Spotsylvania County, Virginia

New Issue Report

Ratings

Long-Term Issuer Default Rating	AAA

New Issue

$30,000,000 General Obligation Public Improvement Bonds, Series 2017A	AAA

Outstanding Debt

Spotsylvania County (VA) General Obligation Bonds	AAA
Spotsylvania County Economic Development Authority (VA) Revenue and Refunding Bonds	AA+

Rating Outlook

Stable

Analysts

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New Issue Summary

Sale Date: Aug 2 via competition.

Series: $30,000,000 General Obligation Public Improvement Bonds, Series 2017A.

Purpose: Fund various school and county capital projects.

Security: General obligations of the county, backed by a pledge of its full faith, credit and unlimited ad valorem taxing power.

Analytical Conclusion

The 'AAA' Issuer Default Rating (IDR) and GO ratings reflect Spotsylvania County's strong revenue framework, low long-term liability burden, healthy reserves and broad budgetary tools.

The revenue bond ratings are one notch lower than the IDR at 'AA+', reflecting the requirement for annual budgetary appropriation in support of lease payments.

Key Rating Drivers

Economic Resource Base: The county is located along the Interstate 95 corridor, within commuting distance of the Washington, D.C. and Richmond, VA metropolitan areas at about 55 miles from each. As of 2016, the county's population was 132,010; growth has averaged approximately 1% annually over the previous decade.

Revenue Framework: 'aaa' factor assessment. The county's strong tax base growth during the economic recovery, coupled with the increase of tax rates in down years, generated consistent general fund revenue growth through the previous decade. Over time, Fitch expects solid natural revenue growth above the rate of inflation, but likely below the level of U.S. GDP growth. The county has the independent legal ability to raise property tax revenues in an unlimited amount.

Expenditure Framework: 'aa' factor assessment. Fitch Ratings expects the natural pace of spending growth to remain in line with to marginally above revenue growth. Moderate carrying costs and broad flexibility to manage labor-related costs allow the county solid leeway to adjust spending.

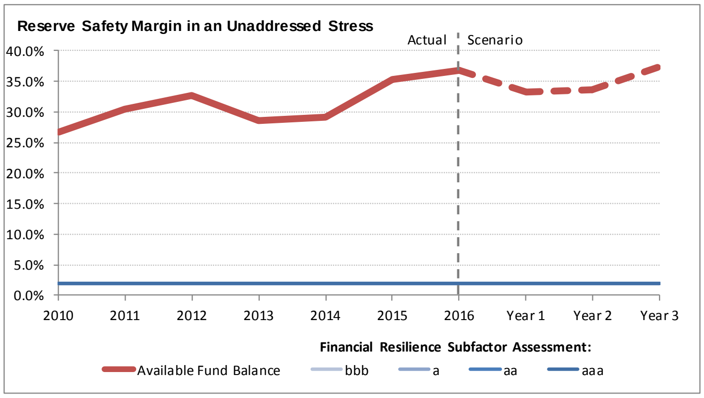
Long-Term Liability Burden: 'aaa' factor assessment. The combined burden of debt and unfunded pension liabilities is low at just under 10% of personal income. The metric should remain stable over time despite a rising net pension liability; future debt issuance plans generally match the amortization of existing debt. The county participates in the Virginia Retirement System (VRS) for defined benefit pension plans.

Fitch believes the state's decision to return to full funding of the actuarially determined contribution and improved investment returns should slow the increase in the net pension liability.

Operating Performance: 'aaa' factor assessment. The county's superior budget flexibility and ample general fund balance position it to comfortably manage through economic downturns without diminishing its overall financial flexibility.

Spotsylvania County (VA)

Scenario Analysis v. 2.0 2017/03/24



Analyst Interpretation of Scenario Results:

Given the moderate economic sensitivity of the county's revenues and its superior inherent budget flexibility in the form of revenue-raising ability and cost controls, Fitch expects the county to manage through economic downturns while maintaining a high level of fundamental financial flexibility. Available general fund reserves exceeded the county's reserve policy in fiscal 2016 totaling $70.9 million, or 28% of spending net of refundings, and 37% of spending when including readily accessible reserves available in the capital fund.

The county demonstrated its financial resilience and strong budget management through the most recent recession by delaying capital spending, shifting cash back to the general fund from available reserves in the capital projects fund as necessary to address budget gaps, reducing the appropriation to the schools, and controlling cost through workforce reduction and freezing salaries.

