



Fitch Affirms San Benito, TX's LTGOs & COs at 'A+'; Outlook Stable

Fitch Ratings-Austin-10 June 2016: Fitch Ratings affirms San Benito, Texas' (the city) Long-Term Issuer Default Rating (IDR) and the following limited tax obligations at 'A+':

--\$5.2 million limited tax general obligation bonds (LTGOs), series 2011 and 2012;
--\$16.5 million of combination tax and limited pledge revenue certificates of obligation (COs), series 2007 and 2011.

The Rating Outlook is Stable.

SECURITY

The GOs and COs are payable from an ad valorem tax levied on all taxable property within the city, limited to \$2.50 per \$100 taxable assessed valuation (TAV). The COs are additionally payable from a limited subordinate lien pledge of the net revenues of the city's waterworks and sewer system, not to exceed \$1,000.

KEY RATING DRIVERS

The 'A+' rating reflects the city's solid growth prospects, strong gap-closing capacity, and moderate fixed costs; however, spending pressure for services reduces some of the city's flexibility. Fitch expects that long-term liabilities will continue to be a moderate burden on resources due to the modest debt issuance plans.

Economic Resource Base

The city is located in Cameron County at the southern tip of Texas in the Lower Rio Grande Valley. It is situated between the cities of Harlingen and Brownsville. The population has remained fairly flat since 2000 and is estimated at 25,000 for 2014. The city's economy is based on agriculture, retail/service industries, manufacturing, and tourism.

Revenue Framework: 'aa' factor assessment

Historical revenue growth has been solid, exceeding the pace of inflation but falling short of GDP. Independent revenue-raising capacity is high, as the city's property tax rate remains well below statutory limits.

Expenditure Framework: 'a' factor assessment

The pace of recurring general fund spending has exceeded revenues, although annual transfers have boosted reserves in recent years. Carrying costs are affordable and are not expected to shift materially, due to modest borrowing needs.

Long-Term Liability Burden: 'aa' factor assessment

Debt levels are moderate and are expected to remain a reasonable burden on resources given limited future borrowing plans.

Operating Performance: 'aa' factor assessment

Revenue and spending flexibility provides solid gap-closing ability through a typical economic cycle. A normal downturn is not expected to impair the city's overall financial flexibility.

RATING SENSITIVITIES

Spending Pressure: The rating is sensitive to continuing expenditure pressure and the city's ability to balance these pressures against available resources.

CREDIT PROFILE

Wealth and income levels in the city are substantially below state and national levels. Per capita money income

is less than 50% of the state and national averages, and the city's per capita market value is a low \$29,000. Unemployment levels have improved to 5.2% as of April 2016 from a post-recession high of 11% due to growth in employment.

Revenue Framework

The general fund revenue base is made up of roughly 40% in property taxes, 30% sales taxes, and 12% franchise taxes. Another revenue stream has been transfers from the water utility system, which has grown in recent years to almost a fifth of general fund sources.

Over the last decade, the city's general fund revenues have grown at a rate in excess of CPI, driven by steady, incremental increases in both sales and property tax collections with minimal recessionary contraction. Similar growth rates are expected to continue in the near- to mid-term.

Statutory limitations on sales tax rates do not allow for any rate increases. The city has ample legal room to raise property tax revenue, as the current tax rate of \$0.7281 per \$100 of TAV is well under the limit of \$2.50 per \$100; however, there are practical limitations to raising the rate given the size and wealth of the resource base. If a proposed tax rate results in an 8% year-over-year levy increase (based on the prior year's values), the rate increase may be subject to election if petitioned by voters.

Expenditure Framework

The city's largest spending area is public safety, which makes up over half of general fund spending. Spending growth in that area has trended in line with general government spending.

Spending growth has exceeded revenue growth in recent years, partly due to capital spending for general government as well as for the water utility system. The utility system has been reimbursing the general fund for spending done on its behalf by way of transfers. Management can transfer up to \$4 million to the general fund from the water utility without having to go to voter referendum or public announcement.

