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Ratings

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Summary:

St. Joseph, Minnesota; General Obligation

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Summary:

St. Joseph, Minnesota; General Obligation

Credit Profile		
US$4.72 mil GO imp bnds ser 2019A due 12/15/2029		
Long Term Rating	AA-/Stable	New
St. Joseph GO		
Long Term Rating	AA-/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA-' long-term rating to St. Joseph, Minn.'s series 2019A general obligation (GO) improvement bonds. At the same time, S&P Global Ratings affirmed its 'AA-' rating on the city's existing GO bonds. The outlook is stable.

The city's full faith and credit pledge and ability to levy unlimited ad valorem property taxes secures the bonds; it intends to pay debt service with special assessments. The city's existing GO bonds are also secured by its full faith and credit pledge. Proceeds will be used to finance various street improvement projects, as well as provide funding to expand an industrial park in the city.

The 'AA-' rating reflects our assessment of the city's:

- Adequate economy, with projected per capita effective buying income (EBI) at 65.2% and market value per capita of $53,678, though that benefits from access to a broad and diverse metropolitan statistical area (MSA) and a local stabilizing institutional influence;
- Strong management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with balanced operating results in the general fund and an operating surplus at the total governmental fund level in fiscal 2018;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2018 of 77% of operating expenditures;
- Very strong liquidity, with total government available cash at 138.2% of total governmental fund expenditures and 5.1x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability position, with debt service carrying charges at 27.3% of expenditures and net direct debt that is 304.8% of total governmental fund revenue, but rapid amortization, with 73.1% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

In recent years, St. Joseph has maintained stable operational performance, with year-end results fluctuating right around break-even. Its reserves have been historically maintained at very strong levels, in line with the city's fund balance policy, a trend that we expect to continue. While the debt profile has moderated minimally since our last review, it still remains at a level we consider weak. However, it has been historically stable and managed within its budget. In addition, the city's other long-term liabilities, specifically pensions, are manageable, further supporting its underlying credit quality. Therefore, we believe the city will maintain its operational performance and debt profile at a level that is comparable with the current rating.

Adequate economy

We consider St. Joseph's economy adequate. The city, with an estimated population of 6,836, is in Stearns County in the St. Cloud MSA, which we consider to be broad and diverse. It also benefits, in our view, from a stabilizing institutional influence. The city has a projected per capita EBI of 65.2% of the national level and per capita market value of $53,678. Overall, market value was stable over the past year at $366.9 million in 2019. The county unemployment rate was 2.9% in 2018.

The city's residents benefit from participation in the nearby St. Cloud MSA economy with many commuting there for employment opportunities. The large student population at the College of St. Benedict/St John's University (roughly 3,500 students), located in the city, suppresses income levels somewhat. In our view, the college acts as a stabilizing institution that we believe adds to the city's credit strength. Management has indicated that overall, there has been steady growth, including a revitalization of the downtown area, as well as an expanding industrial park and some development in the commercial and residential sectors. The city's history of maintaining stable economic metrics and management's expectation for continued slow growth support our view that the economy will remain adequate over the near term.

Strong management

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

The city uses three years of historical trends and considers current economic conditions when making revenue and expenditure assumptions in its budget. Management provides the council with a monthly budget-to-actual report and quarterly investment holdings reports. The city does not have a long-term financial plan but has a five-year capital improvement plan that is updated annually and identifies funding sources for the projects. It has its own investment and debt management policies. The city's reserve policy requires a minimum general fund reserve of four-to-six months of the next year's budgeted expenditures in the general fund (excluding the fire department) for cash-flow purposes.

Strong budgetary performance

St. Joseph's budgetary performance is strong, in our opinion. The city had balanced operating results in the general fund of 0.5% of expenditures, and surplus results across all governmental funds of 7.1% in fiscal 2018.

In assessing budgetary performance, we adjusted general fund revenues and expenditures, as well as total governmental fund revenues to include annually recurring transfers. We also removed one-time capital spending funded with bond proceeds. Continued development throughout the city has helped generate its stable operational performance in recent years, with items like building permit revenues coming in higher than budgeted. Beginning in 2017, the council opted to begin transferring excess money in the general fund into a debt service reserve fund (DSRF) to help set aside funds for capital improvement projects. After accounting for these transfers, the city still posted positive operating results in 2018, so management plans to continue them.

The current 2019 budget is set to increase fund balance by roughly $57,000, but management expects actual results to be slightly better than budgeted due to the sale of a piece of property. It does not expect to draw down general fund reserves in the near term. Across governmental funds, there will likely be fluctuations in performance, due to spending in the DSRF on various projects, as well as a trail project that will be funded by cash from the local option sales tax and a federal grant. Based on current projections and no impending budgetary pressures, we expect our view of the city's budgetary performance to remain unchanged over the next two years.

Very strong budgetary flexibility

St. Joseph's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2018 of 67% of operating expenditures, or $2.4 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

Stable operating results in recent years have helped St. Joseph sustain a strong reserve position that it has consistently maintained in excess of 65% of expenditures for the past several years, and which is also in line with its fund balance policy. Management monitors reserves closely, and often make use of reserve flexibility at the end of each year, transferring out monies in excess of its policy to other funds to pay for projects. With the budget for fiscal 2019 showing an increase to fund balance, which we view as an achievable result, and no plans to draw down reserves, we expect budgetary flexibility to remain very strong.

