



City of McMinnville, Oregon

Audit Committee Reserve Discussion: Credit Rating Considerations

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Discussion Topics

- I. Overview of Credit Ratings
- II. Moody's Local Government Methodology and Scorecard
- III. City of McMinnville Rating Report Highlights
- IV. Historical Trends and Peer Comparison
- V. Credit Spreads / Cost of Borrowing



What is a Credit Rating?

- Three major rating agencies are Moody's Investors Service, S&P Global Ratings, and Fitch Ratings
- Ratings assess the probability of the debt instrument returning all of the principal to the investor
- Municipal credit ratings are opinions of the investment quality of debt issuers and issues in the municipal bond market
- Underwriters and investors rely upon the credit quality judgment made by the rating agencies
- General obligation / full faith & credit ratings are generally scored along 4 or 5 categories:
 1. Economy & tax base
 2. Financial condition of the general fund
 3. Management
 4. Debt and pension obligations
 5. Institutional framework



Hierarchy of Credit Ratings

- Most municipal governments carry one or more investment-grade ratings
- Ratings are assigned to each credit (e.g., full faith & credit obligations, water revenue bonds, etc.)

	Moody's	S&P	Fitch
Investment Grade	Aaa	AAA	AAA
	Aa1	AA+	AA+
	Aa2	AA	AA
	Aa3	AA-	AA-
	A1	A+	A+
	A2	A	A
	A3	A-	A-
	Baa1	BBB+	BBB+
	Baa2	BBB	BBB
	Baa3	BBB-	BBB-
Non-Investment Grade	Ba and below	BB and below	BB and below



Moody's Local Government Rating Scorecard

- Moody's uses a "scorecard" approach to provide a composite score of a local government's credit profile based on weighted factors as well as potential "below the line" notching factors
- Of the rating factors, only some are directly controllable by actions or inactions of the City

Broad Scorecard Factors	Sub-Factors	Sub-Factor Weighting	Level of Control
Economy/Tax Base (30%)	Tax Base Size (Full Value)	10%	Less/No Direct Control
	Full Value Per Capita	10%	Less/No Direct Control
	Wealth (Median Family Income)	10%	Less/No Direct Control
Finances (30%)	Fund Balance (% of Revenues)	10%	More Direct Control
	Fund Balance Trend (5-year Change)	5%	More Direct Control
	Cash Balance (% of Revenues)	10%	More Direct Control
	Cash Balance Trend (5-year Change)	5%	More Direct Control
Management (20%)	Institutional Framework	10%	Less/No Direct Control
	Operating History	10%	More Direct Control
Debt/Pensions (20%)	Debt to Full Value	5%	More Direct Control
	Debt to Revenue	5%	More Direct Control
	Moody's-Adjusted Net Pension Liability (3-Year Average) to Full Value	5%	Less/No Direct Control
	Moody's-Adjusted Net Pension Liability (3-Year Average) to Revenue	5%	Less/No Direct Control



City of McMinnville Rating – Moody’s Investors Service

- On February 1, 2018, Moody’s affirmed the “Aa3” rating on the City’s outstanding general fund-secured obligations
 - Below are highlights of the February 2018 opinion and subsequent July 2019 annual comment:

Credit Strengths:

- Strong financial position with cash balance as a % of operating revenues (38.5%) comparable to US median, despite significant contractions from 2014-2018
- Reliance on property taxes that benefit from regular, moderate growth

Credit Weaknesses:

- Elevated fixed costs burden reduces operating flexibility
- Somewhat inflated yet manageable pension liability in comparison to Aa3 rating

Factors that could lead to an upgrade:

- Substantial tax base growth and economic diversification
- Appreciation in socioeconomic measures
- Material reduction in fixed costs burden
- Persistently stronger reserves and liquidity

