S&P Global Ratings

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Summary:

Morris County, New Jersey; General Obligation

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Credit Profile		
US$21.865 mil gen imp bnds ser 2018 due 01/15/2028		
Long Term Rating	AAA/Stable	New
US$3.3 mil cnty coll bnds ser 2018 due 01/15/2028		
Long Term Rating	AAA/Stable	New
US$1.715 mil pk bnds ser 2018 due 01/15/2026		
Long Term Rating	AAA/Stable	New

Rationale

S&P Global Ratings assigned its 'AAA' long-term rating and stable outlook to Morris County, N.J.'s series 2018 general obligation (GO) bonds, consisting of general improvement bonds, park bonds, and county college bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating and stable outlook on the county's previously issued GO debt.

Morris County's full faith and credit pledge and its agreement to levy ad valorem property taxes without limitation as to rate or amount secure the series 2018 bonds and its GO debt outstanding. We understand county officials intend to use proceeds from the series 2018 bonds to finance various capital and park improvements in the county and county college projects at the County College of Morris.

Morris' GO bonds are eligible to be rated above the sovereign because we believe the county can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect), Morris has a predominantly locally derived revenue source, with almost two-thirds of current fund revenue coming from property taxes. The county also has independent taxing authority and independent treasury management from the federal government.

The ratings reflect our assessment of the following factors, including our view of the county's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with "strong" financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with balanced operating results in the general fund in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 15% of operating expenditures, and the flexibility to raise additional revenues despite statewide tax caps;
- Very strong liquidity, with total government available cash at 28.0% of general fund expenditures and 2.3x governmental debt service, and access to external liquidity we consider strong;

- Adequate debt and contingent liability profile, with debt service carrying charges at 12.0% of expenditures and net direct debt that is 101.8% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 95.4% of debt scheduled to be retired in 10 years, but a large pension and other postemployment benefit (OPEB) obligation; and
- Strong institutional framework score.

Very strong economy

We consider Morris County's economy very strong. With an estimated population of 500,000, the county is located in the New York-Newark-Jersey City MSA, which we consider broad and diverse. It has a projected per capita market value of $188,068 and per capita effective buying income of 174% of the national level, indicators of the county's wealth and income levels. Overall, the county's market value grew by 1.7% over the past year to $94.2 billion in 2017. The county's average unemployment rate was 3.6% in 2017, which was below the state's (4.2%) and the nation's (4.4%) averages.

Morris County is an affluent and suburban county in the center of northern New Jersey, about 25 miles from New York City. Tax base composition is primarily composed of singe- and multi-family residential (79.7% of assessed value [AV]), commercial (14.7%), and industrial (3.5%) properties. The county's taxable base has grown by approximately 6.75% over the last five years, supported by a balanced mix of property value appreciation and new developments in the area.

A developed network of rail and highways traverses the county, connecting residents to regional employment opportunities in the greater New York City and Northern New Jersey metropolitan area. In addition, the county features a diverse local employment base, anchored by the headquarters of several large industries, healthcare providers, and pharmaceutical firms. The county's leading employers include the U.S. Army Armament Research and Development Center (6,400 employees), Atlantic Health System (6,350), Novartis Corporation (4,607), Bayer Healthcare, LLC (2,800), and ADP, Inc. (2,242). Despite the presence of sizable pharmaceutical and industrial firms, the 10 leading taxpayers account for approximately 2% of AV, which we consider very diverse.

Although limited vacant, but developable land remains in the county, officials report that it has benefited from infill redevelopment, mixed-use developments, and expansion of available office space. Notable new developments include a mixed-use development that will feature 139 townhomes, 295 apartments, retail, and a hotel; a 214-unit complex in Dover; and a 185-unit apartment complex in Morristown. Officials also note that several new commercial developments will generate thousands of new jobs and over 1 million square feet of new office and retail space. Based on the county's very strong wealth and income conditions, coupled with potential for substantial growth over the coming years, we do not expect to modify our view of its economic profile in the next two years.

Very strong management

We view the county's management as very strong, with "strong" financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable. The revised assessment of management -- to very strong from strong -- reflects management's adoption of a formal reserve policy that established a minimum unreserved fund balance (carry forward) and reserves at 12% of current fund expenditures. It also reflects the county's approval of a comprehensive debt policy that sets forth governance and measurability standards for managing existing and future debt obligations.

In developing its annual budget, management reviews historical trends and considers forward-looking projections when arriving at revenue and expenditure assumptions. According to management, it bases its budget on conservative revenue projections and the county works closely with underlying communities to identify budgetary changes and prioritize expenditures. Furthermore, the county's formal cash management policy governs investments, which officials report monthly.

During each fiscal year, county finance officials monitor budget-to-actual results closely, providing monthly budget reports to the county's freeholder board and posting this information on its website. Amendments, while infrequent, can occur through emergency appropriations and transfers, as permitted under statute. The county has a formal six-year capital improvement plan with all sources identified; it updates the plan annually. In addition, Morris maintains formalized, five-year financial projections that the governing body reviews and updates annually. These projections are integrated into the budget planning process and can take into account different financial scenarios and the effect on the budget.

