FITCH RATES WICOMICO COUNTY (MD)'S $20.3MM GOS 'AA'; OUTLOOK STABLE

Fitch Ratings-New York-28 October 2016: Fitch Ratings has assigned a rating of 'AA' to the following general obligation (GO) bonds of Wicomico County, Maryland:

--$20.3 million general obligation public improvement bonds of 2016.

The bonds are expected to be sold competitively on November 1. Proceeds will be used to finance projects for the Wicomico County Board of Education, the Board of Elections and the County's Emergency Services.

In addition, Fitch has affirmed the county's Issuer Default Rating (IDR) and approximately $106.3 million of outstanding GO bonds at 'AA'.

SECURITY

The bonds are backed by the full faith, credit, and taxing power of the county, but are subject to tax limitation constraints set forth in the county's charter. Revenues derived from taxes on properties shall not increase, compared with the previous year, by more than 2% or by the consumer price index for all urban consumers, whichever is less. New construction and funding the local board of education's budget are not subject to the charter limitations.

KEY RATING DRIVERS

The 'AA' IDR reflects the county's sound level of expenditure flexibility, expectations for limited revenue growth absent tax policy changes, and exceptionally strong gap-closing capacity.

Economic Resource Base
Centrally located on the Delmarva Peninsula, Wicomico County is at the intersection of U.S. Routes 13 and 50, the two major trans-peninsular highways. The County is 115 miles from Washington, D.C. and Baltimore. With a 2015 population of 102,370 the county's population has increased by an average annual rate of less than 1% since 2010.

Revenue Framework: 'aa' factor assessment
Revenues have been rising at a pace below both the rates of inflation and U.S. GDP growth which is due to a combination of the county's limitation on property tax revenue growth and recent sizable AV declines. The county's independent legal ability to raise revenues is strong despite a limitation on real property tax revenues by county charter.

Expenditure Framework: 'aa' factor assessment
Education drives the county's spending needs and any reduction would require approval from the state. As such, the county's ability to make spending cuts when needed is somewhat limited. Carrying costs related to debt and pensions are moderate.

Long-Term Liability Burden: 'aaa' factor assessment
The county's liability burden is low and debt amortization is rapid.

Operating Performance: 'aaa' factor assessment

The 'aaa' operating performance assessment reflects the district's ample gap closing capacity relative to Fitch's expectations of revenue sensitivity to economic cycles, with a solid level of spending flexibility supplemented by a large reserve cushion.

RATING SENSITIVITIES

IMPROVEMENT IN REVENUE GROWTH: The rating assumes continued slow revenue growth. Sustained improvement in growth prospects could put positive pressure on the rating.

CREDIT PROFILE

The local economy has a deep history of poultry production and manufacturing and most of its land area is undeveloped (39%) or designated as agricultural (31%). Perdue is headquartered in the county, employs about 1,600 and is the third largest private employer in the county and the fifth largest taxpayer. Education and health care are also important economic sectors. Salisbury University employs approximately 1,800 and Wor-Wic Community College 700 or together about 5% of the labor force. Peninsula Regional Medical Center, the county's largest employer (2,900 employees) and a full-service hospital, is one of the primary care facilities for Maryland's Eastern Shore. The county's unemployment rate was above the national average through the great recession, and remains above the U.S. level but continues to decline.

Revenue Framework
The county relies on a combination of property and income tax revenues, which equates to 48% and 36% of general fund revenues respectively in fiscal 2015.

The county's general fund revenue growth has trended below the rate of inflation on a compound average annual (CAGR) basis over the 10 years ended in fiscal 2014. The county's assessed value (AV) CAGR for the same period was above the rate of GDP growth, but more recent history includes five consecutive years of declines. More recent performance has shown minimal growth in income tax revenues had been sluggish but improvement in the employment base has led to very recent robust growth; evidence of a trend of growth could affect Fitch's view of overall revenue growth prospects.

