

## CREDIT OPINION

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# Montgomery County Municipal Utility District No. 132, TX

New issuer

## Summary

[Montgomery Co. MUD 132, TX](#) (Baa2 stable) benefits from a healthy financial position with strong reserves that have been bolstered by property tax revenue growth and modest expenditures. The district does not have any utility operations, which are provided by the [City of Conroe](#) (Aa1 stable), limiting the operating risk of the credit profile. The district has a modestly sized, though rapidly growing residential tax base, which will continue to grow as homebuilding continues. The credit profile is challenged by an elevated debt burden, which will remain high for the foreseeable future as additional debt is issued to reimburse developers for the cost of constructing infrastructure improvements. Following the current issuance, the district will owe developers approximately \$60 million for capital advances. The district's credit profile is further constrained by a tax rate limitation imposed by a utility agreement with Conroe, which prevents the district from levying a total tax rate greater than \$7 per \$1,000 of taxable property value.

## Credit strengths

- » Rapidly growing residential tax base
- » Strong financial reserves and liquidity
- » Lack of utility operations

## Credit challenges

- » Elevated debt burden with plans for additional debt
- » Total tax rate limited by utility agreement with City of Conroe

## Rating outlook

The stable outlook reflects our expectation that the debt burden will remain manageable and new debt will be issued along with commensurate tax base allowing for adequate coverage of operating and debt service expenditures under the \$7 tax rate limit. The financial position of the district will remain healthy, despite a budgeted draw on reserves in fiscal 2023.

## Factors that could lead to an upgrade

- » Significant tax base expansion
- » Moderation of the debt burden

## Factors that could lead to a downgrade

- » Increase in debt service requirements that pose budgetary pressure under tax rate limitation
- » Significant and/or prolonged tax base contraction
- » Trend of operating deficits leading to weakened reserves

## Key indicators

Exhibit 1

Montgomery County Municipal Utility District No. 132, TX	2018	2019	2020	2021	2022
<b>Economy/Tax Base</b>					
Total Full Value (\$000)	\$21,149	\$52,952	\$82,000	\$110,352	\$141,528
Population	N/A	1,152	1,061	1,337	3,038
Full Value Per Capita	N/A	\$45,965	\$77,286	\$82,537	\$46,586
Median Family Income (% of US Median)	132.0%	131.6%	128.9%	N/A	N/A
<b>Finances</b>					
Operating Revenue (\$000)	\$202	\$401	\$653	\$868	\$1,006
Fund Balance (\$000)	\$42	\$276	\$674	\$1,341	\$1,671
Cash Balance (\$000)	\$83	\$299	\$910	\$1,312	\$1,786
Fund Balance as a % of Revenues	20.8%	68.9%	103.3%	154.5%	166.1%
Cash Balance as a % of Revenues	41.1%	74.7%	139.4%	151.1%	177.5%
<b>Debt/Pensions</b>					
Net Direct Debt (\$000)	\$0	\$3,029	\$5,990	\$8,521	\$17,725
3-Year Average of Moody's ANPL (\$000)	\$0	\$0	\$0	\$0	\$0
Net Direct Debt / Full Value (%)	0.0%	5.7%	7.3%	7.7%	12.5%
Net Direct Debt / Operating Revenues (x)	0.0x	7.6x	9.2x	9.8x	17.6x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.0x	0.0x	0.0x	0.0x	0.0x

Median family income of Conroe ISD used as a proxy for the district. Population estimated based on 3.5 persons per single family home.  
Source: US Census Bureau, Montgomery County Municipal Utility District No. 132's financial statements and Moody's Investors Service

## Profile

The district comprises about 434 acres, which consist of five separate non-contiguous subdivisions, all located within the city limits of Conroe. Conroe lies roughly 40 miles north of [Houston](#) (Aa3 stable). The district has an estimated population of 3,038 residents. All utility service is provided by Conroe.

## Detailed credit considerations

### Economy and tax base: modestly sized though growing residential tax base

Tax base growth will continue at a healthy rate given ongoing homebuilding and ample land available for future development. The district's tax base is modestly sized with fiscal 2023 certified assessed value (AV) of \$206.9 million, a 46% increase over the prior year. An estimate of value as of November 15, 2022 reflects a further 22% increase to \$252.8 million, which is just below the median for similarly rated districts. The estimate of value reflects the certified fiscal 2023 AV at January 1, 2022 (\$206.9 million) plus the value of new construction through November 15, 2022, suggesting strong pace of new home construction. Housing demand in the area is likely to remain strong, despite headwinds in the housing market such as rising mortgage rates.

The district consists entirely of single family residential lots and roughly 86% of developable acreage has been provided utility and roadway infrastructure necessary to begin homebuilding. Current development consists of about 1,099 single-family residential lots across 323 acres, containing 868 completed homes, 45 homes under construction and 186 vacant lots. The 51 developable acres

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remaining for future development is part of a tract of land annexed by the district in August 2022. Remaining land will be developed as single family residential lots.

