

## CREDIT OPINION

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### New Issue

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## City of Mesquite, TX

New Issue: Moody's Assigns Aa2 to Mesquite, TX's Series 2016 GOLT and CO

### Summary Rating Rationale

Moody's Investors Service assigns a Aa2 to the City of Mesquite, TX's approximately \$40 million General Obligation Refunding and Improvement Bonds, Series 2016, and \$12.1 million Combination Tax and Limited Surplus Revenue Certificates of Obligation, Series 2016. At the same time, we affirm the Aa2 rating on \$35.2 million in previously issued debt.

The rating reflects the city's large tax base with recovering assessed values, following multiple years of softening. Additional considerations include lower than median wealth levels, satisfactory financial position, and a manageable debt profile.

### Credit Strengths

- » Strategic location within the Dallas-Fort Worth metropolitan area
- » Large tax base
- » Recent return to assessed valuation growth
- » Stable financial position

### Credit Challenges

- » Reserve levels are weaker than the national Aa2 median
- » Somewhat elevated debt ratios

### Rating Outlook

Outlooks are not usually assigned to local governments with this amount of debt outstanding.

### Factors that Could Lead to an Upgrade

- » Strong operating performance bolstering reserve levels
- » Continued economic activity that supports growth in assessed values; strengthened wealth indices

### Factors that Could Lead to a Downgrade

- » Reduction in reserves

- » Revenue failure of budget gaps that reduce current reserve levels
- » Contraction in local economy, reducing assessed values

## Key Indicators

Exhibit 1

Mesquite (City of) TX	2010	2011	2012	2013	2014
<b>Economy/Tax Base</b>					
Total Full Value (\$000)	\$ 6,005,488	\$ 5,683,237	\$ 5,619,670	\$ 5,475,557	\$ 5,464,027
Full Value Per Capita	\$ 42,950	\$ 40,632	\$ 40,155	\$ 39,044	\$ 38,422
Median Family Income (% of US Median)	93.7%	93.7%	90.4%	90.4%	90.4%
<b>Finances</b>					
Operating Revenue (\$000)	\$ 99,340	\$ 99,243	\$ 98,891	\$ 99,919	\$ 100,577
Fund Balance as a % of Revenues	17.3%	16.3%	16.3%	16.8%	16.8%
Cash Balance as a % of Revenues	14.6%	11.6%	12.3%	12.8%	11.5%
<b>Debt/Pensions</b>					
Net Direct Debt (\$000)	\$ 116,953	\$ 121,540	\$ 122,581	\$ 121,809	\$ 124,303
Net Direct Debt / Operating Revenues (x)	1.2x	1.2x	1.2x	1.2x	1.2x
Net Direct Debt / Full Value (%)	1.9%	2.1%	2.2%	2.2%	2.3%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	N/A	1.2x	1.4x	1.6x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	N/A	2.1%	2.6%	2.9%

Source: City of Mesquite, TX Comprehensive Annual Financial Reports 2010 - 2014

## Recent Developments

Recent Developments are incorporated into the Detailed Rating Considerations

## Detailed Rating Considerations

### Economy and Tax Base: Economic Activity Drives Increases in AV

The City of Mesquite is located in Dallas County (Aaa stable), just east of the City of Dallas' (Aa2 stable) city limits on Interstate 20. The local economy is anchored by retail, distribution and manufacturing. Population growth within the city has been stable with the most recent census reporting an increase of 12.3% to 139,824 residents in 2010. Despite population increase, wealth indices within the city have fallen over the years, reaching an estimated 87.7% (median family income), and 77.3% (per capita income) in 2013; both expressed as a percentage of national levels. The November 2015 unemployment rate of 4.1% was lower than both the state's 4.5%, and the nation's 4.8%.