Fitch considers the county's ability to increase revenues to be high. A charter-imposed revenue limit, which was approved by county voters and effective in fiscal-year (FY) 2002, constrains the county's ability to raise property tax revenues annually to the lesser of the Consumer Price Index (CPI) or 2%, excluding revenue from new construction. Credit concerns about this constraint are somewhat offset by the county's ability to increase property tax revenue above the cap for educational operating purposes with county council approval. Otherwise the tax revenue cap can only be exceeded or changed by voter referendum. In addition, the county currently levies income taxes at the maximum rate of 3.2%. The county gains additional flexibility from the ability to increase fines and fees, increase the recordation tax rate and impose a transfer tax, which are not subject to a cap.

Expenditure Framework
The county's largest expenditure is education at roughly 38% of general fund expenditures, followed by public safety at 12%.

Fitch expects the natural pace of spending growth to remain below or in line with revenue growth as modest population growth should result in limited increases in expenditure demands.

Moderately low carrying costs and adequate flexibility to manage labor-related costs allow the county sufficient spending flexibility. According to the state maintenance of effort mandate, education spending cannot decline from year to year without approval from the state. In response to declining general fund revenues during the recession, the county was granted approval to reduce spending on education fiscal years 2010-2012.

The County Council has adopted legislation permitting collective bargaining with deputy sheriffs (approximately 10% of county staff) and includes for binding arbitration. A collective bargaining agreement was executed for July 1, 2016 through June 30, 2021. The majority of county employees are not unionized providing substantial control over workforce costs.

The county's fixed cost burden is affordable, with carrying costs for debt, pensions (including the normal cost for teachers' pensions), and other post-employment benefits (OPEB) equaling 14% of fiscal 2015 governmental expenditures, with debt service accounting for 8%.

Long-Term Liability Burden
Overall net debt plus the county's unfunded pension liability equals approximately 4% of personal income. Debt amortization is rapid with 65% of principal retired in 10 years. The county's $118.5 million capital improvement plan does not include any approved additional debt plans following the current issuance. As such, overall debt is expected to remain low.

The county provides a single employer retirement system which has historically been well funded. The plan was 82% funded as of June 30, 2016. Funded levels are an estimated 80% using Fitch's 7% investment rate of return. The county did reduce the interest rate of return to 7.25% from 7.75% during the 2016 valuation process, which is reflected in the increase in the net pension liability. The county has over-funded the actuarially required contribution (ARC) for four years. The fiscal 2016 contribution of $1.4 million was $534,326 over the ARC. Management will review on a budget to budget basis the contribution in excess of the ARC.

The county has overfunded its OPEB actuarial contributions in fiscals 2013 -- 2016 including a fiscal 2016 contribution of $5.4 million which represented 161% of the ARC. The county's OPEB liability is 40% funded as of July 1, 2016.

Operating Performance
Given Fitch's assessment of the county's inherent budget flexibility as superior, with solid control over revenues and moderate spending flexibility, Fitch expects the county to manage through economic downturns while maintaining a high level of fundamental financial flexibility. Reserves are expected to remain well above the policy floor of 8% and closer to the 35% target -- a level of financial cushion far higher than is sufficient for a 'aaa' assessment of financial resilience. The unrestricted general fund balance of $48.5 million in fiscal 2015 was a high 38.4% of spending.

The county proved its financial resilience and strong budget management through the most recent recession by suspending salary increases, suspending pension and OPEB contributions, reducing spending on education, freezing capital spending, reducing staff through attrition and offering a retirement incentive among other tactics. Fitch expects the county to make similar operational changes as needed during an economic downturn.

Preliminary fiscal 2016 year-end general fund operating results show income tax revenues exceeding budget by $7.4 million and expenses $6.2 million under budget; fund balance is expected to increase by $8.8 million.

The fiscal 2017 budget is a 5% ($5.9 million) increase over fiscal 2016 and includes an approximately $6 million fund balance appropriation while maintaining the real property tax rate. Some of the budget increases included a 3% COLA for county employees, a $3.5 million one-time contribution to pay-go, and $626,648 in increased board of education funding. Based on the county's multi-year financial forecast and financial history, Fitch expects operations to be balanced and reserve levels to remain within the reserve policy, which should keep gap-closing capacity exceptionally strong.

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In addition to the sources of information identified in the applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Applicable Criteria
U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)
https://www.fitchratings.com/site/re/879478

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