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Mayor



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August 9, 2017

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Honorable Alan Arakawa  
Mayor, County of Maui  
200 South High Street  
Wailuku, Hawaii 96793

For Transmittal to:

Honorable Mike White, Chair  
and Members of the Maui County Council  
200 South High Street  
Wailuku, Hawaii 96793

APPROVED FOR TRANSMITTAL  
  
Mayor Date 8/15/17

Dear Chair White and Members:

**SUBJECT: MOODY'S AND FITCH SURVEILLANCE REPORTS**

Enclosed please find recent surveillance reports by both Moody's (8/3/17) and Fitch Ratings (2/17/17) for your review and information.

In its report Moody's said that, "The credit position for Maui County is very strong", and reaffirmed its Aa1 rating. Fitch Ratings affirmed its AA+ rating citing the "county's very strong revenue profile and adequate spending flexibility as reflected by its excellent operating performance."

Should you have any questions, please feel free to contact me at extension no. 7475.

Sincerely,

  
for DANILO F. AGSALOG  
Director of Finance

Attachments

COUNTY COMMUNICATION NO. 17-332

## ISSUER COMMENT

3 August 2017

### RATING

General Obligation (or GO Related)<sup>1</sup>

Aa1 Stable

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## Maui County, HI

### Annual Comment on Maui County

#### Issuer Profile

Maui County consists of the islands of Maui, Lanai, Molokai (except for a portion of Molokai that comprises Kalawao County), Kahoolawe, and Molokini. The latter two islands are uninhabited. The county islands lie between the islands of Hawaii to the south and Oahu to the the west. The county has a population of 160,863 and a moderate population density of 133 people per square mile. The county's median family income is \$76,195 (1st quartile) and the May 2017 unemployment rate was 3% (1st quartile)<sup>2</sup>.

#### Credit Overview

The credit position for Maui County is very strong, and its Aa1 rating is slightly above the US counties median of Aa2. Key credit factors include an extensive tax base, slightly above average resident wealth levels and a healthy financial position. Additional credit factors include an exceptionally light debt burden and a somewhat elevated pension liability.

**Economy and Tax Base:** Overall, the county has an exceptionally strong economy and tax base, which are slightly favorable in relation to the Aa1 rating assigned. The full value (\$40.7 billion) is well above the US median, and increased dramatically between 2012 and 2016. In addition, the full value per capita (\$253,083) is much stronger than the US median. Yet, the median family income is a healthy 115.4% of the US level.

**Finances:** The county has a very solid financial position overall, which is aligned with its Aa1 rating. The cash balance as a percent of operating revenues (27.3%) is slightly lower than the US median, and declined between 2012 and 2016. Also, the fund balance as a percent of operating revenues (24.8%) is a little weaker than other Moody's-rated counties nationwide.

**Debt and Pensions:** The debt burden of Maui County is negligible and is slightly favorable in relation to the assigned rating of Aa1. The net direct debt to full value (0.7%) is consistent with the US median, and stayed the same from 2012 to 2016. That said, the pension liability of the county is somewhat elevated and is unfavorable in comparison to its Aa1 rating. The Moody's-adjusted net pension liability to operating revenues (2.4x) is above the US median.

**Management and Governance:** Maui County's management team complies with strong internal financial policies while proactively improving reserve levels and addressing long-term benefit-related fixed costs through timely expenditure controls and prudent revenue adjustments.

Hawaii counties have an Institutional Framework score<sup>3</sup> of Aa, which is high compared to the nation. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector's major revenues source is property taxes

which is not subject to any caps. Unpredictable revenue fluctuations tend to be minor, or under 5% annually. Across the sector, fixed and mandated costs are generally greater than 25% of expenditures. Hawaii has public sector unions and additional constraints, which limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be moderate, between 5-10% annually.

### Sector Trends - Hawaii Counties

Hawaii counties will continue to benefit from the state's improving economy. Increased visitor levels, record hotel occupancy rates and strong growth in construction activity and taxable values have all provided counties with sound operating flexibility. However, a high cost of living and above average home prices will present obstacles to attracting employment diversity and in-migration. Finally, Hawaii's pension liabilities are well above average compared to other states and counties will be faced with significant increases in these long-term fixed costs.

