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**Summary:**

# Frisco, Texas; General Obligation

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## Table Of Contents

## Summary:

# Frisco, Texas; General Obligation

| Credit Profile | | |
|---|---|---|
| US$70.415 mil GO rfdg and imp bnds ser 2019 dtd 06/15/2019 due 02/15/2039 | | |
| *Long Term Rating* | AAA/Stable | New |
| US$16.725 mil comb tax and surplus rev certs of oblig ser 2019B dtd 06/15/2019 due 02/15/2039 | | |
| *Long Term Rating* | AAA/Stable | New |
| US$9.37 mil comb tax and surplus rev certs of oblig ser 2019A dtd 06/15/2019 due 02/15/2039 | | |
| *Long Term Rating* | AAA/Stable | New |

## Rationale

S&P Global Ratings assigned its 'AAA' rating to Frisco, Texas' series 2019 improvement bonds, combination tax and surplus revenue certificates of obligation, and taxable combination tax and surplus revenue certificates. At the same time, S&P Global Ratings affirmed its 'AAA' rating on the city's parity general obligation (GO) bonds and certificates of obligation outstanding. The outlook is stable.

S&P Global Ratings' highest rating of 'AAA' reflects continued strength within the local economy that benefits from the greater Dallas-Fort Worth metropolitan statistical area (MSA), good fiscal management practices that yield positive results, and consistently very strong reserve levels that have grown commensurate with the overall budget. Despite a high debt profile that is somewhat reflective of significant market value growth, and the need to manage a large and steady increase in service demand and infrastructure needs, the city's key credit metrics and financial flexibility are reflective of our highest rating category.

The bonds and certificates are payable from a direct annual ad valorem tax levied, within the limits prescribed by law, on all taxable property located within the city. The certificates are further secured by a pledge of the surplus net revenues of the city's waterworks and sewer system. Given the limited revenue pledge of the water system, we rate the certificates based solely on the limited tax pledge. State statutes limit the maximum ad valorem tax rate for home rule cities to $2.50 per $100 of taxable assessed valuation for all city purposes. The Texas attorney general permits the allocation of $1.50 of the $2.50 maximum tax rate for ad valorem tax debt service. Frisco levies 44.66 cents, of which 15.3233 cents is dedicated to debt service and 29.333674 cents to operations. Based on the application of our criteria, "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness," (published Jan. 22, 2018), we do not differentiate between the city's limited-tax GO debt and its general creditworthiness, since the ad valorem tax is not derived from a measurably narrower tax base and there are no limitations on the fungibility of resources.

Frisco's debt outstanding is eligible to be rated above the sovereign because we believe the city 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), U.S. local governments are considered to have moderate sensitivity to country risk. The city's GO pledge is the primary source of security on the debt; this severely limits the possibility of negative sovereign intervention in the payment of the debt or in the operations of the city. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy, independent treasury management, and no history of government intervention. Frisco has considerable financial flexibility, as demonstrated by the very high general fund balance as a percent of expenditures, as well as very strong liquidity.

Proceeds of the sale of the 2019 bonds will be used for constructing, improving and equipping public safety facilities, and purchasing public safety equipment. The proceeds will also be used for streets and roads; the public works facility, including equipment and technology; municipal libraries; and the George A. Purefoy Municipal Center.

Proceeds from the sale of the 2019A certificates will be used to pay contractual obligations incurred by the city for water, sewer, and water reuse infrastructure improvements.

Proceeds from the sale of the 2019B certificates will be used for acquiring, constructing, and equipping a public conference center, and meeting and exhibit center.

The rating reflects our opinion of the city's:

- Very strong economy, with access to a broad and diverse MSA;
- Strong management, with good 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 2018;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2018 of 42% of operating expenditures;
- Very strong liquidity, with total government available cash at 39.6% of total governmental fund expenditures and 1.6x governmental debt service, and access to external liquidity we consider strong;
- Very weak debt and contingent liability profile, with debt service carrying charges at 25.0% of expenditures and net direct debt that is 257.2% of total governmental fund revenue; and
- Strong institutional framework score.

