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Ratings

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Summary:

North St. Paul, Minnesota; General Obligation

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Summary:

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Credit Profile		
US$6.555 mil taxable GO tax incre rev bnds ser 2020A due 08/01/2048		
Long Term Rating	AA/Stable	New
US$1.98 mil taxable GO util rev bnds ser 2020B due 02/01/2035		
Long Term Rating	AA/Stable	New
North St. Paul GO		
Long Term Rating	AA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AA' rating and stable outlook to North St. Paul, Minn.'s roughly $6.555 million series 2020A general obligation (GO) tax-increment revenue bonds and roughly $1.98 million series 2020B GO utility revenue bonds and affirmed its 'AA' rating, with a stable outlook, on the city's existing GO debt.

The city's full-faith-and-credit pledge and ability to levy unlimited ad valorem property taxes secure the 2020A bonds. Officials intend to pay series 2020A debt service with net tax-increment revenue from the city's Redevelopment District No. 4-8, but the rating reflects an unlimited-ad valorem-tax pledge.

Officials intend to use series 2020A bond proceeds to finance capital and administrative expenditures in the tax-increment district.

The city's full-faith-and-credit pledge and ability to levy unlimited ad valorem property taxes secure the series 2020B bonds. Officials intend to pay series 2020B debt service with net water, storm, and sanitary sewer systems rev. The rating, however, reflects the unlimited-ad valorem-tax pledge.

Officials intend to use series 2020B bond proceeds to finance various city utility improvements.

Credit overview

With a strong history of mostly stable operational performance, complete with very strong available reserves, we think North St. Paul can hold steady during uncertain economic times. While somewhat elevated, the city has historically managed debt within its budget; despite sizable debt service carrying charges, we expect this to continue. In addition, we consider its other long-term liabilities, such as pension and other postemployment benefits (OPEB), manageable, further supporting underlying credit quality.

Due to uncertainty in the current economic environment from COVID-19, and the possible financial repercussions and pressure that could occur, in our view, the city could face pressure similar to the Great Recession, possibly including reduced property values and state aid receipts, which could lead to decreased revenue during the next few fiscal years. Even with a recession, we think North St. Paul has sufficient financial flexibility to address uncertainties and budget pressure.

The rating reflects our opinion of the city's:

- Strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong financial management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with operating results we expect could deteriorate in the near term relative to fiscal 2019, which closed with operating surpluses in the general fund and at the total governmental-fund level;
- Very strong budgetary flexibility, with available fund balance in fiscal 2019 at 30% of operating expenditures;
- Very strong liquidity, with total government available cash at 2.7x total governmental-fund expenditures and 15.9x governmental debt service, and access to external liquidity we consider strong;
- Weak debt-and-contingent-liability position, with debt service carrying charges at 17% of expenditures and net direct debt that is 218.4% of total governmental-fund revenue, but rapid amortization, with 70.8% of debt scheduled to be retired within 10 years; and
- Strong institutional framework score.

Environmental, social, and governance factors

We analyzed the city's environmental; social, which incorporates our view regarding health-and-safety risks posed by COVID-19; and governmental risks relative to its economy, management, financial measures, and debt-and-liability profile and determined all are in-line with our view of the sector standard.

Stable Outlook

Downside scenario

We could lower the rating if budgetary performance were to weaken and budgetary flexibility were to deteriorate, coupled with weaker economic metrics.

Upside scenario

While we do not view it as likely due to current macroeconomic conditions, we could raise the rating if economic indicators and debt were to improve to levels we consider commensurate with higher-rated peers.

Credit Opinion

Strong economy

We consider North St. Paul's economy strong. The city, with a population estimate of 12,036, is in Ramsey County in the Minneapolis-St. Paul-Bloomington MSA, which we consider broad and diverse. The city has a projected per capita effective buying income at 90.4% of the national level and per capita market value of $83,449. Overall, market value grew by 9.3% during the past year to $1 billion in fiscal 2019. County unemployment was 3% in 2019.