The tax base is diverse, with the top 10 taxpayers accounting for a modest 11.8% of fiscal 2023 AV and are comprised of developers, homebuilders and individual landowners. Home values range from \$200,000 to \$323,000. Income levels in the area are above average with median family income equal to 129% of the US, using Conroe Independent School District as a proxy.

#### **Financial operations and reserves: healthy finances; constrained flexibility due to tax rate limitation**

The district's reserves will remain healthy given strong property value growth and modest expenditures due to the lack of utility operations. All utility service is provided by the city of Conroe, and the district's operating expenditures consist primarily of administrative costs, professional services and modest maintenance of drainage detention ponds. The district reported a \$44,000 general fund surplus in fiscal 2022 (May 31 year end), which increased available fund balance to \$809,000 representing a very strong 251% of revenue. Fiscal 2022 operating fund balance (inclusive of the general fund and debt service fund) totaled \$1.7 million or 166% of operating revenues. The district's fiscal 2023 budget reflects a roughly \$250,000 draw on general fund reserves, which if realized will bring fund balance to about 125% of revenue, which is in line with the Baa2 median.

Voters of the district have authorized the district to levy a property tax for maintenance and operations (M&O) not to exceed \$15 per \$1,000 of assessed property value. However, pursuant to a utility agreement between the district and Conroe, the district's total tax rate (M&O and debt service) is not to exceed \$7 per \$1000. While the district's debt service (I&S) tax rate is still unlimited as to rate or amount, the district's M&O rate cannot exceed \$0.50 if the I&S rate is \$7 or higher in a given year. This tax rate provision somewhat limits the district's financial flexibility, though will likely not have a material impact on the district's financial position given its modest operating expenditures. In actuality the impact of the tax rate limitation is more likely to materialize as a barrier to how quickly the district will issue additional debt to reimburse developers. In fiscal 2023 the district's total tax rate was \$7, consisting of \$0.75 for operations and \$6.25 for debt service.

#### **Liquidity**

Liquidity is strong and in line with fund balance. Operating fund cash at the close of fiscal 2022 totaled \$1.8 million equal to 178% of total revenue, of which \$841,000 was in the general fund representing 261% of general fund revenue.

#### **Debt and pensions: significant future debt issuance needed to reimburse developers**

The district's debt profile will remain high given significant amounts owed to developers to reimburse cost of infrastructure improvements, which will be funded with debt over the next few years. Including the Series 2023 bonds, the direct debt burden totals 10.9% of certified fiscal 2023 assessed value and 8.9% of the November 15, 2022 estimate of value, which compares favorably to the Baa2 median. When including debt issued by overlapping local governments the district's overall debt burden is 16.9% of fiscal 2023 AV. Following the issuance of the Series 2023 bonds, the developer will be owed about \$60 million.

The district will issue future debt as tax base growth allows it to be afforded under a \$7 total tax rate.

#### **Legal security**

The bonds are payable from an annual ad valorem tax levied, without legal limit as to rate or amount, against all taxable property located within the district.

#### **Debt structure**

All of the district's debt is fixed rate and amortizes over the long term. Payout is slower than average with 33% of debt amortized within ten years.

#### **Debt-related derivatives**

The district is not party to any debt related derivative agreements.

#### **Pensions and OPEB**

The district has no employees and does not have a pension liability.

## ESG considerations

### Environmental

The district's proximity to the Texas Gulf Coast increases its susceptibility to physical risks resulting from occasional destructive weather events including hurricanes and flooding from exceptional periods of rain. Most recently, the district was impacted by Hurricane Harvey in late 2017 and Hurricane Imelda in 2019. No facilities or homes were constructed prior to Hurricane Harvey. The district's facilities and homes were not materially damaged by Hurricane Imelda.

### Social

Social considerations do not present material risks to the district's credit profile. Using the Conroe ISD as a proxy, median family income equals to 128.9% of the US (2019 American Community Survey). Strong demand for housing in the greater Houston metropolitan area will continue to drive tax base and revenue growth benefitting the district.

### Governance

The district is governed by a five-member board of directors, which has control over and management supervision of all affairs of the district. The directors are elected to four-year staggered terms. The district does not have a general manager or other full-time employees, but contracts for certain necessary services.

Texas MUDs have an Institutional Framework score of Aa, which is strong compared to the nation. Property taxes, one of the sector's major revenue sources, are not subject to any caps for debt service. MUDs that are considered over 95% developed, are subject to a property tax cap of 3.5% for maintenance and operations. Unpredictable revenue fluctuations tend to be minor, or under 5% annually. Across the sector, fixed and mandated costs specifically for debt service are generally greater than 25% of expenditures. MUDs have no full time employees. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

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