## Very strong economy

We consider Frisco's economy very strong. The city, with an estimated population of 190,620, is located in Collin and Denton counties in the Dallas-Fort Worth-Arlington MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 170% of the national level and per capita market value of $153,978. Overall, the city's market value grew by 10.6% over the past year to $29.4 billion in 2019. The weighted-average unemployment rate of the counties was 3.3% in 2018.

Located about 30 miles north of downtown Dallas, Frisco continues to experience rapid development, and is one of the fastest-growing cities in the region. The tax base is primarily made up of single-family residential properties (64% of the total tax base), commercial properties (16%), multi-family residential properties (6%), and acreage (5%). The top 10 taxpayers make up a modest 5% of the total tax base and include a shopping mall, several retail developments, an entertainment complex, apartment complex, and hospital. Frisco is home to several national corporate headquarters.

Several hospitals have also recently expanded operations in the city. In addition to the school district, leading employers are associated with pharmaceutical distribution, health care management, telecommunications, and information technology. Operations at other large developments, such as the Star and Texas Scottish Rite Hospital for Children, remain stable.

Keurig Dr Pepper's new Frisco headquarters, announced in February 2019, is under construction. The projected 350,000-square-foot office building is being built next to the Dallas Cowboys' facility at The Star and will be home to over 1,000 employees. Massachusetts-based Keurig Green Mountain Inc. recently purchased Dr Pepper Snapple Group Inc. The company will maintain dual headquarters in both states.

Residential growth is also strong in the city and resident wealth levels have historically remained above average. Given ongoing and future expected development, we anticipate continued stable growth and for the local economy to remain very strong.

### Strong management

We view the city's management as strong, with good financial policies and practices under our FMA methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis.

Financial management practices include the use of at least five years of historical trend analysis in developing revenue and expenditures assumptions for budgeting purposes. Officials provide monthly budget-to-actual reports to the city council and can amend the budget on an ad hoc basis. Frisco maintains a five-year capital improvement plan (CIP), which is updated annually. The city's CIP coincides with its bond program. The city uses a multi-year financial forecast where future issues are identified, and revenue and expenditure decisions are made from a long-term perspective. The council has adopted a formal investment management policy that it reviews and approves annually. Management also provides the city council with quarterly investment holdings and returns. While Frisco has a debt management policy and has implemented new enhancements, in our view, the policy is not overly restrictive in nature. The city also maintains a formal reserve policy of 25% of operating expenditures, which it exceeds.

### Strong budgetary performance

Frisco's budgetary performance is strong, in our opinion. The city had operating surpluses of 4.2% of expenditures in the general fund and of 14.4% across all governmental funds in fiscal 2018.

A solid trend of steady growth in revenues and positive fiscal performance is a key credit positive for the city. In 2018, general fund revenues were primarily derived from property taxes (46%), sales taxes (27%), licenses and permits (8%), and franchise taxes (6%). General fund revenues (following analytical adjustments for transfers in and out of the general fund) increased to $160 million from $151 million in the previous year. Solid revenue collections over budget, close monitoring of expenditures, and other positive budget variances aided the strong budgetary performance for the year. Officials report the expected use of built-up reserves for one-time capital expenditures in 2019, but do not anticipate significant deterioration of overall reserves. Sales tax collections are trending slightly below budget in 2019, yet are still 3% higher than in the previous year. The city is monitoring collections to identify if there is any particular factor spurring more volatile collections in recent months. Officials also note recent state revenue cap legislation could potentially affect Frisco's budget. At this point, the extent to which the revenue cap would affect the city is unknown, but officials note cuts in discretionary spending could be used to balance future budgets. Given current year-to-date estimates and historical performance, we expect Frisco will sustain, at least, strong budgetary performance in the near term.

