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Summary:

Dayton, Texas; General Obligation

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Summary:

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Credit Profile		
US$7.155 mil GO rfdg bnds ser 2016		
Long Term Rating	AA-/Stable	New
Dayton GO		
Long Term Rating	AA-/Stable	Affirmed
Dayton GO		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rationale

S&P Global Ratings assigned its 'AA-' long-term rating to Dayton, Texas' series 2016 general obligation (GO) refunding bonds. At the same time, we affirmed our 'AA-' long-term rating and underlying rating (SPUR) on the city's parity GO bonds and the city's series 2015 combination tax and limited pledge revenue certificates of obligation. The outlook on all ratings is stable.

The 2016 bonds are payable from a limited ad valorem tax levied on all taxable property in Dayton. The state maximum for city tax rates is $2.50 per $100 of assessed value (AV): The city is currently levying 68 cents per $100 of AV, well under the state cap. Due to the remaining flexibility under the state cap, coupled with the city's rating level, we rate the series 2016 GO bonds under our limited-tax GO criteria; however, we are not making a distinction compared to the unlimited-tax GO pledge. We understand officials intend to use series 2016 bond proceeds to refund debt outstanding for annual debt service savings purposes.

The series 2015 certificates of obligation are secured by ad valorem taxes, limited by law to $2.50 per $100 of AV and levied against all taxable property in the city. In addition, a limited pledge of $1,000 of the net revenues of city's water and sewer system provide support to the bonds.

The 'AA-' rating reflects our assessment of the following factors for the city, specifically its:

- Weak economy, with access to a broad and diverse metropolitan statistical area (MSA), yet a concentrated local tax base;
- Adequate management, with "standard" financial policies and practices under our financial management assessment (FMA) methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2015;
- Very strong budgetary flexibility, with a high available fund balance in fiscal 2015 at 122% of operating expenditures;
- Very strong liquidity, with total government available cash at 1.5x total governmental fund expenditures and 5.4x

governmental debt service, as well as access to external liquidity we consider strong;
- Weak debt and contingent liability position, with debt service carrying charges at 27.8% of expenditures, net direct debt at 216.5% of total governmental fund revenue, but rapid amortization, with 66.7% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Weak economy

We consider Dayton's economy weak. The city, with an estimated population of 7,454, is roughly 40 miles northeast of downtown Houston in southwest Liberty County. It is in the Houston-The Woodlands-Sugar Land MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 89.7% of the national level and per capita market value of $100,605. Overall, market value grew by 4.9% over the past year to $749.9 million in 2016. Weakening Dayton's economy is a concentrated local tax base, with the 10 largest taxpayers accounting for 46.7% of the total tax base. The county unemployment rate was 6.9% in 2014.

The city's tax base concentration is primarily caused by Dayton's significant oil and gas industry presence. Four of the top five taxpayers are directly related to that industry and account for approximately 37% of the total tax base. Each of these taxpayers are in the petrochemical products and polymers, however, which is somewhat shielded from the current price of oil. City officials indicate limited effects related to the current decline in oil and gas prices outside of a reduction in sales tax revenues.

The city's tax base has continued to see positive growth over the past two years, averaging 7% each year. With a number of developments currently underway that include new neighborhoods and new office space, officials indicate that annual growth projections are for 3%-4% each year from now on. Currently, the largest local employers are Dayton Independent School District, a wire products company called Global Tubing, and the city itself.

Adequate management

We view the city's management as adequate, with "standard" financial policies and practices under our FMA methodology, indicating the finance department maintains adequate policies in some, but not all, key areas.

Key management policies include formalized investment management that requires monthly reporting of holdings and earnings to the board, and a formal fund balance policy stating a minimum available reserve balance equal to three months of operating expenditures, or currently roughly $1.5 million, or 25% of fiscal 2015 expenditures. The city council is updated monthly regarding budget performance, with amendments made on an as-needed basis throughout the year. The city's capital plan only looks out four years as of the fiscal 2016 budget year and identifies funding to be from the budget each year. The city lacks formal policies related to GO-backed debt and does not engage in long-term financial planning.

Strong budgetary performance

Dayton's budgetary performance is strong, in our opinion. The city had operating surpluses at 10.5% of expenditures in the general fund and 2.4% across all governmental funds in fiscal 2015. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from 2015 results in the near term.

The city typically budgets for the use of some reserves in its budget. For fiscal 2015, it ended with close to break-even results, the slight deficit being the result of a transfer out of the general fund for $650,000. After adjusting for this one-time transfer for capital, the general fund posted a 10% surplus.

For fiscal 2016, the city is projecting a deficit of roughly $100,000, following declines in sales tax revenues for the year, which would result in a general fund operating result of negative 1.1% of expenditures. Given this and the expectation for more modest operating performance for fiscal 2017 following some pullback in sales tax revenues, we have adjusted our budgetary performance to strong from very strong. Management states that sales tax declines for fiscal 2016 have partially been offset by the majority of expenditures remaining below budget to this point. Sales tax revenues represent roughly 30% of the city's general fund revenue, while property taxes account for just over 50%.

