

# RatingsDirect®

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## Summary:

# Hopkins, Minnesota; General Obligation

### Primary Credit Analyst:

Emily Powers, Santa Fe + 1 (312) 233 7030; emily.powers@spglobal.com

### Secondary Contact:

Emma Drilias, Chicago (1) 312-233-7132; emma.drilias@spglobal.com

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## Summary:

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### Credit Profile

US\$8.89 mil GO bnds ser 2022A dtd 04/26/2022 due 02/01/2038

*Long Term Rating* AA+/Stable New

Hopkins GO

*Long Term Rating* AA+/Stable Affirmed

## Rating Action

S&P Global Ratings assigned its 'AA+' rating to Hopkins, Minn.'s \$8.9 million series 2022A general obligation (GO) bonds. At the same time, we affirmed our 'AA+' rating on the city's existing GO debt. The outlook is stable.

The city's full-faith-and-credit pledge and ability to levy unlimited ad valorem property taxes secure the bonds. Officials intend to pay debt service with special assessments, net revenues of the sewer, water, and storm systems, and ad valorem property taxes, but the rating is based on the unlimited ad valorem tax pledge. The city's existing GO debt also includes various other pledged revenues such as tax-increment, tax abatement, special assessment revenues, and various enterprise fund revenues, but in each case, we rate to the city's GO pledge. Proceeds will be used for two purposes: New money will be used to finance various road and utility system improvements and for equipment purchases, and the remainder will refund the city's series 2014A GO bonds for interest cost savings.

### Credit overview

Hopkins' financial profile remains strong, as highlighted by its history of mostly stable operational performance, complete with very strong available reserves. While the city has historically maintained sizable general fund receivables, including loans to its permanent improvement, Arts Center, and water funds, and various other governmental funds, it has managed to sustain very strong reserves. Given new information in its 2020 audit, as well as more recent updates from management, we expect the total receivable to shrink in the coming years as the city prioritizes eradicating reliance of other funds on the general fund. However, if these interfund loans continue to grow, there could be pressure on the city's general fund, which could worsen our view of its available reserves. Hopkins is backed by a strong management team that has implemented robust policies and practices, helping it maintain stability in operations. The city's debt profile, while somewhat elevated, has been historically managed within its budget and, even given sizable debt service carrying charges, we expect that to continue. Additionally, its other long-term liabilities (pension and other postemployment benefits [OPEBs]) are manageable, further supporting its underlying credit quality.

The rating further reflects our assessment of the city's:

- Healthy incomes and wealth levels in a Twins Cities suburb, supported by consistent valuation growth on a \$2.5 billion tax base;
- Solid financial position with very strong available reserves, even after adjusting for receivables due to the general fund, with stable operational performance;

- Strong financial policies and practices under our Financial Management Assessment (FMA) methodology, and strong institutional framework; and
- Weak debt and liabilities profile with elevated debt costs, but a manageable pension and OPEB burden.

### **Environmental, social, and governance**

The rating incorporates our view of Hopkin's environmental, social, and governance (ESG) risks relative to the city's economy, management, financial measures, and debt and liability profile, which we view as in line with the sector.

## **Stable Outlook**

### **Upside scenario**

We could raise the rating if the city's balance sheet continues to improve and if economic measures, such as its income levels and per capita market values, were to improve to levels commensurate with those of higher-rated peers, all other credit factors remaining equal.

### **Downside scenario**

We could lower the rating if budgetary pressures outside of the general fund, such as with the enterprise and Arts Center funds, continue to drain general fund resources, and if debt were to increase substantially beyond current expectations.

## **Credit Opinion**

Consistently growing tax base, with high income and wealth levels and access to a broad and diverse metropolitan statistical area (MSA).

Hopkins' proximity to the Twin Cities allows easy access to employment and retail opportunities and will become even more easily accessible with the expansion of the Minneapolis METRO light-rail system, which will include three new stops in Hopkins that are currently under development. Development throughout the city remains strong, including ongoing expansions and new developments near the light-rail stops, as well as steady growth in both multi- and single-family housing. The tax base consists primarily of residential (homestead/non-homestead) properties (63%), followed by commercial and industrial properties (36%). We think that the city's historic tax base growth, coupled with general economic stability and access to the larger Twin Cities MSA, will lead to continued strength in our view of the local economy.