Strong budgetary performance

Morris County's budgetary performance is strong, in our opinion. The county had balanced operating results in the current fund of negative 0.2% of expenditures in fiscal 2017. Current fund operating results have been stable over the last three years, with a result of 0.1% in 2016 and a result of 0.0% in 2015.

Morris has a history of conservative budgeting and balanced financial operations. Before fiscal 2015, the county had generated current fund surpluses in the previous four fiscal years. In fiscal 2015, it drew down reserves by $7.3 million primarily because of the use of $7.0 million relating to the settlement of litigation associated with the developer of solar projects constructed in the past few years. Excluding this one-time expense, the county's operations were balanced.

The county achieved almost balanced results in fiscal 2017, regenerating almost all the $25.3 million of reserves it appropriated in the budget. Officials attribute the slight negative current fund result to anticipated one-time costs and lower-than-budgeted state aid revenue for patients in county medical institutions, as the county transitioned its operation of the Morris View Healthcare Center to a private operator that will lease the county-owned facility, effective Nov. 1, 2017. However, the county anticipates that this decision will likely produce savings that support operating flexibility and expenditure predictability to address other strategic initiatives in future budgets.

The adopted fiscal 2018 budget, totaling $305.8 million, includes a tax levy increase of 1.79%. The increase includes exceptions to the property tax for allowable debt service, health care costs, and pension increases, demonstrating Morris' willingness to align revenues with expenditures to maintain structural balance. At the same time, the significant $31.1 million decrease in the current fund reflects the difference in the budget following the transition of operations for the Morris View Healthcare Center. While the budget includes a fund balance appropriation of $25.3 million, in line with that of previous years, officials report they expect to replenish these funds and have close to balanced results. In addition, management conservatively estimates the aggregate fund balance will be between $48 million and $53 million at year-end.

Property and other county purpose taxes, the main revenue source, generated about 67% of current fund revenue in fiscal 2017. The underlying municipalities guarantee the county 100% of property tax collections, providing additional stability. Given the county's history of maintaining structurally balanced operations, coupled with overall strong budget planning and management of current year finances, we generally expect budgetary performance to remain strong.

Very strong budgetary flexibility

Morris County's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 15% of operating expenditures, or $52.7 million. Over the past three years, the total available fund balance has remained at a consistent level overall, totaling 14.7% of expenditures in 2016 and 16% in 2015. In addition, the county has the flexibility to raise additional revenues despite statewide tax caps, which we view as a positive credit factor.

Morris has a history of maintaining strong-to-very strong available current fund balances. In fiscal 2015, management used about $7.0 million of reserves in connection with the settlement of litigation associated with its solar renewable energy program. Despite this, current fund reserves remained above 15% of expenditures at fiscal year-end. The fiscal 2017 surplus decreased available reserves to $52.7 million, but they were[?] up slightly as a percentage of fiscal 2017 expenditures.

In addition to the county's uncommitted reserves, officials said they have dedicated reserves for accumulated absences, storm recovery (snow removal), and other purposes, which they would turn to first to meet qualifying costs above budgeted amounts. Including these additional reserves of almost $8.8 million brings total noncapital reserves to about 17.7% of 2017 current fund expenditures.

Furthermore, Morris can raise its tax levy by 2% annually, not including allowable exceptions, which officials have been willing to use to maintain balanced operations. In addition, the county had about $8.5 million of banked levy capacity available for the 2019 budget, which provides it additional flexibility to raise revenues. However, given the rolling nature of the levy bank cap and reductions to banked cap seen recently year over year, should we no longer view banked cap amounts as providing sufficient additional financial flexibility, our view of the county's flexibility could weaken.

The adopted fund balance policy governs decisions about minimum reserve levels, permitting the use of reserves, and recovery plans for when drawdowns are required. Therefore, we expect reserves will remain strong despite the use of fund balance appropriations in the budget because we generally expect the county will continue to appropriate no more than it anticipates regenerating during the year.

Very strong liquidity

In our opinion, Morris County's liquidity is very strong, with total government available cash at 28.0% of general fund expenditures and 2.3x governmental debt service in 2017. In our view, the county has strong access to external liquidity if necessary.

Morris does not invest aggressively and is not exposed to variable-rate or privately placed debt. Current holdings are largely in bank deposits. The county maintains what we view as strong access to external liquidity, with long-term GO bond issuances in the past 20 years. Management indicates it does not expect to materially draw down total cash, so we expect liquidity to remain very strong.

