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## Summary:

# Granite Shoals, Texas; General Obligation

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## Table Of Contents

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Rationale

Outlook

Related Research

## Summary:

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### Credit Profile

Granite Shoals GO

*Long Term Rating*

AA-/Stable

Upgraded

## Rationale

S&P Global Ratings raised its rating on Granite Shoals, Texas' general obligation (GO) debt two notches to 'AA-' from 'A'. At the same time, S&P Global Ratings removed the rating from CreditWatch with developing implications, where it was placed Dec. 18, 2018. The outlook is stable.

The upgrade is based on the improvement in Granite Shoals' economic profile from weak to adequate. The city's wealth and income indicators have improved; market value has increased, due in part to an annexation during 2017; and residential development has continued. The improvement in the city's budgetary flexibility to a relatively low fund balance of \$810,000 or very strong 28% of expenditures in fiscal 2017 from a nominally low \$232,000 or a strong 7% in fiscal 2016 further supports the upgrade. Based on projections for 2018 and 2019 budgets, we anticipate at least stable financial results during the next two years.

S&P Global Ratings placed the rating on CreditWatch developing because the city only partially supplied the information S&P Global Ratings requested. We have removed the CreditWatch placement and assigned a stable outlook because we now have information to confirm the city's local economic health, debt plans, financial estimates and projections for fiscal years 2018 and 2019, and we have completed a thorough review of existing financial policies and practices due to the finance director's departure in August 2018.

The certificates are payable from a limited ad valorem tax levied on all taxable property within the city and surplus net revenue, not to exceed \$1,000, from the city's utility system. Granite Shoals' current property tax rate is 59.60 cents per \$100 of assessed value (AV), well below the maximum allowable rate of \$1.50 per \$100 of AV. We do not make a rating distinction between the city's unlimited and limited tax pledge because we factor these limitations and the fungibility of resources into our overall assessment of the city's general creditworthiness, and the levy is not on a narrower tax base.

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

- Adequate economy, with market value per capita of \$113,985 and projected per capita effective buying income at 70.2% of the national level;
- 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 2017;

- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 28% of operating expenditures;
- Very strong liquidity, with total government available cash at 56.2% of total governmental fund expenditures and 3.4x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability profile, with debt service carrying charges at 16.7% of expenditures and net direct debt that is 179.8% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 82.3% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

### **Adequate economy**

We consider Granite Shoals' economy adequate. The city, with an estimated population of 5,194, is located in Burnet County. The city has a projected per capita effective buying income of 70.2% of the national level and per capita market value of \$113,985. Overall, the city's market value grew by 20.7% over the past year to \$592.0 million in 2019. The county unemployment rate was 3.2% in 2017.

The roughly 5.7-square-mile city is about 60 miles northwest of Austin in Texas' Hill Country region. Granite Shoals is located along the shores of Lake LBJ, one of seven Texas Highland Lakes. The region contains numerous waterways and several golf courses within a 20-mile radius. Wealth and income reflect the city's primarily residential and limited economy.

Building activity in the city has increased during the past three years. The city voluntarily annexed Beaver Island and Web Isle during 2017, which is contributing to the increase in taxable AV of 20% for 2018. Officials expect economic growth to continue, with AV projected to increase, although at a more moderate pace than in 2018.

### **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 management team has had turnover in the city manager and finance director positions within the past year. The city manager position has been filled and the city is seeking candidates for the finance position. The current management team does not intend to materially change the practices and policies in place.

Key practices include management's use of conservative revenue and expenditure projections that take into account historical data and information from outside sources, where applicable. Management provides quarterly reports on budget-to-actual financial results to the city council. Granite Shoals has a 10-year capital improvement plan (CIP) that it updates annually during the budget process. The CIP identifies projects, costs, and funding sources.

The city employs an annually reviewed investment policy that mirrors the Texas Public Funds Investment Act. Management provides quarterly investment reports to the city council that detail investment holdings and returns. The city's basic debt management policy limits debt to no more than 10% of AV, and its formal policy maintains at least 25% of general fund expenditures in reserve. While the city did not reach its fund balance target during fiscal years 2001-2016, reserves became compliant in fiscal 2017 and are expected to remain in compliance during the next two

years. Granite Shoals lacks a formal long-term financial forecast.

### **Strong budgetary performance**

Granite Shoals' budgetary performance is strong, in our opinion. The city had operating surpluses of 8.1% of expenditures in the general fund and of 17.7% across all governmental funds in fiscal 2017. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from 2017 results in the near term.

After adjustments for recurring transfers into the general fund from utility funds for administrative reimbursements, the city's fiscal 2017 budget performance is strong. The city's general fund primary revenues are composed of property taxes (54%), charges for services (14%), and intergovernmental revenues (11%). The fiscal 2017 budget did trend as budgeted, with stronger property tax revenue growth due to annexation of properties.

