Fitch Ratings

Fitch Rates Charleston County, SC's $200MM GOs 'AAA' & Rev Bonds 'AA+'; Outlook Stable

Fitch Ratings-New York-06 October 2017: Fitch Ratings has assigned the following ratings to Charleston County, SC:

--$103 million GO capital improvement bonds, series 2017A 'AAA';
--$15.8 million GO refunding bonds, series 2017B 'AAA';
--$94.3 million GO transportation sales tax refunding bonds, series 2017C 'AAA';
--$36.0 million special source revenue bonds (taxable), series 2017 'AA+'.

The GO bonds proceeds will finance various county capital projects including a library and refund various callable bonds for debt service savings. Proceeds of the special source revenue bonds will finance capital improvements to the manufacturing facility of Mercedes-Benz Vans, LLC located inside the county's business park. The GO bonds will price competitively on November 15 and the revenue bonds will price competitively on October 26.

In addition, Fitch has affirmed the following ratings:

--The county's Issuer Default Rating (IDR) at 'AAA';
--$173.7 million general obligation (GO) bonds at 'AAA';
--$86.4 million special source revenue bonds, series 2013 at 'AA+'.

The Rating Outlook is Stable.

SECURITY

The GO bonds are backed by the county's full faith and credit and unlimited ad valorem taxing ability. GO transportation sales tax bonds are additionally payable from a first lien on the revenues from a one-half-cent transportation sales tax imposed by the county.

The special source revenue bonds are a limited obligation of the county, payable from certain fees-in-lieu of taxes (FILOT). If FILOT funds are insufficient to cover debt service, the county shall make provision through a budgetary directive to apply other available moneys to satisfy the FILOT deficiency, such obligation being subject to budgetary appropriation.

ANALYTICAL CONCLUSION

The 'AAA' IDR and GO rating reflect the county's strong revenue framework associated with the strong natural growth of general fund revenues and independent ability to adjust revenues as necessary. The county maintains a very healthy level of reserves available to close budgetary gaps in the event of an economic or fiscal stress. The long-term liability burden associated with debt and pensions is low.

The special source revenue bond's 'AA+' rating, one notch below the county's IDR, is based on the county's covenant to appropriate to pay any deficiency in debt service. The special source revenue bonds do not carry any of the additional risk features that Fitch identifies for rating more than one notch below the IDR. In Fitch's view, the back-up appropriation pledge provides a higher level of credit quality than the pledged FILOT revenue stream.

Economic Resource Base

Charleston County encompasses an area of 945 square miles in southeastern South Carolina including 97 miles of Atlantic coastline. The county's 2016 estimated population of 396,484 represents a rapid 13% increase from the 2010 Census and ranks Charleston the third most populous county in the state.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

General fund revenues have averaged just under 3% annual growth over the previous decade and Fitch expects the county's population expansion and growing economy to continue to drive revenue growth at or ahead of GDP growth. The county's banked millage under the state's revenue cap provides significant independent ability to raise revenues if necessary.

Expenditure Framework: 'aa'
Flexibility of the county's main expenditure items are solid, which benefits from management's full control over headcount, salaries, and benefits. Fixed carrying costs, primarily driven by debt service costs, totaled 20% of fiscal 2016 governmental expenditure. Principal repayment is rapid at 75% within 10 years. Spending demands are expected to remain in line with revenue growth.

Long-Term Liability Burden: 'aaa'
The county's long-term liability burden for debt and pension is low at just under 10% of personal income. The region's economic growth will continue to drive issuance by the county and the overlapping school system, though Fitch anticipates that the pace of amortization and the growth of personal income will keep the burden level. Despite the poor funding ratio of the pension plans the county participates in, the exposure to the net pension liability is very small at less than 2% of personal income.

Operating Performance: 'aaa'
Fitch's Analytical Sensitivity Tool (FAST) generates only a modest estimated revenue decline from a potential economic stress. The superior budgetary control and very healthy reserves available to address a stress scenario contribute to the 'aaa' assessment for financial resilience.

RATING SENSITIVITIES
ECONOMIC REVERSAL: An unexpected and material reversal of the economy and associated erosion of economically sensitive revenues could stress operations and negatively pressure the rating.

DEBT ISSUANCE ABOVE EXPECTATIONS: The rating is sensitive to an increase in the burden of debt, including overlapping debt of the school district, and pension liabilities on the personal income resource base of the county. An increase in carrying costs that pressures the county's expenditure flexibility could also pressure the rating.

