

RatingsDirect®

Summary:

Kaukauna, Wisconsin; Appropriations; General Obligation

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Credit Profile

US\$10.1 mil GO prom nts ser 2020A dtd 09/03/2020 due 09/01/2030

Long Term Rating AA-/Stable New

Kaukauna GO

Long Term Rating AA-/Stable Affirmed

Kaukauna Redev Auth, Wisconsin

Kaukauna, Wisconsin

Kaukauna Redev Auth APPROP

Long Term Rating A+/Stable Affirmed

Rating Action

S&P Global Ratings assigned its 'AA-' rating and stable outlook to Kaukauna, Wis.' roughly \$10.1 million series 2020A general obligation (GO) promissory notes and affirmed its 'AA-' rating, with a stable outlook, on the city's existing GO debt.

S&P Global Ratings also affirmed its 'A+' rating, with a stable outlook, on Kaukauna Redevelopment Authority's redevelopment lease revenue debt, supported by the city.

Kaukauna's unlimited-ad valorem-property-tax pledge secures the series 2020A GO notes.

Officials intend to use series 2020A note proceeds to fund park improvements and street construction and improvements and finance the acquisition of vehicles and equipment. They also plan to use series 2020A note proceeds to refund a portion of series 2010C bonds for debt-service-cost savings.

The authority's lease revenue bonds are payable from the city's lease-rental payments, in accordance with a lease agreement between the city and authority. The city's conditional obligation to pay rental payments reflects its quiet enjoyment of the leased property. We rate the authority's bonds one notch below the city's GO debt due to annual appropriation risk.

Credit overview

Kaukauna has direct access to, and participates in, Appleton's and Green Bay's economies. Although state law provides Kaukauna with little revenue flexibility, management has built and retained very strong reserves through careful fiscal planning and budgetary oversight. We view the city's weak debt profile as a credit concern. As a Wisconsin Retirement System (WRS) participant, one of the nation's best-funded pension plans, however, Kaukauna's pension liabilities and ability to keep up with employer contributions are not a concern.

COVID-19 has caused the national economy to fall into recession, as reported by S&P Global Economics. (For further information, please see the article, titled "The U.S. Faces A Longer and Slower Climb From The Bottom," published June 25, 2020, on RatingsDirect.) We think this likely foreshadows a near-term economic slowdown at both the local and state levels, and it could result in a pressured state-funding environment.

Still, we recognize Kaukauna's very strong reserves provide a meaningful hedge against near-term revenue volatility. Therefore, we expect near-term finances will likely remain strong and in-line with similar-rated peers. While the scope of economic and financial challenges posed by COVID-19 remains unknown, they could include delayed state payments or local property taxes, based on the city's historical property tax base stability and resilience, coupled with very strong reserves. We, however, think Kaukauna is well positioned to navigate COVID-19's possible negative effects on finances. We will continue to monitor the effects of COVID-19 on revenue and expenses.

Generally, our rating outlook timeframe is up to two years; due to the current uncertainty surrounding COVID-19, however, our view of credit risks to the city centers on more-immediate budget effects in fiscal 2020.

The GO rating reflects our opinion of the city's:

- Adequate economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong financial management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with an operating surplus in the general fund and breakeven operating results at the total governmental-fund level in fiscal 2019;
- Very strong budgetary flexibility, with available fund balance in fiscal 2019 at 34% of operating expenditures;
- Very strong liquidity, with total government available cash at 148.3% of total governmental-fund expenditures and 6.4x governmental debt service, and access to external liquidity we consider strong;
- Weak debt-and-contingent-liability position, with debt service carrying charges at 23.2% of expenditures and net direct debt that is 230% of total governmental-fund revenue, but rapid amortization, with 72.7% of debt scheduled to be retired within 10 years; and
- Adequate institutional framework score.

Environmental, social, and governance (ESG) factors

The rating incorporates our view of health-and-safety risks posed by COVID-19, which we consider a social-risk factor. Although the scope of economic and financial challenges posed by the pandemic remains unknown, we think a prolonged disruption could weaken the city's local economy and potentially affect state and local revenue. COVID-19, however, is not affecting Kaukauna more than other sector standards. We have also analyzed the city's environmental and governance risks relative to its economy, management, financial measures, and debt-and-liability profile and have determined all are in-line with our view of the sector standard.

Stable Outlook

Downside scenario

We could lower the rating if the city does not maintain balanced operations and, at least, adequate budgetary performance, resulting in material flexibility deterioration.

Upside scenario

While we do not view this as likely due to current macroeconomic conditions, we could raise the rating if key economic indicators were to improve materially while management maintains structural balance.

Credit Opinion

Adequate economy

We consider Kaukauna's economy adequate. The city, with a population estimate of 16,458, is in Outagamie County in the Appleton MSA, which we consider broad and diverse. Kaukauna has a projected per capita effective buying income at 92.2% of the national level and per capita market value of \$70,105. Overall, market value has grown by 6% during the past year to \$1.2 billion in fiscal 2020. County unemployment was 3% in 2019.

Kaukauna is in east-central Wisconsin on Fox River, about 25 miles southwest of Green Bay and 105 miles north of Milwaukee. Leading employers include:

- Ahlstrom Munksjo (1,800 employees),
- Kaukauna School District (450), and
- St. Paul Elder Care (299).

