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March 14, 2012

Summary:
Calhoun County, Michigan; General Obligation

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Credit Profile		
US$1.805 mil wtr supp & sanitary swg sys rfdg bnds (Charter Township Of Emmett) ser 2012 dtd 03/29/2012 due 05/01/2021		
Long Term Rating	AA-/Stable	New
Calhoun Cnty GO		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'AA-' long term rating on Calhoun County, Mich.'s series 2012 water supply and sanitary sewage disposal system refunding bonds (Charter Township of Emmett). At the same time, Standard & Poor's affirmed its 'AA-' long-term and underlying ratings (SPUR) on the county's existing general obligation (GO) debt. The outlook on all ratings is stable.

The ratings reflect our opinion of the county's:

- Deep tax base, anchored by the City of Battle Creek;
- Strong general fund reserve position, which is further supported by additional liquidity in its delinquent tax revolving fund; and
- Moderate debt burden with low carrying charges and no additional debt plans.

Ongoing and potential future financial pressures resulting from rising expenditures and declining revenues, notably state aid and property taxes, partly offset these strengths. In light of these pressures, county officials have consistently taken an active role in making budget adjustments to maintain mostly balanced operations.

The bonds are secured by contractual payments received by the county from Emmett Charter Township. The township has assigned its limited-tax GO pledge to the contract, payable from ad valorem taxes levied on all taxable property within the township, subject to statutory limitations, as well as from all other available revenue sources. The bonds are also secured by the county's limited-tax GO pledge. The 'AA-' rating reflects our assessment of the stronger pledge, which is that of the county.

Officials intend to use the series 2012 bond proceeds to refund existing series 2000 Calhoun County water supply and sewage disposal system (Charter Township of Emmett) bonds for interest-cost savings. County officials tell us the township has historically made timely payments toward the debt service and expect continued performance going forward.

Located in south-central Michigan, Calhoun County covers 720 square miles, encompasses roughly 136,616 residents, and includes the cities of Battle Creek, Marshall, and Albion. County income levels are adequate in our view, with median household and per capita effective buying equal to 84% and 80% of national levels, respectively. During the recession, the county saw its unemployment rate grow from a 6.8% average in 2007 to a peak of 11.4% in 2009. The unemployment rate has declined since then, to 10.9% in 2010 and to a preliminary 8.9% in 2011, but we note that county employment and its labor force have also declined. Manufacturing, trade, government, and services are key employment sectors. The county's leading employers include:

- Denso Manufacturing (automobile parts, 1,950 employees);
- Kellogg Co. (headquarters; 1,900);
- U.S. Department of Defense (1,900);
- Battle Creek Health System (1,554); and
- Kraft General Foods Co. (1,500).

Additionally, the Fort Custer Industrial Park, located in Battle Creek, encompasses 3,000 acres and has a combined workforce of more than 9,000 people within 85 companies. Denso Manufacturing is the largest employer in the industrial park.

Mirroring regional trends, the county's tax base, which predominantly consists of residential (58% of taxable value), commercial (14%), and agricultural (10%) properties, has seen declines in recent years due mostly to decreasing home values. Assessed value (AV) fell by 3.6% and 2.2% in 2010 and 2011, respectively, to $3.63 billion. The county's actual market value has seen slightly steeper decreases, falling by 5.3% and 3.7% in the past two years to $8.35 billion, which equates to $61,135 per capita, which we consider strong. We understand that management is planning for another market value decrease in 2012, though not as severe as those seen in recent years, and that assessors are indicating that values are close to bottoming out. The tax base is very diverse in our view, with the 10 leading taxpayers accounting for only 10.6% of total AV.

The county's financial performance remains steady, despite pressures from falling revenues and rising expenditures. The county has reported positive financial operations in four of the past five years, including a $162,000 surplus in fiscal 2010, which brought the Dec. 31, 2010 general fund balance to $4 million, of which $3.9 million or 12% of expenditures, is unreserved, which we consider strong. The county balanced the fiscal 2011 budget by using $1.7 million from its delinquent tax fund, but without the use of general fund reserves, and officials expect to finish the year on target with balanced operations and possibly a small general fund surplus. In an effort to curb expenditure growth and to offset declining property taxes and state aid, the county continued its trend of annul expenditure reductions by reducing staffing levels, a measure that was aided by an early retirement incentive offered in late 2010. For fiscal 2012, the county closed a $3.5 million budget gap without the use of general fund reserves, which are budgeted to stay at 10%, although it relies on its customary, albeit slightly larger, $1.8 million transfer from the delinquent tax fund. The $40 million budget was aided by personnel-related cost cuts, including health care reforms, layoffs, and other reductions. Property taxes (49% of general fund revenues) are the major source of general fund revenues, followed by charges for services (29%) and state-shared revenues (6%).

Although the county closed fiscal 2010 with a general fund cash balance of only $1.5 million (17 days cash on hand), it maintains additional unrestricted cash reserves in its delinquent tax revolving fund, mitigating concerns about low general fund liquidity. This fund carried $9 million in unrestricted net assets to close fiscal 2010, which includes $8.64 million in cash and cash equivalents, equal to 97 days' cash on hand. This enterprise fund accounts for the purchase of delinquent taxes from the county's underlying taxing jurisdictions and the subsequent collections of those taxes with interest and penalties. The county historically transfers about $1.5 million from this fund to the general fund to subsidize general fund operations.

The county's management practices are considered "good" under Standard & Poor's Financial Management Assessment. This indicates that practices exist in most areas, although not all may be formalized or regularly monitored by governance officials. The county prepares and regularly updates a comprehensive five-year financial and capital plan. It has a formal investment policy, and the county board monitors investment holdings, earnings, and budget-to-actual performance on a monthly basis. Budget amendments can be made by the board as needed, and the county has a reserve policy to maintain a general fund balance equal to 8% to 12% of annual general fund expenditures.

The county's overall debt burden is moderate at 5.4% of market value and $3,352 per capita. Carrying charges are low at only 1.5% of total governmental funds expenditures, less capital outlay. Debt service amortization begins rapidly, with 71% of principal paid within 10 years; but then slows as 100% maturity is not until 2032. Officials have indicated no plans for additional long-term debt issuances.

The county met 100% of its annual required contribution amounts for its three pension plans in fiscal 2010, which amounted to $2.3 million in annual costs. The three plans have funded ratios ranging from 47% to 59%. The county also pays retiree health care benefits on a pay-as-you-go basis, which has led to a $12.6 million unfunded retiree health-care liability.

Outlook

The stable outlook reflects our expectation that the county will maintain at least good general fund reserves and high levels of additional liquidity in the delinquent tax revolving fund. The outlook also reflects our expectation that county officials will continue to actively monitor the budget and make spending adjustments as needed to maintain compliance with the formal reserve policy. The county's deep tax base and expansive employment opportunities further support the outlook. In the event that the county experiences any pattern of declining reserve levels due to an inability to continually balance the annual budget, the rating could be lowered. However, given management's historical budget performance and a sizable budget that lends itself to more flexibility, we do not expect to change the rating during the two-year outlook horizon.

Related Criteria And Research

USPF Criteria: GO Debt, Oct. 12, 2006

Ratings Detail (As Of March 14, 2012)		
Calhoun Cnty GO		
Long Term Rating	AA-/Stable	Affirmed
Calhoun Cnty GO (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Calhoun Cnty GO		
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Many issues are enhanced by bond insurance.

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