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Ratings

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Summary:

Manchester, Tennessee; General Obligation

Primary Credit Analyst:
Matthew T Martin, New York + 1 (212) 438 8227; Matthew.Martin@spglobal.com

Secondary Contact:
Stuart Nicol, Chicago + 1 (312) 233 7007; stuart.nicol@spglobal.com

Table Of Contents

Summary:

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Credit Profile		
US$9.995 mil GO rfdg bnds ser 2021A due 06/01/2037		
Long Term Rating	AA/Stable	New
US$4.3 mil GO rfdg bnds ser 2021B due 08/01/2030		
Long Term Rating	AA/Stable	New
Manchester GO		
Long Term Rating	AA/Stable	Affirmed
Manchester GO bnds ser 2020B due 06/01/2050		
Long Term Rating	AA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AA' long-term rating and underlying rating to the City of Manchester, Tenn.'s approximate $10.0 million series 2021A and $4.3 million series 2021B general obligation (GO) bonds. At the same time, we affirmed our 'AA' rating on the city's GO debt outstanding. The outlook is stable.

The city's full-faith-and-credit pledge secures the bonds. Officials plan to use 2021A bond proceeds to refund various existing obligations of the city, including the series 2011 and 2014 rural development bonds and series 2016B GO bonds, for interest cost savings. In addition, the series 2021B proceeds will refund the city's existing series 2016A GO refunding bonds for interest cost savings.

Credit overview

The 'AA' rating reflects our view of the city's very strong balance sheet, with a very strong reserve position, manageable debt burden, and no meaningful retirement benefit liabilities. The rating also reflects our view of the city's stable and growing economy, which continues to see year-over-year growth both residentially and commercially. The stable outlook reflects our view that the city's financial positions will remain strong as macroeconomic conditions continue to improve to accent ongoing economic development. This prospect is supported by our most recent forecast, "Economic Outlook U.S. Q3 2021: Sun, Sun, Sun, Here It Comes," published June 24, 2021, on RatingsDirect. The outlook is further supported by financial and economic resiliency as demonstrated during the 2020 downturn.

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

- Weak economy, with projected per capita effective buying income (EBI) at 84.4% of the national level and market value per capita of $79,336;
- Adequate management, with standard 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 62% of operating expenditures;
- Very strong liquidity, with total government available cash at 17.7% of total governmental fund expenditures and 3.6x governmental debt service, and access to external liquidity that we consider strong;
- Adequate debt and contingent liability profile, with debt service carrying charges at 4.9% of expenditures and net direct debt that is 61.4% of total governmental fund revenue; and
- Very strong institutional framework score.

Environmental, social, and governance (ESG) factors

We analyzed the city's ESG risk factors relative to its economy, management, financial measures, and debt and liability profile, and determined that all are in line with our view of the sector standard. In our view, oversight provided by the Tennessee comptroller's offices provides basis for strong governance across the state.

Stable Outlook

Downside scenario

All else equal, if the city materially reduces its reserve position because of one-time spending or a period of structural imbalance, we could lower the rating.

Upside scenario

All else equal, should the city realize improvements in its economic metrics while sustaining its very strong reserves amid modest growth in its budget and potential capital spending, we could consider a higher rating. Supporting upward rating potential would be the development and formalization of its management and financial policies.

Credit Opinion

Weak economy

We consider Manchester's economy weak. The city, with an estimated population of 11,724, is in Coffee County. The city has a projected per capita EBI of 84.4% of the national level and per capita market value of $79,336. Overall, the city's market value grew by 19.2% over the past year to $930.1 million in 2021. The county unemployment rate was 7.8% in 2020, spiking to 20.7% in April 2020 at the onset of the pandemic before moderating to 4.4% as of May 2021.

Interstate 24--the main artery between Nashville and Chattanooga--traverses the city, connecting residents with regional employment centers. The broader regional economy remains stable, in our view, with anchoring employers in aerospace, automotive, and materials manufacturing, as well as the education and health care sectors.

