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New Issue

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St. Charles (City of) IL

New Issue - Moody's Assigns Aa1 to St. Charles, IL's GO Bonds, Ser. 2016A&B

Summary Rating Rationale

Moody's Investors Service has assigned a Aa1 to the City of St. Charles, IL's $7.3 million General Obligation Corporate Purpose Bonds, Series 2016A and $11 million General Obligation Corporate Purpose Refunding Bonds, Series 2016B. Concurrently, Moody's maintains the Aa1 rating on the city's outstanding General Obligation (GO) debt. Post sale, the city will have $94.5 million in debt outstanding.

The Aa1 rating reflects the city's large tax base, healthy operating trend, conservative budgeting practices resulting in strong reserve levels, financial flexibility derived from home rule status, the city's somewhat elevated debt burden, and growing unfunded pension liabilities.

Credit Strengths

» Stable economy located in the Chicago (Ba1 negative) metropolitan region

» Affluent socioeconomic profile

» Stable financial operations supported by strong reserve levels with alternate liquidity in the Capital Fund

» Financial flexibility derived from home rule status

Credit Challenges

» Reliance on economically sensitive revenues from sales and income tax

» Elevated debt burden for the rating category

» Structurally imbalanced operations in some of the city's TIF Funds

Rating Outlook

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

Factors that Could Lead to an Upgrade

» Significant growth in the city's tax base

» Moderation of debt and pension liabilities

» Improved performance across the city's TIF districts

Factors that Could Lead to a Downgrade

» Weakening of the city's tax base or demographic profile

» Declines in operating reserves or economically sensitive revenues

» Increases in the city's debt or pension liabilities

» Ongoing operating support for the city's TIF districts that negatively impacts the city's operations or reserves

Key Indicators

Exhibit 1

St. Charles (City of) IL	2011	2012	2013	2014	2015
Economy/Tax Base					
Total Full Value ($000)	$ 4,649,033	$ 4,382,578	$ 4,125,870	$ 4,000,887	$ 3,903,094
Full Value Per Capita	$ 141,773	$ 132,621	$ 124,172	$ 119,708	$ 117,326
Median Family Income (% of US Median)	154.5%	158.1%	161.5%	167.4%	167.4%
Finances					
Operating Revenue ($000)	$ 40,494	$ 41,756	$ 42,203	$ 41,583	$ 43,298
Fund Balance as a % of Revenues	51.9%	50.6%	47.7%	49.6%	50.1%
Cash Balance as a % of Revenues	48.0%	40.6%	27.0%	37.3%	46.0%
Debt/Pensions					
Net Direct Debt ($000)	$ 99,263	$ 98,464	$ 98,514	$ 97,145	$ 93,325
Net Direct Debt / Operating Revenues (x)	2.5x	2.4x	2.3x	2.3x	2.2x
Net Direct Debt / Full Value (%)	2.1%	2.2%	2.4%	2.4%	2.4%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)		1.4x	1.8x	2.1x	2.3x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)		1.4%	1.8%	2.2%	2.6%

The above table does not include the most recent sale data. Post sale, the city will have $94.5 million of outstanding debt, equal to an above average 2.4% of full value and 2.2 times fiscal 2015 operating revenues.
Source: Audited Financial Statements, Moody's Investors Service and U.S. Census Bureau

Recent Developments

The city closed fiscal 2015 with a $890,000 operating surplus which increased the city's available fund balance to $21.7 million, or a very strong 50.1% of operating revenues. Management reports that the city closed fiscal 2016 with a $1.8 million operating surplus, $1 million of which was subsequently transferred out to the Capital Improvement Fund. The city's fiscal 2017 budget is balanced.

Detailed Rating Considerations

Economy and Tax Base: Large Tax Base Near Chicago

The city's tax base is beginning to recover from the shock of the 2007-09 recession. Current full valuation of $4 billion remains 20% below the 2009 peak, but grew by 1.8% during the last year. The city's tax base is comprised of approximately 67% residential, 23% commercial and 10% industrial. Future valuation growth will largely be limited to the appreciation and redevelopment of existing properties because the city is relatively built out, with little space available for new commercial or residential development. Management reports relatively stable operations among the city's larger taxpayers and employers. The city's top 10 taxpayers comprise 5.5% of the city's EAV, primarily consisting of Q Center LLC (1.2%), AMLI at St. Charles LLC (1%) and the St. Charles County Club (0.5%). Between 2011 and 2016, Honeywell and Pheasant Run Resort and Convention Center reduced employment by a combined 550 employees while RR Donnelly & Sons and Omron Electrics LLC increased employment by a combined 900 employees.

The city's population grew in each of the previous four census periods, including a recent increase of 18.2% during the 2010 census. Median Family Income of the city is estimated at 167.4% of the national figure. As of May 2016, the city's unemployment rate (4.3%) was below the state's rate (5.6%) and on par with the national rate (4.5%).

Financial Operations and Reserves: Healthy Operations with Strong Reserve Position; Operating Support for TIF Debt Expected to Continue

A recent series of operating surpluses have enhanced the city's fund balance and liquidity, positioning it for continued fiscal stability. St. Charles closed fiscal 2015 with a fourth consecutive operating surplus across the major operating funds - the General Fund and Debt Service Fund. The $890,000 operating surplus increased the city's available fund balance to $21.7 million, or a very strong 50.1% of operating revenues. The city has achieved these positive operating results while meeting full actuarial funding requirements of its pension plans. Management reports that the city closed fiscal 2016 with a $1.8 million operating surplus, $1 million of which was transferred out to the Capital Improvement Fund. The city's fiscal 2017 budget is balanced.