The city's access to, and participation in, the Twin Cities allows easy access to employment and retail. The property tax base is primarily residential (63%). Despite uncertainty among wider macroeconomic factors, the city is still experiencing steady economic activity with most businesses still operating and economic and residential development projects continuing. Since the U.S. economy is currently in a recession, as reported by S&P Global Economics, economic metrics and property values could face pressure during the next few years. (For further information, please see the article, titled "An Already Historic U.S. Downturn Now Looks Even Worse," published April 16, 2020, on RatingsDirect.)

Leading employers include:

- Independent School District No. 622 (1,550 employees),
- Target Corp. (172), and
- Berwald Roofing Co. Inc. (155).

Strong management

We view the city's financial management as strong, with good financial policies and practices under our FMA methodology, indicating that financial practices exist in most areas but that governance officials might not formalize or regularly monitor all of them.

Management performs a line-by-line budgeting approach with each department, using three years to five years of historical trend analysis. It presents quarterly budget-to-actual results to the city council and lacks a long-term financial plan; management, however, indicates it might adopt one. The formal capital improvement plan includes details on street-improvement, stormwater, water-supply, sanitary-sewer, and electric projects with identified sources; it reviews the plan annually. The city's own investment-management policy adheres to state guidelines, and management makes quarterly holdings-and-investment-performance reports to the city council.

North St. Paul lacks a formal debt-management policy but adheres to state guidelines. The formal reserve policy calls for maintaining, at least, 35% of subsequent-year budgeted operating expenses with any excess split between the equipment and street-improvement funds.

Adequate budgetary performance

North St. Paul's budgetary performance is adequate, in our opinion. The city had operating surpluses at 7.1% of expenditures in the general fund and 14.1% across all governmental funds in fiscal 2019. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from fiscal 2019 results in the near term due to recessionary pressure or COVID-19 pressure that could ensue.

Current-year fiscal 2020 performance is tracking the budget closely; officials are projecting breakeven results. Management has already begun assessing potential revenue pressure that could occur due to the current recessionary environment, and management has identified savings it has either already implemented or could implement in the fiscal 2020 and 2021 budgets if substantial revenue decreases were to occur. We expect the city will likely continue to manage its overall operating budget to alleviate any potential general fund pressure.

Officials reported better-than-budgeted audited fiscal 2019 results with a $521,566, or 7.2% of expenditures, general fund balance increase, reflecting positive inspection-revenue, permits-and-fees, and unbudgeted state-and-county-grants variances.

The general fund benefits from a historically stable and predictable revenue structure, consisting mostly of property taxes at 57% with state aid--referred to as local government aid in Minnesota--accounting for 24%. In prior recessionary times, particularly during the Great Recession, management notes tax collections remained very stable; therefore, it does not expect any substantial revenue reductions. Even if property tax receipts or local government aid decreased substantially, however, we expect the city will likely manage its budget to maintain mostly balanced operations. Although budgetary performance has generated net positive results during the past three fiscal years, we think uncertainty due to the unknown duration of COVID-19 and recession-related economic challenges could pose near-term budgetary challenges.

Very strong budgetary flexibility

North St. Paul's budgetary flexibility is very strong, in our view, with available fund balance in fiscal 2019 at 30% of operating expenditures, or $2.2 million.

Officials do not currently plan to spend down reserves during the next few fiscal years. Therefore, we expect budgetary flexibility will likely remain very strong. In addition, management bolstered its minimum-fund-balance-policy requirement, raising the minimum to 35% from 25%.

Very strong liquidity

In our opinion, North St. Paul's liquidity is very strong, with total government available cash at 2.7x total governmental-fund expenditures and 15.9x governmental debt service in fiscal 2019. In our view, the city has strong access to external liquidity if necessary.

