

RatingsDirect®

Summary:

Naperville, Illinois; General Obligation

Primary Credit Analyst:

David H Smith, Chicago (312) 233-7029; david.smith@spglobal.com

Secondary Contact:

Andrew J Truckenmiller, Chicago (1) 312-233-7032; andrew.truckenmiller@spglobal.com

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Summary:

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Credit Profile

US\$8.01 mil GO bnds (General Obligation Bonds) ser 2017 due 12/01/2037

Long Term Rating AAA/Stable New

Naperville GO

Long Term Rating AAA/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' long-term rating to the City of Naperville, Ill.'s series 2017 general obligation (GO) bonds. At the same time, we affirmed our 'AAA' long-term rating on the city's existing GO debt. The outlook is stable.

The series 2017 bonds are secured by the city's unlimited tax GO pledge. Proceeds from the bonds will be used for capital improvements within the city.

The rating reflects the following credit characteristics of the city:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with "strong" financial policies and practices under our financial management assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could improve in the near term relative to fiscal 2016, which closed with a slight operating deficit in the general fund and an operating deficit at the total governmental fund level in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2016 of 22% of operating expenditures;
- Very strong liquidity, with total government available cash at 40.4% of total governmental fund expenditures and 5.9x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 6.8% of expenditures and net direct debt that is 75.9% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 81.1% of debt scheduled to be retired in 10 years, but a large pension and other postemployment benefit (OPEB) obligation; and
- Strong institutional framework score.

Very strong economy

We consider Naperville's economy very strong. The city, with an estimated population of 145,443, is located in DuPage and Will counties in the Chicago-Naperville-Elgin, IL-IN-WI MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income (EBI) of 167% of the national level and per capita market value of \$137,532. Overall, the city's market value grew by 11.3% over the past two years to \$20.0 billion in 2016. The weight-averaged unemployment rate of the counties was 5.2% in 2016.

Naperville is located in southwestern DuPage County, with a portion of the city in Will County, and covers

approximately 40 square miles. Major employers in the city include Edward Hospital (4,500 employees), School District No. 204 (3,022 employees), Alcatel Lucent (3,000 employees). The city's largest employer, Edward Hospital, recently announced that it will be making layoffs. City management has indicated that it has insufficient information regarding this change to determine its impact on the local economy, but based on its discussions with hospital officials, it is optimistic that the impact will not be major. We consider the city's tax base to be very diverse, with top 10 taxpayers representing 2.5% of equalized assessed valuation (AV). The city has seen continued growth in the residential real estate market, with housing prices approaching their pre-recession peaks. Based on expected growth in the next year and the city's participation in the broad and diverse MSA, we expect the local economic base will remain very strong for the foreseeable future.

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.

In developing its annual budgets, the city uses in-house revenue and expenditure projections based on historical trends and economic data. The city also consults the Illinois Municipal League for projections regarding state income tax. In addition, the city also provides monthly budget-to-actual reports to the city council. The city has a four-year comprehensive long-term financial plan that is updated annually. In addition, the city maintains a five-year capital improvement plan, which is updated annually, with funding sources and costs for projects identified. With regard to investments, the city maintains its own investment policy, and provides quarterly investments to the council summarizing investment earnings and holdings. The city has a formal debt management policy, which includes limits on debt issuance. The city also maintains a formal fund balance policy of 20% of general fund expenditures, with provisions in place to ensure the replenishment of its fund balance should the city fall below its stated 20% reserve policy. In addition, the city has a goal of increasing its reserve policy to 25% of general fund expenditures.

Adequate budgetary performance

Naperville's budgetary performance is adequate in our opinion. The city had slight deficit operating results in the general fund of negative 1.3% of expenditures, and deficit results across all governmental funds of negative 1.8% in fiscal 2016. Our assessment accounts for the fact that we expect budgetary results could improve from 2016 results in the near term.

Our analysis of the city's budgetary performance reflects adjustments made for recurring transfers and one-time revenues and expenditures. In fiscal 2016 (year ended Dec. 31), the city reported a general fund deficit of \$1.5 million, which was primarily because of a shift of \$1.0 million in food and beverage tax revenues away from the general fund. In addition, the city experienced delays in income tax revenues received from the state, which contributed to this result.

For unaudited fiscal 2017, the city forecasts a 0.9% general fund surplus, or \$1.1 million. Contributing to this expected result is stronger than anticipated real estate transfer tax revenues and higher permit and license fee revenue. In addition, the city incurred slightly lower expenditures to date than anticipated. With regard to fiscal 2018, the city indicates that the budget will be structurally balanced. Based on the fiscal 2017 trend, we expect the city's budgetary performance to remain adequate.

Very strong budgetary flexibility

Naperville's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 22% of operating expenditures, or \$26.8 million.

The city has a formal fund balance policy requiring it to maintain 20% of general fund expenditures. In addition, the city has recently committed to raising its fund balance to 25% of general fund expenditures. We do not anticipate the city's budgetary flexibility weakening in the near term.

Very strong liquidity

In our opinion, Naperville's liquidity is very strong, with total government available cash at 40.4% of total governmental fund expenditures and 5.9x governmental debt service in 2016. In our view, the city has strong access to external liquidity, if necessary.

After adjusting for restricted funds, the city held approximately \$63 million in cash and investments at the end of fiscal 2016. We consider the city's access to external liquidity to be strong as it is a frequent issuer of GO debt. We do not anticipate a weakening of the city's liquidity position during the next few years.

Strong debt and contingent liability profile

In our view, Naperville's debt and contingent liability profile is strong. Total governmental fund debt service is 6.8% of total governmental fund expenditures, and net direct debt is 75.9% of total governmental fund revenue. Overall net debt is low at 2.1% of market value, and approximately 81.1% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

The city may issue between \$8 million and \$15 million in GO debt annually within the next two years for capital improvements.

In our opinion, a credit weakness is Naperville's large pension and OPEB obligation. Naperville's combined required pension and actual OPEB contributions totaled 11.5% of total governmental fund expenditures in 2017. The city made 107% of its annual required pension contribution in 2016. The funded ratio of the largest pension plan is 72.7%.

The city has adopted Governmental Accounting Standards Board (GASB) Statement No. 68, regarding the accounting of pension liabilities. The city participates in the Illinois Municipal Retirement Fund (IMRF), and two single-employer defined benefit pension plans, the Police Pension Plan and the Firefighters' Pension Plan. At the end of fiscal 2016, the plan fiduciary net position of the total pension liability for the IMRF, Police Pension, and Firefighters' Pension plans were 89%, 75%, and 73%, respectively. The city has committed to reach 100% funding of the past service cost with its police and fire pension plan by 2033.

Strong institutional framework

The institutional framework score for Illinois home-rule cities and villages is strong.

Outlook

The stable outlook reflects our anticipation that the city's budgetary flexibility, management conditions, and local economy will remain very strong. We do not expect to change the rating in the next two years, given these factors.

The city's participation in the broad and diverse Chicago MSA provides additional support for the rating.

Downside scenario

Should the city's budgetary performance or the city's debt profile and contingent liability profile were to weaken significantly, we could lower the rating.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- 2016 Update Of Institutional Framework For U.S. Local Governments

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.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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