For fiscal 2018, management has estimated a \$200,000 net operating surplus. Across governmental funds, the city spent a portion of its \$3 million private placement during the fiscal year-end; \$350,000 remains unspent. The fiscal 2019 budget is balanced; however, we anticipate another operating surplus similar to that in fiscal 2018. Therefore, we believe Granite Shoals will maintain at least strong budgetary performance.

### **Very strong budgetary flexibility**

Granite Shoals' budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 28% of operating expenditures, or \$810,000.

The city's total available fund balance improved to a very strong level in fiscal 2018 from a nominally low, yet adequate level in 2015. The city has continued to build up reserves from a negative position in fiscal 2013 and achieved its formal fund balance reserve policy in 2017. Based on fiscal 2018 unaudited estimates and 2019 budget, we anticipate reserves will remain very strong.

### **Very strong liquidity**

In our opinion, Granite Shoals' liquidity is very strong, with total government available cash at 56.2% of total governmental fund expenditures and 3.4x governmental debt service in 2017. In our view, the city has strong access to external liquidity if necessary.

Granite Shoals' three privately placed loans amount to about \$6.5 million or 92% of the city's net direct debt. The series 2010 private placement with Texas Independent Bank has a variable interest rate and represents just 4% of total direct debt. The minimum interest rate allowed on the certificates is 4.25% and the maximum rate is 6%; the interest rate resets in August 2020 and again in August 2025. Should the interest rate be reset to the maximum allowed rate, we believe the city has sufficient liquidity to meet the required debt payments. In addition, we do not believe the city's private placements have permissive remedies that could result in a material reduction in its very strong liquidity position in the next two years.

All of Granite Shoals' investments comply with Texas statutes and the city's internal investment policy. At fiscal year-end 2017, investments included certificates of deposit and the TexPool Investment Pool, neither of which we consider aggressive.

### **Adequate debt and contingent liability profile**

In our view, Granite Shoals' debt and contingent liability profile is adequate. Total governmental fund debt service is 16.7% of total governmental fund expenditures, and net direct debt is 179.8% of total governmental fund revenue. Overall net debt is low at 2.7% of market value, and approximately 82.3% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

The city does not have any tax-secured additional debt plans but it is in the early phases of planning for a potential revenue-backed bond to finance water system improvements.

The city has \$510,000 outstanding in privately placed debt with a variable rate, which is reset every five years. The most recent reset occurred in August 2015 at an interest rate of 4.25%; the next resets are scheduled for August 2020 and August 2025. The minimum interest rate allowed is 4.25% and the maximum rate is 6.0%. The city has determined that if the rate were to be reset to the maximum of 6% in 2020, total debt payment requirements for fiscal 2021 would increase only about \$7,500. Debt payment requirements for fiscal 2022 and beyond would fluctuate by no more than \$3,500 per fiscal year until the obligations mature in fiscal 2027. Based on this, we do not believe that the obligations pose an interest rate risk.

Granite Shoals' combined required pension and actual other postemployment benefits (OPEB) contributions totaled 2.3% of total governmental fund expenditures in 2017. The city made its full annual required pension contribution in 2017.

The city participates in the Texas Municipal Retirement System (TMRS), which is administered by the State of Texas. Granite Shoals' required pension contribution is its actuarially determined contribution (ADC), which is calculated at the state level. Using updated reporting standards in accordance with Governmental Accounting Standards Board Statement No. 67, the city's net pension liability was measured as of Dec. 31, 2017, and was \$1.3 million. The TMRS plan maintained a funded level of 90%, down from 97% reported in 2015, using the plan's fiduciary net position as a percent of the total pension liability. The pension plan uses a 6.75% discount rate, which we view as reasonable. TMRS calculates the ADC using a level percent of payroll amortization, assuming 3.5%-10.5% annual growth, which adds risk given that contributions are deferred with the idea that growth will enhance affordability. The city also provides OPEB through participation in the TMRS Supplemental Death Benefits Fund. We do not expect costs to rise substantially over the near term.

### **Strong institutional framework**

The institutional framework score for Texas municipalities is strong.

## **Outlook**

The stable outlook reflects our expectation that the rating will not change over the two-year outlook horizon. We expect Granite Shoals will likely continue to make strides in maintaining its very strong budgetary flexibility and strong budgetary performance. We believe strong management conditions will continue to support the city's financial position.

### **Upside scenario**

We could raise the rating if the city can build and sustain its available fund balance at a very strong level in compliance with its fund balance policy, supported by ongoing strong budgetary performance, and sufficient contingency reserves comparable with those of higher-rated peers.

### **Downside scenario**

We could lower the rating if the city's budgetary performance or reserve position were to materially deteriorate.

## **Related Research**

- 2018 Update Of Institutional Framework For U.S. Local Governments

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](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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