EXHIBIT 1

#### Key Indicators <sup>4</sup> <sup>5</sup> Maui County

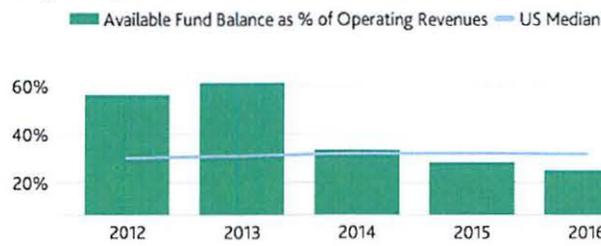
	2012	2013	2014	2015	2016	US Median	Credit Trend
<b>Economy / Tax Base</b>							
Total Full Value	\$32,920M	\$32,473M	\$33,411M	\$36,249M	\$40,711M	\$7,552M	Improved
Full Value Per Capita	\$212,477	\$207,321	\$210,382	\$225,342	\$253,083	\$80,731	Improved
Median Family Income (% of US Median)	116%	117%	115%	115%	115%	94%	Stable
<b>Finances</b>							
Available Fund Balance as % of Operating Revenues	56.1%	61.1%	33.3%	28.2%	24.8%	31.6%	Weakened
Net Cash Balance as % of Operating Revenues	51.8%	64.8%	20.2%	28.1%	27.3%	35.9%	Weakened
<b>Debt / Pensions</b>							
Net Direct Debt / Full Value	0.6%	0.7%	0.6%	0.7%	0.7%	0.5%	Stable
Net Direct Debt / Operating Revenues	0.79x	0.84x	0.74x	0.94x	0.89x	0.61x	Stable
Moody's-adjusted Net Pension Liability (3-yr average) to Full Value	N/A	1.9%	2.1%	1.8%	1.7%	1.0%	Stable
Moody's-adjusted Net Pension Liability (3-yr average) to Operating Revenues	N/A	2.31x	2.52x	2.33x	2.37x	1.23x	Stable
	2012	2013	2014	2015	2016	US Median	
<b>Debt and Financial Data</b>							
Population	154,937	156,633	158,814	160,863	N/A	N/A	
Available Fund Balance (\$000s)	\$142,561	\$164,642	\$91,801	\$80,682	\$74,263	\$20,856	
Net Cash Balance (\$000s)	\$131,685	\$174,601	\$55,749	\$80,422	\$81,492	\$22,190	
Operating Revenues (\$000s)	\$254,264	\$269,486	\$275,690	\$286,127	\$298,977	\$64,065	
Net Direct Debt (\$000s)	\$200,633	\$225,549	\$202,786	\$270,320	\$265,325	\$36,705	
Moody's Adjusted Net Pension Liability (3-yr average) (\$000s)	N/A	\$621,491	\$694,286	\$666,689	\$707,326	\$73,224	

Source: Moody's Investors Service

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on [www.moody's.com](http://www.moody's.com) for the most updated credit rating action information and rating history.

EXHIBIT 2

Available fund balance as a percent of operating revenues decreased from 2012 to 2016



Source: Issuer financial statements; Moody's Investors Service

EXHIBIT 3

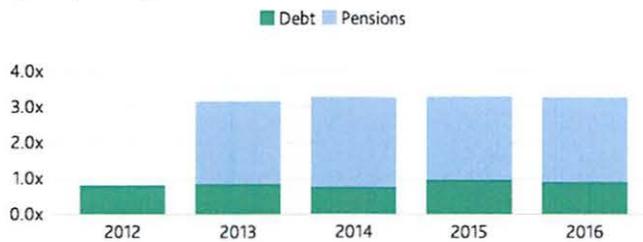
Full value of the property tax base increased from 2012 to 2016



Source: Issuer financial statements; Government data sources; Offering statements; Moody's Investors Service

EXHIBIT 4

Moody's-adjusted net pension liability to operating revenues increased from 2012 to 2016



Source: Issuer financial statements; Government data sources; Offering statements; Moody's Investors Service

