FitchRatings

Fitch Affirms Indian River County (FL)'s Spring Training Revs and IDR; Outlook Stable

Fitch Ratings-New York-26 March 2019: Fitch Ratings has affirmed the following ratings on Indian River County, FL:

--Long-Term Issuer Default Rating (IDR) at 'AAA';
--Approximately $5.7 million spring training facility revenue bonds, series 2001 at 'AA+'.

The Rating Outlook is Stable.

SECURITY

The spring training facility revenue bonds are limited obligations of the county, secured by a first lien on a statutory annual distribution of funds from the State of Florida general revenue fund for new or retained professional sports facilities, and proceeds from the fourth-cent tourist development tax (TDT) levied by the county and 86% of the local government half-cent sales tax distributed to the county by the state. The lien on the TDT and half-cent sales tax is automatically released as of April 1, 2021 (10 years before the final maturity date of the bonds of April 1, 2031). The bonds are additionally secured by a cash-funded reserve equal to maximum annual debt service (MADS).

IDR ANALYTICAL CONCLUSION

The 'AAA' IDR reflects the county's exceptional financial resilience including its superior budget flexibility and high reserves in relation to expected revenue volatility through the economic cycle. The rating also considers the county's very low long-term debt and retiree benefit liabilities.

DEDICATED TAX ANALYTICAL CONCLUSION
The 'AA+' rating on the spring training facility revenue bonds is based on Fitch's dedicated tax analysis and the structure's resilience to pledged revenues through the economic cycle. Debt service coverage is currently very high and provides significant protection against historical revenue stress and declines via the Fitch Analytical Sensitivity Tool under a moderate economic downturn scenario. The rating also reflects Fitch's expectation that pledged revenues will not be leveraged to the 1.25x ABT, which could otherwise pressure the rating. Growth prospects for the TDT and half-cent sales tax are modest based upon expectations for population and economic growth within the county over time.

Upon the release of the TDT and half-cent sales tax, the bonds will only be payable from the statutory payment from the state's general revenue fund, the creditworthiness of which Fitch views as equivalent to one-notch below the state IDR. Given the release of the TDT and half-cent sales tax prior to final maturity of the bonds, Fitch caps the rating at one-notch below the state IDR. The rating is also capped at the IDR on the county, as the pledged revenues do not meet the requirements set out in Fitch criteria for treatment as "pledged special revenue" under section 902(2) of the bankruptcy code and are not otherwise insulated from the operating risk of the county.

(SEE BELOW FOR DEDICATED TAX ANALYSIS)

Economic Summary
Indian River County is located on the Atlantic coastline, approximately 135 miles north of Miami, and includes the cities of Vero Beach and Sebastian. The county's population has shown steady growth with a 2017 census estimate of 154,383, up almost 12% since 2010.

IDR KEY RATING DRIVERS

Revenue Framework: 'aa'
Fitch expects revenues to rise at a slow pace but one that exceeds historical trends over the last decade, driven by growth in population and economic development. The county has considerable legal revenue raising ability with current millage rates well below the 10-mill statutory limit.

Expenditure Framework: 'aa'
The county's pace of spending is expected to be in line with or marginally above revenue trends in the absence of policy action. Carrying costs for debt and retiree liabilities are moderately low despite recent large increases in contributions to the state-administered Florida Retirement System (FRS) the county participates in.

Long-Term Liability Burden: 'aaa'
County debt and pension benefit liabilities are very low, estimated at below 3% of personal income. Liabilities are expected to remain low based on the county's participation in FRS, absence of additional debt issuance plans and very rapid repayment of outstanding debt.

Operating Performance: 'aaa'
Fitch expects the county will continue to demonstrate a high level of financial resilience and gap-closing ability throughout economic cycles based on its high reserves, superior budget flexibility, and prudent financial management record.

RATING SENSITIVITIES
IDR: The IDR is sensitive to unexpected and significant changes in the county's financial resilience and/or long-term liability burden.

