

RatingsDirect®

Summary:

Edina, Minnesota; Appropriations; General Obligation

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Credit Profile

US\$5.26 mil GO bnds ser 2020A dtd 06/25/2020 due 02/01/2037

Long Term Rating AAA/Stable New

Edina GO

Long Term Rating AAA/Stable Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to Edina, Minn.'s \$5.26 million, series 2020A general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the city's GO debt outstanding, and its 'AA+' long-term rating on the existing lease-revenue debt issued by the Edina Housing and Redevelopment Authority. The outlook is stable.

The city's unlimited-tax, full faith and credit GO pledge secures the series 2020A bonds. Proceeds will be used to finance the city's 2020 street and utility improvement projects.

The series 2020A bonds and some of the city's GO debt outstanding are additionally secured by various revenue sources, but we rate all GO debt to the city's GO pledge. The 'AA+' appropriation rating is based on the city's pledge to annually appropriate the necessary lease payments to make annual debt service; accordingly, the lease bonds are rated one notch below the city's general creditworthiness.

Edina's GO bonds are eligible to be rated above the sovereign because we believe the city can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria, "Ratings Above The Sovereign—Corporate And Government Ratings: Methodology And Assumptions" (published Nov. 19, 2013), U.S. local governments are considered to have moderate sensitivity to country risk. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy, independent treasury management, with no history of federal government intervention. We believe Edina's financial flexibility is sufficiently demonstrated by its very strong budgetary reserves and liquidity.

Credit overview

While the scope of economic and financial challenges posed by COVID-19 remains to be seen, given the city's extremely high reserve levels and lack of reliance on sales or income taxes, we believe Edina is well positioned to navigate the possible impact of the pandemic in the short-to-medium term. Edina embodies many of the typical characteristics of a 'AAA' rated issuer, including a diverse economy that is independently strong, but also part of a broad and diverse metropolitan statistical area (MSA); consistently stable financial operating results with no discernible budgetary pressures (despite the current recession), as the city relies primarily on residential and property taxes; and a

sophisticated and knowledgeable management team. Generally, our rating outlook timeframe is up to two years. Given the current uncertainty around the pandemic, our view of the credit risks to the city are centered on the more immediate budget effects in 2020. (For additional information, see "COVID-19 Deals A Larger, Longer Hit To Global GDP," published April 16, 2020; "Coronavirus Impact: Key Takeaways From Our Articles," published April 23, 2020; and "COVID-19 Activity In U.S. Public Finance," published April 27, 2020.)

The rating reflects our assessment of the following factors for Edina, specifically its:

- Very strong economy, with access to a broad and diverse MSA;
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2018;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2018 of 99% of operating expenditures;
- Very strong liquidity, with total government available cash at 1.5x total governmental fund expenditures and 12.0x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability profile, with debt service carrying charges at 12.7% of expenditures and net direct debt that is 107.8% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 82.2% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Environmental, social, and governance factors

The rating also incorporates our view of the health and safety risks posed by the COVID-19 pandemic, which we consider social risk factors. Although the scope of economic and financial challenges posed by the pandemic remains unknown, we believe a prolonged disruption could weaken the city's local economy. Absent the implications of COVID-19, we consider the city's social risks to be in line with those of the sector. We also view governance and environmental risks as being in line with our view of the sector as a whole.

Stable Outlook

Downside scenario

Significant financial deterioration could result in a lower rating.

Credit Opinion

Very strong economy

We consider Edina's economy very strong. The city, with an estimated population of 50,996, is located in Hennepin County in the Minneapolis-St. Paul-Bloomington MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 209% of the national level and per capita market value of \$254,262. Overall, the city's market value grew by 5.4% over the past year to \$13.0 billion in 2019. The county unemployment

rate was 2.8% in 2019.

Edina remains one of the Twin Cities' premier, wealthy, inner-ring suburbs. Despite being fully built out, the city has seen substantial growth over the past five years, as residents and business owners tear down and replace older homes and buildings with new construction, or heavily remodel existing structures. Management reports that disruption to the economy due to COVID-19 and the ensuing recession is concentrated in the city's retail and restaurant community but, given that Edina is largely residential, we believe that if the recession is prolonged it may affect the city in the medium-to-long term. Residences make up a majority of the tax base (66%), followed by commercial/industrial (26%).

Edina's retail centers are likely the most vulnerable area of the city's economy during the recession. One of the city's primary retail centers is Southdale Mall, the oldest climate-controlled shopping center in the country. The Southdale-area properties total less than 5% of total market value, illustrating the diversity of properties and lack of tax base concentration in the city. The mall itself and the area around it have experienced a continual renaissance, as high-end, stand-alone retail stores have been added; existing obsolete retail square footage has been converted to fitness centers and other purposes; and luxury apartments have been built near the perimeter of the property.

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.

The city council adopts a detailed two-year budget and maintains a five-year capital improvement plan that is updated every two years and identifies sources and uses of funds. The council reviews budget-to-actual results, along with investment holdings, quarterly. Edina meets its policy to maintain an unassigned general fund balance at 42%-47% of the subsequent year's budgeted tax revenue. When the unassigned fund balance falls below or exceeds this range, the city council either creates a plan to restore fund balance or considers transferring the excess to other funds. In the past several years, the council has made transfers to the construction fund. The city also has its own debt management policy and investment policy.

Strong budgetary performance

Edina's budgetary performance is strong, in our opinion. The city had operating surpluses of 8.7% of expenditures in the general fund and of 12.1% across all governmental funds in fiscal 2018. General fund operating results of the city have been stable over the past three years, with a result of 8.1% in 2017 and a result of 6.9% in 2016.