Scenario Parameters:	Year 1	Year 2	Year 3
GDP Assumption (% Change)	(1.0%)	0.5%	2.0%
Expenditure Assumption (% Change)	2.0%	2.0%	2.0%
Revenue Output (% Change)	(1.0%)	3.9%	5.3%
Inherent Budget Flexibility	Superior		

Revenues, Expenditures, and Fund Balance	Actuals							Scenario Output		
	2010	2011	2012	2013	2014	2015	2016	Year 1	Year 2	Year 3
Total Revenues	209,519	219,056	222,751	223,415	231,150	238,739	247,537	245,061	254,560	267,978
% Change in Revenues	-	4.6%	1.7%	0.3%	3.5%	3.3%	3.7%	(1.0%)	3.9%	5.3%
Total Expenditures	196,460	208,784	212,295	225,905	233,768	231,454	246,904	251,842	256,878	262,016
% Change in Expenditures	-	6.3%	1.7%	6.4%	3.5%	(1.0%)	6.7%	2.0%	2.0%	2.0%
Transfers In and Other Sources	-	2,630	6,088	44,237	23,498	79,440	31,478	31,163	32,371	34,077
Transfers Out and Other Uses	3,469	6,681	9,249	48,619	19,124	76,434	25,875	26,393	26,921	27,459
Net Transfers	(3,469)	(4,051)	(3,161)	(4,382)	4,374	3,007	5,602	4,770	5,450	6,618
Bond Proceeds and Other One-Time Uses	-	-	6,017	43,496	11,584	70,419	16,414	-	-	-
Net Operating Surplus(+)/Deficit(-) After Transfers	9,590	6,221	7,295	(6,872)	1,756	10,292	6,235	(2,010)	3,131	12,579
Net Operating Surplus(+)/Deficit(-) (% of Expend. and Transfers Out)	4.8%	2.9%	3.4%	(3.0%)	0.7%	4.3%	2.4%	(0.7%)	1.1%	4.3%
Unrestricted/Unreserved Fund Balance (General Fund)	48,052	54,748	60,683	53,924	55,538	65,310	70,910	68,900	72,031	84,611
Other Available Funds (Analyst Input)	5,384	10,718	9,630	12,118	14,690	18,630	23,466	23,466	23,466	23,466
Combined Available Funds Balance (GF + Analyst Input)	53,436	65,466	70,313	66,042	70,228	83,940	94,376	92,366	95,497	108,076
Combined Available Fund Bal. (% of Expend. and Transfers Out)	26.7%	30.4%	32.6%	28.6%	29.1%	35.3%	36.8%	33.2%	33.6%	37.3%

Reserve Safety Margins	Inherent Budget Flexibility				
	Minimal	Limited	Midrange	High	Superior
Reserve Safety Margin (aaa)	16.0%	8.0%	5.0%	3.0%	2.0%
Reserve Safety Margin (aa)	12.0%	6.0%	4.0%	2.5%	2.0%
Reserve Safety Margin (a)	8.0%	4.0%	2.5%	2.0%	2.0%
Reserve Safety Margin (bbb)	3.0%	2.0%	2.0%	2.0%	2.0%

Notes: Scenario analysis represents an unaddressed stress on issuer finances. Fitch's downturn scenario assumes a -1.0% GDP decline in the first year, followed by 0.5% and 2.0% GDP growth in Years 2 and 3, respectively. Expenditures are assumed to grow at a 2.0% rate of inflation. Inherent budget flexibility is the analyst's assessment of the issuer's ability to deal with fiscal stress through tax and spending policy choices, and determines the multiples used to calculate the reserve safety margin. For further details, please see Fitch's US Tax-Supported Rating Criteria.

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AAA	Affirmed	Stable	7/24/17
AAA	Upgraded	Stable	8/9/16
AA+	Upgraded	Stable	6/13/12
AA	Revised	Stable	4/30/10
AA–	Assigned	Stable	10/14/04

Related Research

Fitch Rates Spotsylvania County, VA's $27MM GOs 'AAA'; Outlook Stable (July 2017)

Related Criteria

U.S. Public Finance Tax-Supported Rating Criteria (May 2017)

Rating Sensitivities

Maintenance of Strong Financial Profile: The ratings assume the county's continued strong financial flexibility, revenue growth prospects and budgetary controls.

Long-Term Liabilities: A larger than expected increase of the county's long-term liability metric for debt and pensions could pressure the ratings.

Credit Profile

Spotsylvania County functions as a bedroom community for the D.C. metro area. Approximately 64% of county residents commute to outside the county for work. Employment trends inside the county are positive. Over the past six years, the county has continued to add jobs on par with that of the rest of the growing state economy. The unemployment rate tracks that of the state and remains well below the U.S. level. The county's wealth indicators are mixed with per capita personal income averaging that of the nation at about 10% below the state average.

