S&P Global Ratings

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Summary:

Wake County, North Carolina; Appropriations; General Obligation

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Credit Profile		
US$209.275 mil GO pub imp bnds ser 2018A due 03/01/2037		
Long Term Rating	AAA/Stable	New
Wake Cnty GO		
Long Term Rating	AAA/Stable	Affirmed

Rationale

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

We rate the county's GO bonds above the sovereign because we believe the county can maintain better credit characteristics than the nation in a stress scenario. Under our criteria, titled "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions," published Nov. 19, 2013, on RatingsDirect, the county primarily has a locally derived revenue source, as approximately 70% of general fund revenue is derived from property taxes with independent taxing authority and independent treasury management from the federal government.

The county's faith-and-credit pledge and ability to levy ad valorem taxes without limit as to rate or amount secures its GO bonds. We understand 2018A proceeds will refund the county's outstanding 2016A&B GO bond anticipation notes (BANs). The county expects to continue its practice of utilizing short-term debt instruments through private placements to fund capital needs.

Installment payments made by the county to the trustee pursuant to the trust agreement secure the limited-obligation debt. We rate these obligations one notch lower than Wake County's general creditworthiness to account for the appropriation risk associated with the installment payments. Pursuant to the trust agreement, the county budget officer is required to include installment payments in the budget. The county can only delete the budget item by a resolution approved by the board of commissioners with a statement that explains the reason for the deletion. There is no abatement of installment payments. In addition, the county has assigned all of its rights in the deed of trust to the trustee pursuant to the trust agreement. The county is responsible for all taxes, operations and maintenance, and insurance for the full replacement value. The contract constitutes a triple-net lease with no right to setoff or counterclaim.

In our view, the county has considered the affordability of the installment payments in its long-term financial planning. We considered the affordability and the likelihood of the installment payment, which is reflected in the appropriation-backed obligation rating and in our view of Wake County's general creditworthiness.

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

- 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 methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 25% of operating expenditures;
- Very strong liquidity, with total government available cash at 50.4% of total governmental fund expenditures and 2.4x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability position, with debt service carrying charges at 21.4% of expenditures and net direct debt that is 164.6% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 74.4% 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. Wake County, with an estimated population of 1 million, is located in the Raleigh MSA, which we consider to be broad and diverse. The county has a projected per capita effective buying income of 119% of the national level and per capita market value of $140,737. Overall, the county's market value grew by 2% over the past year to $144.3 billion in 2018. The county unemployment rate was 4.2% in 2016.

Wake County encompasses 864 square miles in north-central North Carolina, and is the state's second most populous county. The county is home to Raleigh, the state capital. Wake County's economy is anchored by manufacturing, service industries, health care, educational institutions, and state and local government. Leading employers include:

- State of North Carolina (24,083)
- Wake County Public School System (18,554)
- IBM Corp. (10,000)
- NC State University (9,069) and;
- WakeMed Health & Hospitals (8,943).

Approximately 25% of the Research Triangle Park (RTP)--an internationally prominent center for high technology research and light manufacturing -- is located in the county. It is estimated that 250 international organizations that employ 50,000 people are currently located in the RTP. Wake County itself is home to North Carolina State University in Raleigh, with approximately 34,400 students.

The county continues to experience employment growth. Significant recent employment announcements include Credit Suisse, which plans to add 1,200 jobs in the county, and Infosys, which selected Wake County as one of its U.S. innovation and technology hubs and is expected to add 2,000 jobs over the next five years. Given the county's broad and diverse local economy, we expect economic growth to continue over the next few fiscal years.

Very strong management

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

The county has extensive formal policies covering key areas such as debt management and fund balance reserves, as well as a formal investment policy and detailed swap management policy. When arriving at revenue and expenditure assumptions, Wake County tracks historical trends for the past five years and forecasts operations for a minimum of four years and capital needs for a minimum of seven years. County management prepares monthly reports for the board of commissioners that outline budgeted and actual results.