Within the past decade, assessed values have contracted in six of the past 10 years. However, recent trends have been positive with values growing an increase of 5% and 4% in fiscal 2015 and 2016, to reach almost \$6 billion. The tax base itself is largely residential with single family residences accounting for 53.6%, and commercial and industrial properties accounting for 33.2% of assessed valuation. Economic activity is strong within the city and officials report several ongoing projects within the local economy that should continue to augment recent increases in assessed values. Several distribution and manufacturing companies are leasing new space, or expanding operations. Retail activity is ongoing with multiple gas stations, restaurants, and grocery stores expected to opening within the next year. The city also continues to see residential development including single and multifamily construction. Despite the activity, city officials are conservatively budgeting for a 4% increase in assessed values for fiscal 2017. The city will continue to benefit from its strategic location within the metropolitan area, with ongoing economic activity driving tax base growth.

Major taxpayer concentration within the city is limited as the top 10 taxpayers accounted for 7.6% of total assessed values in fiscal 2015; all are reportedly stable.

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.

### Financial Operations and Reserves: Satisfactory, but Stable, Financial Position

The city's financial position is satisfactory, but remains stable. Over the past five years, the financial history includes a combination of operating surpluses and draws as the city experienced reduced revenues from weakened economic conditions, which were met with cost cutting measures. During that period, the General Fund balance remained above the 15% policy, which is adequate but below similarly rated credits across the nation. In fiscal 2014 (ended September 30), the General Fund reported a \$255,000 draw due to an additional \$500,000 contributions made to the Health Claims Fund, from higher than normal claims during the year. At fiscal year end, the fund balance was reduced to \$17.2 million (17.3% of revenues). Including the Debt Service Fund, total operating fund balance was \$17.6 million (18.9% of total operating revenues). The majority of the operating revenues during the year were received from property taxes (35%), sales taxes (29.9%), and charges for services (12.9%).

As mentioned above, the city experienced higher than normal health care claims in 2014, which have resulted in a deficit position in the General Liability, and Health funds. Starting in fiscal 2015, the implemented plan changes including rate and plan design changes are expected to return the two funds to positive operations within three years. The city also carries a Stop Loss policy with a \$350,000 limit per claim to mitigate years of heavy activity.

The fiscal 2015 budget reflected a modest surplus. However, unaudited numbers reflect a \$488,000 decrease due to delayed grant reimbursements for transit service. The reimbursement is expected to be received in May (fiscal 2016).

The city adopted a balanced budget for fiscal 2016. Year to date, officials report that the budget is tracking closely with original assumptions and expects a modest surplus in the General Fund at fiscal year end. Continued favorable operating practices will augment credit fundamentals and grow reserves in line with Aa2 peers.

#### LIQUIDITY

The General Fund cash position is satisfactory with net cash totaling \$11.1 million (11.2% of General Fund revenues) at fiscal year end 2014. Including the Debt Service Fund, total cash was relatively unchanged at \$11.6 million.

### Debt and Pensions: Manageable Debt Ratios

In November 2015, voters authorized a \$125 million bond election for residential street reconstruction over a 10 year period. This issue is the first installment from the authorization. Officials expect the debt service tax rate will increase modestly by a total of \$0.94 per \$1,000 of assessed values for the total authorization; in fiscal 2016, the debt service tax rate was \$2.04. Including the current issue, the city has a total of \$164.9 million outstanding; \$35.2 million is rated by Moody's. The city's debt burden is higher than Aa2 peers, but manageable with a direct debt burden of 2.8% (9.8% overall) on a fiscal 2016 valuation. Debt service as a percentage of operating expenditures is a manageable 10.9%. Principal payout is less than national median with 60.3% principal retired within 10 years.

#### DEBT STRUCTURE

The debt service level is descending with the maximum annual debt service scheduled for fiscal 2017. Final maturity on the bonds is in 2036.

#### DEBT-RELATED DERIVATIVES

All of the city's debt is fixed rate, and the city is not party to any derivative agreements. The city also does not have any privately placed issues.