We adjusted fiscal 2018 (year-end Dec. 31) total governmental fund expenditures to exclude the one-time \$10 million expenditure for the construction of a parking garage. Although budgetary performance has generated net positive results for several years, we believe the pressures resulting from the pandemic and recession could pose budgetary challenges in the medium-to-long term. The budgetary performance score of strong reflects our view of budgetary uncertainty facing Edina in the current economic climate, particularly related to the city's revenue from property taxes (63% of general fund revenues) and charges for services (11%).

Unaudited 2019 results indicate a general fund deficit of \$1.5 million after transfers, or 3.8% of expenditures, but the city had \$3.3 million of larger-than-usual one-time capital expenditures. With the exclusion of these, Edina would show a \$1.9 million surplus (4.4% of expenditures). Management attributes the positive year to building permits being up

considerably over the previous year and expenses coming in under budget.

The 2020 budget includes break-even results in the general fund, and year to date, management reports that revenue and expenditures are tracking in line with the budget. The city amended the budget to transfer \$600,000 to the budget stabilization fund, held within the construction fund. Given the city's history of outperforming its budget and its growing revenue related to the ongoing development, we believe the year will likely close with another surplus (excluding the one-time transfer to the budget stabilization fund). Similarly, the city has demonstrated strong performance across total governmental funds, after adjustments for one-time expenditures, which we expect to continue. Property taxes for 2020 are currently in process, and the city is expecting an immaterial amount of delays in property tax collections. Nevertheless, the city has identified areas where it can cut expenditures and set up a budget stabilization fund. With the historical surpluses, we think Edina could absorb some reduced or delayed revenues.

Very strong budgetary flexibility

Edina's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2018 of 99% of operating expenditures, or \$40.3 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 available fund balance includes \$18.9 million (46.6% of expenditures) in the general fund and \$21.4 million (53% of expenditures) that is outside the general fund but legally available for operations.

The amount of available fund balance outside the general fund consists of the liquor fund's cash balance (\$1.8 million) and the assigned portion of the construction fund balance (\$19.7 million), which the general fund contributes to each year through transfers. The construction fund portion has been growing each year, and while it is assigned for capital purposes (equipment, vehicles, etc.), it could be reassigned for general operations at any time without restrictions. We expect general fund reserves will remain in compliance with the city's policy to maintain 42%-47% of the subsequent year's budgeted tax revenue, and so we expect budgetary flexibility will remain very strong.

Very strong liquidity

In our opinion, Edina's liquidity is very strong, with total government available cash at 1.5x total governmental fund expenditures and 12.0x governmental debt service in 2018. In our view, the city has strong access to external liquidity if necessary.

Edina holds over \$92 million in available cash and investment. The city has issued bonds frequently during the past 15 years and maintains a strong credit profile, so we believe it would have strong market access if needed for external liquidity. The majority of Edina's investments are in municipal securities, U.S. agencies, and U.S. treasury bonds and notes, although the city does have a small amount in commercial paper. Overall, we do not view these investments as aggressive. Edina has no direct-purchase or variable-rate debt. We expect the city's liquidity profile to remain very strong.

Strong debt and contingent liability profile

In our view, Edina's debt and contingent liability profile is strong. Total governmental fund debt service is 12.7% of total governmental fund expenditures, and net direct debt is 107.8% of total governmental fund revenue. Overall net debt is low at 2.7% of market value, and approximately 82.2% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

The city has \$104.5 million in debt outstanding and management plans to issue up to \$18 million of bonds over the next two years, but will amortize that amount over the same period, leaving the overall debt profile unchanged.

Edina's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 4.8% of total governmental fund expenditures in 2018. The city made its full annual required pension contribution in 2018.

- We do not believe that pension and OPEB liabilities represent a medium-term credit pressure, as contributions are only a modest share of the budget, and we believe the city has the capacity to absorb higher costs without pressuring operations.
- The city's two largest pension plans have seen improvements in funded status in recent years, although plan statutory contributions have regularly fallen short of actuarial recommendations. Along with certain plan-specific actuarial assumptions and methods, this introduces some long-term risk of funding volatility and cost acceleration.
- Although the city funds its OPEB on a pay-as-you-go basis, exposing it to cost acceleration and volatility, we expect that medium-term costs will remain only a small share of total spending and therefore are not a significant budgetary pressure.

The city participates in the following defined-benefit plans:

- Minnesota General Employees Retirement Fund (GERF): 79.5% funded (as of June 30, 2019), with a city proportionate share of the plan's net pension liability at \$14.7 million;
- Minnesota Police and Fire Fund (PEPFF): 88.8% funded (June 30, 2019), with a proportionate share of \$8.6 million; and
- A single-employer OPEB plan, which is funded on a pay-as-you-go basis with a net OPEB liability of \$3.5 million (as of Dec. 31, 2018).

Annual contributions are based on a statutory formula, which we view as a negative credit factor. We think this increases risk of underfunding over time if future funding shortfalls are not met with offsetting adjustments by the state legislature. Statutory rates did not meet our minimum funding progress metric last year; however, these fixed rates are scheduled to increase in 2020. Another key risk is a 7.5% investment rate of return assumption (for both plans), which is higher than our 6.5% guideline. This indicates some exposure to liability acceleration from market volatility. Regardless, costs remain only a modest share of total spending and, in our view, 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
- 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 28, 2020)		
Edina GO recreational rev bnds ser 2017B dtd 06/29/2017 due 02/01/2033		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Edina GO CIP rfdg bnds		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
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Edina GO		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Edina Hsg & Redev Auth, Minnesota		
Edina, Minnesota		
Edina Hsg & Redev Auth (Edina)		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Edina Hsg & Redev Auth (Edina) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Edina Hsg & Redev Auth (Edina) APPROP		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

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