S&P Global
Ratings

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Summary:

Victoria, Minnesota; Appropriations; General Obligation

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Credit Profile		
US$6.435 mil GO abatement, imp & CIP rfdg bnds ser 2020A due 02/01/2036		
Long Term Rating	AAA/Stable	New
Victoria GO tax abatement and rfdg bnds ser 2016C dtd 11/01/2016 due 02/01/2032		
Long Term Rating	AAA/Stable	Affirmed
Victoria Economic Development Authority, Minnesota		
Victoria, Minnesota		
Victoria Economic Development Authority (Victoria) APPROP		
Long Term Rating	AA+/Stable	Affirmed

Rating Action

S&P Global Ratings assigned is 'AAA' rating to the City of Victoria, Minn.'s $6.435 million series 2020A general obligation (GO) abatement, improvement, and capital improvement plan refunding bonds. At the same time, S&P Global Ratings affirmed its 'AAA' underlying rating on the city's GO bonds outstanding and its 'AA+' rating on the Victoria Economic Development Authority's series 2014A lease revenue and limited-tax bonds, issued for the city. The outlook is stable.

Series 2020A bonds are general obligations of the city and are secured by Victoria's full faith and credit pledge to levy ad valorem taxes, without limitation of amount. The bonds are also payable from special assessments levied against benefitted properties and a tax abatement levy. Bond proceeds will be used to fund construction of Victoria's first regional park, road improvements, a fire suppression improvement project, and to current-refund the city's series 2014A lease revenue and limited tax bonds outstanding for interest savings.

Victoria's GO bonds are eligible to be rated above the sovereign because we believe the city can maintain better credit characteristics than the nation 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, and no history of government intervention.

Credit overview

Victoria is located southwest of Minneapolis-St Paul and is part of the seven-county metropolitan area. In our view, the city's economy is very strong, with high incomes and a predominantly residential tax base that contributes to extremely strong market values. The city's strong management and stable local economic base have supported a long-standing record of consistently positive operating results and very strong reserves and liquidity. Management reports that the onset of the COVID-19 pandemic and recession have slowed local business operations beginning with the governor's stay-at-home orders in late March. However, businesses have begun reopening in recent weeks and will operate under social distancing requirements specified under the state's Stay Safe Plan over the near term. Management reports no immediate general fund budgetary effects as a result of the recession, but anticipates revenues at the city's recreation center could be pressured due to underuse over the summer. Given the general fund's historically stable revenue composition and considering the city's very strong flexibility and liquidity, we believe Victoria has adequate resources to address potential fiscal pressures over the next six-to-12 months.

The rating reflects our assessment of the city's:

- 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 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 60% of operating expenditures;
- Very strong liquidity, with total government available cash at 2.1x total governmental fund expenditures and 6.7x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability profile, with debt service carrying charges at 31.0% of expenditures and net direct debt that is 242.5% of total governmental fund revenue, but rapid amortization, with 74.2% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Environmental, social, and governance factors

We analyzed Victoria's overall environmental, social, and governance risks relative to the city's economy, management, budgetary outcomes, and debt and liability profile. Considering the city's continental Midwestern climate, stable population and tax base, and consistently positive general fund operations and strong governance practices, we determined that all are in line with our view of the sector standard.

Stable Outlook

Downside scenario

We could lower the rating if Victoria's budgetary performance were to decline, causing a deterioration in reserves to a level we view as no longer comparable to that of similarly rated peers. We could also lower the rating if potential increases to the city's debt burden place greater pressure on its budgetary performance or tax base.

Credit Opinion

Very strong economy

We consider Victoria's economy very strong. The city, with an estimated population of 8,453, is located in Carver 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 222% of the national level and per capita market value of $197,316. Overall, the city's market value grew by 13.4% in 2018 to $1.7 billion in 2019. The county unemployment rate was 2.8% in 2019. In April 2020, the county unemployment rate was 7.3%.