Despite the expected continuation of sales tax revenue declines, we believe the city will manage its financial performance in a way that will not significantly affect its available reserves or lead to a reduction in reserves below what we consider very strong. Additionally, the city's reliance on property tax revenues as its major general fund revenue source provides a level of financial performance stability.

Very strong budgetary flexibility

Dayton's budgetary flexibility is very strong, in our view, with a high available fund balance in fiscal 2015 at 122% of operating expenditures, or $7.2 million. We expect the available fund balance to remain above 75% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

We believe budgetary flexibility will remain very strong for the next two fiscal years. For fiscal 2016, the city is projecting a decline in total fund balance of roughly $100,000, following declines in sales tax revenues for the year. It does not currently plan for any significant spending in fiscal 2017. The city maintains reserves well in excess of its informal fund balance policy minimum of $1.5 million, or roughly 25% of fiscal 2015 expenditures and three months of operating expenditures.

Despite the expected continuation of sales tax revenue declines, we believe the city will manage its financial performance in a way that will not significantly affect its available reserves or lead to a reduction in reserves below what we consider very strong. Given that there are no plans to draw down on current reserves, we expect reserves to remain at a level in excess of 75% of expenditures.

Very strong liquidity

In our opinion, Dayton's liquidity is very strong, with total government available cash at 1.5x total governmental fund expenditures and 5.4x governmental debt service in 2015. In our view, the city has strong access to external liquidity if necessary.

The city demonstrates its strong access to external liquidity through its access to the market within the past 20 years and issuance of mainly tax-backed bonds. It has historically had what we consider very strong cash balances; we do not believe its cash position will worsen over the next two fiscal years. Currently, all investments comply with state guidelines; we do not consider them aggressive. At Sept. 30, 2015, the city's investments were primarily in money market accounts and certificates of deposits.

Weak debt and contingent liability profile

In our view, Dayton's debt and contingent liability profile is weak. Total governmental fund debt service is 27.8% of total governmental fund expenditures, and net direct debt is 216.5% of total governmental fund revenue.

Approximately 66.7% of the direct debt is scheduled to be repaid within 10 years, which is, in our view, a positive credit factor.

Though there are no concrete plans for additional new money at this time, officials indicate that they could potentially issue $3 million to $7 million for capital needs next year.

Dayton's combined required pension and actual other postemployment benefit (OPEB) contributions totaled 2.7% of total governmental fund expenditures in 2015. The city made its full annual required pension contribution in 2015.

The city provides pension benefits for all full-time employees through the statewide Texas Municipal Retirement System (TMRS), a multiemployer, public employee retirement system. The city's required pension contribution is its actuarially determined contribution, which was $217,000 in fiscal 2015. Under state law governing the TMRS, an actuary determines the contribution rate annually. The city has historically met required annual contributions.

Using updated reporting standards in accordance with Governmental Accounting Standards Board (GASB) Statement No. 67, the city's net pension liability was $443,838 as of Dec. 31, 2014. The plan was 92.69% funded based on its net position as a percent of the total pension liability. (For additional details on GASB Nos. 67 and 68, please see our report, titled "Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria," published Sept. 2, 2015, on RatingsDirect.)

The city also participates in the cost-sharing, multiemployer, defined-benefit, group-term life insurance plan operated by TMRS known as the supplemental death benefits fund; these costs, however, are minimal compared to overall expenditures.

Strong institutional framework

The institutional framework score for Texas municipalities is strong.

Outlook

The stable outlook reflects our opinion that Dayton's economy will likely remain weak due to below-average wealth and incomes, but that ongoing economic activity will likely foster steady tax base growth despite sales tax declines. The outlook also reflects our expectation that the city will likely continue to demonstrate very strong budgetary flexibility and liquidity during a period of potential sales tax revenue volatility. Due to this, we do not expect to change the rating during the outlook's two-year period.

Upside scenario

Assuming all other rating factors remain stable or improve, we could raise the rating if economic growth were to lead to materially improved wealth and income more in line with the city's higher rated peers, assuming all other rating factors remain stable or improve.

Downside scenario

We could lower the rating if reserves were to deteriorate significantly to a level we no longer consider very strong, following either an ongoing structural imbalance or planned use of reserves for capital.

Related Criteria And Research

Related Criteria

- USPF Criteria: Local Government GO Ratings Methodology And Assumptions, Sept. 12, 2013
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Limited-Tax GO Debt, Jan. 10, 2002
- USPF Criteria: Methodology: Rating Approach To Obligations With Multiple Revenue Streams, Nov. 29, 2011
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- Institutional Framework Overview: Texas Local Governments

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings public website at www.standardandpoors.com. Use the Ratings search box located in the left column.