SPRING TRAINING FACILITY BONDS: Due to the nature of the revenue pledge and the automatic release of the TDT and half-cent sales tax, the rating on the bonds is capped at the lower of the IDR on the county or one notch below the state's IDR. The rating is also sensitive to a material change in coverage resulting from additional leverage or a shift in the performance of pledged TDT and/or half-cent sales tax revenues prior to their automatic release.

ECONOMIC RESOURCE BASE
The local economy of Indian River County is traditionally centered on agriculture and tourism, although it has diversified with an increased presence of health care and information technology, light manufacturing, wholesale and retail trade and service sector jobs. The county's tax base has picked up solid momentum in recent years after enduring steep declines during the recession and a slow initial recovery. The county's unemployment rate has improved considerably but still exceeds the state and the U.S. average. The tourism sector continues to strengthen, with tourist development taxes up 7% in fiscal 2018 over the prior year.

IDR CREDIT PROFILE
Revenue Framework
Property tax revenues are the county's largest revenue source, comprising 66% of fiscal 2019 general fund budgeted revenues.

The county's 10-year historical general fund revenue growth has lagged both U.S. GDP and inflation increases through fiscal year ending 2018, due to the severe impact of the great recession and housing market decline as well as the state property tax reform. Growth prospects are somewhat more positive, absent policy action, driven by continued population growth, property appreciation and development.

The county has ample legal revenue raising authority as the current millage is well below the property tax cap of 10 mills. The adopted general fund tax rate remained stable at 3.4604 mills in fiscal 2019.

Expenditure Framework
The county maintains solid expenditure flexibility with moderate carrying costs. Public safety is the largest spending item, with fiscal 2018 outlays comprising 50% of total general fund and MSTU expenditures. General government spending is the second largest spending category equal to about 23%.

The county's pace of spending is expected to be in line with or marginally exceed revenue growth trends, absent policy action, with increased demands associated with population growth largely offset by growth in the tax base and other non-ad valorem revenues.

Employee wages and benefits are the main expenditure driver. Wages and benefits are collectively bargained, as county employees are largely represented by two unions. However, under state law, if an impasse is declared, both parties are required to engage in a non-binding mediation process after which the local government may impose contract terms for one year.

The county was able to manage the budget through the great recession by privatizing certain services, implementing hiring and wage freezes and layoffs, and using reserves. It has since increased staffing levels in recent years (albeit to a level that is still below pre-recession highs) and reinstated pay increases. The county's high proportion of public safety spending may present some practical restrictions on future expenditure flexibility. Fixed carrying costs associated with debt and retiree liabilities are equal to about 9% of total government spending in fiscal 2018.

Long-Term Liability Burden
The county's long-term liability burden approximates 3% of personal income and is expected to remain very low. The county's overall debt burden mainly reflects the overlapping obligations of the county school board. The county's direct debt amortizes at an aggressive pace with over 90% of principal to be repaid within 10 years. Capital needs from 2019 through 2023 are manageable and are largely focused on transportation and utility system improvements financed from gas and sales tax revenues, impact fees, user fees and grants. The county does not have any debt issuance planned.

During the November 2016 general election, county voters approved the extension of the optional sales tax beginning in Jan. 1, 2020 for an additional 15 years through Dec. 31, 2034. The local option sales tax generated approximately $19 million in revenues in fiscal 2018. The county plans to continue to use the funds to support its infrastructure and capital needs on a pay-as-you-go basis in lieu of higher amounts of debt financing.

The county participates in the state-administered Florida Retirement System, a cost sharing multiple employer plan. FRS is adequately funded with a reported asset to liability ratio estimated at 84% (as of the June 30, 2018 measurement date), or 75% using Fitch's standard 6% investment rate of return. The county's net pension liability (excluding the HIS plan) totaled $104 million, or approximately $190 million (less than 2% of personal income) using the Fitch adjustment. The county historically funds 100% of the actuarially determined FRS contribution.