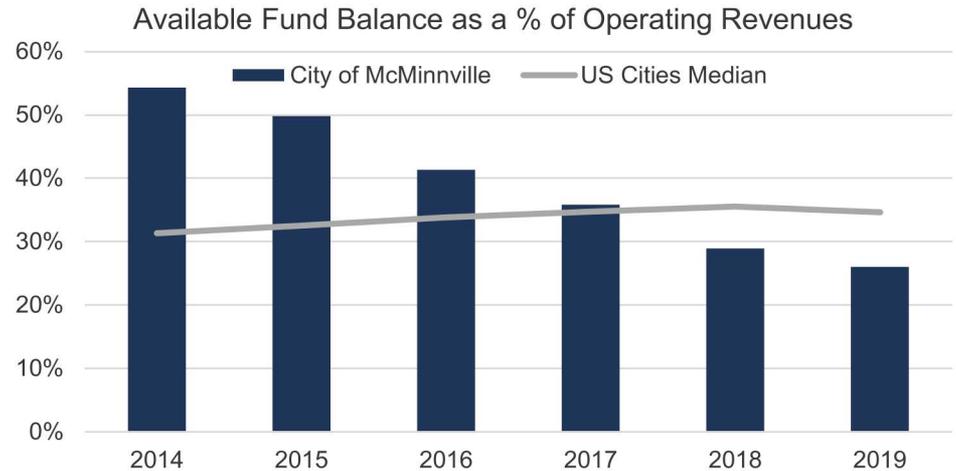
Factors that could lead to a downgrade:

- Significant deterioration of the city’s financial position
- Material growth in leverage and fixed costs burden from debt and pension liabilities
- Trend of substantial tax base contractions or economic decline

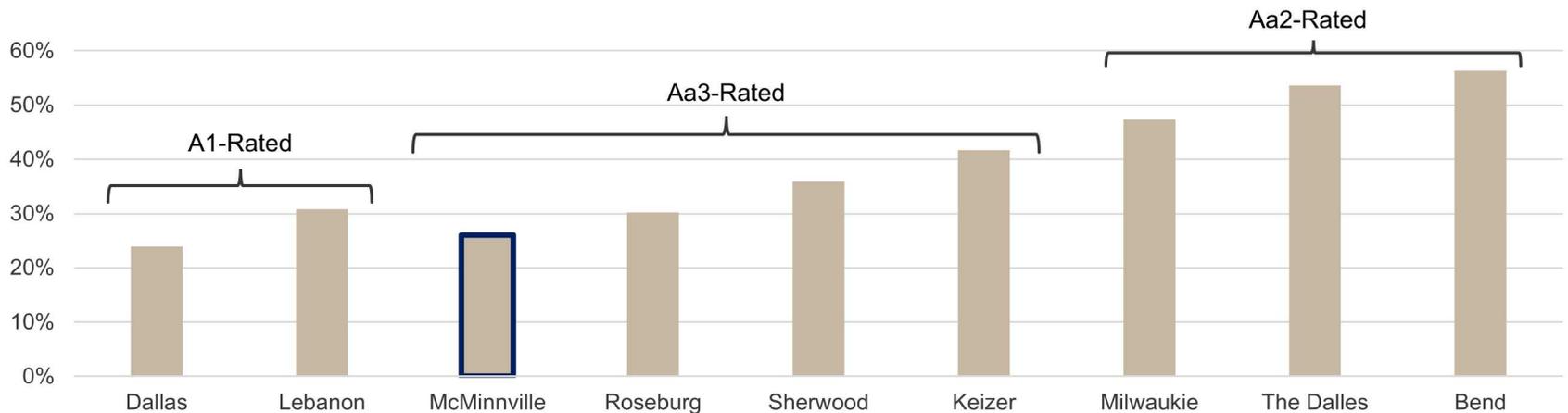


Credit Ratings – Moody’s Investors Service

- Moody’s notes the significant contraction of the City’s operating fund balance as a % of operating revenues over the past several years
- The chart below shows a comparison of this metric to selected in-state peer cities



Peer Comparison – Available Fund Balance as a % of Operating Revenues (2019)





Credit Spreads

- Lower credit ratings typically translate to a higher cost of borrowing
- The “MMD” index is the industry standard means of evaluating tax-exempt bond rates
- The spread between the 10-year “A” MMD and 10-year “AA” MMD averaged 0.38% over the past ten years, and is currently 0.24%



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