The city's carrying costs for debt service, pension and other postemployment benefits equaled a moderate 16% of fiscal 2015 governmental expenditures. The city participates in collective bargaining with the San Benito Police Employee Association, which includes about a fifth of total government employees. Management reports positive relations with the organization and contract negotiations occur on an annual basis. No significant changes are anticipated in contractual provisions over the near term.

Long-Term Liability Burden

The city's long-term liability burden is estimated by Fitch at a moderate 15% of personal income and is expected to remain stable given limited debt issuance plans. Approximately 63% of the city's direct debt is repaid by net enterprise and special revenues, and thus is excluded from the calculation. Debt service supported by taxes consumed a manageable 12.3% of fiscal 2015 governmental expenditures, with amortization rapid at 66% retired in 10 years.

Water and sewer utility operations remain satisfactory and net system revenues provided 1.3x coverage of fiscal 2015 tax-backed debt service, down from 2.0x two years prior. The last of a series of rate increases occurred in fiscal 2015 in line with recommendations from an external rate study. The rate increases are supporting recent plant improvement costs and debt service.

The city participates in the Texas Municipal Retirement System (TMRS), an agent multiple-employer defined benefit plan. Additionally, the city is the administrator of the Firemen's Relief and Retirement Fund, a single-employer defined benefit pension plan.

Under GASB Statement 68, the city reports a fiscal 2015 TMRS net pension liability (NPL) of \$1 million, with fiduciary assets covering 91% of total pension liabilities at the plan's 7% investment return assumption and based on a Dec. 31, 2014 valuation date. The city reports a fiscal 2015 Firemen's NPL of \$2.2 million, with fiduciary assets covering 60% of total pension liabilities at a 7% return assumption. The Firemen's valuation date is Dec. 31, 2013. The total NPL represents a low 0.74% of personal income.

Operating Performance

The city has maintained healthy reserve levels and continued to do so during the most recent recession, which was relatively mild in the region. The city is expected to manage through economic downturns while preserving a high level of financial flexibility. General fund reserves are well above the city's reserve policy and are at a level that withstands the moderate economic downturn stress evaluated using the Fitch Analytical Sensitivity Tool (FAST).

Historically, the city has practiced conservative budgeting and has implemented cost-saving initiatives when necessary. Fitch believes that the city will continue these financial practices, as evidenced by sales tax revenues that are typically budgeted for no increase.

The city's fiscal 2015 unrestricted reserves rose to \$4.1 million or a high 38% of spending. The city projects breakeven fiscal 2016 results, with sales tax revenue modestly exceeding the budget.

Contact:

Primary Analyst
Leslie Cook
Associate Director
+1-512-215-3740
Fitch Ratings, Inc.
111 Congress Avenue
Austin, TX 78701

Secondary Analyst
Barbara Ruth Rosenberg
Senior Director
+1-212-908-0731

Committee Chairperson
Steve Murray
Senior Director
+1-512-215-3729

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at 'www.fitchratings.com'.

In addition to the sources of information identified in the applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

Applicable Criteria

U.S. Tax-Supported Rating Criteria (pub. 18 Apr 2016)
(https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=879478)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
(https://www.fitchratings.com/creditdesk/press_releases/content/ridf_frame.cfm?pr_id=1005935)
Solicitation Status (https://www.fitchratings.com/gws/en/disclosure/solicitation?pr_id=1005935)
Endorsement Policy (<https://www.fitchratings.com/jsp/creditdesk/PolicyRegulation.faces?context=2&detail=31>)

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK:
[HTTP://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](http://fitchratings.com/understandingcreditratings)
(<http://fitchratings.com/understandingcreditratings>). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF

USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE 'WWW.FITCHRATINGS.COM'. PUBLISHED RATINGS, CRITERIA AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE 'CODE OF CONDUCT' SECTION OF THIS SITE. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

Endorsement Policy - Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the EU Regulatory Disclosures (<https://www.fitchratings.com/regulatory>) page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.