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Ratings

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Summary:

Queen Anne's County, Maryland; General Obligation

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Table Of Contents

Rationale

Outlook

Related Research

Summary:

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Credit Profile		
US$16.0 mil pub fac bnds ser 2018 due 07/01/2038		
Long Term Rating	AAA/Stable	New

Rationale

S&P Global Ratings assigned its 'AAA' rating, and stable outlook, to Queen Anne’s County, Md.'s series 2018 public facilities general obligation (GO) bonds.

The full-faith-and-credit pledge of Queen Anne's County and agreement to levy ad valorem property taxes without limitation as to rate or amount secure the bonds. We understand officials intend to use bond proceeds to finance various capital projects.

The county's GO bonds are eligible to be rated above the sovereign because we believe Queen Anne's County can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect), the county has a predominately locally derived revenue source, with most of general fund revenues coming from local property and income taxes.

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

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with an operating surplus in the general fund and break-even operating results at the total governmental fund level in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 20% of operating expenditures;
- Very strong liquidity, with total government available cash at 43.8% of total governmental fund expenditures and 4.9x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability position, with debt service carrying charges at 8.9% of expenditures and net direct debt that is 99.0% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value; and
- Very strong institutional framework score.

Very strong economy

We consider the county's economy very strong. Queen Anne's County, with an estimated population of 49,077, is located in the Baltimore-Columbia-Towson MSA, which we consider to be broad and diverse. The county has a projected per capita effective buying income of 139% of the national level and per capita market value of $158,776.

Overall, the county's market value grew by 2.2% over the past year to $7.8 billion in 2017. The county unemployment rate was 3.8% in 2016.

Queen Anne's County is located on the Eastern Shore of Maryland, and is linked to the Western Shore by the Chesapeake Bay Bridge; as such, it is commonly known as the "gateway to the Eastern Shore." Queen Anne's County is predominately rural in character, but has experienced significant growth within the past two decades, with assessed value (AV) more than doubling during this period.

Many residents commute across the Bay Bridge to employment opportunities throughout the Baltimore-Washington metropolitan statistical area. Private sector jobs account for about 85% of county employment, while federal state and local government employment combined account for roughly 15% of county employment.

Management indicates positive momentum in residential home prices as well as a number of commercial and residential economic developments underway should lead to additional AV growth. The property tax base remains very diverse, with the 10 leading taxpayers accounting for 2.6% of AV.

Very strong management

We view the county's management as very strong, with "strong" financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

Highlights include management's:

- Conservative budget assumptions as well as management looking back at least five years at revenue and expenditures when budgeting;
- Formal monthly reports to council on budget-to-actual performance;
- Formalized five-year financial projections that are updated annually;
- Formal six-year capital improvement plan (CIP) that management updates annually;
- Formal investment management policy with monthly investment reports;
- Formal debt policy established in 2009 and revised in 2013, which includes a number of affordability parameters, consisting of GO debt outstanding will equal 2.5% or less than taxable AV; debt per capita will remain $3,000 or less; and debt to expenditures will remain less than 10%; and
- Formal reserve policy established in 2012 and revised in 2017, which includes the maintenance of a rainy-day fund equal to 8% of operating revenues, as well as a stabilization fund.

Strong budgetary performance

Queen Anne's County's budgetary performance is strong in our opinion. The county had surplus operating results in the general fund (GF) of 2.5% of expenditures, despite a transfer of excess revenues to the capital projects fund of $3.8 million, and balanced results across all governmental funds of negative 0.1% in fiscal 2017 after accounting for capital outlay funded with bond proceeds. The county's GF operating results have been stable over the last three years, with a result of 1.3% in 2016 and a result of 2.3% in 2015.

In fiscal 2017, the county's GF revenues increased by $3.5 million over the previous year, while expenses decreased by $3.3 million. We understand that the positive variances were due primarily to better-than-expected property and income taxes as well as conservative budgeting practices. In addition, the fiscal 2017 results include the county transferring roughly $3.7 million to the capital projects fund to help fund pay-as-you-go capital expenses. Queen

Anne's County has a history of transferring excess revenues to the capital projects fund to help fund one-time expenditures. Despite the transfer, the county increased available reserves by nearly $430,000 during the year.

The fiscal 2018 GF budget totals $133.8 million, which is a 1.6% increase over the previous year's budget. The budget conservatively shows the use of $1.2 million of reserves for one-time purposes. However, according to current estimates, we understand that revenues are again coming in above budget and that the county should end the year with close to breakeven operations.

The county receives about half of GF revenues from property taxes, while income taxes account for about 37%.

