FITCH RATES HOWARD COUNTY, MD'S $227.135MM GOS 'AAA'; OUTLOOK STABLE

Fitch Ratings-New York-05 December 2017: Fitch Ratings has assigned a 'AAA' rating to the following Howard County bonds:

--$159.39 million consolidated public improvement refunding bonds, 2017 series D;
--$67.7 million metropolitan district refunding bonds, 2017 series E.

The county's Issuer Default Rating (IDR) is 'AAA'.

The Rating Outlook is Stable.

SECURITY
The GO bonds are payable from the county's full faith and credit pledge and its unlimited taxing power.

ANALYTICAL CONCLUSION

The 'AAA' Long-Term IDR and GO ratings reflect the county's strong growth prospects, low long-term liability burden, healthy reserves, and broad budgetary tools.

Economic Resource Base
Howard County is a wealthy Baltimore-Washington, D.C. suburban enclave with a diverse economy of its own. As of 2016, the county's population was 317,233; growth has averaged approximately 1.7% annually.

KEY RATING DRIVERS

Revenue Framework: 'aaa'
Revenues have been rising at a pace well above the rate of U.S. GDP growth and Fitch expects this trend to continue. The county has the independent legal ability to raise property tax revenues in an unlimited amount.

Expenditure Framework: 'aa'
Education drives the county's spending needs and any reduction would require approval from the state. Nevertheless, the county's ability to make spending cuts when needed is solid. Carrying costs related to debt and pensions are moderate.

Long-Term Liability Burden: 'aaa'
The county's liability burden is low and future debt needs are manageable.

Operating Performance: 'aaa'
Fitch expects the county to maintain a high level of fundamental financial flexibility throughout economic cycles based on its expenditure and revenue flexibility and conservative fund balance policy. Financial operations are supported by solid economic and revenue prospects.

RATING SENSITIVITIES
MAINTENANCE OF STRONG FINANCIAL PROFILE: The rating assumes the county's continued strong financial flexibility, revenue growth prospects and budget controls.

CREDIT PROFILE

The county is among the wealthiest in the nation, featuring a highly educated workforce. Residents are employed throughout a deep and diverse economy, led by the federal government. Fort Meade, located in nearby Anne Arundel County (AA+/Stable), is a major driver of long-term regional growth and Maryland's top employer. The fort, already a home base to all five military services and several federal agencies including the National Security Agency, has been named the headquarters for the U.S. cyber-security center. The county estimates that federal agencies located at Fort Meade employ approximately 12,500 county residents.

The education and healthcare sectors, led by John Hopkins University Applied Physics Laboratory, play a pivotal role in the economy and lend diversity to the notable concentration in government. While employment growth has slowed, the county continues to generate and retain jobs through its economic development efforts. The unemployment rate remains below the state and national averages.

The county continues to focus its economic development efforts in downtown Columbia. Most recently Tenable, Inc., a cybersecurity software company, announced its plan to expand its company headquarters to downtown Columbia bringing 900 employees to the county.

Revenue Framework

Property taxes are the largest revenue source for the county at 49% of general fund revenues followed by income taxes at 42%. Homes values have consistently increased over the past five years according to Zillow and the one-year forecast shows a 1.6% increase. Assessed values, which lag the actual housing market due to the rolling three-year reassessment cycle, have increased consecutively over the past four years. The fiscal 2018 budget includes a 2% increase in assessed value to $50.6 billion. According to unaudited fiscal 2017 results, income tax revenues increased for the seventh consecutive year and are budgeted to increase 3.2% in fiscal 2018.

The county's natural pace of general fund revenue growth has trended above U.S. GDP growth without any tax policy changes. Given ongoing economic development as well as positive housing and employment trends, revenue growth prospects are strong.

The property tax levy and rate are not subject to a cap. The county has not increased the property tax rate in 16 years. The income tax rate was increased in 2004 to the maximum rate of 3.2%.

Expenditure Framework

The county's largest expenditure is education at roughly 58% of general fund expenditures, followed by public safety at 12%.

Based on the county's history of structural balance and no immediate significant spending pressures, Fitch expects spending growth to remain in line with revenues.

According to the state's maintenance of effort (MOE) mandate, education spending cannot decline YOY without state approval. Approximately 50% of the county's workforce is unionized with one- or two-year contracts. However, strikes are not permitted and arbitration is not binding on the county council's budget. Carrying costs associated with debt service, actuarially determined pension payments (including the normal cost for teachers' pensions) and other post-employment benefits (OPEB) actual contributions totaled about 15% of unaudited fiscal 2017 governmental spending; debt service accounted for about 8%.

Long-Term Liability Burden

Overall net debt plus the county's unfunded pension liability equals a low approximately 7% of personal income excluding self-supporting metropolitan district utility debt. The county will repay 65% of outstanding principal within 10 years, leaving adequate capacity to fund future borrowing needs. The county's fiscal 2019-2023 capital plan totals $1.3 billion, excluding utility-related projects. While the plan includes nearly $1 billion of bond proceeds, the county expects actual future borrowing to approximate $100 million annually, allowing the county to maintain debt service costs at 10% of revenue or less. Fitch expects currently low debt levels to increase modestly but remain low relative to personal income.

The county provides pension benefits to its employees through two single-employer defined benefit plans -- a general employees plan and a fire and police plan -- and annually makes the actuarially required contribution. As of July 1, 2017, the general employees' plan was funded at 86% and police and fire employees at 76%. Fitch estimates the funded ratios at approximately 72% and 62%, respectively, using Fitch's more conservative 6% discount rate compared to the county's rate of 7.5%. The aggregate adjusted net pension liability totaled approximately $447 million or about 2% of personal income. The county also provides a length of service plan for volunteer public safety employees, which is currently unfunded but has a minimal net pension liability.

The county administers an OPEB trust fund that provides benefits for its retirees, which has a balance of about $86 million as of fiscal year-end (FYE) 2017. As of the 2016 valuation the unfunded liability is $908.5 million or 4% of personal income and the plan is 10% funded.

Operating Performance
Fitch assesses the county's inherent budget flexibility as superior given the county's strong legal ability to increase revenue and reduce expenditures. In response to a weak revenue growth environment during the last recession, the county used reserves to balance operations. During the recovery the county rebuilt reserves to currently healthy levels. The unrestricted fund balance at FYE 2017, according to unaudited results, was $125.5 million or 11.7% of general fund spending, well above the county's 7% policy. Additionally, the county funds fire and rescue and recreation services outside of the general fund. When Fitch combines these funds with the general fund, available fund balance increases to $184.4 million or 15% of combined spending at YE 2017.

Based on historical results, Fitch would expect a moderate economic downturn to result in a modest decline in revenues in the first year of a downturn, followed by a prompt rebound. The county's financial position should remain solid throughout the economic cycle given strengthened reserves and conservative management practices.

The fiscal 2018 budget is a 3.6% increase over fiscal 2017 and includes a $9.9 million fund balance appropriation while maintaining the property and income tax rates. The budget increases included $2.9 million above the MOE required level for education, an additional $3 million for county employer OPEB over the fiscal 2017 total contribution, a cost of living salary increase and $295 million for capital spending. According to management, year to date operations are in line with budget. Based on the county's multi-year financial forecast, Fitch expects operations to be balanced and reserve levels to remain above the county's 7% policy.

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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.

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Applicable Criteria
U.S. Tax-Supported Rating Criteria — Effective April 18, 2016 to May 31, 2017 (pub. 18 Apr 2016)
https://www.fitchratings.com/site/re/879478