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Ratings

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Summary:

St Mary's County, Maryland; General Obligation

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Credit Profile		
US$30.0 mil GO cons pub imp bnds ser 2022 due 08/01/2042		
Long Term Rating	AA+/Stable	New
St Marys Cnty		
Long Term Rating	AA+/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AA+' rating to St. Mary's County, Md.'s, series 2022 general obligation (GO) consolidated public improvement bonds, totaling $30 million. At the same time, S&P Global Ratings affirmed its 'AA+' rating on the county's existing GO debt. The outlook is stable.

The bonds are a GO of the county, secured by its full-faith-and-credit pledge. Proceeds from this issue will fund various general government and school capital projects.

Credit overview

The rating reflects the county's strong financial position following years of balanced operating results, supported by a durable local economy that benefits from its exurban access to employment markets surrounding Washington D.C., as well as from a strong management team that maintains conservative budgeting and formalized financial policies. The county managed well through the pandemic, continuing to grow available general fund reserves through fiscals 2020 and 2021, and we understand that it is on track to end fiscal 2022 with another strong year. We believe that the county's employment and income tax base will remain solid, in part due to the Pax River Naval Air Base within its borders, as well as to a stable health care and education base. St. Mary's County has a history of managing its operating expenses well. In addition, it maintains some financial flexibility based on its ability to increase its property tax rate as well as on an income tax rate that is slightly below the state maximum. Given this flexibility and strong economic fundamentals, we believe that the county will maintain strong financial operations.

In our opinion, the rating reflects the county's:

- Stable, durable local economy with average wealth and income indicators and consistent growth;
- Formalized financial policies and practice underpinning its strong financial performance;
- Low overall net debt with manageable capital improvement needs and retirement costs; and
- Very strong institutional framework score.

Environmental, social, and governance

St. Mary's County's location along the Potomac and Patuxent rivers and Chesapeake Bay exposes it to coastal and inland flooding, sea-level rise, and severe storms. We note that the county maintains an array of formalized policies and plans to help mitigate these risks, including:

- An adopted multi-jurisdictional hazard mitigation plan, which was approved by the Maryland Department of Emergency Management and the Federal Emergency Management Administration in 2017 and incorporates climate, weather, and disaster planning;
- An Emergency Operations Plan, approved by county commissioners in 2018 and updated annually; and
- A Nuisance Flooding Plan, adopted in October 2020.

In addition, the county has taken steps to assess its critical infrastructure for vulnerabilities to climate change. We view the county's strong oversight and comprehensive risk management strategies relating to the environment as a strength compared to those of peers.

We view its social and governance risks as being generally in line with those of peers. We have spoken with officials regarding cyber security and consider management conversant in the relevant risks and proactive in managing them.

Stable Outlook

Upside scenario

If St. Mary's County were to experience material improvement in its economic metrics and maintain its positive financial operations, while holding all other factor scores constant, we could raise the rating.

Downside scenario

Although in our opinion it is unlikely, if the county were to experience significant fiscal pressures and reserves were used to bridge any imbalances over a prolonged period, we could lower the rating.

Credit Opinion

Stable, durable local economy with average wealth and income indicators and consistent growth

St. Mary's County, with an estimated population of 114,568, is located on a peninsula in southern Maryland and bounded by the Patuxent River, Chesapeake Bay, and the Potomac River. Leonardtown is the county seat and sole overlapping municipality in the county. Although St. Mary's County is not considered a part of the Washington D.C. metropolitan statistical area (MSA), its northern portion is about 40 miles southeast of the capital and residents have direct access to employment opportunities throughout the county and the D.C. MSA. The Naval Air Station Patuxent River (Pax River) is the county's largest employer and anchors the area economy. Pax River is headquarters for the Naval Air Warfare Center Aircraft Division and Naval Air Systems Command, and more than 50 other tenant commands. The military installation employs about 20,200 people and continues to foster growth, particularly in the form of additional defense, engineering, and technology jobs. In that way, it also boosts talent attraction and training. In addition, it hosts more than 50 different tenants, which we believe increases resilience to policy or military funding changes.