Very strong liquidity

In our opinion, St. Joseph's liquidity is very strong, with total government available cash at 138.2% of total governmental fund expenditures and 5.1x governmental debt service in 2018. In our view, the city has strong access to external liquidity if necessary.

St. Joseph held approximately $7.7 million in available cash in fiscal 2018 (less unspent bond proceeds). We do not consider the city's investments aggressive, as it primarily invests in U.S. government securities, certificates of deposit, 4M funds, and money market funds. In our opinion, the city has strong access to external liquidity because it has issued GO debt within the past 20 years.

The city maintains three privately placed bank loans, entered into in August 2017 and February 2018. The loans, with a total of $1.2 million outstanding, were issued for various purposes, including additional costs associated with the new government center project, an alley project, water treatment plant improvements, and purchasing general equipment. The agreements for each contain no events of default or covenant violations which we consider nonstandard pursuant to our contingent liquidity criteria.

Weak debt and contingent liability profile

In our view, St. Joseph's debt and contingent liability profile is weak. Total governmental fund debt service is 27.3% of total governmental fund expenditures, and net direct debt is 304.8% of total governmental fund revenue. Approximately 73.1% of the direct debt is scheduled to be repaid within 10 years, which is, in our view, a positive credit factor.

We calculate total direct debt at about $50.4 million; our net direct debt calculation excludes revenue bonds supported by the city's water and sewer sanitary funds. The city could potentially issue an additional $1.5 million in GO bonds and equipment certificates in 2020 for parking lot repairs and general city equipment. We do not expect the addition of this debt to weaken our view of its debt and contingent liability profile.

St. Joseph's pension contributions totaled 3.0% of total governmental fund expenditures in 2018. The city made 102% of its annual required pension contribution in 2018. The liability for other postemployment benefits no longer exists as a result of the city opting for small group health insurance. Under the current medical plan, the implicit rate for retirees went away in 2017.

St. Joseph participates in the General Employees Retirement Fund (GERF) and the Public Employees Police and Fire Fund (PEPFF), which are cost-sharing, multiple-employer, defined-benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). Required pension contributions to these plans are determined by state statute. Contributions are not based on an actuarial determined contribution (ADC) and have not been keeping up with the plans' increasing liabilities, which indicates that employer contributions may rise in the future. The state recently passed pension legislation that will marginally increase contributions (for PEPFF only), reduce the investment rate of return to 7.5% (from 8.0%), and reduce some employee benefits (primarily cost-of-living adjustments). While we view these as positive changes for future plan funding levels, the lack of an actuarial funding policy remains a weakness in these plans. (For more information about the reforms included in the 2018 omnibus retirement bill and the potential for future cost increases, see our article titled, "Minnesota's New Pension Bill Is A Positive Step Toward Sustainable Funding," published on June 7, 2018, on RatingsDirect.)

The GERF and PEPFF were 79.5% and 88.8% funded, respectively, in fiscal 2018. The city's proportionate share of the net pension liability for these plans totaled $1.4 million in fiscal 2018, the most recent year for which data are available. We consider historical plan funding levels somewhat weak, and we believe that the history of pension contributions below the ADC increases the risk of payment acceleration. Despite these weaknesses, we believe St. Joseph has sufficient taxing and operational flexibility to manage future increases in pension contributions. However, if pension contributions come to absorb a larger share of the city's budget, our view of its debt and contingent liability profile could weaken.

St. Joseph also participates in a single-employer defined-benefit pension plan, administered by the City of St. Joseph Volunteer Fire Department Relief Association. The city received roughly $54,000 in on-behalf payments from the state in fiscal 2018 for the plan. The plan did not require any additional contribution from the city.

Strong institutional framework

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

Outlook

The stable outlook reflects our expectation that St. Joseph will maintain stable budgetary performance, coupled with a very strong liquidity and budgetary flexibility profile. In addition, we expect the city's economy to remain stable, so do not anticipate changing the rating within the two-year outlook period.

Upside scenario

If the debt profile moderates significantly while the city maintains very strong budgetary flexibility or if economic indicators improve significantly, we could raise the rating.

Downside scenario

We could lower the rating if the city's budgetary performance or flexibility materially deteriorate to levels no longer commensurate with the current rating.

Related Research

- 2018 Update Of Institutional Framework For U.S. Local Governments
- 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

Ratings Detail (As Of July 18, 2019)		
St. Joseph GO bnds		
Long Term Rating	AA-/Stable	Affirmed
St. Joseph GO bnds ser 2013A dtd 09/01/2013 due 12/01/2014-2020 2022-2024 2026 2028		
Long Term Rating	AA-/Stable	Affirmed
St. Joseph GO cap imp plan rfdg bnds		
Long Term Rating	AA-/Stable	Affirmed
St. Joseph GO imp bnds ser 2010B dtd 09/01/2010 due 12/01/2011-2020 2023 2025		
Long Term Rating	AA-/Stable	Affirmed
St. Joseph GO tax abatement bnds ser 2015B dtd 08/01/2015 due 12/01/2030		
Long Term Rating	AA-/Stable	Affirmed
St. Joseph GO wtr rev crossover rfdg bnds ser 2012A dtd 04/01/2012 due 12/01/2016-2025 2028		
Long Term Rating	AA-/Stable	Affirmed
St. Joseph GO (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		