The county uses a long-term financial planning model for its general fund and debt service fund, taking into account revenues, expenditures, transfers, and the fund balance. It uses the model to project operating expenses and makes decisions regarding tax rates, resource allocation, and the fund balance level. It reviews all financial models at least twice a year to ensure that all assumptions are still accurate. Additional reviews occur when significant issues are discussed that affect these models.

Wake County has a formal seven-year capital improvement plan with all funding sources identified for each year, and the county's financial forecasting model is linked to its capital plan and operating budget.

Following the implementation of Governmental Accounting Standards Board 54, the board of commissioners approved a new fund balance policy, which states that management will maintain a total general fund balance of at least 15% and an amount committed for working capital of at least 10% of the following fiscal year's general fund adopted budget in order to provide the county with adequate working capital and investment income. Wake County intends to keep the unassigned balance at zero. However, if reserves are needed for a catastrophic economic event, the county can use working capital committed funds with board approval. The board will also adopt a plan that outlines how to return these funds to working capital in order to maintain fiscal health. The board of commissioners has formally adopted a policy of maintaining a combined general fund and debt service fund total fund balance of at least 30% of general fund and debt service fund combined revenues.

Wake County applies several debt ratio policy parameters, which it monitors annually. The county adopted three debt-limitation policies, and it monitors combined county and overlapping debt per capita and compares it with those of other 'AAA' rated counties. The county also has combined county and overlapping debt at or less than 4% of the countywide tax base, and maintains direct debt at or less than 1.75%. It also monitors debt service payments so that they may not exceed 20% of total governmental expenditures.

Strong budgetary performance

Wake County's budgetary performance is strong in our opinion. The county had operating surpluses of 1.6% of expenditures in the general fund and of 2.8% across all governmental funds in fiscal 2017. General fund operating results of the county have been stable over the past three years, with a result of 2.7% in 2016 and a result of 1.1% in 2015.

For fiscal 2017, we adjusted the general fund expenditures to account for recurring transfers to other governmental funds. In addition, we adjusted total governmental fund expenditures down by removing capital expenditures paid for with debt proceeds. After the adjustment, the county experienced a surplus across total governmental funds.

The original budget for fiscal 2017 included a nominal $8.8 million fund balance appropriation; however, the county ultimately posted an operating surplus largely due to higher-than-budgeted ad valorem tax revenue and lower-than-expected expenditures, specifically expenditures related to human services. Ad valorem taxes account for the majority of general fund revenue, at 70%, followed by sales taxes, at 15%.

The approved $1.26 billion fiscal 2018 budget included a small fund balance appropriation of approximately $3.3 million and a 1.45-cent ad valorem tax increase, bringing the ad valorem tax rate to 61.5 cents per $100 of AV. Officials adopted the ad valorem tax increase to account for increased demands on county services due to continued population growth occurring throughout the county. Management reports that sales tax revenue has increased over fiscal 2017, and based on current trends management projects the county will likely post an operating surplus for fiscal 2018. Officials do not expect to use the fund balance appropriation, as was the case in previous fiscal years.

The county has a history of maintaining balanced operations based on its general practice of only budgeting for the use of general fund reserves for one-time expenditures, and its long-term capital and debt models that aim to maintain combined general and debt service reserves--the county's two largest governmental funds--in excess of 30% of combined revenue. Given this, and the county's very strong management policies and practices, we expect Wake County's operating performance to remain strong.

Very strong budgetary flexibility

Wake County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 25% of operating expenditures, or $301.3 million. The available fund balance includes $193.9 million (16.2% of expenditures) in the general fund and $107.4 million (9.0% of expenditures) that is outside the general fund but legally available for operations.

In our view, Wake County consistently maintains what we consider very strong reserves. For fiscal 2017 year-end, we estimate available reserves--including committed working capital funds and the assigned debt service fund balance—were at 25.1% of adjusted general fund expenditures. In accordance with the expected operating surplus for fiscal 2018 and established reserve policies, we expect budgetary flexibility to remain very strong in the next few years.

Very strong liquidity

In our opinion, Wake County's liquidity is very strong, with total government available cash at 50.4% of total governmental fund expenditures and 2.4x governmental debt service in 2017. In our view, the county has strong access to external liquidity if necessary.