CREDIT PROFILE

Since 2010, employment in Charleston County has increased well ahead of the state and national rates. Area employment remains heavily influenced by the government sector and the military, though continued diversification into manufacturing, by Boeing specifically (rated 'A'/Outlook Stable), has added a significant number of jobs. The government sector accounts for a high 20% of area employment, 125% of the national norm. Additionally, a fairly sizable health and education sector lends depth and stability to the economy. Unemployment remains very low compared to the state and national averages.

Federal employment at Joint Base Charleston accounts for 22,000 active-duty military personnel and civilians and about 7% of total employment within the greater Charleston metropolitan area. The Joint Base is home to the Space and Naval Warfare Systems Center (SPAWAR) supporting critical communications, intelligence, surveillance and reconnaissance operations for the Navy.

The Port of Charleston remains an important economic engine for the region, anchoring international trade, transportation activity and tourism. In December 2016, the federal Water Infrastructure Improvements for the Nation Act was authorized, calling for the deepening of the port to 52 feet to better accommodate the larger ships expected from the expanded Panama Canal project. The project is on track for completion in 2020. The port also anchors the region's tourism in the form of an expanding cruise industry. Retail increased in fiscal 2016 for a sixth consecutive year since the fiscal 2010 recessionary low.

In 2013, Boeing announced a $1 billion expansion, citing the benefits of the healthy labor environment and access to distribution channels including the port, and opened two new research and design centers. Boeing now employs 7,600 in the region and continues to expand the 787 Dreamliner manufacturing facilities. Mercedes-Benz began a $500 million plant expansion in 2016 to manufacture Sprinter vans and expects to employ 1,300 upon completion.

Revenue Framework

Property taxes account for the largest portion of general fund revenues at about 45% of the total, followed by sales taxes at 27%. Intergovernmental revenues are the next largest category at about 12%, primarily from state aid and a smaller portion from federal grants.

Fitch expects the county's tax base, benefitting from new private investment, to continue to increase in line with or ahead of the rate of national expansion. The fiscal year 2016 revaluation was an increase of 8%. Home values continue to increase sharply and are well above the pre-recession peak at an average of $184,000 in the Charleston metro area according to Zillow. Other population and trade and industry growth is driving strong increases in economically-sensitive sales tax revenues, which averaged over a 3% annual increase over the prior decade and a 6% increase in fiscal 2016.

Ad valorem revenue-raising ability is broadly capped by the provisions of South Carolina's Act 388, which limits increases in the millage rate for operations to annual population growth plus inflation. The law provides for the carry-forward of unused millage increases for up to three years. The limitation may be suspended for some circumstances including a deficiency of the preceding year, any catastrophic event and the loss of significant tax payers. The county maintains significant flexibility to independently raise operating revenues under the cap and banked unused millage in the fiscal 2018 budget that would generate over $13 million annually or 6% of general fund spending. The county could also independently impose other fees and charges that would generate a moderate amount of revenues.

Expenditure Framework

Public safety, the largest spending category of the county, represents just under half of general fund spending. General government is the next largest spending item at 39%, followed by culture and recreation at 8%.

As with most local governments, personnel costs drive the county's spending and Fitch believes cost increases will continue to grow in line with to marginally ahead of the strong general fund revenue growth. Management proactively identifies and manages areas of future growth as demonstrated by the discontinuation of other post-employment benefits (OPEB) for new hires beginning in fiscal year 2017.

Fixed carrying costs for debt service, pension and OPEB account for 20% of governmental spending. Debt service costs represent a majority of the metric and have increased in recent years. Theses fixed costs are likely to continue increasing as the county expands. Pension and OPEB costs remain a small percentage of spending.

Other pieces of the budget are solidly flexible. The workforce environment in South Carolina lends control to management over headcount, benefits and salaries. Headcount decreased slightly during the Great Recession as management addressed spending growth by delaying hiring, limiting departmental budget increases and postponing discretionary capital spending. Recent budgets have filled open positions and increased headcount during the economic recovery to about 10% above pre-recession levels. Similarly, Fitch views management's reintroduction of pay-go capital spending in recent budgets as a point of modest flexibility.

Long-Term Liability Burden

The county's long-term liability burden is just under 10% of personal income including the current issuance. After this issuance, the county's five-year capital plan includes at least another $100 million in general government debt funding. Issuance of this debt would not have a significant impact on the county's long-term liability burden, given the county's rapid payout ratio of debt at 67% retired in 10 years. Fitch includes the debt of overlapping entities in this metric and a large portion of this burden is associated with the Charleston County School District. School debt issuance in fiscals 2016 and 2017 for capital expansion has increased the liability burden in recent years and Fitch expects the growing school district's capital needs to continue to increase.

