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Fitch Ratings: North & South Carolina USPF Credits Can Withstand Fallout from Hurricane Florence

Fitch Ratings-New York-01 October 2018: Fitch Ratings expects credit ratings for Fitch-rated public entities in North Carolina and South Carolina affected by Hurricane Florence to remain stable despite challenges posed by significant property damage and unprecedented flooding.

The financial and budgetary strength of these municipalities can withstand credit risks associated with various recovery costs and revenue disruption in the aftermath of the hurricane. Fitch considers prospects for rebuilding sound based on the underlying demographic and economic characteristics of the affected areas, coupled with support from the federal government via the Federal Emergency Management Agency or FEMA, which has made federal disaster assistance available for affected counties in both states.

Hurricane Florence made landfall near Wrightsville Beach, NC two weeks ago, yet many parts of the Carolinas remain submerged and/or remain at risk to additional flooding. Thousands remain without power, and the heavy rainfall has led to crop damage and the discharge of untreated wastewater and other pollutants into drinking water supplies. Conditions on the ground have forced the closure of many roadways and businesses and the temporary dislocation of area residents. Property damage assessments are still preliminary and vary widely, with several reports indicating a total impact upwards of $50 billion. The damage caused by Florence is fairly nominal in relation to the roughly $20 trillion U.S. economy (about 0.3%) whose 2Q'18 annualized rate of growth registered 4.2% (according to IHS Markit, the North Carolina and South Carolina combine to account for 0.7% of U.S. GDP).

Fitch expects FEMA to shoulder much of the damage costs from the storm along with the National Flood Insurance Program (NFIP) and, to a lesser degree, the state governments and the private sector insurance market. For counties covered by the federal emergency declaration, federal aid will be made available to state and local governments and certain non-profit organizations for eligible costs incurred in connection with the protection of life and property, for public health and safety, debris clearance, and facility and equipment damage, among other outlays. Assistance to individuals can include grants for temporary housing and home repairs and low-cost loans to cover uninsured property losses.

For local governments in the Carolinas, general fund budgets are largely supported by property taxes which generally become due each year on Sept. 1 in NC (which was prior to Florence's landfall) and on Jan. 15 in South Carolina, which allows time for property owners to address financial difficulties associated with the hurricane. As for mortgage-backed properties, lenders will make property tax payments when due from pre-funded escrow accounts established on the property owner's behalf. Property taxes are generally based on valuations updated each January, with the upcoming valuation effective for the fiscal year that will not end for another 21-24 months for most local governments in each state.

Sales tax and other consumption-based fees and charges may experience a temporary decline.

However, in most cases following the initial interruption, economic activity and related revenue are likely to increase, as residents and business purchase items related to repair and rebuilding and workers are hired to assist in this effort. The majority of Fitch-rated local government debt in North and South Carolina are backed by a general obligation pledge of the government or an appropriation-backed lease or rental payment payable from all legally available funds. Bonds backed by dedicated tax pledges are fairly uncommon across both states. Fitch-rated local governments in both states exhibit a high degree of credit quality with the majority of Issuer Default Ratings in the 'AA' or 'AAA' rating categories.

Utilities in the Carolinas experienced significant short-term disruption with over 900,000 total customer outages at the peak of the storm. The U.S. Energy Information Administration reports that 16% of the population in South Carolina was without power at one point. However, most customers were restored to power within a few days with assistance provided by standing mutual aid agreements among electric utilities that provide crew and equipment during natural disasters. Concerns remain related to widespread flooding and the potential for coal ash ponds at power plants to spill into rivers in both North and South Carolina. The coal ash ponds are being protected with additional temporary measures and the rivers closely monitored for any contamination. Longer-term, the public power and cooperative utilities in the region have the financial flexibility and liquidity to mitigate the risk of lost revenue and fund capital repairs until FEMA funding reimbursements are received.

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