S&P Global
Ratings

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## Summary:

# Horseshoe Bay, Texas; General Obligation


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| Credit Profile | | |
|---|---|---|
| US$4.02 mil combination tax and rev certs of oblig ser 2016 dtd 09/15/2016 due 08/15/2031 | | |
| *Long Term Rating* | AA+/Stable | New |
| Horseshoe Bay GO | | |
| *Long Term Rating* | AA+/Stable | Affirmed |

## Rationale

S&P Global Ratings assigned its 'AA+' rating and stable outlook to Horseshoe Bay, Texas' series 2016 combination tax and revenue certificates of obligation and affirmed its 'AA+' rating, with a stable outlook, on the city's existing general obligation (GO) debt.

The certificates are payable from an annual ad valorem tax levied against all taxable property in the city within the limits prescribed by law. The certificates are also payable through a limited $1,000 pledge of surplus revenue from the city's water and wastewater system. However, we rate the certificates based on the city's ad valorem pledge.

State statutes provide for a maximum ad valorem tax rate of $2.50 per $100 of taxable assessed valuation (AV) for all city purposes, including a maximum $1.50 for all GO debt service calculated at the time of issuance based on 90% tax collections. For fiscal 2016, the total tax rate is 25 cents per $100 of AV, which includes 2.8 cents for debt service. Due to the city's current tax rate flexibility, very strong liquidity, and high investment-grade rating, we do not differentiate between limited- and unlimited-tax pledges. We understand officials will use series 2016 certificate proceeds to finance improvements to the city's water and wastewater system and acquire two fire engines and related equipment.

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

- Very strong economy, with projected per capita effective buying income at 208% of the national level and market value per capita of $263,132;
- Strong management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2015;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2015 of 56% of operating expenditures;
- Very strong liquidity, with total government available cash at 110.6% of total governmental fund expenditures and 10.9x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability position, with debt service carrying charges at 10.2% of expenditures and net direct debt that is 142.5% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

### Very strong economy

We consider Horseshoe Bay's economy very strong. The city, with an estimated population of 6,711, is located in Burnet and Llano counties. The city has a projected per capita effective buying income of 208% of the national level and per capita market value of $263,132. Overall, the city's market value grew by 4.4% over the past year to $1.8 billion in 2017. The weight-averaged unemployment rate of the counties was 4.2% in 2015.

Horseshoe Bay is near Marble Falls, about 55 miles northwest of Austin. The 14-square-mile city consists predominately of luxury homes for retirees and vacation homeowners. Therefore, the property tax base is very diverse with the 10 leading taxpayers accounting for just 5.5% of AV. We expect tax base growth to continue, supported by the ongoing activity within the Summit Rock development, the annexation of properties in the surrounding areas, and the expansion of some commercial areas.

Due to the city's sizable retiree population and current construction of additional residential units targeting the 55-year-and-older segment, we believe, over the long term, the city's economy could be negatively affected by a highly dependent population--one we define as greater than 55% of the total population.

### 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.

Key practices include management's:

- Revenue and expenditure assumptions based, in part, on five years of historical trends and the use of outside sources to assist with forecasting;
- Monthly budget updates to the city council for review, including budget-to-actual comparisons;
- Use of a five-year capital plan that it updates annually with funding sources identified for some projects;
- Formal investment management policy that follows state guidelines with monthly holdings and performance reports to the council; and
- Formal reserve policy of maintaining six months' total operating expenses in reserve.

The city does not currently have any formal long-term financial forecasting or debt management practices.

### Strong budgetary performance

Horseshoe Bay's budgetary performance is strong in our opinion. The city had operating surpluses of 1.8% of expenditures in the general fund and 10% of expenditures across all governmental funds in fiscal 2015.

We have adjusted the city's expenditures for significant one-time items such as the spending down of bond proceeds and cash used for its large street project. We expect budgetary performance to remain strong over the next two fiscal years. Current fiscal year-end 2016 estimates suggest a strong performance with surpluses of 2.8% of expenditures in the general fund and 1.4% of expenditures across all governmental funds.

The proposed fiscal 2017 budget suggests a 2.2% surplus for the general fund. We also expect performance across all governmental funds to be similar to fiscal 2016 results. In fiscal 2015, property taxes generated about 53% of general revenue while charges for services accounted for 15% and sales taxes generated 14%. All revenue streams have historically been relatively reliable.

### Very strong budgetary flexibility

Horseshoe Bay's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2015 of 56% of operating expenditures, or $3.5 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

We expect budgetary flexibility to remain very strong over the next two fiscal years, supported by the city's formal policy of maintaining six months' operating expenses in reserve. We estimate the city will end fiscal 2016 with an available fund balance of roughly 55.6% of expenditures. We expect officials to continue to build available fund balance since the completion of a large street improvement project. The city cash funded a portion of street improvements recently rather than incur additional debt.

### Very strong liquidity

In our opinion, Horseshoe Bay's liquidity is very strong, with total government available cash at 110.6% of total governmental fund expenditures and 10.9x governmental debt service in 2015. In our view, the city has strong access to external liquidity if necessary.

The city's access to the market within the past 20 years and issuance of mainly tax-backed bonds demonstrate its strong access to external liquidity. It has historically had, what we consider, very strong cash balances. In addition, we do not believe its cash position will deteriorate over the next two fiscal years. Currently, all of its investments comply with state guidelines. As of July 2016, city investments were primarily in the state investment pool and local banks. We do not consider these investments aggressive.

### Adequate debt and contingent liability profile

In our view, Horseshoe Bay's debt and contingent liability profile is adequate. Total governmental fund debt service is 10.2% of total governmental fund expenditures, and net direct debt is 142.5% of total governmental fund revenue. Overall net debt is low at 1.5% of market value, which is, in our view, a positive credit factor.

We understand management is discussing issuing additional debt for its wastewater plant expansion, which could occur within two years to three years, depending on the rate of residential growth and its effect on capacity. The city's five-year capital plan includes $400,000 to issue in fiscal 2018 to cover engineering costs and $2.5 million in fiscal 2019 for the actual plant expansion.

Horseshoe Bay provides pension benefits for all full-time employees through Nationwide Retirement Solutions Inc.; it makes annual contributions to the plan equal to the amounts accrued for pension expenses. The plan is a defined-contribution plan, and the city does not currently have ongoing or unfunded liabilities. Horseshoe Bay contributes an amount currently equal to 5% of the employee's regular base salary, not including overtime, into the effective pension plan until the employee's five-year anniversary date. After five years of continuous employment, the city's contribution to the plan will increase by 2.5% of regular salary to a total of 7.5%. The city does not offer other postemployment benefits to its retirees.

### Strong institutional framework

The institutional framework score for Texas municipalities is strong.

## Outlook

The stable outlook reflects S&P Global Ratings' opinion that it will not change the rating over the two-year outlook period. We expect the city's budgetary flexibility and liquidity to remain very strong, supported by strong management and a formal policy to maintain six months' operating expenses in reserve. We also expect ongoing residential development will support the city's growth and very strong economic indicators. Although the city's debt profile has improved to adequate levels, we believe a significant portion of the city's future debt for the planned wastewater plant expansion will be self-supporting.

### Upside scenario

We could raise the rating if available fund balance were to exceed 75% of general fund expenditures consistently or if projected per capita effective buying income were to exceed 225% of the national level. We could also raise the rating if the city's debt profile does not weaken with the additional planned bond issuance to expand the wastewater plant.

### Downside scenario

We could lower the rating if a weak budgetary performance trend were to develop, resulting in available fund balance falling below the policy requirement.

## Related Research

S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013