Operating Performance
Fitch believes that the county's broad revenue raising ability and spending flexibility provide it with the ability to maintain reserves well in excess of a level consistent with a 'aaa' financial resilience assessment through economic cycles. Fitch's Analytical Sensitivity Tool (FAST) generates a general fund revenue decline of nearly 4% in a moderate economic downturn scenario. The county continues to comply with its financial reserve policy requiring unassigned reserves equal to 20% of total operational spending plus an additional 5% for both budget stabilization and emergency use.

The county has demonstrated robust financial management by maintaining ample reserves. Despite modest operating deficits that occurred from fiscal 2015-2017, the county's unrestricted reserve levels have remained in excess of 44% of total general fund expenditures and transfers out.

Fiscal 2018 results ended with approximately $50 million in unrestricted reserves, equal to about 46% in total general fund spending, reflecting continued growth in property tax and sales tax revenues and lower than budgeted spending, specifically in the areas of transportation and culture and recreation.

The fiscal 2019 adopted budget is balanced and represents an approximate 3.5% increase from the 2018 original budget, reflecting an increase in the tax base, no millage rate increase, new positions, and various capital improvements and technology upgrades.

DEDICATED TAX CREDIT PROFILE

The spring training facility revenue bonds are payable from combination of a first lien on certain statutorily defined payments received from the State of Florida for professional sports facilities, the proceeds from the fourth cent TDT revenues levied by the county and 86% of the local government half-cent sales tax distributed to the county by the state. The lien on the TDT and half-cent sales tax will automatically release after April 1, 2021 (the final maturity date of the bonds is April 1, 2031). The state distribution payment is derived from the state general revenue fund.

Fitch calculates the pledged revenue CAGR for the 10 year period ending fiscal 2018 at less than 3%. Pledged revenues, comprised largely of sales tax revenues, were adversely impacted by the outsized effects of the great recession, resulting in a 20% decline over from 2005 to 2010. Fitch expects future revenue growth to track the rate of inflation over time, due to economically sensitive nature of sales tax revenues and the county's continued growth in population and development.

To evaluate the sensitivity of the dedicated revenue stream to cyclical declines, Fitch considers both revenue sensitivity results (using a 1% decline in national GDP stress scenario) and the largest consecutive decline in revenues. Based on the pledged revenue history, FAST generates a 3.7% revenue decline in a -1% U.S. GDP decline scenario. The largest decline in historical revenues was equal to a steep 20% from fiscal 2005 to fiscal 2010.

Fiscal 2018 pledged revenues of approximately $10 million provided very high MADS coverage of roughly 20x. MADS has been reduced to an amount that is just below the $500,004 annual state payment following a series of early bond redemptions from surplus funds. The current structure could tolerate a 96% decline in pledged revenues before MADS coverage reaches 1.0x. This level of tolerance is equivalent to almost 26x the FAST result and about 5x the worst historical loss during the time series of data reviewed by Fitch. Fitch considers these results to be consistent with an 'aaa' assessment.

Although not expected, an increase in leverage to the 1.25x coverage requirement of the ABT would dilute the structure's resilience to potential revenue stress through the economic cycle, and would lead to a downgrade of the rating on the spring training facility revenue bonds. The ABT is based on a 1.25x coverage requirement from historical half-cent sales tax revenue alone, and is structured in a manner that limits risk to overleveraging given the release of the lien on such revenue in 2021.

At that point in time, bondholders will only be backed by a lien on the statutory annual distribution of funds from the State of Florida general revenue fund. As noted above, the annual debt service on the bonds will be just below the amount of the state payment.

EXPOSURE TO ISSUER OPERATIONS
Fitch believes the pledged revenues would not meet the requirements set out in Fitch's criteria for treatment as "pledged special revenue" under section 902(2) of the bankruptcy code. Given the bond structure and the release of the lien on TDT and half-cent sales tax revenues, the rating on the bonds is capped by both the county's IDR and the rating that is one-notch below the state's IDR.

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In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

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The following issuer(s) did not participate in the rating process, or provide additional information, beyond the issuer's available public disclosure:
Indian River County (FL)

Applicable Criteria
U.S. Public Finance Tax-Supported Rating Criteria (pub. 03 Apr 2018)

Additional Disclosures
Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Policy

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