Management primarily held $28.9 million of available cash and investments, after removing unspent bond proceeds, in federal and municipal securities; money-market accounts; and certificates of deposit, which we do not consider aggressive. Based on past debt issuance, we posit the city has strong access to capital markets to provide liquidity, if needed.

It does not have any direct-purchase or variable-rate debt we expect could pose a liquidity risk. Despite current recessionary pressure, we imagine that management has sufficient cash and that it will likely maintain very strong liquidity.

We note Ramsey County has extended the deadline for the first half of property taxes to July 15 from May 15 for qualifying property owners to nonescrowed homesteads and small businesses. We understand if payments were late or delayed, this will not have a material effect on the city's liquidity because qualifying properties represent a very minor part of the budget.

Weak debt-and-contingent-liability profile

In our view, North St. Paul's debt-and-contingent-liability profile is weak. Total governmental-fund debt service is 17% of total governmental-fund expenditures, and net direct debt is 218.4% of total governmental-fund revenue. Officials plan to retire about 70.8% of direct debt within 10 years, which is, in our view, a positive credit factor.

As part of the city's long-term capital plan, officials currently intend to issue roughly $5.8 million of additional GO debt during the next two years to finance major street-and-utility-reconstruction projects. We understand the city does not have any contingent liabilities, direct-purchase, or bank-placed debt that could pressure the budget.

Pension and OPEB highlights include:

- The city's combined required pension and actual OPEB contribution totaled 5.1% of total governmental-fund expenditures in fiscal 2019. The city made 106% of its annual required pension contribution in fiscal 2019.
- In our opinion, pension liabilities do not represent a medium-term credit pressure because contributions are only a modest share of the budget and we think the city can absorb higher costs without pressuring operations.
- North St. Paul participates in two multiple-employer, defined-benefit pension plans that have seen recent funding improvements, but statutory plan contributions have regularly fallen short of actuarial recommendations. Along with certain plan-specific actuarial assumptions and methods, this introduces some long-term funding-volatility and cost-acceleration risk. Although the city funds OPEB on a pay-as-you-go basis, exposing it to cost acceleration and volatility, we expect medium-term costs will likely remain only a small share of total spending and, therefore, not a significant budgetary pressure.

At June 30, 2019, the city participates in:

- Minnesota General Employees' Retirement Fund (GERF), which is 80.2% funded, with the city's proportionate share of the plan's net pension liability at $2.4 million;
- Minnesota Public Employees' Police & Fire Fund (PEPFF), which is 89.3% funded, with the city's proportionate share at $1.6 million; and
- North St. Paul's single-employer, defined-benefit OPEB plan, which is 0% funded with a net OPEB liability of $566,000.

Total GERF and PEPFF contributions were 81% and 88%, respectively, of our minimum-funding-progress metric and slightly above our static-funding metric. Annual contributions reflect a statutory formula that has typically produced lower-than-actuarially determined contributions for each plan. In our view, this increases underfunding risk over time if the Minnesota Legislature does not adjust to offset future funding shortfalls. Other key risks include:

- A 7.5% investment rate-of-return assumption for both plans, indicating some exposure to cost acceleration due to market volatility; and
- A lengthy, closed 30-year amortization period based on a level 3.25% payroll-growth assumption, which significantly defers contributions.

Regardless, costs remain only a modest share of total spending; we think they are unlikely to pressure the city's medium-term operational health.

Strong institutional framework

The institutional framework score for Minnesota cities with a population greater than 2,500 is strong.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local

Government GO Criteria, Sept. 2, 2015

- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019
- 2019 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of May 14, 2020)		
North St. Paul GO		
Long Term Rating	AA/Stable	Affirmed
North St. Paul GO		
Long Term Rating	AA/Stable	Affirmed
North St. Paul GO bnds		
Long Term Rating	AA/Stable	Affirmed
North St. Paul GO bnds ser 2016A due 02/01/2037		
Long Term Rating	AA/Stable	Affirmed
North St. Paul GO imp bnds		
Long Term Rating	AA/Stable	Affirmed