

RatingsDirect®

Summary:

Palm Coast, Florida; Water/Sewer

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Summary:

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Credit Profile

Palm Coast Util Sys

Unenhanced Rating

A+(SPUR)/Stable

Affirmed

Rationale

S&P Global Ratings affirmed its 'A+' rating on Palm Coast, Fla.'s utility system revenue secured bonds. The outlook is stable.

The affirmation incorporates our analysis of documents related to the city's series 2016 utility system refunding revenue note. The note was directly placed, and is on parity with the city's other outstanding utility system revenue bonds. There are no additional events of default or remedies associated specifically with the direct purchase. The notes were issued to refund existing utility bonds.

The rating reflects the system's strong enterprise and very strong financial risk profiles. The strong enterprise risk profile reflects our view of the system's:

- Service area's participation in the Daytona-Daytona Beach-Ormond Beach metropolitan statistical area (MSA);
- Rates that we generally view as affordable when benchmarking against Palm Coast's median household effective buying income (MHHEBI) and Flagler County's poverty rates; and
- Good-to-strong operational management practices and policies, in our view.

The very strong financial risk profile reflects our view of the system's:

- Financial metrics that include debt service coverage (DSC) of no less than about 1.5x over the prior three completed fiscal years and a days' cash equivalent no less than 150 days operating expenses; and
- Generally good financial management practices and policies that pertain to the utility.

Palm Coast is in eastern Flagler County, straddling Interstate 95 and extending almost to the Intracoastal Waterway. The city was incorporated in 1999 and has been one of the more rapidly growing cities in Florida. Palm Coast's economy has weakened considerably since 2008, with a sharp decline of 45% in assessed value (AV) from 2008-2015, although AV has remained relatively flat since 2013.

The utility services the city and some customers outside the city limits. We understand the majority of the existing customer base is residential with no specific customer concentration. Both utility systems serve about 34,000 equivalent residential units. The 10 leading customers account for less than 2% of revenues.

The city's 2016 budget indicates total utility capital needs of \$67 million from 2016-2020. About \$30 million of this, funded with a state revolving fund loan, is related to a second sewer treatment plant that management expects to go online by the end of 2017. It is our understanding that its initial capacity will be 2 million gallons per day (mgd),

expandable to 6 mgd.

Enterprise and financial risk profile details

We benchmark our analysis of market position, which is an input to the enterprise risk profile, to both MHHEBI and the county poverty rate. MHHEBI for Palm Coast is 92% of the national average. Although monthly equivalent water and sewer rates are around \$80 for 6,000 gallons of use, when considering that the county's poverty rate is about 15%, our view of the market position is somewhat more negative compared to a situation where a utility has both low nominal rates and a lower poverty rate. Our methodology measures affordability for not only the median household, but also takes into account sensitivity to rate affordability based on the county poverty rate. The city has recently approved a multiyear rate increase that would adjust rates by inflation.

All of the other components of the very strong enterprise risk score reflect the participation in an MSA economy, as well as operational management policies that indicate to us the existence of generally good-to-strong internal governance and controls and asset management policies.

The strong financial risk score is supported by the moderately sized liquidity position and its DSC of no less than about 1.5x. At the fiscal year ended Sept. 30, 2015, unrestricted cash and investments totaled just under \$13 million, which equated to 303 days' cash. Based on our calculations, net operating revenues have provided coverage of total annual debt service from 2013-2015 ranging from 1.5x to 2.2x, and it was 1.9x in 2015.

Also supporting the financial risk profile is the "good" financial management assessment pertaining to the utility system, indicating that, in our view, financial practices are well embedded and likely sustainable. Examples include the existence of long-term capital planning, formal debt and investment policies, and consistent communication between management and elected officials regarding financial performance.

Outlook

The stable outlook reflects our expectation that Palm Coast should be able to attain financial metrics consistent with historical trends since it has approved multiyear rate increases.

Upside scenario

Given the additional capital plans and debt being issued to fund the additional sewer treatment plant facility, we do not expect to raise the rating over the two-year outlook horizon. We would want to wait until the project is completed to see exactly how the financial situation ends up after additional fixed debt service costs are layered in and additional capital costs continue to be funded from funds on hand.

Downside scenario

Additional debt and capital expenses that would place downward pressure on financial ratios would also likely place downward pressure on the rating or outlook.

Related Criteria And Research

Related Criteria

- USPF Criteria: Rating Methodology And Assumptions For U.S. Municipal Waterworks And Sanitary Sewer Utility Revenue Bonds, Jan. 19, 2016
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

Ratings Detail (As Of June 17, 2016)

Palm Coast imp & rfdg rev bnds		
<i>Long Term Rating</i>	A+/Stable	Affirmed
Palm Coast imp & rfdg (MAC)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Palm Coast util sys (AGM)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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