

RatingsDirect®

Summary:

Big Lake, Minnesota; General Obligation

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Credit Profile

US\$3.765 mil GO imp bnds ser 2021A due 02/01/2032

<i>Long Term Rating</i>	AA/Stable	New
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Big Lake taxable GO rfdg bnds ser 2016A dtd 04/15/2016 due 02/01/2030

<i>Long Term Rating</i>	AA/Stable	Affirmed
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Rating Action

S&P Global Ratings assigned its 'AA' rating to Big Lake, Minn.'s series 2021A GO improvement bonds. At the same time, we affirmed our 'AA' rating on the city's outstanding GO debt and removed our rating on the series 2010A bonds, which were fully defeased in 2019. The outlook is stable.

The series 2021A bonds are secured by special assessments and by the city's full faith and credit GO pledge and ability to levy unlimited ad valorem taxes on all taxable property within its borders. We rate the bonds to the city's GO pledge. City officials will use bond proceeds for street improvement projects.

Credit overview

Located in Sherburne County approximately 45 miles northwest of Minneapolis-St. Paul, the city is mostly residential with a stable population of young families. The economy has been largely resilient during the pandemic with a mix of new residential and commercial building or expansion over the past year that management expects to continue based on demand need for single family and affordable housing and both residential and commercial development proposals, which should extend the steady growth trend for the city's major revenue sources in our view given the ebbing pandemic and overall economic outlook. Given these trends in parallel with the ongoing economic development and a management team we view as strong, we believe the credit will remain stable over our outlook horizon.

The stable outlook reflects our expectation that the city will maintain its historic economic and financial resiliency supported by very strong management and a stable operating budget, despite ongoing uncertainty regarding the trajectory of the pandemic and pace of economic recovery. The stable outlook also reflects our expectation that Big Lake's extremely strong reserves will provide solid liquidity and budgetary flexibility against any potential variability in the overall economic recovery as the pandemic wanes.

The 'AA' rating reflects our view of the city's:

- Strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with operating results that we expect could weaken in the near term relative to fiscal 2020, which closed with operating surpluses in the general fund and at the total governmental fund level in fiscal

2020;

- Very strong budgetary flexibility, with an available fund balance in fiscal 2020 of 91% of operating expenditures;
- Very strong liquidity, with total government available cash at 1.7x total governmental fund expenditures and 7.2x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability profile, with debt service carrying charges at 23.9% of expenditures and net direct debt that is 127.8% of total governmental fund revenue, but rapid amortization, with 94.7% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Environmental, social, and governance (ESG) factors

We analyzed Big Lake's ESG factors relative to its economy, budgetary outcomes, management, and debt and long-term liabilities, and view them as being in line with those of the sector. While the city is not immune to negative implications of the pandemic and resulting restrictions and behavioral changes, we do not believe these risks are elevated compared with the sector standard. The city has not experienced a cybersecurity attack and works with an outside consultant to continually enhance security protocols, which includes an upgrade to its technology infrastructure this year.

Stable Outlook

Upside scenario

A positive rating action is possible if the city's economic metrics improve to levels consistent with those of its more highly rated peers, and if its debt burden moderates.

Downside scenario

A negative rating action is possible should there occur a sustained and material decline in the city's budgetary performance, leading to a diminution of reserves in parallel with weaker liquidity and budgetary flexibility.

Credit Opinion

Strong economy

We consider Big Lake's economy adequate. The city, with an estimated population of 11,720, is in Sherburne County in the Minneapolis-St. Paul-Bloomington, MN-WI MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 90.8% of the national level and per capita market value of \$81,532. Overall, the city's market value grew by 6.6% over the past year to \$955.6 million in 2020. The county unemployment rate was 3.5% in 2019.

City residents have access to employment in both St. Cloud and the Twin Cities, and the city is the terminal point of the Northstar commuter train, which connects Big Lake to downtown Minneapolis, passing through several northwest suburbs. Top local employers include Xcel Energy (employs 700), Centracare Medical Center (550), Cargill Kitchen Solutions (450), Independent School District No. 727 (431) and Wal-Mart Supercenter (300).

The city's net tax capacity is 68% residential homestead, 17% commercial and industrial, and 12% residential non-homestead properties. We understand that recent growth reflects a number of factors, including favorable trends in the local residential and commercial markets, steadily increasing market values, new construction for industrial and housing developments, and local businesses that remained open during the pandemic. Given a healthy commercial development pipeline and the pace of new-home construction in particular, we expect to continue to see moderate increases in market value and tax capacity through the next few years.

Very strong management

We view the city's management as very strong, with strong financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

We view the city's management as strong following the adoption of a robust, multi-year financial plan and a debt management policy. Highlights to the FMA include:

- A line-item budget incorporating approximately five years of historical data and information from external sources, with annual budgeting done in the context of a multi-year financial plan and with a view toward long-term sustainability and structural balance;
- Monthly budget-to-actual reporting to the city council and the ability to amend the budget as needed;
- A detailed financial projection that extends three years beyond the budget year and that is included in each year's annual budget;
- A formal, rolling five-year capital improvement plan that includes funding sources for projects;
- A formal investment policy with monthly reporting on investment holdings and earnings to the city council;
- A formal debt management policy that includes qualitative guidelines and limits direct debt to 3.5% of estimated market value; and
- A formal fund balance policy requiring an unrestricted reserve equal to 50% of the subsequent year's expenditures.

Strong budgetary performance

Big Lake's budgetary performance is strong in our opinion. The city had operating surpluses of 6.4% of expenditures in the general fund and 10.3% across all governmental funds in fiscal 2020.

