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Ratings

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Summary:

Mecklenburg County, North Carolina; Appropriations; General Obligation

Primary Credit Analyst:
Nora G Wittstruck, New York + (212) 438-8589; nora.wittstruck@spglobal.com

Secondary Contact:
Kaiti Vartholomaios, New York + 1(212) 438 0866; kaiti.vartholomaios@spglobal.com

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Credit Profile		
US$225.0 mil GO sch bnds ser 2021 due 03/01/2041		
Long Term Rating	AAA/Stable	New
Mecklenburg Cnty GO		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to Mecklenburg County, N.C.'s 2021 general obligation (GO) school bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the county's GO debt outstanding and its 'AA+' long-term rating on the county's appropriation-backed obligations outstanding. The outlook is stable.

The series 2021 bonds and GO bonds outstanding are secured by the county's faith and credit, including the levy and collection of ad valorem property taxes that are unlimited as to rate or amount. The county's appropriation-backed obligations are rated one notch lower to account for the annual appropriation risk of lease payments. Bond proceeds will fund capital costs for the county's school facilities as part of the bond referendum passed by voters on Nov. 7, 2017. Following the current sale, the county will have about $1.76 billion of net direct debt outstanding (including capital leases) with about $490.1 million in remaining GO authorization from the 2017 referendum expected to be issued over the next several years.

Credit overview

Despite modest revenue weakness in fiscal 2020, particularly in sales taxes that account for about 14.6% of general fund resources, the county's strong management team quickly implemented expenditure controls at the onset of the pandemic. These efforts led to operations ending with a nearly $130 million positive variance to budget in the general fund (nearly 9%). In addition, the county's receipt of $39.2 million in Coronavirus Aid, Recovery, and Economic Security (CARES) Act funding partly offset its COVID-19-related response costs, with $24.0 million allocated toward county expenditures and the remainder toward supporting food insecurity and vulnerable populations as well as the business community. As a result, the county maintained its very strong flexibility in fiscal 2020 with available reserves (including those in the debt service fund) reaching nearly $522 million when considering assigned and unassigned amounts (nearly 31% of operations). The AAA/Stable rating also reflects our view of Mecklenburg County's economic diversity and expansion that continued during the pandemic and that we expect will remain robust over the long term. Although the county's debt position has improved in recent years and total fixed costs for debt service, pension and other postemployment benefit (OPEB) contributions remain manageable at 14.3% of total governmental expenditures, we expect population growth to lead to additional infrastructure requirements during the outlook period.

The county GO rating is eligible to be higher than the sovereign rating because we believe the county can maintain strong credit characteristics relative to the U.S. sovereign in a stress scenario. Under our criteria "Ratings Above the Sovereign: Corporate and Government Ratings--Methodologies and Assumptions," published Nov. 19, 2013, on RatingsDirect, the county has predominantly locally derived revenue with independent taxing authority and independent treasury management from the federal government.

The rating further reflects the county's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area;
- Strong management, with good financial policies and practices under our financial management assessment methodology;
- Adequate budgetary performance, reflecting the ongoing uncertainty and challenges facing the county in fiscal 2021 despite solid operating results in fiscal 2020;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2020 of 30% of operating expenditures;
- Very strong liquidity, with total government available cash at 60.7% of total governmental fund expenditures and 5.5x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 11.0% of expenditures and net direct debt that is 95.9% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 66.0% of debt scheduled to be retired in 10 years; and
- Very strong institutional framework score.

Environmental, social, and governance factors

We analyzed the county's environmental, social, and governance risks relative to its economy, budgetary outcomes, management, and debt and long-term liability profile, and view them as consistent with those of the sector. However, when compared with the population loss in some areas of the nation, the county's substantial population growth of 17.5% since 2011 exhibits a demographic trend that we believe is a social opportunity, as service costs are spread across a larger base and could help with maintenance of long-term affordability. Furthermore, the county is addressing other community social risks, including disparities in access to education and health services, through certain fiscal commitments in the budget.

Stable Outlook

Downside scenario

We could lower the rating in the unlikely event that the county realized persistent fiscal stress leading to substantial deterioration in reserves and consecutive years of noncompliance with its policies and practices.

Credit Opinion

Very strong economy

We consider the county's economy very strong. Mecklenburg County, with an estimated population of 1.1 million, is located in the Charlotte-Concord-Gastonia metropolitan statistical area, which we consider broad and diverse. The county has a projected per capita effective buying income of 115% of the national level and per capita market value of $164,014. Overall, the county's market value grew by 42.7% over the past year to $185.6 billion in 2020 as a result of a regular revaluation of the tax base.

