



## Fitch Affirms Indian River County, FL Water & Sewer Revs at 'AAA'; Outlook Stable

Fitch Ratings-Austin-12 November 2018: Fitch Ratings has affirmed the rating on the following Indian River County, FL (the county) revenue bonds at 'AAA':

--\$13.5 million water and sewer system revenue refunding bonds, series 2009.

The Rating Outlook is Stable.

### SECURITY

The bonds are supported by the net revenues of the county's water and sewer system (the system).

### KEY RATING DRIVERS

**EXCELLENT FINANCIAL PROFILE:** The system has produced over 2.6x debt service coverage (DSC) for the past five years and has maintained excellent liquidity. Audited fiscal 2017 results show 3.0x Fitch-calculated DSC and over \$45 million in unrestricted available cash, equating to approximately 780 days cash on hand.

**MINIMAL CAPITAL NEEDS, LOW DEBT:** The system's capital improvement program (CIP) is limited and primarily addresses renewal and replacement (R&R) projects, septic to sewer conversions, and automatic meter reading implementation. The system is able to fund its CIP via pay-go due to its strong margins and ample cash balances. Debt levels are very low and all debt matures by 2024.

**AFFORDABLE AND FLEXIBLE RATE STRUCTURE:** Rates are affordable at approximately 1.5% of median household income (MHI) as a result of almost twenty years of no rate increases. Management did indicate that future rate increases based on the consumer price index may be needed moving forward. This is not a concern, as affordability is good and rates are below Fitch's rate affordability threshold of 2%.

**HEALTHY SERVICE AREA:** The County is experiencing healthy customer growth, averaging about 2% over the past five years. Housing starts increased over 15% in the last two years as the County continues to recover from the recession. This growth and economic development is expected to continue, and the system has ample capacity and water sources available to service these needs.

### RATING SENSITIVITIES

**MAINTENANCE OF STRONG FINANCIAL POSITION:** Indian River County, Florida water and sewer system's very strong underlying credit fundamentals, which include healthy financial performance, limited and rapidly amortizing debt, and limited capital needs, support the 'AAA' rating. A significant decline in one or more of these positive attributes, although unexpected, could affect the rating.

## CREDIT PROFILE

Indian River County (Issuer Default Rating 'AAA') is located on Florida's central Atlantic coast about 86 miles southeast of the city of Orlando. The county covers nearly 500 square miles and has a population of roughly 150,000. The economy is supported by construction, manufacturing, health care, tourism, educational services, retail and distribution.

## STRONG CURRENT AND FUTURE FINANCIAL PROFILE

The system's financial performance has been historically solid, with above 2.0x DSC consistently since 2009 and 3.0x Fitch-calculated DSC in fiscal year 2017. The county's conservative management maintains this positive coverage level as well as substantial cash reserves in an effort to guarantee available cash for unforeseen system needs. According to the management provided forecast, Fitch-calculated unaudited coverage for fiscal year 2018 is expected to be 3.8x, and 3.3x and above through fiscal year 2023. Based on historic performance and limited capital and expenditure needs, Fitch expects that positive financial results will continue.

Liquidity is extremely strong, with the system ending fiscal year 2017 with more than \$45 million in unrestricted cash on hand in addition to roughly \$27 million in restricted construction funds. Strong cash balances are expected to continue as capital needs are limited.

## LOW DEBT, MANAGEABLE CAPITAL NEEDS

The system's debt profile is a key credit strength. Debt per customer is very low at approximately \$280 in fiscal year 2017, well below average compared with other similarly rated systems. Debt to net plant is also strong at 12% for the same period, and amortization is very fast, with all debt maturing by 2024.

The county's five year 2018-2022 CIP of \$47 million is expected to be funded entirely via pay-go with some grant support. Major projects include septic to sewer conversions, automated meter reading, and overall improvements to the system. Historic capital spending since 2013 has been low, with capex relative to the rate of annual depreciation averaging only 31% during that time. While Fitch views this level of capex as somewhat weak and possibly as an indicator of deferred maintenance, the system is relatively new (estimated age of plant is 18 years, slightly above the AAA median of 15 years) and underwent substantial capital investment in 2008 to ensure long-term supply and capacity availability. Positively, the system increased the amount it spent on R&R in fiscal year 2017 and expects to continue this level moving forward.

## LOW CUSTOMER CHARGES

The average residential customer bill of \$60 for combined service assuming 7,500 gallons of water use and 6,000 gallons of sewer use is affordable at 1.5% of MHI. Rates should stay competitive as the county has a very manageable capital program that is expected to be funded with cash and grants.

The system is in the process of finalizing a rate study that calls for a new rate structure. As part of its conservation initiatives, the recommended structure adjusts the consumptive tiers and, as a result, discourages heavy water usage. This change is expected to increase revenues. In addition, the County is requesting approval from the board for any future incremental increases based on CPI adjustments. The system currently exhibits solid rate affordability, so this should not pose any significant issues.

## ABUNDANT WATER SUPPLY AND SOUND INFRASTRUCTURE

The county's water and sewer system provides services to a mostly residential customer base of approximately 49,000 water and 29,000 sewer accounts as of fiscal year 2017. Water is supplied through various wells from the Floridian Aquifer, with treatment provided by two county-owned treatment facilities. The water treatment plants have a combined 22.5 million gallons per day (mgd) of treatment capacity, which is more than sufficient to meet the system's average daily demand in fiscal year 2017 of 10.2 mgd. Water use is regulated by the St. Johns River Water Management District through a consumptive use permit that expires in 2031. The system can produce over 20.0 mgd of water, and the Utility Department is proactively researching alternative water supplies in order to support future growth needs over the longer term.

Wastewater is treated at one of four regional treatment plants, with a combined current treatment capacity of 12.0 mgd. Current maximum daily demand is 6.1 mgd, leaving plenty of treatment capacity to meet future growth. Effluent is treated to 100% re-use standards, and as a result the county does not expect to face significant capital or other regulatory compliance costs related to numeric nutrient mandates for effluent discharged into local surface water.

## STABLE LOCAL ECONOMY

The county's economy continues to see improvement following the economic downturn, categorized by increasing housing starts, sales tax and taxable value. The county's unemployment rate has declined to 4.9% as of August 2018 from 12.7% in 2011, yet remained higher than that of the state and national averages of 3.8% and 3.9%, respectively. The county's MHI is on par with the state and just about 15% below the national average, which is somewhat driven by the larger-than-average retiree population.

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