

CREDIT OPINION

22 June 2018



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Nisswa (City of) MN

Update to credit analysis

Summary

The City of Nisswa (Aa2) benefits from a healthy operating trend with very strong liquidity and reserves. The credit attributes are balanced by a small tax base, limited local economy and moderate leverage related to long-term debt and pension liabilities.

Credit strengths

- » Healthy operating trend
- » Very strong liquidity and reserves

Credit challenges

- » Relatively small tax base and limited local economy

Rating outlook

Outlooks are typically not assigned to local governments with this amount of debt.

Factors that could lead to an upgrade

- » Sustained tax base and economic expansion

Factors that could lead to a downgrade

- » Deterioration of the tax base or local economy
- » Significant and sustained reduction in reserves or liquidity
- » Materially increased leverage

Key indicators

Exhibit 1

Nisswa (City of) MN	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value (\$000)	\$627,505	\$650,421	\$640,430	\$659,043	\$645,385
Population	2,273	2,386	2,068	2,135	2,135
Full Value Per Capita	\$276,069	\$272,599	\$309,686	\$308,685	\$302,288
Median Family Income (% of US Median)	101.4%	106.2%	109.8%	102.3%	102.3%
Finances					
Operating Revenue (\$000)	\$2,413	\$2,507	\$3,579	\$3,305	\$3,127
Fund Balance (\$000)	\$3,553	\$3,765	\$4,525	\$5,224	\$5,396
Cash Balance (\$000)	\$3,553	\$3,765	\$4,525	\$5,224	\$5,549
Fund Balance as a % of Revenues	147.3%	150.2%	126.4%	158.0%	172.6%
Cash Balance as a % of Revenues	147.3%	150.2%	126.4%	158.0%	172.6%
Debt/Pensions					
Net Direct Debt (\$000)	\$4,482	\$4,348	\$3,929	\$3,671	\$3,241
3-Year Average of Moody's ANPL (\$000)	\$3,687	\$4,083	\$3,785	\$4,263	\$4,455
Net Direct Debt / Full Value (%)	0.7%	0.7%	0.6%	0.6%	0.5%
Net Direct Debt / Operating Revenues (x)	1.9x	1.7x	1.1x	1.1x	1.0x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	0.6%	0.6%	0.6%	0.7%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	1.6x	1.1x	1.3x	1.4x

Sources: Moody's Investors Service; US Census Bureau; city's audited financial statements

Profile

Nisswa is located in central [Minnesota](#) (Aa1 stable) in a resort area approximately 135 miles northwest of the [Minneapolis](#) (Aa1 negative) [St. Paul](#) (Aa1 negative) metro area, 115 miles southwest of [Duluth](#) (Aa2 stable), and 15 miles north of [Brainerd](#) (A1). The city has a land area of approximately 6,720 acres. City services include fire (26 volunteers), police (chief, sergeant and 4 officers) and sewer.

Detailed credit considerations

Economy and tax base: relatively small tax base and limited local economy

We expect the city's tax base to remain small in the near term given the limited economic development underway. The city's \$645 million tax base has remained relatively flat, with a 5 year compound annual growth rate of only 0.5%. Resort and recreation based activities are a primary driver of economic activity in the local economy. The Grand View Lodge is the city's largest employer (800 employees) and one of the county's largest employers. The lodge is currently undergoing a \$50 million expansion and renovation.

Median family income is estimated at 102% of the national median. As of March 2018, the Crow Wing County unemployment rate (5.6%) was above the state's rate (3.8%) and the national rate (4.1%). Current population estimates total approximately 2,100 residents, an increase from 1,400 residents in the early 1990s.

Financial operations and reserves: healthy operating trend with very strong reserves

The city's financial profile will remain strong in the near to medium term given a very strong liquidity position driven by a history of annual operating surpluses. The city closed each of the last six fiscal years with operating surpluses. These surpluses increased the combined available fund balance to \$5.4 million in fiscal 2017 from \$3.3 million in fiscal 2012, a more than 60% increase across the General Fund, Fire Fund, Park and Recreation Fund, Community Center Fund and the Debt Service Fund. The fiscal 2017 figure corresponds to with a very healthy 172.5% of operating revenue. Fiscal 2018 is more than half over and management expects to close the year with balanced operations.

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Property taxes are the city's primary revenue source (66%), followed by intergovernmental revenue (9%), and charges for services (8%).

LIQUIDITY

The city closed fiscal 2017 with a net cash position of \$5.5 million, equal to 177.5% of operating revenue. Of the city's \$5.5 million cash position, \$4.8 million is held in the General Fund, \$136,000 is held in the Debt Service Fund, \$400,000 is held in the Fire Fund, \$98,000 is held in the Park and Recreation Fund.

Debt and pensions: moderate leverage

The city's leverage related to long-term debt and pension liabilities is moderate. Inclusive of the 2018A bonds and exclusive of approximately \$860,000 of general obligation debt associated with the self-supporting sewer fund, the city has \$4.7 million in net direct debt, equal to 0.7% of full value and 1.5x fiscal 2017 operating revenue. The city's adjusted net pension liability (ANPL) totaled \$4.5 million in fiscal 2017, equal to 0.7% of full value and 1.4x operating revenue. In comparison, the city's reported net pension liability, based on the use of higher discount rates, was \$1.2 million. The city's total fixed costs, inclusive of debt service and retirement contributions, are equal to 19% of fiscal 2017 operating revenue.

DEBT STRUCTURE

All of the city's debt is fixed rate and long term with more than 90% of outstanding principal retired within 10 years. The city's GO bonds are secured by the city's pledge and authorization to levy a dedicated property tax unlimited as to rate and amount. The security benefits from a statutory lien, but there is no lockbox structure.

DEBT-RELATED DERIVATIVES

The city has no exposure to any debt-related derivatives.

PENSIONS AND OPEB

The city participates in two multiple-employer cost-sharing plans, the General Employees Retirement Fund (GERF) and the Public Employees Police and Fire Fund (PEPFF). Minnesota statutes establish local government retirement contributions as a share of annual payroll. The fiscal 2017 employer contribution rates were set at 7.5% of payroll for GERF and at 16.2% of payroll for PEPFF. The city's total fiscal 2017 pension contribution was \$121,000.

Contributions to PEPFF from all participating governments in aggregate amounted to only 90% of the plan's "tread water" indicator in 2017. Employer contributions that tread water equal the sum of current year service cost and interest on reported net pension liabilities at the start of the year, using reported assumptions. If plan assumptions are met exactly, contributions equal to the tread water indicator will prevent the reported net pension liabilities from growing.

Management and governance: strong institutional framework

Minnesota cities have an Institutional Framework score of Aa, which is high. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. The sector has one or more major revenue sources that are not subject to any caps. Revenues tend to be predictable, as cities rely primarily on property taxes and state Local Government Aid (LGA), which is distributed based on demographic and tax base factors. Revenue-raising flexibility is moderate as cities generally benefit from unlimited levying authority, except during years in which the state has imposed limits. Levy limits are not in place for the 2017-2018 biennium. Across the sector, fixed and mandated costs are relatively high. Minnesota has public sector unions, which can limit the ability to cut expenditures. Expenditures mostly consist of personnel costs, which are highly predictable.

Management has a history of generating operating surpluses that have resulted in a very strong liquidity position. The city does not currently have a formal fund balance policy but is in the process of developing one.

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REPORT NUMBER

1130682

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