The city uses conservative practices when developing its general fund budgets and typically finishes the year ahead of the balanced budgets. We understand that fiscal 2020 budgetary performance was supported in part by additional home permits and developments that were not anticipated. We have adjusted for recurring transfers out to the city's infrastructure improvement fund and accounted for routine transfers into the general fund from the city's municipal liquor store by including that revenue in both the general and total governmental funds.

Big Lake received about \$863,000 in Coronavirus Aid, Relief, and Economic Security (CARES) Act funds in 2020. We understand that roughly \$548,000 was issued to businesses within city limits in the form of grants and the remaining \$315,000 was used by the city for unexpected expenditures related to the pandemic, primarily the procurement of personal protective equipment, enhancement of facility and protocol requirements to allow voting and meetings to adhere to public safety guidelines, and technology purchases to facilitate the ability to conduct city business virtually.

The fiscal 2021 balanced budget reflects \$5.6 million of general fund revenue, a 3.7% increase over the prior year budget with increased expenses primarily due to higher personnel costs. We understand that the city anticipates a small surplus at year-end based in part on favorable year to date results and management's anticipation for continued healthy development activity and single-family home permitting.

Given the city's recent history, including effective navigation of pandemic related challenges in fiscal 2020, combined with an overall steady and predictable operating environment, management's close monitoring of expenditures, and multi-year planning discipline, we expect budgetary performance to remain stable and strong.

Very strong budgetary flexibility

Big Lake's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2020 of 91% of operating expenditures, or \$5.3 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. The available fund balance includes \$3.8 million (65.8% of expenditures) in the general fund and \$1.5 million (25% of expenditures) that is outside the general fund but legally available for operations.

We include the city's municipal liquor store cash in available reserves. The city's fund balance requires a minimum unrestricted fund balance of 50% of the subsequent year's expenditures to mitigate risks associated with lower than expected or delayed tax revenues. Big Lake consistently meets or exceeds this minimum level.

We anticipate that the city's reserves will remain very strong in the near term as management reports no plans to spend down reserves in the next few years. Moreover, we understand that the city could receive a total roughly \$1.3 million of funding from the American Rescue Plan Act, which would be used for water and sewer infrastructure investment per funding guidelines further mitigating the need to draw down on reserves for these capital improvements over the next two years.

Very strong liquidity

In our opinion, Big Lake's liquidity is very strong, with total government available cash at 1.7x total governmental fund expenditures and 7.2x governmental debt service in 2020. In our view, the city has strong access to external liquidity, if necessary.

The city's total available cash and investments was \$18 million at the end of 2020. The asset allocation of its investment portfolio is conservative, in our view, with its only holdings in certificates of deposit and money market accounts. We expect the liquidity position to remain very strong.

Weak debt and contingent liability profile

In our view, Big Lake's debt and contingent liability profile is weak. Total governmental fund debt service is 23.9% of total governmental fund expenditures, and net direct debt is 127.8% of total governmental fund revenue.

Approximately 94.7% of the direct debt is scheduled to be repaid within 10 years, which is in our view a positive credit factor.

We have adjusted the city's direct debt to reflect GO debt paid from enterprise revenues that we consider self-supporting. The city's high carrying charges are somewhat offset by the rapid amortization scheduled for its direct debt, and we note as well that the city is paying much of its debt through a variety of non-ad valorem tax sources.

The city could finance approximately \$6.0 million of infrastructure projects with additional new debt within the next two years. Following the series 2021A issuance, we believe the city will still have some new debt capacity remaining at the current rating.

Big Lake's pension contributions totaled 3.7% of total governmental fund expenditures in 2020. The city made its full required pension contribution in 2020.

Big Lake participates in two cost-sharing multiple-employer defined-benefit pension plans, including the General Employees Retirement Fund (GERF) and the Public Employees Police and Fire Fund (PEPFF). The plans are administered by the Public Employees Retirement Association of Minnesota (PERA). Required pension contributions to these plans are determined by state statute. Statutory contribution rates have generally not kept pace with actuarially determined contribution (ADC) rates, suggesting the potential for future payment acceleration.

The GERF and PEPFF were 79.1% and 87.2% funded, respectively, in fiscal 2020. The city's proportionate share of the net pension liability for these plans totaled \$3.2 million in fiscal 2020. We consider historical plan funding levels somewhat weak, and we believe that the history of pension contributions below ADC increases the risk of payment acceleration. Additionally, in our view, the plan's investment portfolio is exposed to significant market risk, with only 20% of its investments allocated to fixed income and cash, which increases the risk for volatility in plan funding levels.

Despite these weaknesses, the city's pension payments as a share of total spending remain low and pension-related expenses do not create budgetary pressure. That said, the payments are somewhat understated in our view due to statutory rates not matching the plans' ADCs. Still, we believe the city has sufficient taxing and operational flexibility to manage future increases in pension contributions. Further, we understand that management's maintenance of the city's healthy fund balance is due in part to mitigate risks associated with any future payment shortfalls. While we have not made any negative adjustments to the city's debt and liability profile related to pension risk, we could revise that view should future pension costs accelerate creating budgetary pressure.

The city does not offer other postemployment benefits.

Strong institutional framework

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

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 2020 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of May 4, 2021)		
Big Lake GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Big Lake GO cap imp pln bnds ser 2016B dtd 04/15/2016 due 02/01/2028		
<i>Long Term Rating</i>	AA/Stable	Affirmed

Ratings Detail (As Of May 4, 2021) (cont.)		
Big Lake GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Big Lake GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Big Lake GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed

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