

Summary:

# Talladega, Alabama; Water/Sewer

## Credit Profile

Talladega wtr & swr (ASSURED GTY)

*Unenhanced Rating*

A+(SPUR)/Stable

Affirmed

Many issues are enhanced by bond insurance.

## Rationale

Standard & Poor's Ratings Services has affirmed its 'A+' long-term rating on Talladega, Ala.'s series 2010 water and sewer revenue bonds. The outlook is stable.

The rating reflects our opinion of the system's:

- Strong financial profile including strong debt service coverage (DSC) and a liquidity position that provides more than one year's cash on hand;
- Diverse customer base, which has stabilized after experiencing customer losses during the recession; and
- Limited capital needs.

In our view, these credit strengths are partly offset by the following:

- The city's weak economic indicators including low income levels; and
- The system's high leverage position.

The city's net water works and sanitary sewer system revenues are pledged to secure the series 2010 bonds.

Talladega, with a population estimate of 15,600, is in Talladega County, about 50 miles southeast of Birmingham, Ala. and 105 miles west of Atlanta, Ga. The local economy is primarily based on manufacturing, including nearby Honda Manufacturing of Alabama. The city is also home to Talladega International Superspeedway and the Motorsports Hall of Fame. Incomes for the area are what we consider low, with median household effective buying income at just 63% of the national average. The unemployment rate for October 2013 was 7.1%; historically it has been on pace with national (7%) averages but above state (6.3%) averages.

The system provides services to residents within the city limits as well as a small adjacent area. In 2013 it served 6,520 water customers and 3,810 sewer customers. During the recession the system's customer base shrunk due to the weakened local economy, but management has indicated that it has since stabilized. Although approximately 50% of the system's water supply is taken up by industrial, governmental, and commercial customers, we consider the customer base diverse, as the top 10 customers accounted for only 20% of revenues for fiscal 2013. Water for the system is sourced from Talladega Creek and five deep wells. Current water treatment capacity is 5.26 million gallons per day (mgd), which is sufficient for both average daily and peak demand levels. Water loss levels are high, averaging about 35% but management indicated that it is actively replacing lines to lower loss levels. Wastewater treatment is done by three treatments plants with the main one servicing the developed central portion of the city. Total

wastewater treatment for the system is 4.5 mgd, which can meet average daily and peak demand levels, 2 mgd and 3 mgd, respectively.

The system's financial performance remains strong, including strong DSC levels and a strong liquidity position. Coverage levels in fiscal 2012 were, in our opinion, strong at 2.87x and 2.05x net of transfers. Transfers out were to the general fund for payment of garbage collection fees. Net revenues have remained stable since 2010, about \$3.2 million, but debt service requirements have increased, causing coverage levels to decrease from previous levels of 3.6x, before transfers out. Debt service requirements remain stable for the life of the bonds and management indicates that fiscal 2013 net revenues came in as budgeted. The system's liquidity position improved markedly since fiscal 2009, doubling to \$4.57 million, which provides 341 days' cash on hand, a figure we consider strong. Officials indicated there are no plans to make any significant drawdowns on liquidity.

The city council has sole rate-setting authority. Rates are adjusted based on the consumer price index annually in October. They've risen 2% to 4% annually since 2011 and will rise 1.4% in 2014. A current combined bill for water and sewer stands at \$67.22, which we consider high given the area's low income levels.

The system's \$17.6 million in debt accounts for 95% of the system's total net value, which we consider high. Management has indicated that there are no plans to issue additional debt.

Bond provisions include a 1.25x rate covenant and a 1.25x maximum annual debt service (MADS) additional bonds test. A debt service reserve equal to MADS provides additional liquidity.

## **Outlook**

The stable outlook reflects Standard & Poor's opinion that the system will continue to maintain a strong financial profile. We believe that the system's customer base has stabilized and that plans to fund capital projects with working capital coupled with a willingness to adjust rates will allow for DSC and liquidity levels to remain strong. Given the area's weak economic indicators, we do not expect upward rating mobility over the outlook's two-year horizon. Downward pressure is not likely within the outlook period, given the system's strong financial profile.

## **Related Criteria And Research**

### **Related Criteria**

- USPF Criteria: Key Water And Sewer Utility Credit Ratio Ranges, Sept. 15, 2008
- USPF Criteria: Standard & Poor's Revises Criteria For Rating Water, Sewer, And Drainage Utility Revenue Bonds, Sept. 15, 2008

### **Related Research**

U.S. State And Local Government Credit Conditions Forecast, Dec. 17, 2013

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