The county has a pipeline of economic development projects due to its economic incentives, availability of land and skilled workforce, which is attracting private investment and should foster local employment opportunities. The county's target industries include healthcare, manufacturing, high-tech, defense and tourism. The largest private investment is Lidl, a German grocery store chain, which recently constructed a $125 million, nearly 1 million square foot, distribution center, creating 200 jobs in the county. The grocer recently opened 10 stores in the region and is expanding with two stores expected for Spotsylvania County.

Revenue Framework

The revenue base is dominated by property taxes at about 65% of fiscal 2016 general fund revenues, intergovernmental revenues (primarily state moneys for education) at 14%, and sales taxes at 7%.

Revenues over the previous decade, bolstered by policy action to adjust tax rates as necessary, have steadily increased ahead of inflation and U.S. GDP growth, despite significant swings in the tax base during the recession. Going forward, Fitch expects more moderate revenue growth given ongoing economic development in the region as well as positive housing trends in the county.

The lack of a legal cap on the property tax rate or levy provides the county with high, independent, legal revenue-raising flexibility. The county's property tax rate remains competitive relative to neighboring, similarly sized jurisdictions.

Expenditure Framework

The county's expenditures are primarily composed of public safety and education. These costs compose approximately 60% of total general fund expenditures. Virginia public schools are largely funded by a mix of state and local aid contributions. The amount of local contribution is determined by the county board, and must, at a minimum, meet the state-determined performance standards for the school system.

Given the county's solid revenue growth prospects, Fitch expects spending growth to be in line with to marginally above revenues over time.

The county has solid flexibility to adjust major expenditure items. Fixed carrying costs associated with debt service, required pension costs and OPEB actual spending consume approximately 15% of governmental spending. The state's education funding standards require a minimum funding level, but the required local effort is very low compared to the level at which the county currently funds education. Additionally, the county has broad discretion over the terms of employee wages and benefits given the absence of collective bargaining.

Long-Term Liability Burden

Overall debt and unfunded pension liabilities are just under 10% of the county's personal income. The metric is split between the direct debt of the county and the pension plans. The five-year capital improvement plan (CIP) for general government, schools and transportation totals $211 million. The plan is primarily funded with debt ($159.1 million expected); however, management may cash-fund more than what the plan currently calls for. Fitch does not expect debt to pressure the liability burden, as population and income growth is likely to be aligned with additional debt needs and principal is rapidly amortized at over 75% to be paid down within 10 years.

The county offers defined benefit pension plans administered by the VRS as both agent plans (for general employees and non-teacher employees of the component unit school system) and as a cost-sharing, multiple-employer plan for teachers. Plan assets (combined and adjusted to Fitch's 6% investment rate of return assumption) covered only about 57% of plan liabilities in fiscal 2016. Systemwide funding of VRS declined in recent years, due in part to underfunding of actuarial contributions (partially used as a budget balancing measure for the state). Positively, the commonwealth's biennial budget plan for fiscal years 2017 to 2018 accelerates the phase-in for full actuarial-determined employer contribution payments by one year to fiscal 2018, which should slow the growth in the net pension liability. The use of a 7% investment return assumption is notably conservative compared to other major state systems.

The county also provides OPEB plans for county and school board employees. At the close of fiscal 2016, the UAAL for county employees was reported at $56.4 million and, for school employees, $212.5 million, or a combined 4% of personal income. The county is setting aside assets in trust and plans to reach full funding of the OPEB ARC by 2023.

Operating Performance

Given the moderate economic sensitivity of the county's revenues and its superior inherent budget flexibility in the form of revenue-raising ability and cost controls, Fitch expects the county to manage through economic downturns while maintaining a high level of fundamental financial flexibility. For details, see Scenario Analysis, page 2.

The county estimates a $6 million use of general fund reserves after transfers to the capital fund at year-end fiscal 2017, equaling about 2% of general fund spending and transfers out. The drawdown of reserves is higher than originally budgeted, but includes a portion of fund balance reserved for capital projects in fiscal 2016 that was not expended by year-end 2016 but, instead, used during fiscal 2017. The county has traditionally used a portion of fund balance in excess of its policy for capital expenditures.

The fiscal 2018 budget included a spending increase of about $5 million, or 2% over the previous year's budget. The budget is balanced with a minor $761,000 use of reserves without increasing the operating millage rate.

The ratings above were solicited and assigned or maintained at the request of the rated entity/Issuer or a related third party. Any exceptions follow below.