The city's economic score currently benefits from its participation in the broad and diverse Appleton MSA. If the economy is no longer broad and diverse, the score could weaken.

Within Kaukauna, most large and small employers continued to operate throughout the pandemic. Management reports there were no major shutdowns or layoffs as a direct effect of COVID-19. While we posit COVID-19 could pressure economic metrics and property values during the next few fiscal years, we think the city's historical tax base growth and general economic stability will likely lead to minimal credit implications. Therefore, our view of the city's local economy will likely remain adequate.

Strong management

We view the city's financial management as strong, with good financial policies and practices under our FMA methodology, indicating that financial practices exist in most areas but that governance officials might not formalize or regularly monitor all of them.

Kaukauna uses modified, zero-based budgeting, including two years' to three years' historical data and outside sources at the county and state levels. It does not use long-term financial planning. Management provides monthly reports on budget-to-actual results to the city council. Management annually updates a five-year, formal capital improvement

plan.

While Kaukauna lacks its own investment- and debt-management policies, it follows state guidelines for investment holdings and earnings and reports the results to the city council annually. Management also follows a formally adopted minimum fund-balance policy.

Adequate budgetary performance

Kaukauna's budgetary performance is adequate, in our opinion. The city had surplus operating results in the general fund at 1.6% of expenditures and balanced results across all governmental funds at 0.1% in fiscal 2019. General fund operating results have been stable during the past three fiscal years with 2.4% of expenditures in fiscal 2018 and 0% in fiscal 2017.

Our analysis of Kaukauna's budgetary performance includes adjustments for routine transfers into the general fund and the removal of one-time capital-outlay expenditures. Management attributes the 1.6% fiscal 2019 general fund surplus to midyear adjustments for public-charges-for-services fees to align them with costs.

Kaukauna adopted a balanced fiscal 2020 budget. Management's midyear expectations indicate a \$100,000-\$200,000 general fund surplus. While management expects to adopt a balanced fiscal 2021 budget, it has not yet done so officially. Management has held discussions to address potential expenditure cuts should revenue substantially decrease or face delays, but we consider the city well placed to manage expenditures and make appropriate budgetary adjustments to maintain structural balance. We think the city will likely maintain, at least, adequate budgetary performance during the next two fiscal years.

Very strong budgetary flexibility

Kaukauna's budgetary flexibility is very strong, in our view, with available fund balance in fiscal 2019 at 34% of operating expenditures, or \$5 million. We expect available fund balance will likely remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

Kaukauna intends to neither make any material draws on available funds nor draw down general fund reserves materially during the next few fiscal years. Due to the city's strong operating performance and lack of plans to draw down reserves, we think management will likely maintain very strong budgetary flexibility during the next two fiscal years.

Very strong liquidity

In our opinion, Kaukauna's liquidity is very strong, with total government available cash at 148.3% of total governmental-fund expenditures and 6.4x governmental debt service in fiscal 2019. In our view, the city has strong access to external liquidity if necessary.

Kaukauna's regular GO and revenue debt issuance during the past 15 years demonstrates strong market access. The city does not have any direct-purchase or private-placement obligations. We do not consider investments aggressive because Kaukauna primarily invests in money-market funds, government securities, and the local government investment pool. We do not expect liquidity will likely weaken during the next few fiscal years.

Weak debt-and-contingent-liability profile

In our view, Kaukauna's debt-and-contingent-liability profile is weak. Total governmental-fund debt service is 23.2% of total governmental-fund expenditures, and net direct debt is 230% of total governmental-fund revenue. Officials plan to retire about 72.7% of direct debt within 10 years, which is, in our view, a positive credit factor.

Officials currently expect to issue \$4 million-\$8 million of GO bonds during the next two years for routine capital projects. The city does not have any direct-purchase or variable-rate debt.

Kaukauna's combined required pension and actual other-postemployment-benefit (OPEB) contribution totaled 6.2% of total governmental-fund expenditures in fiscal 2019: 4.5% represented required contributions to pension obligations and 1.7% represented OPEB payments. The city made its full annual required pension contribution in fiscal 2019.

Pension and OPEB

- Kaukauna's pension costs are modest as a share of total spending; they are not likely to accelerate significantly during the next few fiscal years, especially due to the pension plan's strong funding.
- Although Kaukauna funds OPEB on a pay-as-you-go basis, exposing it to potential cost acceleration, we expect medium-term costs will likely remain only a small share of total spending; therefore, we do not consider them a significant budgetary pressure.

The city participates in WRS, which was 96.5% funded at Dec. 31, 2018, with a proportionate share of the plan's net pension liability equal to \$3.4 million.

WRS has routinely been among the nation's best-funded multiple-employer, defined-benefit pension plans. Contributions to WRS are actuarially determined, and the city funds 100% of its required contribution annually. WRS' investment-rate-of-return assumption decreased to 7% in late 2018 from 7.2%. While the revised return assumption exceeds our 6% guideline, WRS employing a shared-risk model mitigates market-volatility exposure; in this model, changes in active-employee contributions and benefit-payment adjustments offset investment-performance fluctuations. Because of these features, we expect contributions will likely remain relatively stable. Due to WRS' strong funding and contribution practices, we expect contributions will likely remain affordable.

Adequate institutional framework

The institutional framework score for Wisconsin cities and villages with a population less than 25,000 is adequate.

Related Research

- 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
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 2019 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

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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.

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