

Summary:

Bay City, Texas; General Obligation

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Credit Profile

US\$3.3 mil tax & rev certs of oblig ser 2010 dtd 05/01/2010 due 09/01/2030

Long Term Rating

A+/Stable

New

Rationale

Standard & Poor's Ratings Services assigned its 'A+' rating, and stable outlook, to Bay City, Texas' series 2010 tax and revenue certificates of obligation.

In our view, the rating reflects the city's:

- Strong financial position, evidenced by its diverse revenue stream and very strong unreserved general fund balance;
- Rapid debt amortization schedule; and
- Low debt burden.

In our opinion, the city's adequate, yet below-average, income levels offset, in part, these credit strengths.

The city's annual ad valorem property tax pledge secures the bonds. In addition, the city has pledged, on a subordinate basis, net revenues of its waterworks and sanitary sewer system to the payment of debt service. City officials plan to use bond proceeds to fund various street and drainage, airport, and civic center improvements.

Bay City, with a population estimate of 19,735, is roughly 80 miles south of Houston near the Gulf of Mexico. The city serves as the county seat and commercial center for Matagorda County. Leading local industries include nuclear power generation, education, and health care. Leading city employers are the school district (946 employees), the county hospital (308), and a Wal-Mart Stores Inc. supercenter (284). The South Texas Project Electric Generating Station site, which employs more than 1,700, is between the city and Palacios, Texas. The construction of two new nuclear reactors should be complete by 2015; they might add 1,000 permanent employees when fully operational. County unemployment totaled 12.1% in January 2010, above state and national rates at 8.6% and 9.7%, respectively. We consider city income levels adequate, but median household income equals just 72% of the national average.

The city's diverse property tax base continues to expand steadily. After increasing by an average of 14.0% annually since fiscal 2006 to \$629 million in fiscal 2009, total assessed value (AV) has increased by just 1.2% to \$636 million for fiscal 2010. The city's 10 leading property taxpayers account for a very diverse 6.7% of total AV. The majority of development is occurring on the city's east side; officials expect a new residential development to add 72 new homes.

We consider the city's financial position strong. Following annual general fund surpluses in three of the past four years, the city's unreserved general fund balance rapidly increased to \$1.6 million, or a very strong 20% of expenditures, in fiscal 2009 from \$335,000 in fiscal 2005. Officials attribute the city's good financial performance to higher-than-budgeted sales tax revenues and lower-than-budgeted expenditures. In addition to these reserves, the

city maintained \$832,000, or 10% of expenditures, in its community construction projects fund, which it can transfer into the general fund if necessary.

The city's revenue stream is diverse with property and sales taxes generating the majority of general fund revenues at 34% and 38%, respectively. Actual sales tax revenues declined by 3.4% in fiscal 2009, and officials budgeted for a 9.0% decline in these revenues in fiscal 2010. Current sales tax revenues are 10% below fiscal 2009 revenues; and management implemented several cost-saving measures that it expects to save \$400,000. Despite the decline in sales tax revenues, the city expects to maintain \$2.0 million of reserves for fiscal 2010 and \$2.2 million in fiscal 2011. Officials are assuming flat sales tax growth for fiscal 2011, and they do not plan to draw down reserves.

The city's waterworks and sanitary sewer system is a self-supporting system, and fiscal 2009 net revenues provide an adequate 1.13x outstanding debt service coverage in fiscal 2010. The city council approved 3% annual utility rate increases, effective in January 2010. In addition, officials expect a late payment fee, effective in January 2010, to generate an additional \$700,000 annually.

Standard & Poor's considers Bay City's management practices "standard" under its Financial Management Assessment (FMA) methodology, indicating the finance department maintains adequate policies in some, but not all, key areas. Key management practices include management's:

- Monthly reviews of budgeted numbers compared to actual financial performance,
- Quarterly budget meetings with the city council,
- Quarterly reviews of investment holdings with the city council, and
- Maintenance of a formal reserve policy equal to at least 12% of expenditures.

A formal debt management policy or capital improvement plan, however, do not exist.

The city's overall net debt burden is a low \$1,411 per capita, or 4.4% of market value. Debt amortization is rapid with officials planning to retire 77% of general obligation (GO) debt principal over 10 years. Officials believe the series 2010 debt issuance will address the city's capital needs through 2012, and the city does not currently have any additional debt plans.

Outlook

The stable outlook reflects the city's strong financial position, supported by the city's diverse property and sales tax revenue streams and very strong unreserved general fund balance. Standard & Poor's expects the city to maintain its strong reserves and continue to abide by its formal reserve policy. In addition, we expect the city to monitor its sales tax receipts closely and for the city to continue its conservative budget practices.

Related Criteria And Research

USPF Criteria: GO Debt, Oct. 12, 2006

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