The city's tax base is primarily residential homestead (80%) and residential nonhomestead (15%), with a small commercial and industrial presence (3%). The city has experienced a sizable increase in residential development over the past few years. Before 2016, the three-year average of building permits issued was 598. From 2016 to 2019, annual building permits averaged 1,079, spurred primarily by new home permits. So far in 2020, the city's building permit activity is trending positively, with 247 permits issued through April. Management reports no development plans have been paused because of the COVID-19 pandemic and resulting recession, and that plans for a new 82-unit group home and senior living housing complex are well underway. Due primarily to the increase in residential developments, Victoria is expecting continued growth in terms of economic market values and net tax capacity. Based on our assessment of the city's economic developments, we view these expectations as likely. We also consider the tax base very diverse, with the top 10 taxpayers representing 4.5% of net tax capacity.

City residents primarily commute to the Minneapolis-St. Paul MSA for employment opportunities. Within the city, some of the leading employers include Holy Family Catholic High School (120 employees), Victoria Elementary School (110), Community Living Inc. (100), and Emerald Crest residential homes (100). Although many of the city's commercial businesses had paused operations in March through early June due to the COVID-19 pandemic, we understand many have begun reopening and will adhere to social distancing requirements as they resume operations in the upcoming months. While there is uncertainty regarding how the pandemic and recession will affect Victoria's economy in the long term, we expect the city's access to the Twin Cities MSA, in addition to the city's predominantly residential tax base and high market values and incomes, will lend stability.

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.

Highlights of Victoria's policies and practices include:

- Use of at least three years of historical information in the formulation of the upcoming year's revenue and expenditure assumptions, with the help of outside sources, and a line-by-line approach to budgeting;
- Quarterly reporting of budget-to-actual performance to the council, with the ability to make amendments to the budget, as needed;
- A formalized long-term financial plan that looks out 15 years and is updated throughout the year;
- A formalized long-term capital plan that looks out five years, with sources and uses of funds identified, and that is updated on an annual basis;
- A formalized investment management policy, with quarterly reporting of investments and holdings;

- A formalized debt management policy that restricts the city's debt limitations and refunding savings thresholds; and
- A formalized fund balance policy to maintain at least 30% of the subsequent year's budgeted expenditures.

Strong budgetary performance

Victoria's budgetary performance is strong in our opinion. The city had operating surpluses of 8.1% of expenditures in the general fund and of 15.4% across all governmental funds in fiscal 2019.

Although budgetary performance has generated net positive results in the past three fiscal years, we believe the pressures resulting from the pandemic and recession could pose budgetary challenges in the near term. The strong budgetary performance score reflects our view of the budgetary uncertainty the city faces because of the current economic climate, particularly as it relates to revenues from Victoria's recreation center, which could be pressured because of the pandemic.

We made adjustments for recurring transfers out of the general fund for capital equipment purchases to assess Victoria's recent budgetary performance. We also made adjustments for the spending of bond proceeds and one-time capital purchases across total governmental funds. After these adjustments, Victoria has reported net positive results under the general fund and across total governmental funds for the past three audited fiscal years. Management attributes recent positive variances in the general fund primarily to higher revenues from licenses and permits and conservative budget assumptions.

For fiscal 2020, the city budgeted for a slight general fund surplus of $64,000 (1.1%). The general fund benefits from a revenue structure that has historically been stable and predictable, consisting primarily of property taxes (74%), licenses and permits (11%), and charges for services (10%). Currently, management does not plan to make expenditure adjustments in the general fund, and reports revenues trended higher and expenditures trended lower in the first quarter of fiscal 2020. In response to the pandemic, Carver County has waived the penalty for late property tax payments due in May through mid-July. However, the county's policy also guarantees that Victoria will be made whole for current-year tax collections. Based on the general fund's historically stable revenue composition and management's conservative budgeting practices, we expect the general fund will likely end the year with at least a breakeven result.

From a total governmental funds perspective, we expect the city could report a negative result primarily due to continued capital projects, though once adjusted, results in those funds could be closer to breakeven. Management reports revenue uncertainty at the recreation center because of the pandemic, which could contribute to a year-end deficit in the recreation center fund. Based on management's historically conservative budgeting practices, we anticipate the city will appropriately manage its budget to reduce recreation center variable costs if revenues decline over the upcoming months.