## Endnotes

- 1 The rating referenced in this report is the issuer's General Obligation (GO) rating or its highest public rating that is GO-related. A GO bond is generally backed by the full faith and credit pledge and total taxing power of the issuer. GO-related securities include general obligation limited tax, annual appropriation, lease revenue, non-ad valorem, and moral obligation debt. The referenced ratings reflect the government's underlying credit quality without regard to state guarantees, enhancement programs or bond insurance.
- 2 The demographic data presented, including population, population density, per capita personal income and unemployment rate are derived from the most recently available US government databases. Population, population density and per capita personal income come from the American Community Survey while the unemployment rate comes from the Bureau of Labor Statistics.  
  
The largest industry sectors are derived from the Bureau of Economic Analysis. Moody's allocated the per capita personal income data and unemployment data for all counties in the US census into quartiles. The quartiles are ordered from strongest-to-weakest from a credit perspective: the highest per capita personal income quartile is first quartile, and the lowest unemployment rate is first quartile.
- 3 The institutional framework score assesses a municipality's legal ability to match revenues with expenditures based on its constitutionally and legislatively conferred powers and responsibilities. See [US Local Government General Obligation Debt \(December 2016\)](#) methodology report for more details.
- 4 For definitions of the metrics in the Key Indicators Table, [US Local Government General Obligation Methodology and Scorecard User Guide \(July 2014\)](#). Metrics represented as N/A indicate the data were not available at the time of publication.
- 5 The medians come from our most recently published local government medians report, [Medians – Growing Tax Bases and Stable Fund Balances Support Sector's Stability \(March 2016\)](#) which is available on Moodys.com. The medians presented here are based on the key metrics outlined in Moody's GO methodology and the associated scorecard.

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## **FITCH AFFIRMS MAUI COUNTY, HI'S GOS AT 'AA+'; OUTLOOK STABLE**

Fitch Ratings-San Francisco-17 February 2017: Fitch Ratings has affirmed the following Maui County, HI (the county) ratings at 'AA+':

--\$218.5 million outstanding general obligation (GO) bonds;  
--Issuer Default Rating (IDR).

The Rating Outlook is Stable.

### **SECURITY**

The bonds are payable from an unlimited property tax levied on all taxable property within the county's jurisdiction.

### **KEY RATING DRIVERS**

The 'AA+' IDR reflects the county's very strong revenue profile and adequate spending flexibility as reflected by its excellent operating performance. Its long-term liability burden is moderate given the lack of overlapping debt.

#### **Economic Resource Base**

The county serves a population of approximately 160,000 (11% of the state total) on the islands of Maui, Molokai, and Lanai and the uninhabited island of Kahoolawe. The county's growing economy remains highly concentrated in the tourism sector, with hotels and resorts accounting for most major employers and taxpayers. However, Maui's tourism sector has maintained a strong fundamental base despite volatility associated with economic cycles. Median household income is high at 25% above the U.S. average, and unemployment is consistently below average.

#### **Revenue Framework: 'aaa' factor assessment**

The resource base consists primarily of property tax revenues, which have exhibited low volatility due in part to the county's ability to adjust rates. The county has the unlimited legal ability granted under the state constitution to set and adjust property tax rates. Strong revenue growth has exceeded that of U.S. economic performance, a trend that Fitch expects to continue.

#### **Expenditure Framework: 'aa' factor assessment**

The county has adequate spending control and the natural pace of spending growth is generally in line with that of revenues. Carrying costs are moderate and the pace of spending is expected to generally be in line with revenue growth.

#### **Long-Term Liability Burden: 'aa' factor assessment**

Long-term liabilities are moderate in relation to the county's resource base.

#### **Operating Performance: 'aaa' factor assessment**

The county's financial resilience is strong, and reserves are high given historical revenue volatility and strong budget flexibility. Budget management during the economic expansion has been solid with the county setting aside reserves to address long-term liabilities.

### **RATING SENSITIVITIES**

**Expenditure Management:** The IDR is sensitive to maintenance of the county's solid expenditure flexibility. Material reductions in the county's ability to manage spending, including unexpected increases in fixed carrying costs for debt and retiree benefits, could pressure the rating.