The city also borders Arnold Engineering Development Center (over 2,300 employees), a joint-venture aerospace and flight simulation test facility between the U.S. Air Force and civilian contractors, which contributes significantly to the area's employment base. However, despite Manchester's proximity to the Arnold Air Force Base and several higher education institutions (within a 35-mile radius), we do not believe there is strong evidence demonstrating that colleges,

universities, or the military base provide a direct stabilizing institutional presence that would otherwise alter our view of the city's underlying wealth and income conditions.

Although we believe the city's economy is somewhat limited, in our view, the 10 largest taxpayers make up an estimated 12.7% of net taxable assessed value (AV), which we consider very diverse. Furthermore, the city is the permanent home of Bonnaroo Music Festival, which attracts 50,000-90,000 tourists annually, and provides an economic boost through direct local spending at city and county businesses, hotels, and restaurants. The festival was cancelled after months of postponement in 2020, and we recognize the subsequent loss in these revenues for Manchester. However, the city is not overly reliant on these revenues for fiscal stability and looks to recoup them moving forward as 2021's festival remains on schedule.

In addition to maintaining a stable employment and taxpayer base, the city is exploring opportunities to attract more commercial retail and hospitality development, while also managing expected residential growth. Officials indicate the city continues to see increased housing demand due to its comparative affordability in the region and proximity to surrounding employment and education opportunities. Even during the pandemic and now amid the economic recovery, officials note continued development and planning on both the industrial and residential front.

Adequate management

We view the city's management as adequate, with standard financial policies and practices under our FMA methodology, indicating the finance department maintains adequate policies in some but not all key areas.

In preparation of its annual budget, the city's uses three-to-four years of historical information to formulate annual revenue and expenditure assumptions. In addition, management consults its appraisal district to adjust for annual changes in AV and property tax collections.

During each fiscal year, management monitors budgetary performance regularly, and provides a comprehensive monthly budget-to-actuals report for the city council. According to management, budget amendments are made on an as-needed basis. The city also maintains a formal investment policy that adheres to state guidelines. Although it does not have a substantial amount held in investments, management reports earnings and holdings to the city's governing board monthly. The city does not conduct formal long-term capital or financial planning.

Furthermore, management has historically met and sustained reserves in accordance with its informal fund balance practices. Currently, Manchester maintains an unassigned fund balance target of three months (or 25%) of general fund expenditures. At the same time, its formally adopted debt management policy targets the types of debt it could issue, as well as what percent of debt could be variable-rate. According to the policy, variable-rate debt cannot exceed 35% of total debt outstanding. In addition, the city cannot enter into interest rate swaps or use derivative instruments unless it adopts a debt derivative policy and receives approval from the state. However, the debt policy does not provide quantitative guidelines in terms of debt affordability.

Strong budgetary performance

Manchester's budgetary performance is strong, in our opinion. The city had operating surpluses of 9.2% of expenditures in the general fund and 2.7% across all governmental funds in fiscal 2020. While we expect Manchester will have at least balanced operating results, we do not expect results will be as favorable as they were in 2020.

For analytical consistency, we adjusted fiscal 2020 general fund results to account for recurring transfers out to the general-purpose school, recreation, sanitation, and debt service funds from the general fund. The city attributes the favorable operating result to an increase in local tax revenue, primarily due to a better-than-budgeted sales tax receipts. Officials also reported reduced spending and cost-saving measures across all government departments, which contributed to lower-than-budgeted general fund expenditures.

In line with robust growth in its tax base and limited expenditure growth, the city has realized consistent operating surpluses since 2015. Property taxes are the largest general revenue source at approximately 41% of budgeted recurring revenue, followed by local option sales taxes at 35%. Altogether, the city's local revenue sources accounted for 80.3% of general fund revenues, followed by intergovernmental sources at approximately 12.0%.

The city's fiscal 2021 budget includes a planned drawdown of $1.9 million, partially driven by potential use of reserves to finance capital projects. Officials expect the drawdown will be closer to $1.6 million, but still driven by one-time spending as the city's budget is structurally sound. Manchester's budgets are typically cautious, as the fiscal 2021 budget cuts total local tax revenue figures by approximately 8%, with property taxes and local option sales taxes being cut by approximately 5% and 13%, respectively.