Nondefense industry-related economic development continues at a modest pace, particularly in technology-related and retail developments. The county's health care and higher education component also remains stable, as it is home to St. Mary's Hospital, the College of Southern Maryland, and St. Mary's College. There is no concentration in the tax base, with leading taxpayers accounting for less than 4.0% of total assessed value (AV). Management reports that the housing market remains hot and that residential developments continue to sell quickly.

Historically, the county's unemployment rate has been below state and national averages, and it was not materially affected by the pandemic. County unemployment averaged just 4.5% in 2021, well below state and national levels. The unemployment rate stands at just 3.0% as of April 2022.

Formalized financial policies and practice underpin the county's strong financial performance

Highlights of the county's comprehensive financial policies and practices include:

- Use of historical trend analysis for budget preparation, including review of three to four years of data for both revenues and expenditures;
- Budget-to-actuals monitored monthly, with reports provided to the board monthly from all eight departments;
- Annual adoption of a five-year formal long-term financial plan with detailed anticipated expenditure and revenue trends;
- Maintenance of a six-year rolling capital improvement plan (CIP) that identifies all projects and funding sources;
- Formal investment policy, with investments and performance monitored monthly through reports provided to the board;
- Formal debt management policy that requires total debt not to exceed 2.15% of AV or debt service expenditures above 10% of the general fund budget; and
- Formal reserve policy requiring a minimum 15% of general fund revenues, consisting of the bond rating fund (6% of revenues), the rainy day fund, and the unassigned general fund. In addition, use of a make-up provision requiring replenishment of reserves over one to three years.

History of balanced financial operations and strong performance, consistently outperforming budget

St. Mary's County's maintains a history of sound financial management and strong budgetary performance, characterized by conservative budgeting, strong revenue growth, and consistent positive variances relative to budget.

The county increased its fund balance in fiscal 2021 by a substantial $22.4 million, reflecting conservative revenue estimation for the year, with actual revenues coming in well above budget. Income taxes were especially strong, exceeding expectations by $20.6 million. Property tax collections were also strong, and unaffected by the pandemic. As a result, the available general fund balance increased to $86 million, equal to 32.8% of operating expenses.

The fiscal 2022 general fund budget totaled $289 million, a 14% increase relative to the prior year, including the use of $10.9 million of fund balance reserves for one-time purposes. Although the income tax rate was reduced slightly to 3.1% from 3.17%, management budgeted for an 11.8% increase in income tax revenue for the year. Property tax revenues were expected to increase by 3.7% for the year with an unchanged tax rate of 84.78 cents per $100 of AV. Expense increases were driven by increased public safety and education costs. We understand that the county's revenues and expenses are tracking well relative to the budget, and that in particular, property and income tax revenue receipts remain very strong. We also understand that management estimates being able to end the year with an unassigned fund balance well above its 15% policy level and trend.

The county's fiscal 2023 budget includes a 4.0% increase to property tax revenues and a 6.8% increase to income taxes, despite another slight reduction in the income tax rate to 3.0%. On the expenses side, increases to the budget are driven largely by increases for school spending and salary increases as well as by the use of $25 million in pay-go capital spending, which is larger than in previous years given the very strong growth in reserves leading up to fiscal 2023. Nonetheless, given the county's history of conservative budgeting and sizeable positive revenue and expense variances, we expect its performance to remain strong. In addition, we note that the county received $22 million from the American Rescue Plan Act (ARPA), which will be used for a range of purposes, including one-time capital spending.

Income taxes accounted for approximately 44% of total general fund revenues in fiscal 2021, followed by property taxes at 40%, with both sources showing consistent growth over the past five years. In addition, St. Mary's County maintains some taxing flexibility, in our view, given that its property tax rate compares well to that of peers in Maryland. Additionally, the county has lowered its income tax rate in each of the last two years, which has increased its income tax flexibility given that its tax rate of 3.0% is below the state-mandated 3.20% maximum.

We note that St. Mary's County had maintained a small amount of privately placed equipment leases with TD Equipment Finance Inc. for vehicles and equipment, and that these were fully repaid at the end of fiscal 2022.

