

# RatingsDirect®

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**Summary:**

## Cinco Municipal Utility District No. 1, Texas; General Obligation

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### Table Of Contents

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Rationale

Outlook

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### Credit Profile

US\$13.415 mil contract rev bnds ser 2019A dtd 12/01/2019 due 12/01/2046

*Long Term Rating*

A+/Stable

New

## Rationale

S&P Global Ratings has assigned its 'A+' rating to Cinco Municipal Utility District (MUD) No. 1, Texas' series 2019A contract revenue bonds. At the same time, S&P Global Ratings affirmed its 'A+' rating on the district's debt outstanding. The outlook is stable.

Bond proceeds will be used to make various capital improvements throughout the district including projects for the district's wastewater and storm water systems and equipment.

## Security

The bonds are secured by an unconditional obligation of Cinco MUD No. 1 and 10 other MUD participants to make contract payments pursuant to a master district contract. Under the contract, which is administered by MUD No. 1, each participant pays a pro rata share of annual debt service on the bonds based on the aggregate assessed value (AV) of all participants. Each participant is obligated to make annual payments from the unlimited-ad valorem tax on all property within its respective taxing area. Each of the MUD participants is liable for its own portion and is not liable for the payments owed by any other MUD participant. However, an indenture of trust requires MUD No. 1 to maintain a shared debt service reserve (DSR) equal to the maximum annual debt service (MADS) requirement on contract revenue bonds outstanding. Participant districts pay a pro rata share of debt service, which is based on the participant's portion of the master area's gross AV.

## Credit overview

As the master district, Cinco MUD No. 1 is empowered, among other things, to purchase, construct, operate, and maintain all works, improvements, facilities, and plants necessary for the supply and distribution of water; the collection, transportation, and treatment of wastewater; and the control and diversion of storm water to the service area. The master district contract for Cinco MUD No. 1 with other MUD participants was recently renewed to extend from 2030 to 2060, which is important because it means the contract will extend beyond the life of the contract revenue bonds.

The rating further reflects our view of the district's:

- Participation in the diverse Houston metropolitan statistical area (MSA), with a large \$4 billion tax base;
- Mature development status, which should limit additional capital needs;

- Very strong financial reserves equal to 247% of expenditures in the general fund and 160% of MADS in the debt service fund;
- Very low direct tax rates and low total tax rates; and
- Moderate overall net debt consistent with similarly rated peers.

## **Economy**

The participant districts' pro rata share of the master service area's gross AV determines their share of the overall debt service payments. The district uses gross AV to prevent individual MUD districts from creating tax exemptions and lowering their contributions. Should any participant fail to meet its annual obligation, management would use the DSR, maintained at MADS or higher, to make that year's payment. The district would then suspend or cancel service to that participant. In the following year, the contract payment for the remaining participants would increase to replenish the DSR to the point at which it contains 100% of MADS.

Gross AV increased in the MUD in 2018 by a slight 1.0%, but declined in 2019 by 7.8%. Management attributes the decline to continued protests on home valuations throughout Fort Bend County as well as AV declines in some of the districts, specifically 6, 7, and 8, due to Hurricane Harvey. Approximately 25% of homes throughout the master district flooded and approximately 50% of those were related to release of water from Barker Reservoir by the U.S. Army Corps of Engineers.

In fiscal 2020, the AV rebounded with an 8.9% increase over 2019 reaching \$4.1 billion.

Although the district itself encompasses about 246 acres, the service area for the master district is the Cinco Ranch development, consisting of 11 MUDs on more than 5,345 acres. All developable land within the master planned community has utility infrastructure. Cinco Ranch is primarily in Fort Bend County, just west of downtown Houston. Development within the MUD includes both single-family and multifamily residential along with commercial, educational, and community facilities. Interstate 10, US Highway 59, and Grand Parkway provide access to the broad and diverse economy of the Houston MSA.

## **Finances**

The master district maintains both a debt service fund and a DSR fund. The \$1.6 million general fund balance is equal to a very strong 247.4% of general fund expenditures. The debt service is also very strong equal to 178.9% of MADS for fiscal 2018. The participant districts levy contract tax rates that range from 17-21 cents per \$100 of AV. The highest total property tax rate, including overlapping jurisdictions in Harris County, within the Cinco Ranch development is \$2.71 per \$100 of AV, which we view as low. The contract tax rate has incrementally decreased in the past several years, as the Cinco Ranch development has reached completion. Total collections for the contract tax have never been less than 100%.

## **Debt**

To comply with the Fort Bend Subsidence District's groundwater consumption reduction mandate, the MUD has joined the North Fort Bend Water Authority. This authority helps facilitate the conversion process for special districts by developing a groundwater reduction plan and providing the necessary infrastructure to implement the plan.

Overall net debt for the master district is moderate, in our view, totaling 5.7% on a debt-to-market value ratio.

Including the current issue, the district will have \$70 million in debt outstanding. A large part of the overall debt burden is due to overlapping debt from Katy Independent School District.

The district has \$9.3 million in debt outstanding that was privately placed with Regions Bank in 2014. Given the district's very strong reserves and lack of non-standard bank terms, we do not believe this debt poses unusual risk on the district's debt or liquidity levels.

## **Outlook**

The stable outlook reflects our view of Cinco MUD No. 1's very strong finances, particularly the amount of reserves available for debt service, and healthy tax base. For these reasons, we do not expect to lower the rating within the two-year outlook horizon.

### **Upside scenario**

Maintenance of very strong reserves, with a significant reduction in debt levels and the tax rates, would likely result in a higher rating.

### **Downside scenario**

We could lower the rating if the district's financial reserves or debt position significantly weaken to a level that is no longer consistent with that of its peers.

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