

RatingsDirect®

Summary:

Ocean City, New Jersey; General Obligation

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Credit Profile

US\$38.8 mil gen imp bnds ser 2016 dtd 12/01/2016 due 11/15/2028

Long Term Rating AA/Stable New

Ocean City GO

Long Term Rating AA/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AA' long-term rating to Ocean City, N.J.'s series 2016 general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AA' rating on the city's existing GO debt. The outlook is stable.

The city's full faith and GO credit pledge secures the bonds. We understand proceeds from this issue will permanently finance Ocean City's bond anticipation notes maturing Dec. 2, 2016, and Jan. 6, 2017.

In our opinion, the rating reflects the city's:

- Strong economy, with projected per capita effective buying income at 153% and market value per capita of \$1.1 million, although a high county unemployment rate exceeding 10% limits this slightly;
- Strong management, with good financial policies and practices under our Financial Management Assessment methodology;
- Strong budgetary performance, with a slight operating surplus in the general fund in fiscal 2015;
- Strong budgetary flexibility, with an available fund balance in fiscal 2015 of 9.5% of operating expenditures;
- Very strong liquidity, with total government available cash at 18.8% of general fund expenditures and 128.6% of governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability position, with debt service carrying charges at 14.6% of expenditures and net direct debt that is 125.7% of general fund revenue, and a large pension and other postemployment benefit (OPEB) obligation, but low overall net debt at less than 3% of market value and rapid amortization, and with 83.8% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Strong economy

We consider Ocean City's economy strong. The city, with an estimated population of 11,297, is located in Cape May County. The city has a projected per capita effective buying income of 153% of the national level and per capita market value of \$1.1 million. Overall, the city's market value grew by 2.8% over the past year to \$12.0 billion in 2016. The county unemployment rate was 10.9% in 2015, which we consider high and a negative credit factor.

Ocean City is an island on the northern tip of Cape May County, 65 miles from Philadelphia; 130 miles from New York City; and 20 miles from Atlantic City, N.J. It serves as a regional beach destination for families in New Jersey, New York, Pennsylvania, Delaware, Maryland, and Washington, D.C., with a summertime population estimate that grows to

125,000-175,000.

The city's economy relies heavily on tourism. Residents can find employment in the region, including in one of the two commercial districts or Atlantic City.

Many residential properties are second homes. Ocean City's total assessed value has increased slightly, which officials attribute both to new residential development and renovations to existing properties.

Strong management

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

Management maintains good budgeting practices, including integrated long-term capital and financial planning. Ocean City develops its budget in coordination with department heads and the city council, incorporating two-to-three-year financial forecasts and historical trends. Management presents monthly reports on budget updates and investment holdings and returns to the city council. While there are no formal reserve or debt management policies, the city has been able to maintain reserve levels and works to keep debt levels low with rapid amortization by following adopted guidelines.

Strong budgetary performance

Ocean City's budgetary performance is strong in our opinion. The city had slight surplus operating results in the general fund of 0.8% of expenditures in fiscal 2015. General fund operating results have been stable over the past three years, with a result of 0.7% of general fund expenditures in 2014 and 0.5% in 2013.

Hurricane Sandy hit Ocean City in October 2012, bringing significant flooding and wind damage. The city, however, did not experience widespread catastrophic damage like other shore communities north of Atlantic City.

Ocean City issued \$3.6 million in special emergency notes in 2012 to fund damage repair related expenditures. While the permitted pay off period is five years, the city made its final payment of \$450,000 in 2016, a year ahead of the allowed timeframe. It credits its ability to manage the reimbursement process well for this.

The fiscal 2016 budget is using \$3.7 million in reserves. However, due to Ocean City's conservative budgeting practice, it is anticipating at least break-even operations with the potential to have a small surplus, which would go to the fund balance. While the city is just starting to plan its fiscal 2017 budget, we would expect the pattern of at least break-even operations to continue.

Strong budgetary flexibility

Ocean City's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2015 of 9.5% of operating expenditures, or \$6.9 million.

The city has been slowly-but-steadily increasing fund balance reserves since using it in 2012 for the Hurricane Sandy cleanup. Expectations for 2016 indicate no use of fund balance and the potential for a small increase coming from \$525,000 of unexpected revenues from new ratables. Although the city does have some banked levy capacity, at less than 3% of operating revenues, we do not consider this substantial enough to give additional budget flexibility.

Very strong liquidity

In our opinion, Ocean City's liquidity is very strong, with total government available cash at 18.8% of general fund expenditures and 128.6% of governmental debt service in 2015. In our view, the city has strong access to external liquidity if necessary.

We believe the city has strong access to external liquidity having issued GO bonds over the past 20 years. Management has confirmed it has no contingent liquidity risks from financial instruments with payment provisions that change upon the occurrence of some events. In addition, the city does not have any investments we deem aggressive.

Weak debt and contingent liability profile

In our view, Ocean City's debt and contingent liability profile is weak. Debt service is 14.6% of general fund expenditures, and net direct debt is 125.7% of general fund revenue. Overall net debt is low at 1.3% of market value, and approximately 83.8% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

We understand Ocean City does not have plans to issue additional debt in the next two years but does plan to issue \$108 million in fiscal years 2019 or 2020, in line with its long-term capital plan.

In our opinion, a credit weakness is Ocean City's large pension and OPEB obligation, without a plan in place that we think will sufficiently address it. The combined required pension and actual OPEB contributions totaled 9.7% of general fund expenditures in 2015. Of that, 5.7% represented required contributions to pension obligations, and 4.0% represented OPEB payments. The city made its full annual required pension contribution in 2015. We expect these costs to increase due to the low funded ratios of the state plans (38.21% for the Public Employees' Retirement System (PERS) and 52.84% for the Police and Firemen's Retirement System (PFRS) in fiscal 2015). OPEB is funded on pay-as-you-go basis. The OPEB plan's unfunded accrued actuarial liability is \$119 million, about 1.6x of the current fund revenues.

Strong institutional framework

The institutional framework score for New Jersey municipalities is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion of Ocean City's strong budgetary flexibility and good financial management, with consistent performance. We believe the city's diverse and sizable tax base and rapidly amortizing debt provide additional rating stability. Therefore, we do not expect to raise or lower the rating over the outlook's two-year period.

Upside scenario

If the city should improve its debt position or pension funding ratios improve, we could raise the rating.

Downside scenario

If budgetary performance were to weaken, causing reserve levels to decrease to levels we consider low or inadequate, we could lower the rating.

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: New Jersey 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.

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