#### PENSIONS AND OPEB

The city participates in the Texas Municipal Retirement System (TMRS), which is a multi-employer agent plan for pension systems. Over the past four years through fiscal 2014, the city has made its annually required contribution into the system. In fiscal 2014, the city paid \$4.5 million, and reported an unfunded liability of \$35.3 million. Moody's adjusted net pension liability (ANPL) for Mesquite was \$148.8 million at fiscal year end 2014, or a manageable 1.48 times operating revenues (2.20% of the full valuation). The three year average ANPL was 1.55 times operating revenues (2.31% of the full valuation). Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported contribution information, or the reported liability information of the state-wide cost-sharing plans, but to improve comparability with other rated entities. For more information on Moody's insights on employee pensions and the related credit impact on companies, governments, and other entities across the globe please visit Moody's on Pensions at [www.moody.com/pensions](http://www.moody.com/pensions).

The city offers other post employment benefits (OPEB) in the form of healthcare benefits. OPEB is currently funded on a pay as you go basis. In fiscal 2014, the city contributed almost \$2 million, 63.9% of the required contribution. At fiscal year end, the city reported a total liability of approximately \$31 million, all of which was unfunded.

Total fixed costs including pensions, OPEB and debt service payments was \$17.4 million (17.3% of total operating expenditures) in fiscal 2014.

### Management and Governance

Texas cities have an institutional framework score of "Aa," or strong. Cities rely on stable property taxes for 30% -40% of their operating revenues, while 25%-35% comes from economically sensitive sales taxes, resulting in moderate predictability overall. Cities maintain moderate flexibility under the state-mandated cap (\$25 per \$1,000 of AV, with no more than \$15 for debt) to raise property taxes as most cities are well below the cap. Expenditures primarily consist of personnel costs, which are highly predictable. Cities have high flexibility to reduce expenditures given no union presence.

The City of Mesquite has a Council/Manager form of government in which the mayor and six council members are elected for staggered two year terms with elections held annually in May. The city demonstrates good governance by multiyear capital and financial planning with capital plans going out 5 to 10 years depending on the need, and financial planning going out 10 years. As discussed above, the city also maintains a codified policy of a minimum of 15% of expenditures for its reserve fund, as well as a debt service tax rate requirement of 35% of the city's total tax rate.

### Legal Security

The bonds and certificates are secured by a direct and continuing annual ad valorem tax, levied on all taxable property in the city, within the limits prescribed by law. The certificates are additionally secured by a limited pledge (not to exceed \$10,000) of surplus net revenues of the City's waterworks and sewer system.

### Use of Proceeds

Proceeds from the sale will be used to refund certain portions of the city's Series 2007 and 2008 certificates for an expected net present value savings, and no extension of final maturity. The remaining portion will be used to make needed infrastructure development and redevelopment.

### Obligor Profile

The City of Mesquite is located in Dallas County (Aaa, stable outlook), just east of the City of Dallas' (Aa2 stable) city limits on Interstate 20. The local economy is anchored by retail, distribution and manufacturing. Population growth within the city has been stable with the most recent census reporting an increases of 12.3% to 139,824 residents in 2010. The estimate for 2014 shows a total population of 142,210 residents.

### Methodology

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Ratings Methodologies page on [www.moody.com](http://www.moody.com) for a copy of this methodology.

### Ratings

Exhibit 2

#### MESQUITE (CITY OF) TX

Issue	Rating
Combination Tax and Limited Surplus Revenue	Aa2
Certificates of Obligation, Series of 2016	
Rating Type	Underlying LT
Sale Amount	\$12,145,000
Expected Sale Date	03/07/2016
Rating Description	General Obligation Limited Tax

General Obligation Refunding and Improvement Bonds, Series 2016	Aa2
Rating Type	Underlying LT
Sale Amount	\$39,965,000
Expected Sale Date	03/07/2016
Rating Description	General Obligation Limited Tax

Source: Moody's Investors Service

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