County employees participate in defined benefit pension plans administered by the state as cost-sharing multiple-employer plans. General employees participate in the South Carolina Retirement System (SCRS) and police officers in the South Carolina Police Officers Retirement System (PORS). Using Fitch's 6% investment return assumption and the most recent actuarial reports, the state plans' assets have decreased to 44.8% of the total liability for SCRS and 50.8% for PORS. The plans' funded levels are low compared to other state plans and will continue to drive increases in the county's associated carrying costs; however, from a liability burden perspective the county's portions of the net pension liabilities remains very low at less than 2% of personal income. The OPEB liability is minimal.

Operating Performance

The county's financial position has strengthened over the last decade and current reserves are very healthy. At the conclusion of fiscal 2016, the available general fund balance was up a strong 13% year over year to $59.5 million or 28.5% of spending. Fitch views the county's reserve policy, which requires maintenance of a general fund reserve of two months or roughly 17% of general fund spending, as ample and well above the 'aaa' minimum reserve safety margin under the FAST model. The model takes into account the stable historical revenue performance and superior budgetary flexibility available for management to negotiate a fiscal stress. The county's current level of reserves did not materially decrease at any point during the previous recession.

The approved fiscal 2018 operating budget is an 8.9% increase from the prior budget and totals $235.6 million. Hiring and raises drive the budgetary growth. The budget includes $5 million of reserves for paygo capital projects without changing the millage rates. Outside the general fund, the budget also includes the passing of the new half-cent transportation local option sales tax in the November 2016 referendum, which will fund $2.1 billion in transportation capital projects over 25 years.

The county's historically conservative five-year forecast currently depicts modest reductions in reserves through fiscal 2021. However, the budget remains operationally balanced and the county's financial policies state that reserves in excess of its policy requirement may be used for one-time purposes only.

Special Source Revenue Bonds - Ratings Based on Appropriation Backup

While the rating on the special source revenue bonds reflects the county's creditworthiness, Fitch anticipates FILOT revenue stream will cover annual debt service. Receipt of the FILOTs stem from the designation in 1995 of certain properties as part of a joint county industrial and business-park for the purpose of stimulating economic development. Currently 32 property owners comprise the park with Boeing as the largest owner. Boeing continues its economic expansion in the park and the expansion of the Mercedes-Benz plant (opened in 2006), which the current issuance of revenue bonds help finance, broke ground in 2016.

FILOT payments are collected with real property taxes for county, municipal and school purposes under a single tax bill which must be paid in full by the taxpayer due Jan. 15. MADS, including the new series of bonds, is equal to less than 4% of the county's general fund spending in fiscal 2016, which Fitch considers a manageable sum to absorb in the remote scenario where no FILOT revenues are available to cover debt service on the bonds. The county annually appropriates the upcoming fiscal year's full debt service from general revenues in each budget.

MADS including the proposed bonds is $12.0 million, resulting in 1.3x coverage from fiscal 2016 collections. Mercedes-Benz will increase its FILOT payments by $5.3 million beginning in fiscal 2020, accounting for a cumulative 20% of total FILOTs. Boeing, rated 'A'/Stable by Fitch, made $7.6 million in FILOT payments in fiscal 2017, accounting for over one-third of projected FILOT receipts.

Contact:

Primary Analyst
Parker Montgomery
Associate Director
+1-212-908-0356
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
Michael Rinaldi
Senior Director
+1-212-908-0833

Committee Chairperson
Amy Laskey
Managing Director
+1-212-908-0568

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Media Relations: Benjamin Rippey, New York, Tel: +1 646 582 4588, Email: benjamin.rippey@fitchratings.com.

Additional information is available on www.fitchratings.com

Applicable Criteria
U.S. Public Finance Tax-Supported Rating Criteria (pub. 31 May 2017) (https://www.fitchratings.com/site/re/898466)

Additional Disclosures
Dodd-Frank Rating Information Disclosure Form (https://www.fitchratings.com/site/dodd-frank-disclosure/1030310)
Solicitation Status (https://www.fitchratings.com/site/pr/1030310#solicitation)
Endorsement Policy (https://www.fitchratings.com/regulatory)

responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided “as is” without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to

US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.
For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001

Solicitation Status

Fitch Ratings was paid to determine each credit rating announced in this Rating Action Commentary (RAC) by the obligatory being rated or the issuer, underwriter, depositor, or sponsor of the security or money market instrument being rated, except for the following:

Endorsement Policy - Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the EU Regulatory Disclosures (https://www.fitchratings.com/regulatory) page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.