Mecklenburg County is located in south central North Carolina and is anchored by the City of Charlotte. The regional economy and population center are the largest between Washington, D.C., and Atlanta. As a result, despite a temporary uptick in the county's unemployment rate to 12.8% in April and 13.6% in May, the rate declined to 6.5% in November 2020. Consistent with other cities, the largest job losses in 2020 occurred in the leisure and hospitality sector, with a year-over-year decline of nearly 26,000 jobs, or 39.3%. However, with the county's diverse employment base, including its role as one of the nation's leading financial centers, the county experienced gains in finance and insurance (up 9.2%) and in transportation and warehousing (up 10.7%), bolstering the county's economic strength in the Southeast region. The employment expansion has driven housing demand, including a nearly 11% increase in median sales price calendar-year-to-date through November 2020 when compared with the prior-year period and a decline of the number of days on market to 31 from 37. The region's growth is partly the result of the strategic importance of Charlotte Douglas International Airport to American Airlines Inc. Despite depressed activity in business and leisure travel as a result of the pandemic, the airport remains an important hub once air passenger traffic rebounds.

We believe the county's economy will remain very strong during the outlook period as fiscal 2020 (ended June 30) experienced the highest building permit activity since 2015, resulting in nearly $5.6 billion in construction value (about 70% commercial, 30% residential). New construction complements nearly 6 billion square feet of commercial space under development or renovation, signaling that the county will remain a key economic area for the state and region.

Strong management

We view the county's management as strong, with good financial policies and practices that may not be formally adopted by the governing body in all cases.

Financial management practices include comprehensive budget development processes that include performance-based and service-level considerations. The county typically outperforms its budget. Budget-to-actual performance is monitored through regular reports provided to the governing body, and amendments can be made throughout the year. While a traditional long-term financial forecast is not published and approved by the board, management uses projections and forecasting when developing budgets, and considers long-term costs with capital improvement plan and debt service obligations. The county maintains multiple five-year capital plans that identify funding sources and require board approval. Furthermore, the county maintains a separate deferred maintenance plan and allocates annual amounts toward ensuring completion of projects. A formal investment and banking policy is maintained with monthly reporting of investment earnings and holdings to the governing body. A number of years ago, the county modified its debt policy to strengthen affordability metrics. As a result, the policy requires maintenance of direct debt at 1.75% of assessed value, direct debt per capita of $2,000, and general debt service at 17.00% of operational expenditures. A formally adopted fund balance policy stipulates that the combined total general fund and debt service fund balance will equal 28% of prior-year actual revenue, a benchmark that the county currently adheres to.

Adequate budgetary performance

Our forward-looking view of the county's budgetary performance reflects macroeconomic conditions facing all local governments across the U.S. that could lead to a weaker financial result in fiscal 2021. S&P Global Economics' report "Staying Home for the Holidays," published Dec. 2, 2020, underpins this, stating that the strength of the economic rebound may remain uncertain, particularly with demand-driven revenue sources, until a larger swath of the population is vaccinated later this year. However, we note that the county's budgetary performance is historically strong, including in fiscal 2020, which ended balanced in the operating funds as well as across total governmental funds. Furthermore, we adjust audited results to combine the county's general fund and debt service fund to inform our budgetary performance analysis given that the debt service fund carries a dedicated property tax levy and is considered a major operating fund. In addition, the county's fund balance policy addresses reserves based on the combined funds.

At the onset of the pandemic, the county implemented aggressive cost containment measures to shore up its financial position over the final months of fiscal 2020. Mandatory freezes on nonessential hiring and nonessential services as well as a pause on discretionary spending offset modest revenue deterioration that occurred following implementation of a stay-at-home proclamation restricting nonessential activity. In addition, with the receipt of more than $39 million in CARES Act funding, the county's fiscal 2020 general fund ended with a modest draw on fund balance of $9.8 million following a $75.5 million transfer to capital projects. Despite the small draw for capital pay-as-you-go funding, revenue ended favorably to budget at $3.4 million (0.2%). Although sales taxes collected in the general fund were $7.1 million lower than budget (3.4%), overall revenue performance was positive as a result of strong property tax collections that support 65% of general fund operations. Furthermore, with management's aggressive cost containment measures, expenditures ended about $130 million lower (9%) than budget.

The fiscal 2021 budget totals $1.9 billion, basically flat from the prior-year adopted budget. The county revised its revenue projections for fiscal 2021 and lowered growth to $19.0 million from $46.0 million, mainly by reducing sales tax collections by $8.5 million (3%) and interest earnings by $11.3 million (51%). In addition, the county continued its hiring and spending freezes and shifted three quarters of one cent of the dedicated 2.25-cent debt service fund property tax rate to the general fund. We believe these changes indicate the county's strong budgeting practices and will likely help maintain budgetary balance despite the uncertainty in the economic rebound.