The city maintains six Tax Increment Financing (TIF) districts. The TIF Funds closed fiscal 2015 with a combined unassigned deficit balance of approximately $3.6 million and owe the General Fund approximately $3.8 million, primarily due to annual transfers to cover debt service payments as increment revenues are insufficient. Management expects that at least two of the city's TIFs will require continued General Fund support over the near to medium term.

The city's ample financial flexibility enhances its credit profile. The city benefits from its home rule authority as it is not subject to levy limits, has no statutory debt ceiling and can impose a variety of taxes including sales, utility, hotel, and food/beverage. Utilizing this authority, the city is in the process of identifying three new revenue streams during the next five years with the goal of increasing operating revenues to mitigate any potential operating pressure stemming from the State of Illinois' fiscal pressures. Additionally, the city currently pays for a majority of its debt service with General Fund revenues, which provides the city with additional revenue flexibility as it could chose to levy for debt service payments in its debt service fund.

LIQUIDITY

The city closed fiscal 2015 with a net cash position across its operating funds of $20 million, or a strong 46% of operating fund revenues. The city closed fiscal 2015 with an additional $7.5 million in available alternate liquidity in its Capital Projects Fund. While these funds are earmarked for capital projects, they are available for General Fund operations should it become necessary, further strengthening the city's reserve levels.

The city also oversees three enterprise operations: water, sewer and electric. The city's electric utility closed fiscal 2015 with $1.7 million in cash (12 days cash on hand), the water utility closed fiscal 2015 with $3.9 million in cash (399 days cash on hand) and the sewer utility closed fiscal 2015 with $4.1 million in cash (281 days cash on hand). Cash across all major utilities totaled $6.3 million (60 days cash on hand) at the close of fiscal 2015.

Debt and Pensions

We expect the city's debt burden to remain somewhat elevated compared to similarly rated credits. Post sale, the city will have $94.5 million of outstanding debt, equal to an above average 2.4% of full value and 2.2 times fiscal 2015 operating revenues. The city may issue up to $15 million in GO debt to finance a new police station. The Moody's adjusted net pension liability (ANPL) for the city, which we discuss in more detail below, is $100 million, or a moderate 2.5% of full value and 2.3 times operating fund revenue. Fiscal 2015 fixed costs, inclusive of debt service and pension contributions totaled 30% of operating fund revenues.

DEBT STRUCTURE

All of the city's debt is fixed rate, with 52.7% of principal amortized over the next ten years.

DEBT-RELATED DERIVATIVES

The city is not a party to any derivative agreements.

PENSIONS AND OPEB

The city's pension liabilities are moderate. The city's liabilities are related to single employer defined benefit police and fire pension funds and the Illinois Municipal Retirement Fund, a multi-employer agent plan. The city's three year Moody's adjusted net pension liability (ANPL), under our methodology for adjusting reported pension data, is $100 million, or a moderate 2.5% of full value and

2.3 times operating fund revenue. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace city's reported liability information, but to improve comparability with other rated entities.

Management and Governance: Moderate Institutional Framework; Strong City Management

Illinois cities have an institutional framework score of “A,” or moderate. Revenue predictability is moderate, with varying dependence on property, sales, and state-distributed income taxes. Revenue-raising ability is also moderate but varies. Home rule entities, including the City of St. Charles, have substantial revenue-raising authority. Non-home rule entities are subject to tax rate limitations, and total operating tax yield for non-home rule entities subject to the Property Extension Limitation Law (PTELL) is capped at the lesser of 5% or CPI growth, plus new construction. Expenditures are moderately predictable but cities have limited ability to reduce them given costs for pension benefits that enjoy strong constitutional protections.

The city maintains a diverse revenue stream but is exposed to economically sensitive revenues. In fiscal 2015, the city's largest revenue sources included sales taxes (39.4%), property taxes (28.7%) and utility taxes (8.1%). The state has proposed cutting the state shared income taxes to local governments by 50%. The city's state income tax revenue totaled $3.3 million in fiscal 2015, or 7.5% of total operating revenues.

City management follows a number of strong financial practices including monthly budget surveillance, maintaining a four year capital improvement plan for the city and a 10 year capital improvement plan for the utilities, following a formal fund balance policy of maintaining an unassigned reserve of no less than 25% of expenditures, and has a history of making 100% of the actuarially required pension contributions.

Legal Security

Debt service on the city's GOULT bonds, inclusive of the current issuance (Series 2016A & Series 2016B), is secured by the city's pledge and authorization to levy a dedicated property tax unlimited as to rate and amount.

Use of Proceeds

Proceeds from the Series 2016A bonds will be used to fund capital improvements in the city, road improvements, electric utility improvements and water main improvements.

Proceeds from the Series 2016B bonds will be used to refund portions of the city's outstanding GO bonds Series 2006, Series 2007A-C and Series 2008A-C. The refunding is for interest cost savings.

Obligor Profile

The city is located on the Fox River in Kane (Aa1) and DuPage (Aaa) counties approximately 34 miles west of the City of Chicago. The city's population totals approximately 33,000 residents and has grown consistently in recent decades, increasing by 24% between 1990 and 2000 and by an additional 18% between 2000 and 2010.

Methodology

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

Ratings

Exhibit 2

St. Charles (City of) IL

Issue	Rating
General Obligation Corporate Purpose Bonds, Series 2016A	Aa1
Rating Type	Underlying LT
Sale Amount	$7,285,000
Expected Sale Date	08/24/2016
Rating Description	General Obligation

General Obligation Corporate Purpose Refunding Bonds, Series 2016B	Aa1
Rating Type	Underlying LT
Sale Amount	$10,970,000
Expected Sale Date	08/24/2016
Rating Description	General Obligation

Source: Moody's Investors Service

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