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Ratings

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Summary:

Kalkaska County, Michigan; General Obligation

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Credit Profile		
Kalkaska Cnty GO bnds		
Long Term Rating	AA-/Stable	Affirmed

Rationale

S&P Global Ratings affirmed its 'AA-' rating, with a stable outlook, on Kalkaska County, Mich.'s general obligation (GO) debt.

The county's full-faith-and-credit pledge secures the bonds.

The rating reflects our opinion of the county's:

- Adequate economy, with market value per capita of $103,244 and projected per capita effective buying income at 75% of the national level;
- Adequate management, with standard financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with operating results we expect could deteriorate in the near term relative to fiscal 2016, which closed with slight operating surpluses in the general fund and at the total-governmental-fund level;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2016 of 112% of operating expenditures;
- Very strong liquidity;
- Very strong debt-and-contingent-liability position, with no debt requiring governmental fund support, as well as low overall net debt at less than 3% of market value and rapid amortization, with all debt scheduled to be retired within 10 years; and
- Strong institutional framework score.

Adequate economy

We consider Kalkaska County's economy adequate. The county has an estimated population of 17,554. The county has a projected per capita effective buying income of 75% of the national level and per capita market value of $103,244. Overall, market value grew by 4% over the past year to $1.8 billion in fiscal 2016. The county unemployment rate was 6.9% in 2016.

Kalkaska County, in northwest Michigan's Lower Peninsula, has a stable local economy, primarily centered on manufacturing, energy, and service-related companies. Taxable value (TV) increased by 0.9% in fiscal 2016 to $739 million. The county's property tax base is diverse with the 10 leading taxpayers accounting for 13.9% of TV. Leading taxpayers include several energy companies such as ANR Pipeline Co., Blue Lake Gas, and Great Lakes Energy. The county, 25 miles from Traverse City, is a regional hub in northwest Michigan known for year-round tourism that includes kayaking, hiking trails, and golf courses. Agricultural business in the area includes growing and processing cherries, grapes, and other fruit crops. The county also includes forestry and state parks.

Adequate management

We consider Kalkaska County's financial management practices standard under our FMA methodology, indicating the finance department maintains adequate policies in some, but not all, key areas.

The county uses historical data to build revenue and expenditure assumptions for the budget. Management currently updates the county board on budget-to-actual performance monthly, and it can make amendments. Management makes monthly reports to the board on investment performance, and its policy follows state guidelines. The county has a formal reserve policy to maintain, at least, 20% of expenditures, which it is currently meeting. The county does not have a debt-management policy or long-term financial or capital plans.

Adequate budgetary performance

Kalkaska County's budgetary performance is adequate, in our opinion. The county had slight operating surpluses of 0.7% of expenditures in the general fund and 1.1% of expenditures across all governmental funds in fiscal 2016. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from fiscal 2016 results in the near term.

For unaudited fiscal 2017, management expects an operating deficit in the general fund of $390,000. Management attributes budgetary pressure primarily to increased childcare costs for state-ward foster children, approximately $300,000 of the deficit. We expect fiscal years 2018 and 2019 results will likely parallel fiscal 2017 performance due to budgetary pressure involving building improvements, technology, and retirement costs.

Based on previous audited results, from fiscal years 2012-2016, the county had five consecutive surpluses. The strong previous financial performance allowed the county to improve reserves. However, revenue growth has been modest while expenditures continue to increase. In audited fiscal 2016, the county had a general fund surplus of approximately $120,000--narrower than the general fund surpluses of $495,000 and $405,000 in fiscal years 2015 and 2014, respectively. We expect fiscal performance to remain pressured; however, overall, we believe the county will likely remain stable due to the flexibility of very strong reserves.

Very strong budgetary flexibility

Kalkaska County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 112% of operating expenditures, or $7.4 million. We expect available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor. Available fund balance includes $2.3 million (34.1% of expenditures) in the general fund.

Reserves increased to $2.3 million in fiscal 2016 from $698,000 in fiscal 2012 due to surpluses during audited fiscal years 2012-2016.

Additional flexibility is available with the county's state-shared revenue, which, in fiscal 2016, totaled $337,989, coupled with additional reserves in its delinquent-tax revolving fund, which held $5.1 million (of which $3.8 million is readily available in cash or cash equivalents) at fiscal year-end 2016.

Very strong liquidity

In our opinion, Kalkaska County's liquidity is very strong, with total government available cash at 104.7% of total-governmental-fund expenditures in fiscal 2016. In our view, the county has satisfactory access to external liquidity if necessary.

The county does not have any exposure to contingent-liquidity risks since it has not entered into any direct-purchase or privately placed debt. In our view, the county has strong access to external liquidity; we expect that access to continue.

Very strong debt-and-contingent-liability profile

In our view, Kalkaska County's debt-and-contingent-liability profile is very strong. Kalkaska County does not have any direct debt outstanding that requires governmental fund support. Overall net debt is low at 1% of market value and all direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

The series 2010 refunding bonds, secured by the county's full-faith-and-credit pledge, originally issued in 1998 to construct an ice arena, are the county's only debt outstanding. The county has $1.47 million of total debt outstanding, which officials expect to retire through rapid amortization in April 2020.

The county does not have any debt service paid from the total-governmental-fund level since the ice arena Sportsplex is an enterprise fund, supported by an electorate-approved millage. Debt amortization is rapid with officials planning to retire 100% of principal over 10 years. The county does not currently have any definitive plans to issue additional debt over the two-year outlook window.

Kalkaska County's combined required pension and actual other-postemployment-benefit (OPEB) contribution totaled 6.4% of total-governmental-fund expenditures in fiscal 2016. Of that amount, 5.8% represented required contributions to pension obligations and 0.6% represented OPEB payments. The county made its full annual required pension contribution in fiscal 2016.

The county participates in the Michigan Municipal Employees' Retirement System (MERS), an agent multiemployer plan administered by the MERS Retirement Board for its employees' pension plans. There were 78 inactive plan members or beneficiaries currently receiving benefits as of the last valuation on Dec. 31, 2015, and 25 inactive employees entitled to receive, but not yet receiving, benefits, as well as 104 active employees. The county has continued to make its required annual contributions for the past three fiscal years. In addition, the county has closed certain divisions within the defined-benefit plan to new hires.

The county's total pension liability increased in fiscal 2016 based on the actuarial date of Dec. 31, 2015, which put the net pension liability in the MERS at $6.6 million, or a 68.5% funded ratio, down from 71.7% in fiscal 2015. Part of the assumptions include the lowering of the assumed annual rate of return, net of all expenses, to 7.75% from 8%; asset smoothing changed to five years from 10 years. We expect the county to manage higher pension costs effectively due to the changes of actuarial assumptions by the MERS board.

The county employment agreement provides for certain OPEB health-care coverage. The county contributes to the plans on a pay-as-you-go basis; it contributed $54,802 in fiscal 2016.

Strong institutional framework

The institutional framework score for Michigan counties with a population greater than 4,000 is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion that the county has strong liquidity and reserves with the flexibility to handle expenditure increases over the two-year outlook period.

Downside scenario

If budgetary performance or reserves were to weaken to levels we no longer consider commensurate with county peers, we could lower the rating.

Upside scenario

If economic indicators, such as per capita effective buying income, were to improve significantly to levels we consider commensurate with higher-rated peers, coupled with improved financial performance, we could raise the rating further.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- 2017 Update Of Institutional Framework For U.S. Local Governments