pension contribution.

The county participates in the North Carolina Local Government Employees' Retirement System (LGERS). In addition, it participates in the Law Enforcement Officers' Special Separation Allowance and the Registers of Deeds' Supplemental Pension Fund, both state-run, defined benefit plans. The county's proportionate share of LGERS, the largest plan to which it contributes, is 94.1% funded, utilizing its plan fiduciary net position as a percentage of the total pension liability. The county funds its OPEB on a pay-as-you-go basis, though it does maintain an OPEB trust equal to $114 million, according to fiscal 2017 results, relative to an unfunded liability of $541 million as of a Jan. 1, 2015 valuation date. The OPEB plan is closed to new employees though retirees may purchase health insurance at group rates.

Very strong institutional framework

The institutional framework score for North Carolina counties is very strong.

Outlook

The stable outlook reflects our view of Mecklenburg County's very strong economy that continues to experience robust, structural growth. The outlook also reflects our view of the county's strong management that has contributed to historically strong financial performance, leading to very strong reserves and liquidity. For these reasons, we do not expect to change the rating within the two-year outlook horizon. In the unlikely event that the county realizes consecutive years of structural imbalance leading to material deteriorations of its flexibility or liquidity positions, we could consider lowering the rating.

Related Research

- U.S. State And Local Government Credit Conditions Forecast, July 26, 2018
- 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
- 2017 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of August 30, 2018)		
Mecklenburg Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Mecklenburg Cnty certs of part (var rate)		
Long Term Rating	AA+/Stable	Affirmed

Ratings Detail (As Of August 30, 2018) (cont.)		
Mecklenburg Cnty ltd oblig		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty ltd oblig bnds		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty taxable ltd oblig bnds		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty COPs - 2008B		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty COPs - 2009A		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty GO pub imp bnds		
Long Term Rating	AAA/Stable	Affirmed
Mecklenburg Cnty APPROP		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty APPROP		
Long Term Rating	AA+/Stable	Affirmed

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.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.