Very strong budgetary flexibility

Mecklenburg County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2020 of 31% of operating expenditures, or nearly $522 million (assigned and unassigned amounts). Despite a modest decline in the general fund balance in fiscal 2020, the debt service fund ended with a $13.3 million contribution to fund balance, which bolstered the combined reserve amount. We believe management's adherence to its fund balance policy, which requires replenishment over two years if it falls to less than 28%, will support the county's very strong flexibility over the long term. Additionally, we believe management is prepared to make budget modifications to ensure reserves remain aligned with the policy.

Very strong liquidity

In our opinion, Mecklenburg County's liquidity is very strong, with total government available cash at 60.7% of total governmental fund expenditures and 5.5x governmental debt service in 2020. In our view, the county has strong access to external liquidity, if necessary, given its regular issuance of debt over the past 20 years. We expect the county will maintain very strong liquidity in the near-to-medium term, based on its long history of stable performance. Mecklenburg eliminated its exposure to variable-rate debt and privately placed debt in 2017, reducing its contingent liquidity risk. As a result, we believe the county's liquidity position will support its credit profile over the outlook period.

Strong debt and contingent liability profile

In our view, Mecklenburg County's debt and contingent liability profile is strong. Total governmental fund debt service is 11.0% of total governmental fund expenditures, and net direct debt is 95.9% of total governmental fund revenue. Overall net debt is low at 2.3% of market value, and approximately 66.0% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

The county manages its capital program with various plans encompassing a specific five-year timeframe. The plan covering fiscal years 2014 to 2018 is nearly complete (sized at $1.06 billion) with all projects closed out in fiscal 2021. The second plan covers fiscal years 2019 to 2023 (sized at $1.75 billion) and is 58% dedicated to Charlotte Mecklenburg schools. The plan ending with fiscal 2023 is funded about 42% with pay-as-you-go funding and reserves, while the remainder is funded with GO bonds authorized but unissued from the 2017 referendum. Finally, the city's dedicated five-year deferred maintenance plan of about $142 million is primarily funded on a pay-as-you-go basis with various reserves and transfers to create a stable annual funding mechanism. Although we anticipate additional debt issuance, we believe the county's sophisticated capital and debt planning will ensure that its debt position remains affordable.

Pension and OPEB liabilities

- We do not view pension and OPEB liabilities as an immediate source of credit pressure for Mecklenburg County, given the modest level of contribution costs totaling 2.7% of total governmental expenditures (1.6% for pensions and about 1.1% for OPEB) in fiscal 2020.
- Furthermore, we believe the largest pension plan's strong funded status, closed amortization, and 7% rate of return could limit contribution volatility as well as escalating cost trajectory.
- In fiscal 2020 the county contributed 105% of its annually determined contribution, which was short of minimum funding progress but equal to static funding, indicating that the county is keeping pace with funding benefit expenditures.

Mecklenburg County participated in the following plans as of June 30, 2020:

- Local Government Employees' Retirement System (LGERS), 90% funded, with a proportional share of the net pension liability equal to $118.4 million
- Law Enforcement Officers' Special Separation Allowance, with a net pension liability of $19.4 million, which it funds on a pay-as-you-go basis
- Register of Deeds' Supplemental Pension Fund, with a net pension asset of $1.3 million with statutory contributions

set by the North Carolina General Assembly. Contributions to the plan are de minimis relative to the county's operations.

The county provides OPEBs through a single-employer, defined-benefit plan to all retirees who have at least 10 years of service and were employed on or before July 1, 2010. Although it funds benefits on a pay-as-you-go basis, the county board of commissioners has the authority to amend the plan and retiree contribution rates. The county's OPEB contribution in fiscal 2020 was approximately $19.5 million (of which $18.1 million was relative to the actuarily determined contribution of $43.3 million) with a net liability of $514.9 million.

Very strong institutional framework

The institutional framework score for North Carolina counties is very strong.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 2020 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of February 5, 2021)		
Mecklenburg Cnty certs of part (var rate)		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty ltd oblig		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty ltd oblig bnds		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty taxable ltd oblig bnds		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty COPs - 2008B		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty COPs - 2009A		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty GO pub imp bnds		
Long Term Rating	AAA/Stable	Affirmed
Mecklenburg Cnty APPROP		
Long Term Rating	AA+/Stable	Affirmed
Mecklenburg Cnty APPROP		
Long Term Rating	AA+/Stable	Affirmed

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.