### **Steady operating performance and strong reserve levels, but including large general fund receivables that we expect to shrink in future audited years**

Hopkins' fiscal 2020 operations outperformed budgeted expectations, partially due to expenditure savings occurring from the COVID-19 pandemic, including hiring freezes and positions remaining open, in addition to one-time CARES Act money, \$800,000 of which was received in the general fund. The budgets for fiscal years 2021 and 2022 are both structured with break-even results; year-end actual performance for 2021 reflected a \$1.2 million general fund surplus, or 7.9% of expenditures, based on better-than-budgeted revenues and savings for salaries and benefits. The city was allotted roughly \$2.0 million in American Rescue Plan Act (ARPA) funding, half of which was received in 2021, with

the remainder coming in 2022. These funds have not yet been spent, but management expects them to be used on public safety, economic development, and revenue loss, as well as supporting some of the city's underperforming funds, primarily the Arts Center fund.

In our calculation of available fund balance, which totaled 17.3% of general fund expenditures in 2020, we have reduced the balance to account for interfund loans to Hopkins' permanent improvement, Arts Center, and water funds, and various other governmental funds, which aggregately amounted to roughly \$4.6 million in 2020. Even with this portion removed, the city's reserves have historically been maintained at levels we consider very strong. The total interfund loan has increased year over year, jumping sizably in 2020, although the largest portion (at \$2.9 million), reflecting the permanent improvement fund, was held in the general fund due to timing of receipts from other government agencies, including Hennepin County and the Department of Transportation, for reimbursement of projects. We expect this to decrease as those reimbursements are received, with \$1.5 million having already been repaid in fiscal 2021.

The receivable from the Art Center fund dropped in 2020, to \$997,000 from \$1.1 million in 2019, and management expects it to continue to fall in 2021 as Arts Center staff worked to reduce expenditures. In addition, the city plans to use roughly \$260,000 of ARPA funds to decrease the balance even further. The water fund receivable was nearly eliminated in fiscal 2020, and the remainder, which makes up only a small portion of the total general fund receivable, remains outstanding and is primarily due to timing of bond proceeds. Due to these developments, we expect that the total amount owed to the general fund will continue to fall in coming years as the receivables are repaid. If, however, the city is unable to reduce this amount, it could put downward pressure on what we consider the available fund balance.

### **Strong financial management assessment, highlighted by long-term planning and formalized policies**

Highlights of the city's financial practices and policies include:

- Historical look-back in the formulation of revenue and expenditure assumptions, using outside sources to produce the annual budget;
- Quarterly reporting of budget-to-actual performance to the council with the ability to make amendments as needed;
- A five-year, rolling long-term financial plan that projects revenues and expenditures;
- A five-year long-term capital plan that addresses capital needs with sources and uses of funds identified;
- Formalized investment management policy with quarterly reporting of investments and holdings;
- Formalized debt management policy that sets guidelines for short-term borrowing, maturity lengths, and minimum allowable coverage on revenue debt; and
- Formalized fund balance policy to maintain 42% of expenditures for cash-flow needs, with which the city has mostly been in compliance, with the exception of 2018, and which we calculate differently than the city given our adjustments to available reserves.

### **Relatively weak debt profile, with elevated costs relative to the budget, but with rapid amortization**

We calculate total direct debt at \$82.6 million; when excluding self-supporting GO debt paid from the city's enterprise funds, net direct debt amounts to approximately \$70.8 million. The city plans to issue approximately \$6.5 million in

new-money GO debt in 2023 and \$8.0 million in 2024 for ongoing street and utility projects. While debt service costs make up a considerable portion of the budget, the city has historically managed these costs well, which we expect will continue. In addition, it amortizes roughly the same amount that it issues every year, so we expect the debt profile will remain stable over the near term.