Adequate debt and contingent liability profile

In our view, Morris County's debt and contingent liability profile is adequate. Total governmental fund debt service is 12.0% of total governmental fund expenditures, and net direct debt is 101.8% of total governmental fund revenue. Overall net debt is low at 0.9% of market value, and approximately 95.4% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

In accordance with debt service goals in its adopted debt management policy, Morris actively manages its capital needs and anticipates issuing $25 million-$28 million a year in debt, depending on market conditions and identification of critical infrastructure needs. We have factored this into our analysis and do not anticipate any material changes to the county's debt profile. Morris also maintains capital reserves of almost $12.4 million that could be used to offset project costs. As well, the county guarantees debt issued through the Morris County Improvement Authority, which we have included in our analysis.

In our opinion, a credit weakness is Morris County's large pension and OPEB obligation. The county's combined required pension and actual OPEB contributions totaled 10.3% of general fund expenditures in 2017. Of that amount, 4.2% represented required contributions to pension obligations, and 6.0% represented OPEB payments. The county made its full annual required pension contribution in the last three audited fiscal years. While Morris is managing these costs, we believe it has limited ability to control the liabilities' growth and, concerning its OPEB obligation, has no mechanism for prefunding its share of them.

The county participates in the cost-sharing multiple-employer Police and Firemen's Retirement System (PFRS) and Public Employees' Retirement System (PERS) pension plans, as defined by the Governmental Accounting Standards Board (GASB). Both PFRS and PERS are, in our view, significantly underfunded. The plan fiduciary net position as a percentage of the total pension liability, as defined in GASB Statement No. 67, was 48.55% for PFRS and 31.20% for PERS as of June 30, 2016. This is a result of numerous years of underfunding by the state, aggressive assumptions, and weak market performance. Under current funding assumptions, PERS is projected to be exhausted by 2034, and PFRS by 2050. This projection is based on a discount rate of 7.65%, the Buck modified mortality projection table, and the projected unit credit actuarial methodology, all of which we consider somewhat aggressive. The state lowered its return assumption to 7.65% from 7.9% in 2016 and is phasing in a reduction to 7.00% over the next five years, a change that while positive in that it lowers the system's reliance on investment returns, will also result in higher contributions for local government units. In fiscal 2017, the county made its portion of the actuarially determined contribution of $5.6 million for PFRS and $9.2 million for PERS.

Although assets and liabilities are separated between local and state employers when calculating the local government's contribution, these are cost-sharing systems as defined by GASB and, therefore, there is no legal separation. Assets are in a common pool and all employer contributions go to this pool. Benefits are paid to plan retirees regardless of whether the corresponding employer fully paid its contribution. Given that the state has not fully funded its contribution requirement for over a decade for either plan, we believe local government annual pension contributions might increase if assets allocated to the state for funding calculations become depleted. Legislation passed in 2017 transfers lottery revenue to PERS, PFRS, and the Teachers' Pension and Annuity Fund , and changes the timing of pension funding payments from end-of-year to quarterly. We believe this legislation will have a moderately positive effect in that the state should no longer be able to completely abstain from making contributions.

However, paying 100% of the actuarially determined contribution into the plans would mitigate the risk of becoming increasingly underfunded. Furthermore, to the extent that the overall system becomes increasingly underfunded, experiences negative cash flows, or needs to revise its return assumptions downward, local governments could face increasing contributions.

Morris also offers OPEB to certain eligible retirees, which it funds on a pay-as-you-go basis. No mechanism allows for prefunding this liability, limiting the county's ability to plan for these costs. Therefore, the unfunded actuarial accrued liability as of Dec. 31, 2017 was $1.16 billion. However, Morris has negotiated to eliminate these benefits for new employees in 18 of its 20 labor contracts, and thus, it expects these liabilities to decline in the future.

The county includes projections for pension and OPEB costs in its financial forecasts, taking actions in current budgets that will allow it to maintain structural balance in the future. Morris has been willing to use levy cap exemptions for increasing pension costs. Given the county's history of managing these costs and proactive financial forecasting, we generally expect officials to maintain balanced operations despite the rising costs associated with these liabilities.

Strong institutional framework

The institutional framework score for New Jersey counties is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion of Morris' very strong and diverse economy and ability to withstand economic downturns while continuing to significantly increase property tax base growth and keep unemployment low. The outlook also reflects our assessment of the county's history of strong-to-very strong budgetary performance, budgetary flexibility, and liquidity. For these reasons, we do not expect to lower the rating within the outlook's two-year period. However, if budgetary pressures from sources such as rising pension and OPEB costs were to cause performance deterioration and draws on reserves, we could lower the rating.

Related Research

- 2017 Update Of Institutional Framework For U.S. Local Governments
- 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
- Local Government Pension And Other Postemployment Benefits Analysis: A Closer Look, Nov.8, 2017

Ratings Detail (As Of June 8, 2018)		
Morris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed
Morris Cnty GO		
Long Term Rating	AAA/Stable	Affirmed

Ratings Detail (As Of June 8, 2018) (cont.)		
Morris Cnty Imp Auth, New Jersey		
Morris Cnty, New Jersey		
Morris Cnty Imp Auth (Morris Cnty) GO		
Long Term Rating	AAA/Stable	Affirmed

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.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.