



## Fitch Affirms St. Mary's County, MD ULTGO's at 'AA+'; Outlook Stable

Fitch Ratings-San Francisco-20 October 2015: Fitch Ratings has affirmed the following rating for St. Mary's County, MD (the county):

--\$70.5 million outstanding unlimited tax general obligation bonds at 'AA+'.

The Rating Outlook is Stable.

### SECURITY

The bonds are general obligations of the county, and its full faith and credit and unlimited taxing power are irrevocably pledged to repayment of the bonds.

### KEY RATING DRIVERS

**ECONOMIC BASE CONCENTRATED IN MILITARY:** Local employment is centered on the Naval Air Station Patuxent River (NAS). Fitch believes this is an important asset to the U.S. military asset and unlikely to be downsized sufficiently to alter the county's credit quality.

**HEALTHY RESERVES AND BUDGETARY FLEXIBILITY:** Reserve levels and financial flexibility remain sound, supported by prudent fiscal policies and planning. Reserve levels somewhat compensate for the limited economic base.

**LOW DEBT, MODEST PENSION LIABILITY:** Continued strong control of capital expenditure growth is expected to result in continued low overall debt levels with rapid amortization. The state pension plan in which the county participates is underfunded, but the county's required pension contribution is a small part of the budget.

### RATING SENSITIVITIES

Fitch's rating assumes that any changes in federal and military funding that affect the NAS would not be sufficiently severe as to alter the county's credit fundamentals. Divergence from this assumption, without sufficient action by the county to preserve a sound financial position, could have an impact on the rating.

### CREDIT PROFILE

St. Mary's County is located in the southern part of Maryland bordering the Patuxent and Potomac Rivers as well as Chesapeake Bay. The county's 2014 population of 110,382 is among the fastest growing in the state, at 28% since 2000. The county's population levels reflect, in part, the expansions at the NAS.

### EMPLOYMENT BASE CONCENTRATED IN MILITARY SECTOR

The NAS is a significant factor in the local economy with over 22,000 workers, nearly one-half of whom are civilian personnel. It is Fitch's understanding that the NAS' role as the Navy's principal research,

engineering and test center makes severe cuts at the federal level unlikely. NAS is reportedly in the process of hiring 1,000 to 2,500 civilians to backfill vacancies due to retirements and attrition.

Other major county employers include St. Mary's Hospital, a 96-bed full service facility with over 1,200 employees. The county's regional airport was designated an FAA test site for unmanned aircraft systems in 2014, in partnership with the University of Maryland, attracting private investments in research and manufacturing.

County average annual employment growth over the past ten years has been 0.8%, helping to maintain unemployment rates, 5.6% in July 2015, below state and national averages. Per capita income levels are 28% higher than the U.S. in part due to a cluster of higher wage technology jobs in the area.

#### HIGH FINANCIAL FLEXIBILITY AND RESERVES A CREDIT STRENGTH

Sound reserves and sustained financial flexibility reflect the county's strong financial management. The county has consistently maintained a separate reserve to preserve its bond rating of around 6% of general fund expenditures (\$12.9 million in 2015) and a rainy day fund of a constant \$1.625 million. The bond rating fund is set by formal debt policy but can be utilized upon a simple majority vote of the County Commissioners. In addition, a minimum unrestricted fund balance policy of 15% of general fund revenue was established in August 2015.

The county concluded fiscal 2014 with a small \$2.4 million general fund operating surplus before transfers. However, unrestricted fund balance was reduced to \$44 million, or 21% of spending, due to \$12.9 million of planned cash funding for capital projects.

Fiscal 2015 is estimated to end with \$6.8 million surplus, after \$1.6 million budgeted pay-go capital spending. Ending unrestricted fund balance is expected to be around 22% of spending, a still sound level and in compliance with the new county policy.

Like all Maryland municipalities, the county benefits from a triennial assessment practice that smoothes annual volatility in tax base performance. The county adopted a homestead percentage of 105%, which means that assessments on certain owner occupied residential property may not increase by more than 5% in any given year. Growth in excess of 5% is credited, or 'banked', and can be used to offset future tax base declines. Significant banked tax base growth coupled with relatively mild tax base declines has permitted the county to maintain consistent property tax collections.

Property tax collections, which comprise about one-half of the revenue stream, have increased an average of 3.4% annually since fiscal 2008. The county's property tax rate is not subject to a cap or limitation on annual growth. The current rate of \$0.8523 per \$100 assessed value (AV) is among the lowest in the state and has not been raised since 2007.

The county's income tax collections, which constitute 37% of revenues, have been flat in recent years. The income tax rate is subject to a statutory cap of 3.2%. The county currently falls below this with a rate of 3.0%, providing some additional revenue flexibility.

#### LOW DEBT AND PENSION LIABILITY LEVELS

The county has carefully managed its capital program spending and issuance of debt, leading to low overall debt levels at \$760 per capita and 0.7% of market value. Amortization is rapid at 86% within 10 years, and debt service represents a low 5% of governmental spending.

The county has adopted a fiscal 2016-2021 capital improvement plan totaling \$257 million, led by \$103 million for public school projects and \$55 million for public facilities projects. Funding sources include

unspent bond proceeds and \$11.8 million in operating funds at the end of fiscal 2015. The county reports a moderate amount of bond issuance is likely to be needed in fiscal 2017 to meet capital needs.

Long-term liabilities related to employment benefits are not expected to pressure future operations because their cost is modest relative to total spending. The county provides pension benefits to its employees through participation in the state plan. The county has consistently contributed 100% of the annual required contribution. The funding of the state pension has improved in recent years, but the June 30, 2014 adjusted funded ratio was still just 62%.

The county also provides other post-employment benefits (OPEB) to its retirees. As of 2014, the unfunded actuarial accrued liability associated with the county's OPEB obligation totaled 0.4% of market value. The county established an OPEB trust in fiscal 2009 and has almost achieved full funding of the annual required contribution (ARC). Total carrying costs consisting of debt service, total pension ARC, and the county's actual OPEB contribution, are a low 8% of spending.

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Additional information is available at '[www.fitchratings.com](http://www.fitchratings.com)'.

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, National Association of Realtors, and Zillow.

**Applicable Criteria**

Exposure Draft: U.S. Tax-Supported Rating Criteria (pub. 10 Sep 2015)  
([https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=869942](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=869942))  
Tax-Supported Rating Criteria (pub. 14 Aug 2012)  
([https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=686015](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=686015))  
U.S. Local Government Tax-Supported Rating Criteria (pub. 14 Aug 2012)  
([https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=685314](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685314))

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Dodd-Frank Rating Information Disclosure Form

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