Moderate pension exposure, with some long-term risks, although medium-term costs are unlikely to accelerate

We do not believe that pensions represent a near-term credit pressure for Hopkins because the cost-sharing, multiple-employer, defined-benefit pension plans in which the city participates are reasonably well funded, and annual costs represent only a modest share of total spending. Although the city funds its OPEBs 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, not a significant budgetary pressure.

Hopkins participates in the following plans:

- Minnesota General Employees Retirement Fund (GERF): 87% funded (as of June 30, 2021), with a proportionate share of the plan's net pension liability (NPL) of \$4.7 million (as of Dec. 31, 2020).
- Minnesota Public Employees Police and Fire Fund (PEPFF): 94% funded (June 30, 2021), with a city proportionate share of the plan's NPL of \$3.9 million (as of Dec. 31, 2020).
- An implicit rate subsidy arising from retirees staying on the city's health insurance plan while paying active premium rates: 12% funded (as of Dec. 31, 2020), with a net OPEB liability of \$1.0 million.

Both GERF and PEPFF have seen improvements in funded status in recent years, although plan statutory formula contributions have regularly fallen short of actuarial recommendations. Annual contributions are based on a statutory formula that has typically produced contributions lower than the actuarially determined contribution for each plan, and we think that this increases the risk of underfunding over time if the state legislature does not make adjustments to offset future funding shortfalls. Other key risks include a 7.5% investment rate-of-return assumptions, above our 6.0% guidance, and lengthy amortization periods. Nevertheless, pension costs remain only a modest share of total spending, and we believe they are unlikely to pressure the city's medium-term operational health.

### Strong institutional framework

The institutional framework score for Minnesota cities with a population less than 2,500 is strong.

Hopkins, MN -- Key Credit Metrics				
	Most recent	Historical information		
		2020	2019	2018
<b>Very strong economy</b>				
Projected per capita EBI % of U.S.	123			
Market value per capita (\$)	128,271			
Population		19,484	19,213	18,808
County unemployment rate(%)		6.6		
Market value (\$000)	2,499,240	2,378,345	2,145,862	2,027,876
Ten largest taxpayers % of taxable value	21.4			

## Hopkins, MN -- Key Credit Metrics (cont.)

	Most recent	Historical information		
		2020	2019	2018
<b>Strong budgetary performance</b>				
Operating fund result % of expenditures		8.5	3.2	(1.7)
Total governmental fund result % of expenditures		10.9	6.9	(7.1)
<b>Very strong budgetary flexibility</b>				
Available reserves % of operating expenditures		17.3	20.9	19.8
Total available reserves (\$000)		2,596	3,024	2,714
<b>Very strong liquidity</b>				
Total government cash % of governmental fund expenditures		120	87	95
Total government cash % of governmental fund debt service		496	363	475
<b>Very strong management</b>				
Financial Management Assessment		Strong		
<b>Weak debt &amp; long-term liabilities</b>				
Debt service % of governmental fund expenditures		24.3	23.8	20.1
Net direct debt % of governmental fund revenue		236		
Overall net debt % of market value		4.4		
Direct debt 10-year amortization (%)		83		
Required pension contribution % of governmental fund expenditures		3.8		
OPEB actual contribution % of governmental fund expenditures		0.7		
<b>Strong institutional framework</b>				

EBI--Effective buying income. OPEB--Other postemployment benefits.

## Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022
- 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

## Ratings Detail (As Of March 30, 2022)

Hopkins GO bnds		
Long Term Rating	AA+/Stable	Affirmed
Hopkins GO bnds ser 2017B dtd 07/13/2017 due 02/01/2033		
Long Term Rating	AA+/Stable	Affirmed
Hopkins GO bnds ser 2021A dtd 04/06/2021 due 02/01/2036		
Long Term Rating	AA+/Stable	Affirmed

## Ratings Detail (As Of March 30, 2022) (cont.)

Hopkins GO imp bnds		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Hopkins GO tax abatement bnds		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Hopkins GO tax increment rev rfdg bnds		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Hopkins GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Hopkins GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Hopkins GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

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