

RatingsDirect®

Summary:

Cambridge, Minnesota; General Obligation

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US\$4.105 mil GO bonds ser 2022A dtd 05/26/2022 due 02/01/2033

Long Term Rating

AA/Stable

New

Rating Action

S&P Global Ratings assigned its 'AA' long-term rating to Cambridge, Minn.'s \$4.105 series 2022A general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AA' long-term rating and underlying rating on the city's GO debt outstanding. The outlook is stable.

The bonds are secured by the city's full faith and credit, including its ability to levy ad valorem property taxes without limitation as to rate or amount. The city plans to finance a portion of the debt service from pledged net revenue of its utility system. Furthermore, the city anticipates paying a portion of debt service from a combination of special assessments levied against benefited properties and a portion from property taxes. However, we rate the bonds based on Cambridge's GO pledge, as we view it as the stronger security. The 'AA' underlying rating reflects our view of the city's GO pledge.

Proceeds from the 2022A bonds will finance various capital improvements to the city's streets and stormwater system.

Credit overview

In our view, Cambridge benefits from very high reserves based on a history of strong budgetary performance and conservative management practices. Growth in building permits has also contributed to strong revenue performance in recent years and building permit revenue continues to outperform projections through fiscal 2022. Cambridge is small, with approximately 9,000 residents; however, with hundreds of housing units under construction, we believe the city is in a period of growth. Officials indicate that they intend to reduce the property tax rate, maintain current reserves, and do not plan to materially increase the debt burden to finance development. Based on year-to-date financials and long-term projections, we believe Cambridge will be able to maintain current credit characteristics during this expansion. Wealth and income metrics are low compared with those of higher-rated peers and constrain upward rating potential, although we expect the city's financial position will remain stable.

The 'AA' long-term rating reflects our view of the city's:

- Role as small regional hub but with significant development, as businesses are expanding and large residential developments are underway;
- Very strong management focused on budgetary balance executed through long-term planning and strong institutional framework;
- Building permit revenue growth driving large surpluses, with continued maintenance of very high reserves; and
- Debt levels that are moderating compared with the city's expenditures and overall taxing base.

Environmental, social, and governance

We have analyzed environmental, social, and governance risks relative to Cambridge's economy, management, financial measures, and debt and liability profile and have determined all are credit neutral.

Stable Outlook

Upside scenario

Although we do not expect to change the rating during the next two years given current wealth and income indicator, we could raise the rating if management's expected economic growth materializes with sustained higher wealth and income indicators, while maintaining current reserves and debt levels.

Downside scenario

If the city's financial performance were to deteriorate significantly, leading to sustained decreases in reserves, we could take a negative rating action.

Credit Opinion

Small regional hub but significant development underway

Cambridge is approximately 40 miles north of the Minneapolis-St. Paul metropolitan area. The city is the seat of Isanti County and although it has a very small population, it is somewhat of a regional hub. Cambridge is situated near two highways and along the Rum River. Management reports that there will be three gas station under development, a 200-single-family-home development is underway, and more than 350 apartment units were recently completed or are under construction. In addition, there are several new businesses (including FLOE International, a boat manufacturer) and retailers, and the state is extending the four-lane highway through the city. The city's second-largest employer, Cambridge Medical Center, is building a \$150 million facility, planned to open in 2025. The city is working to help develop the historic downtown area and beautify the area along the river with parks and bike paths; official identified funding for all developments and do not plan to raise the property tax levy for these projects.

Although there is development underway, the economy is still limited. The largest employers are in health care, government, kindergarten-grade 12 education, and some big box retailers. Management expects 5%-10% growth in net tax capacity over the next year; given the development, we believe that is possible.

Very strong management focused on budgetary balance executed through long-term planning

Cambridge reports budget-to-actual results monthly to the city council. Budget amendments are generally implemented as needed. The city bases its revenue and expenditure assumptions on information gathered from various external sources, with some review of historical trends. The city maintains a rolling, 10-year, comprehensive long-term financial forecast and a 10-year capital improvement plan. Cambridge's investment policy adheres to the state guidelines, with investment reports provided to the city council monthly along with budget-to-actual performance. The city has adopted a debt management policy that provides guidelines around the use of debt, the types of debt that may be issued, and financing structures, among other stipulations. The policy largely follows state guidelines regarding targeted debt capacity metrics. The city's fund balance policy consists of an emergency reserve at

5% of next year's budget, and 30%-50% of next year's tax levy and local government aid. The city maintains high balances to guard against any unforeseen events.

Building permit revenue growth driving large surpluses

In the current fiscal year and during the previous two years, Cambridge has benefited from increasing construction- and permit-related revenue (12% of general fund revenue in fiscal 2022), with stable property taxes (68%) and intergovernmental revenue (19%). Based on the current amount of development, we expect the city's revenue will continue to increase for, at least, the short term. The fiscal 2021 general fund surplus of \$1 million was not inflated by federal stimulus, as the \$500,000 received was deposited into a segregated fund.

The fiscal 2022 budget calls for balanced results in the general fund; based on year-to-date revenue collection the city believes it will likely have better-than-budgeted results. Officials might transfer excess money over the fund balance policy to capital funds for future expenditures. The budget increased the levy by 4% but resulted in an overall rate decline. The city expects to receive an additional \$500,000 in federal stimulus; the entirety of 2021 and 2022 federal receipts will be used to build a new well and other infrastructure.