### Very strong budgetary flexibility

Frisco's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2018 of 42% of operating expenditures, or $64.3 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor. Over the past three years, the total available fund balance has remained at a consistent level overall, totaling 43% of expenditures in 2017 and 41% in 2016.

We expect that the city's budgetary flexibility will remain very strong and in excess of 30% of operating expenditures over the next two years. Stable and strong budgetary performance will allow for maintenance of very strong reserves over the near-to-medium term.

### Very strong liquidity

In our opinion, Frisco's liquidity is very strong, with total government available cash at 39.6% of total governmental fund expenditures and 1.6x governmental debt service in 2018. In our view, the city has strong access to external liquidity if necessary.

We anticipate the city's very strong cash position will remain solid over the next two years. All of Frisco's investments comply with Texas statutes and the city's investment policy. Investments are predominantly held in federal agency notes and rated investment pools, which we don't consider aggressive. Our opinion that the city maintains exceptional access to external liquidity is based on its history of issuing GO debt as well as having issued revenue debt in the past. The city does not have any direct-purchase agreements or privately placed debt that could pressure its liquidity.

### Very weak debt and contingent liability profile

In our view, Frisco's debt and contingent liability profile is very weak. Total governmental fund debt service is 25.0% of total governmental fund expenditures, and net direct debt is 257.2% of total governmental fund revenue.

The city's historically high debt profile is, in part, due to managing significant increases in service demand and population growth. We do not anticipate additional debt or Frisco's very high and weak debt profile will have a material effect on the city's overall credit quality. Plans for additional borrowing are expected in the next two years for various projects, as the city continues to manage in an environment of high growth and development. Frisco has no variable-rate debt nor any swaps outstanding.

Frisco's pension contributions totaled 4.8% of total governmental fund expenditures in 2018. The city made its full annual required pension contribution in 2018.

The city contributes to a nontraditional, joint contributory, hybrid defined benefit pension plan administered by the Texas Municipal Retirement System (TMRS). Under state law governing the TMRS, an actuary determines the contribution rate annually. The city recorded a net pension liability of $32.9 million and the plan reported a funded ratio of 86.5% in 2018, up from 80.7% in the previous year. The city does not provide postretirement health or dental care benefits to retirees. Retired employees are entitled to elect continuation coverage under Frisco's health insurance plan. However, they are responsible for 100% of the premium costs and this plan is not part of the city's active employee plan but included in a separate risk pool. Therefore, the city has no direct or implicit costs for retirees' health care coverage, which is detailed as the OPEB liability of $4.5 million, and no measurable other postemployment benefits liability.

### Strong institutional framework

The institutional framework score for Texas municipalities is strong.

## Outlook

The stable outlook reflects our expectation that the city will continue to benefit from its participation in the Dallas-Fort Worth-Arlington MSA, further supporting its very strong economic metrics. In addition, we anticipate that the city will sustain strong budgetary performance and very strong budgetary flexibility. Consequently, we don't anticipate changing the rating within the two-year outlook horizon.

### Downside scenario

We could lower the rating if the city's budgetary performance weakens, resulting in deterioration of its flexibility to levels no longer comparable with that of its peers. We could also lower the rating if the city's fixed-cost burden negatively affects or challenges its budgetary performance.

## Related Research

- 2018 Update Of Institutional Framework For U.S. Local Governments

| Ratings Detail (As Of June 12, 2019) | | |
|---|---|---|
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |

| Ratings Detail (As Of June 12, 2019) (cont.) | | |
|---|---|---|
| Frisco GO | | |
| *Long Term Rating* | AAA/Stable | Affirmed |
| **Frisco GO** | | |
| *Unenhanced Rating* | AAA(SPUR)/Stable | Affirmed |
| *Long Term Rating* | AAA/Stable | Affirmed |

Many issues are enhanced by bond insurance.

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.