FitchRatings

Fitch Affirms Maricopa County's (AZ) GOs & Lease Revs; Outlook Stable Ratings

01 Apr 2011 2:36 PM (EDT)

Fitch Ratings-Austin-01 April 2011: During the course of routine surveillance, Fitch Ratings has taken the following rating action on Maricopa County, Arizona:

--$156.7 million Public Finance Corporation lease revenue bonds and certificates of participation (COPs) outstanding affirmed at 'AA+';
--General obligation (GO) bond rating (implied) affirmed at 'AAA'.

The Rating Outlook is Stable.

RATING RATIONALE:
--The county's financial profile remains sound, despite various economic and financial pressures that emerged over the past four years.
--County taxable values have declined and further weakness is expected, pressuring property tax rates; other major operating revenues, including local sales tax and state shared revenues, also have declined measurably.
--County debt levels are modest, reflecting the ongoing practice of financing capital needs largely on a pay/go basis.
--County management is tenured and has demonstrated the ability to date to respond effectively to deteriorating economic and revenue forces and maintain a solid financial posture; Fitch has consistently noted management as a positive credit factor.
--Housing remains a vulnerability as prices for both new and existing homes in the Phoenix metropolitan area have shown no signs of a recovery.
--The structure that governs outstanding lease revenue bonds and COPs features many of the characteristics (e.g. essential leased assets, reliance on lease financing, covenant to budget and appropriate) that Fitch considers positive credit factors.

KEY RATING DRIVERS:
--The county's operating forecast suggests additional financial pressures over the near term as increasing outlays, particularly shifts of spending responsibility from the state, threaten to outpace revenue growth.
--While certain economic indicators--e.g. local sales tax revenues--have shown some positive movement in recent months, the region's economic recovery is expected to be gradual; Fitch believes long term prospects are positive, given the area's history of attracting businesses and residents.

SECURITY:
The lease revenue bonds and COPs are secured by lease payments from the county to the corporation, subject to annual appropriation by the county. GO bonds, when issued, are secured by an unlimited ad valorem tax levied against all taxable property in the county.

CREDIT SUMMARY:
Maricopa County is the economic and population center of Arizona, encompassing Phoenix and surrounding suburbs within its over 9,000 square mile boundary. Phoenix was the nation's fastest growing major U.S. city from 1990-2000, with a 34% population increase. Growth in the surrounding cities contributed to a more than 40% increase in county population during this decade, and the period from 2000-2009 saw the county population jump from 3.07 million to slightly more than 4 million. This rapid growth fed the housing construction boom that ultimately led to the collapse of the housing market beginning in 2008. From a peak of nearly 37,000 in 2007, housing starts in the Phoenix metropolitan area plummeted to less than 10,000 by 2010; the average price of an existing home has dropped from more than $310,000 in 2007 to less than $180,000. While some observers anticipate the start of a modest rebound in residential construction in 2012, recent home price data suggest any meaningful recovery may be some months off. Fitch notes that the large number of foreclosures and vacancies, as well as depressed prices, is likely to be a drag on the economic recovery for some time.

After flattening out in 2009 and dipping 3% in 2010, county employment appears to have stabilized and shown some modest improvement. For the period from January 2010 to January 2011 employment increased 0.8% to 1.8 million. Not surprisingly, the loss of construction jobs (down 23% from 2006-2010) is a negative influence on the local employment picture. Most other employment sectors registered smaller drops during this period, with the exception of education and health services which saw a 6% increase. Professional and business services and trade, transportation and utilities represent the largest sectors in the metropolitan statistical area (MSA). The county's unemployment rate, while up sharply from pre-recessionary levels, remains below the state and U.S. averages. The January 2011 rate was 9.1%, compared to the state average of 10% and the U.S. rate of 9.8%. County median household income levels are slightly above the state and national averages.

Despite the economic pressures and their impact on various revenue sources, the county's financial profile remains healthy. Operating reserves remain robust, as management has adjusted spending levels over the past several fiscal years. Fiscal 2010 audited results included an unreserved general fund balance of $489 million, or nearly 50% of total annual spending; this was an increase of nearly $80 million from the prior year. These reserves fluctuate somewhat from year to year as the county continues with its practice of funding capital needs from available resources, but overall they remain substantial. Revenue pressures include declines in state shared sales tax receipts, which dropped roughly 25% from fiscal 2007 to 2010 (a decline of more than $110 million) and vehicle license tax revenues, which dropped by 20% during this period (more than $25 million). The largest operating revenue source, local property taxes, have remained steady as the tax rate has increased modestly to offset loss in taxable value. These increases may be larger over the next several fiscal years as county values continue to drop. The secondary assessed value (SAV) fell nearly 15% in fiscal 2011 to $49.7 billion, and another drop of more than 20% is anticipated for fiscal 2012. While observing that this as a major concern, Fitch also notes the county has the ability to increase its tax rate to offset such valuation declines, the only limitation being a 2% levy increase year-to-year (adjusted for new property).

The fiscal 2011 budget included a 5% decline in operating expenses and modest increases in certain economically sensitive revenues. Year-to-date sales tax revenues are running slightly ahead of budget, while other revenues (e.g. highway user fee revenues) are trailing budget projections slightly. The current projection calls for an ending general fund balance of roughly $390 million, as the county applies a portion of reserves to various capital projects (including the completion of the new criminal court tower). Looking ahead, management identifies continued financial pressure from the state as a major challenge. Since fiscal 2008, the combination of mandated contributions and shifts in funding responsibility have added more than $125 million to county spending totals. The prospect of additional expenditure responsibilities contribute to budgetary imbalances in the county's current five-year operating forecast. However, Fitch notes that county management has adjusted so far to weakening economic conditions and funding challenges and has not exhausted its options regarding both revenue generation and spending reductions.

County direct debt levels are modest and considered a positive credit factor. As noted above, the county contributes significantly to capital projects from available resources, limiting borrowing needs. Direct debt per capita currently is only $43; estimated overall debt is moderate at roughly $2,200 per capita and 2% of market value. The county's five-year capital plan totals $920 million, including some projected carried forward from the prior plan. Public safety is the largest component at roughly 60% of the plan; no borrowings are anticipated at this time. The lease structure that governs the outstanding lease revenue bonds and COPs has characteristics that Fitch considers credit strengths, including essential leased assets, the county's reliance on lease financing as a primary borrowing mechanism, an annual covenant to budget and appropriate lease payments, the buildup of equity ownership over the term of the lease, and the trustee's ability to repossess the asset in the event of nonappropriation or default.

Contact:

Primary Analyst
Steve Murray
Senior Director
+1-512-215-3729
111 Congress Ave., Suite 2010
Austin, TX 78701

Secondary Analyst
Jose Acosta
Senior Director
+1-512-215-3726

Committee Chairperson
Jim Mann
Senior Director
+1-212-908-0148

Media Relations: Cindy Stoller, New York, Tel: +1 212 908 0526, Email: cindy.stoller@fitchratings.com.

Additional information is available at 'www.fitchratings.com'

In addition to the sources of information identified in the Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, LoanPerformance, Inc., and IHS Global Insight.

Applicable Criteria and Related Research:
'Tax-Supported Rating Criteria', dated Aug. 16, 2010.
'U.S. Local Government Tax-Supported Rating Criteria', dated Oct. 08, 2010.

For information on Build America Bonds, visit www.fitchratings.com/BABs.

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria
U.S. Local Government Tax-Supported Rating Criteria