Very strong budgetary flexibility

Queen Anne's County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 20% of operating expenditures, or $25.4 million, after accounting for the county's rainy-day and stabilization reserves.

The county maintains both a rainy-day fund, which was established in 2013 and slightly increased in 2017, and a revenue stabilization fund, which was established in March 2014. The rainy-day fund was established for contingencies and emergencies, and in 2017, the county increased the minimum requirement to 8% from 7% the following year's budget. The required amount in fiscal 2017 was equal to $10.5 million, or 8.2% of GF expenditures and transfer out. The revenue stabilization fund was set up for the purpose of unanticipated projects, initiatives, and other one-time expenses. The maximum amount of the stabilization fund cannot exceed 5% of budgeted GF operating revenues and the transfer to the stabilization fund can only be made after the requirements of the rainy-day fund are met. The balance of the stabilization fund at the end of fiscal 2017 was $4.0 million, or 3.1% of GF expenditures and transfers out. Unassigned and assigned reserves totaled $10.8 million, or 8.4% of operating expenses.

We understand that management expects to end fiscal 2018 with balanced operations and without a material change to reserves. As such, we believe budgetary flexibility will remain very strong in our view at about 20% of operating expenses at fiscal year-end.

The county's income tax rate stands at the maximum allowed level of 3.2% and has not changed since calendar 2012. In addition, the county's property tax rate stands at 84.71 cents per $100 of AV for each of the past five years. We believe this compares favorably to other counties in Maryland, which in fiscal 2017 had an average property tax rate of 95.6 cents per $100 of AV. Although the property tax rate has historically been very stable, the county could generate nearly $800,000 of additional revenue for each penny increase in the tax rate.

Very strong liquidity

In our opinion, Queen Anne's County's liquidity is very strong, with total government available cash at 43.8% of total governmental fund expenditures and 4.9x governmental debt service in 2017. In our view, the county has strong access to external liquidity if necessary.

The county has issued GO bonds frequently in the past 15 years. It does not have any direct purchase debt or material contingent liquidity risks in our view. We understand there are no plans to draw down liquidity and that cash and investments are maintained in maturities of three months or less.

Adequate debt and contingent liability profile

In our view, Queen Anne's County's debt and contingent liability profile is adequate. Total governmental fund debt service is 8.9% of total governmental fund expenditures, and net direct debt is 99.0% of total governmental fund revenue. Overall net debt is low at 2.1% of market value, which is in our view a positive credit factor.

The county's six-year CIP for both governmental and enterprise purposes totals $172.5 million and is funded by a combination of bonds, grants, and pay-as-you-go funding. We understand Queen Anne's County could issue an estimated $16 million of new GO debt within the next year. We do not believe this will materially affect its overall debt profile given the size of the tax base and the above-average amortization schedule of existing debt.

Queen Anne's County's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 3.4% of total governmental fund expenditures in 2017. Of that amount, 1.8% represented required contributions to pension obligations, and 1.6% represented OPEB payments. The county made its full annual required pension contribution in 2017.

The county's employees participate in the Maryland State Retirement and Pension System. The plan is a cost-sharing, multiple-employer, defined benefit plan. The system's pension plan is 69% funded as of June 30, 2017. The county's proportionate share of this plan's net pension liability is $30.0 million, assuming a 7.55% discount rate.

Queen Anne's County also provides OPEB to eligible employees. On June 23, 2009, the county established an OPEB trust to fund the costs of health insurance and OPEB to eligible employees. In fiscal 2017, the county contributed $932,447 to the trust for county OPEB benefits and $1.3 million as pay-as-you-go contributions. The unfunded actuarial liability as of July 1, 2017, totals $45.1 million for the county.

We view the county's pension and OPEB expenses as manageable despite the somewhat below-average funding percent of the state-administered plan. In addition, we do not expect the county's pension and OPEB expenses to materially change over the next couple fiscal years but will continue to monitor them.

Very strong institutional framework

The institutional framework score for Maryland counties is very strong.

Outlook

The stable outlook reflects our view of Queen Anne's County's very strong economic metrics and management policies, which historically have supported stable and consistent financial performance. As such, we do not expect to lower the rating in the next two years.

Downside scenario

Although very unlikely in our view, if the county were to experience unforeseen budgetary pressure that resulted in significantly diminished budgetary flexibility that was inconsistent with the county's strong financial policies and practices, or if the county's debt profile were to significantly deteriorate, this could pressure the rating.

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
- 2017 Update Of Institutional Framework For U.S. Local Governments

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 the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.