

RatingsDirect®

Summary:

Deer Park, Texas; General Obligation

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Credit Profile

US\$7.145 mil certs of oblig ser 2015 dtd 09/01/2015 due 03/15/2025		
<i>Long Term Rating</i>	AAA/Stable	New
Deer Pk Certs of Obligation ser 2014 dtd 11/01/2014 due 03/15/2034		
<i>Long Term Rating</i>	AAA/Stable	Upgraded
Deer Pk GO		
<i>Long Term Rating</i>	AAA/Stable	Upgraded

Rationale

Standard & Poor's Ratings Services raised its long-term rating on Deer Park, Texas' existing general obligation (GO) debt to 'AAA' from 'AA+'. The upgrade reflects management's commitment to maintain very strong reserves, which are currently above 75% of annual expenditures, and a general improvement in the city's wealth and income indicators. At the same time, we assigned our 'AAA' long-term rating to the city's series 2015 certificates of obligation. The outlook on these ratings is stable.

Deer Park GO bonds are eligible to be rated above the sovereign because we believe the city 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," U.S. local governments are considered to have moderate sensitivity to country risk. The city's GO pledge is the primary source of security on the debt; this severely limits the possibility of negative sovereign intervention in the payment of the debt or in the operations of the city. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy, independent treasury management and no history of government intervention. Deer Park has considerable financial flexibility, as demonstrated by the very high fund general balance as a percentage of expenditures, as well as very strong liquidity.

A pledge of the city's full faith credit and resources and an agreement to levy ad valorem property taxes without limitations as to rate or amount to secure these certificates. In addition, the certificates are further secured by a limited pledge of a subordinate lien on the net revenues of the city's waterworks and sanitary sewer system in an amount not to exceed \$1,000. Officials plan to use certificate proceeds for the construction and equipment of an animal shelter, and improvements to streets, sidewalks, and drainage facilities.

The rating reflects our assessment of the following factors for the city, specifically its:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA) and a local stabilizing institutional influence;
- Strong management, with "good" financial policies and practices under our Financial Management Assessment (FMA) methodology;

- Very strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level;
- Very strong budgetary flexibility, with a high available fund balance in fiscal 2014 of 89% of operating expenditures;
- Very strong liquidity, with total government available cash of 1.7x total governmental fund expenditures and 16.3x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability position, with debt service carrying charges of 10.7% of expenditures and net direct debt that is 86.9% of total governmental fund revenue; and
- Strong institutional framework score.

Very strong economy

We consider Deer Park's economy very strong. The city, with an estimated population of 33,600, is located in Harris County in the Houston-The Woodlands-Sugar Land, TX MSA, which we consider to be broad and diverse. The city also benefits, in our view, from a stabilizing institutional influence. The city has a projected per capita effective buying income of 111% of the national level and per capita market value of \$63,134. Overall, the city's market value grew by 8.0% over the past year to \$2.1 billion in 2015. The county unemployment rate was 4.9% in 2014.

In 2014, the city reached a contractual arrangement with 21 separate industrial companies to remove their value from the tax rolls in return for predictable payments-in-lieu-of-taxes (PILOTs), equal to about 63% of what the companies would have owed if they were subject to full ad valorem taxation by the city. We believe the tax base is very diverse; the 10 leading taxpayers account for 8% of total assessed value (AV). However, if those companies in the industrial districts were in the city, the property tax base concentration would substantially increase.

Strong management

We view the city's management as strong, with "good" financial policies and practices under our FMA methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis.

The city prepares the budget based on historical trends, taking into account new development. Also, given the industrial district revenues from the large oil and gas firms, the city looks at the price of oil. It provides budget-to-actuals monthly to the council. It can also amend the budget at any time. The city does long-term financial planning and has an annually adjusted seven-year plan done as part of the budget. However, it lacks a long-term capital plan for the general fund. Deer Park's investment policy mirrors state guidelines and there are monthly updates for management on holdings and earnings. The city has a debt management policy which we do not think is comprehensive but it does place some limitations on debt issuances. It has a formal policy to maintain at least 25% of expenditures in reserves, and historically has far exceeded that minimum.

Very strong budgetary performance

Deer Park's budgetary performance is very strong in our opinion. The city had operating surpluses of 16% in the general fund and 12.1% across all governmental funds in fiscal 2014.

For fiscal 2015, the city is currently projecting a smaller surplus of \$1.1 million, the lower-than-historic surplus partly reflecting lower oil prices, which affect the industrial companies' total values. The city receives PILOTs from 21 industrial companies. The arrangement removes the companies' value from the tax rolls in return for predictable PILOTs, which are equal to about 63% of what the companies would have owed if they were subject to full ad valorem

taxation. The benefit to the city is that the revenue from these companies is no longer subject to volatility and valuation challenges. We expect sales taxes will remain at least level, and, with property taxes remaining healthy, the city will be in a good position to maintain its very strong performance. These PILOT values are expected to decline further in fiscal 2016, where the city is expecting about \$1 million less in industrial contract revenues.

Very strong budgetary flexibility

Deer Park's budgetary flexibility is very strong, in our view, with a high available fund balance in fiscal 2014 of 89% of operating expenditures, or \$27.4 million. We expect the available fund balance will remain above 75% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

Even with the previously mention declines in industrial contract revenues, the city is anticipating that the reserves will stay at the current levels and not shrink.

Very strong liquidity

In our opinion, Deer Park's liquidity is very strong, with total government available cash of 1.7x total governmental fund expenditures and 16.3x governmental debt service in 2014.

In our view, the city has strong access to external liquidity if necessary. We consider its investments conservative as it mainly invests in certificates of deposit and investment pools like TexPool and TexStar.

Weak debt and contingent liability profile

In our view, Deer Park's debt and contingent liability profile is weak. Total governmental fund debt service is 10.7% of total governmental fund expenditures, and net direct debt is 86.9% of total governmental fund revenue.

The city has plans for various projects, from water- and sewer-related to parks and recreation projects, but it has currently identified other revenue sources to repay any potential bond issues.

Deer Park's combined pension and other postemployment benefit (OPEB) contributions totaled 7.3% of total governmental fund expenditures in 2014. Of that amount, 6.3% represented contributions to pension obligations and 1.0% represented OPEB payments. The city made its full annual required pension contribution in 2014.

Strong institutional framework

The institutional framework score for Texas municipalities is strong.

Outlook

The stable outlook reflects our view of Deer Park's continued economic and tax base growth, as well as the success of the renewed PILOTs, providing revenue stability. We also believe the outlook reflects management's historical commitment to maintaining very strong reserves. However, if debt levels remain high and the city experiences any significant operating declines, we could lower the rating.

Related Criteria And Research

Related Criteria

- USPF Criteria: Local Government GO Ratings Methodology And Assumptions, Sept. 12, 2013
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Limited-Tax GO Debt, Jan. 10, 2002
- USPF Criteria: Methodology: Rating Approach To Obligations With Multiple Revenue Streams, Nov. 29, 2011
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions, Nov. 19, 2013
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Institutional Framework Overview: Texas Local Governments

Ratings Detail (As Of August 17, 2015)		
Deer Pk GO		
<i>Long Term Rating</i>	AAA/Stable	Upgraded
Deer Pk		
<i>Unenhanced Rating</i>	AAA(SPUR)/Stable	Upgraded
Deer Pk GO		
<i>Unenhanced Rating</i>	AAA(SPUR)/Stable	Upgraded

Many issues are enhanced by bond insurance.

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