Very strong budgetary flexibility

Victoria's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 60% of operating expenditures, or $3.1 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.

As additional flexibility, we included a committed portion of the general fund balance that is for revenue stabilization and would be available with no restrictions following a city council vote. Based on the current budget for fiscal 2020 and management's plan to maintain it reserves, we believe Victoria's available fund balance as a percentage of expenditures will remain very strong and above 30%.

Very strong liquidity

In our opinion, Victoria's liquidity is very strong, with total government available cash at 2.1x total governmental fund expenditures and 6.7x governmental debt service in 2019. In our view, the city has strong access to external liquidity if necessary.

We believe that the city has strong access to external liquidity, having issued GO debt, which demonstrates access to capital markets. We do not expect its cash position, with respect to its total governmental expenditures and debt service, to change much during the next two years and expect it will remain very strong. We understand that currently, Victoria does not have any potential contingent liabilities that could have an adverse impact on its cash position. As it relates to investments, the city invests primarily in certificates of deposit, U.S. treasuries, and state agencies. Therefore, we do not consider the city's investments aggressive.

Weak debt and contingent liability profile

In our view, Victoria's debt and contingent liability profile is weak. Total governmental fund debt service is 31.0% of total governmental fund expenditures, and net direct debt is 242.5% of total governmental fund revenue. Almost 75%of direct debt is scheduled to be repaid within 10 years, which is in our view a positive credit factor.

Victoria has $25.5 million of total direct debt outstanding, of which we consider $2.3 million self-supporting enterprise debt. We understand the city could issue an additional $9 million of debt in the next two years to fund various street and utility improvement projects. Offsetting the city's high debt burden is its rapid amortization. Overall, we expect the city's debt profile will remain weak in the medium term.

Pension and other postemployment benefits

- We do not believe that Victoria's pension liabilities represent a medium-term credit pressure because 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 participates in two multiple-employer, defined benefit pension plans that have seen recent improvements in funded status, though 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.
- The city offers no other postemployment benefits.

Victoria participates in the following plans:

- Minnesota General Employees Retirement Fund (GERF): 80.2% funded (as of June 30, 2019), with an estimated city proportionate share of the plan's net pension liability of $1.2 million.
- Minnesota Public Employees Police and Fire Fund (PEPFF): 89.3% funded (June 30, 2019), with an estimated city proportionate share of the plan's net pension liability of $86,000.

The city's pension contributions were 2.4% of governmental fund expenditures in fiscal 2019. Total contributions to

GERF and PEPFF were 89.0% and 93.7%, respectively, of our minimum funding progress metric in 2019 and were slightly above static funding in both cases. Annual contributions are based on a statutory formula that has typically produced contributions less than the actuarially determined contribution for each plan, which we think increases risk of underfunding over time if future funding shortfalls are not met with offsetting adjustments by the state legislature. Other key risks include a 7.5% investment rate of return assumption (for both plans) that indicates some exposure to cost acceleration due to market volatility, and amortization methods that significantly defer contributions through lengthy, closed 30-year amortization periods based on a level 3.25% payroll growth assumption. Regardless, costs remain only a modest share of total spending and, we think, are unlikely to pressure Victoria'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

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- The U.S. Faces A Longer And Slower Climb From The Bottom, June 25, 2020
- 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 June 26, 2020)		
Victoria GO		
Long Term Rating	AAA/Stable	Affirmed
Victoria GO		
Long Term Rating	AAA/Stable	Affirmed
Victoria GO		
Long Term Rating	AAA/Stable	Affirmed
Victoria GO		
Long Term Rating	AAA/Stable	Affirmed
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Long Term Rating	AAA/Stable	Affirmed
Victoria GO		
Long Term Rating	AAA/Stable	Affirmed
Victoria GO bnds		
Long Term Rating	AAA/Stable	Affirmed

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.