The fiscal 2022 approved general fund budget totals $15 million, including a deficit of approximately $1.5 million. The city's generally conservative revenue and expenditure projections coupled with intrayear expenditure monitoring will be crucial moving forward, as we expect budgetary performance will hinge on management's ability to manage any one-time spending such that reserve levels are not materially reduced beyond expectations. Given management's historical ability to outperform its budgets, we believe the city's performance should remain stable.

Very strong budgetary flexibility

Manchester's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2020 of 62% of operating expenditures, or $8.1 million. We expect the available fund balance will remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

The city has an informal practice of maintaining a minimum unassigned fund balance at 25% of general fund expenditures. Because of management's budgeting for deficit performance in fiscal years 2021 and 2022, we believe the city's historical maintenance of reserve levels above 30% of expenditures will likely be tested. Even so, were the city to spend down available fund balances in accordance with budgetary figures, it would still sustain a very strong available balance of about $5.1 million, or 33.9% of expenditures.

Very strong liquidity

In our opinion, Manchester's liquidity is very strong, with total government available cash at 17.7% of total governmental fund expenditures and 3.6x governmental debt service in 2020. In our view, the city has strong access to external liquidity if necessary.

Our opinion that Manchester maintains strong access to external liquidity reflects its history of issuing GO debt over the past 20 years. Although the state allows for what we view as somewhat permissive investments, we do not consider the city's investments aggressive. Investments are primarily held in the state's highly liquid local government investment pool or certificates of deposit.

In our opinion, the city does not have contingent liabilities or financial instruments with payment provisions that could cause immediate or material liquidity pressure.

Adequate debt and contingent liability profile

In our view, Manchester's debt and contingent liability profile is adequate. Total governmental fund debt service is 4.9% of total governmental fund expenditures, and net direct debt is 61.4% of total governmental fund revenue.

Furthermore, the city has issued enterprise-related GO debt--which we do not rate--on behalf of the Duck River Utility Commission, which was formed pursuant to an agreement under the provisions of Tennessee Interlocal Cooperation Act, for providing Manchester and the City of Tullahoma with potable water. Although the bonds are secured by the city's GO pledge, they are payable from the net operating revenue of the municipality's water and sewer system. GO-related debt centers on three years of evidence that user charges have provided at least partial coverage to support obligations outstanding. Therefore, we adjusted approximately $21.6 million of enterprise-related GO debt out from our net direct debt calculations.

Officials indicate they have no specific plans to issue additional debt over the next two-to-three years.

Pension and other postemployment benefit highlights

We do not consider the city's pension liabilities as likely to pose a significant credit risk, given the overfunded status and manageable contributions relative to the budget.

Manchester participates in the following pension plans as of fiscal year-end June 30, 2019:

- Tennessee Consolidated Retirement System (TCRS) Public Employee Retirement Plan (PER), an agent multiple-employer, defined-benefit pension plan that is 109.5% funded, with a proportionate share of the plan's net pension asset of $641,958.
- TCRS' Teacher Legacy Pension Plan (TLPP), a cost-sharing, multiple-employer plan that is 104.3% funded with a proportionate share of the plan's net pension asset of $1.994 million.

Significant funding progress was made in the most recent year for PER and TLPP, with contributions significantly in excess of our minimum funding progress metric. We believe that the PER plan's closed, level-dollar amortization of less than 20 years will lead to timely paydown of unfunded liabilities. However, both plans' 7.25% assumed discount rate leaves some risk of rising pension costs because of market volatility.

The city does not provide other postemployment benefits (OPEB) for general and public safety employees, but its school system contributes to a self-insured, multiple-employer, defined-benefit plan, which it funds on a pay-as-you-go-basis. Manchester's combined required pension and actual OPEB contributions totaled 3.7% of total governmental fund expenditures in 2020. The city made its full required pension contribution in 2020.

Very strong institutional framework

The institutional framework score Tennessee municipalities is very strong.

Related Research

- Credit Conditions: U.S. Regions' Economies Perk Up As The Pandemic's Impact Ebbs, April 16, 2021
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- 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
- 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