As the city continues to grow, management intends to maintain service levels but does not want to draw down on reserves or issue debt for development projects. We expect the city's budgetary performance will remain strong, while maintaining budgetary flexibility and liquidity at very strong levels.

For our analysis, we adjusted general fund and governmental performance to account for recurring transfers into the general fund from the municipal liquor store fund. We also adjusted general fund expenditures to account for recurring transfers out of the general fund, and adjusted total governmental expenditures to account for one-time capital expenditures and non-routine transfers to the redevelopment fund. The city has no direct-purchase or variable-rate debt that could pose a liquidity risk, and we believe the liquidity profile will likely remain very strong over the next few fiscal years.

Improved debt position as carrying charges slowly decline

We revised our view of the city's debt position to adequate from weak, as carrying charges declined compared with expenditures. Cambridge plans to issue approximately \$5 million in debt over the next three years to finance street projects but the rapid amortization leads us to expect that this will not weaken the city's debt burden further.

We do not believe that pension liabilities represent a medium-term credit pressure, as contributions are only a modest share of the budget

Cambridge participates in two multiple-employer, defined-benefit pension plans that have seen recent improvements in funded status, 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. The city does not report on its other postemployment benefits.

The city participates in the following plans:

- Minnesota General Employees Retirement Fund (GERF): 87% funded (as of June 30, 2021), with a city proportionate share of the plan's net pension liability of \$1.794 million
- Minnesota Police and Fire Fund (PEPFF): 94% funded (June 30, 2021), with a proportionate share of \$879,000

- Statewide Volunteer Firefighter Retirement Plan: 108% funded (Dec. 31, 202), with a net pension asset of \$199,000

Total contributions to GERF and PEPFF were 98% and 110%, respectively, of our minimum funding progress metric. Annual contributions are based on a statutory formula that has typically produced contributions lower than the actuarially determined contribution for each plan. In our view, this increases the risk of underfunding over time if the state legislature does not adjust to offset future funding shortfalls. Other key risks include a 7.5% investment rate-of-return assumption (for both plans) that indicates some exposure to cost acceleration because of market volatility, and an amortization method that significantly defers contributions through a lengthy, closed 30-year amortization period based on a level 3.25% payroll growth assumption. Regardless, costs remain only a modest share of total spending, and we believe they are unlikely to pressure the city's medium-term operational health.

The Cambridge Fire Relief Assn. participates in the Statewide Volunteer Firefighter Retirement Plan, an agent multiple-employer, lump-sum, defined-benefit pension plan administered by the Public Employees Retirement Assn. of Minnesota. The plan covers volunteer firefighters of municipal fire departments or independent nonprofit firefighting corporations that have elected to join. The city's participation in the plan is more than 100% funded.

The city allows retirees to participate in its health care plan, effectively offering an implicit subsidy, although we understand the liability associated with the implicit is limited.

Strong institutional framework

The institutional framework score for Minnesota cities is strong.

Cambridge, Minnesota--Key Credit Metrics				
	Most recent	Historical information		
		2021	2020	2019
Adequate economy				
Projected per capita EBI % of U.S.	77			
Market value per capita (\$)	85,262			
Population		9,351	9,178	
County unemployment rate(%)		6.8		
Market value (\$000)	797,286	700,450	668,377	
Ten largest taxpayers % of taxable value	12.5			
Strong budgetary performance				
Operating fund result % of expenditures	13.4	14.8	1.2	
Total governmental fund result % of expenditures	16.4	40.1	6.0	
Very strong budgetary flexibility				
Available reserves % of operating expenditures	48.3	53.4	50.1	
Total available reserves (\$000)	3,641	3,570	3,498	
Very strong liquidity				
Total government cash % of governmental fund expenditures	164	151	181	
Total government cash % of governmental fund debt service	1244	2150	905	

Cambridge, Minnesota--Key Credit Metrics (cont.)

	Most recent	Historical information		
		2021	2020	2019
Very strong management				
Financial Management Assessment	Strong			
Adequate debt & long-term liabilities				
Debt service % of governmental fund expenditures		13.2	7.0	20.0
Net direct debt % of governmental fund revenue	139			
Overall net debt % of market value	3.9			
Direct debt 10-year amortization (%)	79			
Required pension contribution % of governmental fund expenditures		4.1		
OPEB actual contribution % of governmental fund expenditures	--			
Strong institutional framework				

EBI--Effective buying income. OPEB--Other postemployment benefits. Data points and ratios may reflect analytical adjustments.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022
- 2021 Update Of Institutional Framework For U.S. Local Governments

Ratings Detail (As Of April 27, 2022)

Cambridge GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Cambridge GO bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Cambridge GO bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Cambridge GO bnds ser 2016A dtd 05/16/2016 due 02/01/2027		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Cambridge GO sales tax rev bnds		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Cambridge GO wtr rev bnds		
<i>Long Term Rating</i>	AAA/Stable	Current
<i>Underlying Rating for Credit Program</i>	AA/Stable	Affirmed

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