Our belief that the county has strong access to external liquidity is based on its history of GO and appropriation-backed debt issuances. The bulk of the county's investments are in U.S. government treasuries and agencies, which we do not consider aggressive. The county has consistently had very strong liquidity, and we expect this to continue over the new few fiscal years.

The county has entered into several private placement transactions. While several of the county's private placement transactions contain acceleration provisions, we believe the liquidity risks are partially mitigated by the provisions of Section 160A-20 of the North Carolina statutes, which do not allow for deficiency judgments. In addition, upon review of these provisions and other terms of the agreements, we believe the events of default are remote and that potential liquidity risks are manageable.

Adequate debt and contingent liability profile

In our view, Wake County's debt and contingent liability profile is adequate. Total governmental fund debt service is 21.4% of total governmental fund expenditures, and net direct debt is 164.6% of total governmental fund revenue. Overall net debt is low at 1.9% of market value, and approximately 74.4% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

The county intends to issue approximately $170 million in limited-obligation bonds in fiscal 2018 to refund outstanding draws on the county's 2017 drawdown installment financing agreement. Like other recent issuances, the county expects to take out the short-term debt with long-term GO and appropriation- backed debt. The county also intends to hold a voter referendum in November 2018 to finance future capital needs. County officials are currently in the process of finalizing the projects and size of the referendum. Given Wake County's debt management policies and rapid amortization, we expect overall net debt will remain below 3% of market value despite the large nominal size of the county's planned future issuances.

Wake County's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 1.7% of total governmental fund expenditures in 2017. Of that amount, 1.1% represented required contributions to pension obligations, and 0.6% represented OPEB payments.

The county participates in three pension plans: the North Carolina Local Government Employees' Retirement System (LGERS), the North Carolina Registers of Deeds' Supplemental Pension Fund (RODSPF), and the Law Enforcement Officers' Special Separation Allowance. According to Governmental Accounting Standards Board Statement No. 68, employers with benefits administered through cost-sharing, multiemployer pension plans, such as LGERS and RODSPF, must report their proportionate share of the net pension liability. As of June 30, 2017, the county's proportion of the LGERS' net liabilities was $68.4 million. In addition, the plan's fiduciary net position as a percent of the LGERS' total pension liability was 91.5%. As of June 30, 2017, the RODSPF was overfunded with a plan fiduciary net position as a percent of total pension liability of 160%. The county's proportionate share of RODSPF's assets was $1.9 million. The county paid 100% of its required contribution to both plans in fiscal 2017.

The Law Enforcement Officers' Special Separation Allowance is a single-employer, defined-benefit pension plan that provides benefits to qualified law-enforcement officers. The county funds this plan on a pay-as-you-go basis from the general fund. In fiscal 2017, the county contributed $1.1 million to the plan, which had a total pension liability of $16.1 million.

The county also participates in a supplemental retirement income plan. This is a defined-contribution plan offered to employees in addition to their pension plan. In fiscal 2017, the county contributed $10.3 million to this plan.

The county provides OPEB through a single-employer, defined-benefit plan. It funds the health care benefits plan on a pay-as-you-go basis. The county board of commissioners has the authority to amend the plan and no longer offers benefits to new employees hired after June 30, 2011. The county's OPEB cost in fiscal 2017 was approximately $8.1 million with an unfunded liability of $260 million.

Very strong institutional framework

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

Outlook

The stable outlook reflects S&P Global Ratings' opinion that the county's very strong management practices will enable the county to maintain its strong financial performance and very strong budgetary flexibility. In addition, we believe the county's very strong and growing local economy provides additional rating stability. Therefore, we do not expect to change the rating within the two-year outlook period.

We could lower the rating if there were a substantial increase in the overall net debt burden, or if budgetary performance or reserves were to experience a sustained deterioration.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015

Ratings Detail (As Of February 9, 2018)		
Wake County GO		
Long Term Rating	AA+/Stable	Affirmed
Wake Cnty ltd oblig		
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 the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.