## CREDIT PROFILE

Tourism remains the chief engine of the county's economy despite increasing diversification. Approximately one-third of county employment is in the leisure and hospitality sector. Resort and time-share properties account for four of the county's top 10 employers and nine of its top 10 taxpayers. Both visitor arrivals and expenditures have recovered from the great recession and are above prior peaks.

### Revenue Framework

Property taxes account for more than 80% of revenues. The county's share of the statewide transient accommodation tax (TAT) provides the county's second largest source of revenue (8% of general fund revenues), but growth is limited by a state cap on allocations to counties.

Revenue growth has been strong, above both the U.S. economic performance and inflation, and Fitch expects this strength to continue given economic fundamentals. Property tax rates have been regularly adjusted by the county. While assessed value (AV) fell a cumulative 25% between fiscal 2010 and 2013, the property tax levy fell by just 8% during the same period, as the council approved recurring tax rate hikes. An additional rate hike in fiscal 2014 was followed by reductions for fiscals 2015 through 2017, as renewed AV growth supported increased tax revenues.

Under the state constitution, all functions, powers and duties relating to taxation of real property are vested in the counties. The rate and classification of real property taxes are reviewed annually as part of the county's budget process. The county's tax structure also provides for large homeowner exemptions and differential rates for the 11 categories of property type. Property tax rate increases have met minimal political opposition.

### Expenditure Framework

Public safety accounts for about one-third of spending, with general government accounting for about 40%.

Spending is expected to be in line with revenue growth, which is likely to continue to be above U.S. economic performance.

Carrying costs for debt service, pension contributions, and contributions related to other post-employment benefits (OPEB) are moderate at about 19% of spending. This metric includes funding of the OPEB annually required contribution (ARC), which the county has been contributing for several years. Carrying costs would be about 16% including just the paygo portion of OPEB. Labor contracts and terms are negotiated at the state level. As such, the county has limited ability to adjust or set terms beyond layoffs/furloughs.

### Long-Term Liability Burden

The county's long-term liability burden, including overall debt and pension liability, is moderate at 11% of personal income. The county has no overlapping debt, as public education is the responsibility of the state. Further, amortization of existing debt is rapid, with about 75% of principal repaid within 10 years. The county's net direct debt totaled \$32 million at fiscal 2016 year-end.

The six-year capital improvement plan (CIP) is sizeable at \$1 billion and reflects the broad responsibilities of county government in Hawaii. Much of the plan focuses on water, sewer,

and road projects financed through non-general fund sources. The county expects to issue approximately \$25 million in general fund-backed bonds in fiscal 2018, which Fitch does not expect to meaningfully impact the debt burden given the relatively modest amount and rapid amortization rate.

The county participates in the Hawaii Employees' Retirement System (ERS), which has a ratio of assets to liabilities of about 58.3% adjusted to a 7% return on investment. The county's net pension liability stands at about \$381 million, or 6.5% of personal income.

The county continues to address its OPEB liability and, has funded its actuarially-determined ARC for such benefits since fiscal 2008, well in advance of a state requirement for full funding by fiscal 2019. In addition, it contributed \$78 million above the ARC in fiscal 2014. As a result, the funded ratio was 33.4% as of July 1, 2015; however, the liability remains high at about \$297 million, or 4% of personal income.

#### Operating Performance

Given high budget flexibility and relatively low historical revenue volatility, Fitch believes the county's financial resilience in a moderate economic contraction would be high. Historical sensitivity of revenues to economic decline is somewhat understated due to the county's periodic adjustment of property tax rates. The county has maintained reserves in excess of 23% for the past three years, down from over 60% due to the large contribution to its OPEB liability in fiscal 2014. A 2012 deficit resulted from the planned drawdown of reserves for one-time purposes.

The county has maintained conservative budget management during the recovery, including paying down of some of its OPEB liability with reserves and continuing to pay the OPEB ARC.

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Additional information is available at '[www.fitchratings.com](http://www.fitchratings.com)'.

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.

## Applicable Criteria

U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)

<https://www.fitchratings.com/site/re/879478>

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