

RatingsDirect®

Summary:

Cape Girardeau, Missouri; Water/Sewer

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Summary:

Cape Girardeau, Missouri; Water/Sewer

Credit Profile

US\$8.515 mil waterworks sys rfdg rev bnds ser 2019 due 01/01/2032

Long Term Rating

A+/Stable

New

Cape Girardeau WTRSWR

Long Term Rating

A+/Stable

Affirmed

Rationale

S&P Global Ratings assigned its 'A+' rating and stable outlook to Cape Girardeau, Mo.'s series 2019 waterworks system refunding revenue bonds and affirmed its 'A+' rating, with a stable outlook, on the city's existing waterworks debt.

The rating reflects our opinion of the combination of a strong enterprise-risk profile and very strong financial-risk profile.

The enterprise-risk profile reflects our opinion of the system's:

- Service-area participation in a limited local area economy,
- Very low industry risk as a monopolistic service provider of an essential public utility,
- Affordable rates compared to the city's median household effective buying income and county poverty, and
- Good operational management practices and policies based on our Operational Management Assessment (OMA) methodology.

The financial-risk profile reflects our opinion of the system's:

- Very strong all-in debt service coverage (DSC);
- Very strong liquidity;
- Low system debt, measured by a debt-to-capitalization ratio; and
- Good financial management practices and policies based on our Financial Management Assessment (FMA) methodology.

Cape Girardeau will use series 2019 bond proceeds to current refund its series 2012A waterworks system refunding revenue bonds.

Net waterworks system revenue secures the debt. Net revenue excludes capital improvement sales tax revenue, which is subject to annual appropriation by the city. We understand the city recently renewed the capital improvement sales taxes with a 0.25% tax being applied for the repayment of sewerage system revenue bonds and a 0.25% tax for water

system, city hall, and city airport improvements and street repairs.

Bond provisions, in our view, are credit neutral, including a 1.1x annual DSC rate covenant and 1.1x average annual DSC additional bonds test, subject to pro forma rate adjustments. We understand the city will not fund a debt-service reserve associated with series 2019 bonds, which we consider weak, albeit mitigated by strong liquidity compared to operations.

Enterprise risk

Cape Girardeau is in Cape Girardeau County, along the state's border with Illinois, about 125 miles from St. Louis, Mo. The city's population estimate is more than 39,000 with the daytime population reaching about 100,000. The relatively shallow local economy is diverse with employers in the health-care, retail, manufacturing, and higher-education sectors. City unemployment in May 2019 was 2.9%, below state and national levels. Income is, what we consider, below average: 2018 median household effective buying income was 79% of the national level.

Cape Girardeau provides its own water supply and treatment, mainly from two plants. Its main plant operates with a 7.5-million-gallons-per-day (mgd) capacity, and a second plant draws water from three wells; the second plant has a 2.8-mgd capacity, sufficient due to the average of 5.6 mgd. The system serves more than 16,500 customers, a number that has been relatively stable. The system had about 14,200 residential customers in 2018. The 10 leading customers accounted for roughly 19% of fiscal 2018 revenue.

Current rates are \$29.67 per 800 cubic feet consumed, including a meter charge. Cape Girardeau increased rates by 3% in fiscal 2017, 2% in fiscal 2018, and 0% in fiscal 2019. Officials are projecting to increase rates by 2% in fiscal 2020. The city maintains rate autonomy; management reviews rates annually. Management expects to adjust rates at a similar pace during the next few years.

Reflecting our OMA, we view the system's operational management as good. The water utility has adequate treatment capacity to meet average daily flow of roughly 5.6 mgd sufficiently. Management maintains a capital improvement plan for managing assets it updates annually. The city has full rate-setting autonomy, and it has established a trend of timely rate adjustments that helps support financial and operating needs.

Consistent with the article titled "Methodology: Industry Risk," published Nov. 19, 2013, on RatingsDirect, we consider industry risk for the system very low, the most-favorable assessment possible on a six-point scale, with '1' being the best and '6' the worst.

Financial risk

The utility's financial-risk profile is very strong, in our opinion. Liquidity has been very strong, in our view, with unrestricted days' cash on hand increasing annually. At fiscal year-end June 30, 2018, unrestricted days' cash on hand was 431 days', or \$6.4 million, up from 409 days', or \$5.9 million, in fiscal 2017. For unaudited fiscal 2019, the city reported cash similar to fiscal 2018 levels; management intends to keep cash relatively stable during the next few fiscal years. Cape Girardeau's policy is to maintain reserves at no less than 15% of operating expenditures.

Annual all-in DSC has been historically very strong with net revenue between roughly 1.4x and 1.5x through fiscal 2018, excluding the city-appropriated sales tax fund. Management expects all-in DSC to remain 1.5x for fiscal 2019 based on unaudited fiscal year-end results. DSC increased to well in excess of 3x when including appropriated sales

tax funds, specifically for water-utility purposes, for fiscal years 2016 and 2017. The capital improvement sales tax was set to expire in 2017; the electorate, however, extended the tax but only to pay debt service on sewerage system revenue bonds. Projections for the fiscal 2020 budget demonstrate, what we consider, very strong DSC with levels at or above 1.5x through fiscal 2025.

The city does not have voter authorization for new waterworks revenue bonds, and it does not currently have any additional debt plans. The system's debt-to-capitalization ratio was, what we consider, low at 20% for fiscal 2018. Currently, funded capital needs total \$2.1 million during the next five years; we recognize management will pay this with internal sources, including available cash and appropriated capital improvement sales tax funds. The city's capital improvement plan outlines prioritized contingent unfunded projects, totaling roughly \$14.5 million for the water fund.

Reflecting our FMA methodology, we view the system's financial management as good, indicating that financial practices exist in most areas but that governance officials might not formalize or regularly monitor all of them.

Highlights include management's use of historical trends for budget and operational performance analysis and annual budget updates to the city council. Management completes and updates five-year financial and capital projections with the annual budget. Management targets maintaining 15% of operating expenses on hand. Management presents accrual-based audits.

Outlook

The stable outlook reflects S&P Global Ratings' opinion Cape Girardeau will likely maintain very strong finances, measured by very strong all-in DSC and liquidity. We believe the city's role as a regional economy provides additional rating stability.

Upside scenario

We could raise the rating over the long term if the system were to address all capital needs while maintaining liquidity and DSC commensurate with higher-rated peers.

Downside scenario

We could lower the rating if DSC or liquidity were to decrease significantly.

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