Low overall net debt with manageable capital improvement needs

We view St. Mary's County's debt levels as low. Following this issuance, we calculate that the county will have approximately $156 million in direct tax-supported debt, net of principal paid in 2022. The county's six-year CIP (2022-27) totals $315.9 million, a little less than half of which management expects to fund with additional debt issuances. We estimate that the county could issue an estimated $25 million to $30 million of new-money GO debt each year over the six-year CIP to finance various capital needs. Despite the expected issuances, given the amortization of existing debt as well as the county's debt policies we do not expect this plan to materially weaken its debt and liability factor score.

Pension and other postemployment benefits

- Pension and other postemployment benefit (OPEB) liabilities are not an immediate source of credit pressure for St. Mary's County.
- Although pension plan assumptions, particularly the 7.4% discount rate associated with the state-administered pension plan and 7.25% discount rate associated with the county's sheriff's plan, could increase contribution volatility, we believe that St. Mary's County can absorb year-to-year increases into the budget without straining finances.
- The county's strong OPEB pre-funding exceeds that of most state and national peers, which mitigates risk from cost and medical claims volatility.

As of the latest measurement date, the county participated in the following plans:

- The State Retirement and Pension System of Maryland, which the state administers and which was 72.9% funded as of June 30, 2021, is a cost-sharing, multiple-employer, defined-benefit plan in which most of the county's employees participate; St. Mary's County's proportionate share of this plan's net pension liability (NPL) is $25.8 million assuming a 7.4% discount rate;

- Sheriff's Office Retirement Plan: A single-employer, defined-benefit plan covering police and correctional officers; 84.6% funded with a NPL for the county of $23.8 million;
- A Length of Service Award Program for volunteer firefighters and rescue workers, with a net liability of $18.5 million that is pay-as-you-go financed; and
- An OPEB plan to eligible employees, which is a single-employer, defined-benefit health care plan that is 113% funded. The county established a trust to fund the plan. It historically has contributed 100% of OPEB costs annually, including a portion of any unfunded actuarial liability, although we note that as of June 30, 2021, the county's OPEB plan had a net asset of $13.9 million due in part to strong market returns during the year.

Pension contributions equaled our static funding metric and, as a result, we do not expect plan liabilities to materially increase over the next couple of years.

Very strong institutional framework score

The institutional framework score for Maryland municipalities is very strong.

St. Mary's County, Md.: Key Credit Metrics

	Most recent	Historical information		
		2021	2020	2019
Strong economy				
Projected per capita EBI % of U.S.	111.8			
Market value per capita ($)	118,868			
Population	114,568	113,777	113,569	113,958
County unemployment rate (%)		4.5		
Market value ($000)	13,618,522	13,196,225	12,849,449	
Ten largest taxpayers % of taxable value	4.2			
Strong budgetary performance				
Operating fund result % of expenditures		10.0	5.5	3.7
Total governmental fund result % of expenditures		9.1	5.1	5.9
Very strong budgetary flexibility				
Available reserves % of operating expenditures		32.8	27.0	28.3
Total available reserves ($000)		86,016	63,381	63,264
Very strong liquidity				
Total government cash % of governmental fund expenditures		46.0	43.2	39.7
Total government cash % of governmental fund debt service		1,030.7	849.8	806.3
Very strong management				
Financial Management Assessment	Strong			
Strong debt & long-term liabilities				
Debt service % of governmental fund expenditures		4.5	5.1	4.9
Net direct debt % of governmental fund revenue	53.9			
Overall net debt % of market value	1.2			
Direct debt 10-year amortization (%)	52.4			
Required pension contribution % of governmental fund expenditures		4.3		

St. Mary's County, Md.: Key Credit Metrics (cont.)				
	Most recent	**Historical information**		
		2021	**2020**	**2019**
OPEB actual contribution % of governmental fund expenditures		1.4		
Very strong institutional framework				
EBI--Effective buying income. OPEB--Other postemployment benefits.				

Data points and ratios may reflect analytical adjustments.

Related Research

Credit Conditions North America Q2 2022: Hazard Ahead: Risk Intersection, March 29, 2022

S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013

Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014

Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

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.