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Ratings

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Summary:
Northbrook Village, Illinois; General Obligation

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Table Of Contents

Summary:

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Credit Profile		
US$12.725 mil GO bnds ser 2019 due 12/01/2039		
Long Term Rating	AAA/Stable	New
Northbrook Vill taxable GO bnds		
Long Term Rating	AAA/Stable	Affirmed
Northbrook Vill GO		
Long Term Rating	AAA/Stable	Affirmed
Northbrook Vill GO bnds		
Long Term Rating	AAA/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' long-term rating to Northbrook, Ill.'s series 2019 general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the village's existing GO debt. The outlook is stable.

Purpose and security

Northbrook village's unlimited-tax GO pledge secures the series 2019 bonds. It will use the bond proceeds to fund capital improvements and refund a portion of the series 2010 bonds, for interest savings.

Northbrook's GO debt is eligible to be rated above the sovereign, because we believe the village can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions" (published Nov. 19, 2013), U.S. local governments are considered to have moderate sensitivity to country risk. Northbrook has pledged its ad valorem unlimited tax GO to the debt--the sole source of security on the bonds. This severely limits the possibility of negative sovereign intervention in the payment of the debt or in the operations of the village. The institutional framework in the U.S. is predictable for local governments, allowing them significant autonomy, independent treasury management, and no history of government intervention. Also, Northbrook has very strong financial flexibility, as its very strong budgetary flexibility and liquidity demonstrate.

Credit summary

Northbrook's economy is unique in that it has access to the large and thriving Chicago metropolitan statistical area (MSA), a significant size retail base (with its top taxpayer Northbrook Court Mall), a very desirable and growing residential sector, and is also home to many small-to-large businesses. Despite the village's very large pension obligation, we expect Northbrook to maintain its very strong liquidity and budgetary flexibility due to our opinion of the village's stable financial performance and management continuing to keep balanced operations. This is exemplified by the village's two-year budget process and its maintenance of reserves in accordance with its 40% fund balance policy, which partially offsets volatility risk due to economic fluctuations related to the village's sales tax--the major tax revenue source.

The 'AAA' rating reflects our assessment of the following factors:

- Very strong economy, with access to a broad and diverse MSA;
- Strong management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with an operating surplus in the general fund and a slight operating surplus at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 54% of operating expenditures;
- Very strong liquidity, with total government available cash at 107.9% of total governmental fund expenditures and 8.9x governmental debt service, and access to external liquidity that we consider strong;
- Very weak debt and contingent liability profile, with debt service carrying charges at 12.2% of expenditures and net direct debt that is 232.1% of total governmental fund revenue, as well as a large pension and other postemployment benefits (OPEB) obligation and the lack of a plan to sufficiently address the obligation; and
- Strong institutional framework score.

Very strong economy

We consider Northbrook's economy very strong. The village, with an estimated population of 32,163, is in Cook County in the Chicago-Naperville-Elgin MSA, which we consider to be broad and diverse. The village has a projected per capita effective buying income of 209% of the national level and per capita market value of $236,305. Overall, the village's market value fell 2.2% over the past year to $7.6 billion in 2020. The county unemployment rate was 4.0% in 2018.

Northbrook is home to the 1-million-square-foot Northbrook Court Mall, in addition to two other shopping centers that add an additional 752,000 square feet of retail space (1,000 employees). Other top employers include Underwriter's Laboratories (product testing; 2,000 employees), Crate & Barrel corporate headquarters (retail; 500), and Hilco Merchant Resources LLC (management consulting; 400). The village is expecting a significant increase in the assessed value (AV) in the coming year, largely due to a reassessment. In addition, there is a wide variety of new development and construction in the village. Highlights include several new housing developments (660 apartment units and more than 200 single-family homes/townhomes), and a $250 million redevelopment of the Northbrook Court Mall. Given the abundance of development, we expect the village's economy to strengthen. The tax base is 68.67% residential, 20.70% commercial, and 8.60% industrial.

Strong management

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

Northbrook has a formal fund balance policy of 40%, which provides a cushion against fluctuations in economically sensitive revenues, a debt policy, and an investment policy. The board receives monthly financial reports, a two-year budget document (but formally adopts a one-year budget), and a formal five-year capital improvement plan that it updates annually. The budget is produced with well-thought-out assumptions that are realistic and forward looking. Management also produces quarterly economic reports that helps monitor and project the sales tax collections.

Strong budgetary performance

Northbrook's budgetary performance is strong, in our opinion. The village had surplus operating results in the general fund of 5.0% of expenditures, and slight surplus results across all governmental funds of 0.8% in fiscal 2019.

We adjusted Northbrook's general fund and total governmental fund expenditures to account for expenses that bond proceeds covered.

Our assessment accounts for the fact that we expect budgetary results will remain consistently strong from 2019 results in the near term. The village reports balanced operations in the general fund in 2020, in line with the budget. The total governmental funds are largely represented by the general fund and will have balanced results similar to the previous year.

The village's largest source of tax revenue is from home rule and state share sales taxes, which accounted for 31.5% of total general fund revenues in fiscal 2019. Property taxes (19%) and state income taxes (7%) were the next leading sources of tax revenue. The Northbrook Court Mall primarily drives sales tax revenue, but during ongoing renovations, the village expects a dip in collections for fiscal 2020. However, management expects revenue to recover the following year. Based on historical revenue, management does not expect this will materially affect the village's financial position.

State law recently allowed for the recreational use of cannabis and the board is considering a dispensary and an additional tax upon its sales, which it projects will produce $750,000, annually, to be deposited into the general fund.

Very strong budgetary flexibility

Northbrook's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 54% of operating expenditures, or $22.3 million. We expect the available fund balance to remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

The village anticipates that total general fund reserves will likely remain at least level in fiscal years 2020 and 2021 compared with 2019 draft audited levels, based on current budgetary performance. Reserve levels will continue in accordance to the formal fund balance policy of 40%.

Very strong liquidity

In our opinion, Northbrook's liquidity is very strong, with total government available cash at 107.9% of total governmental fund expenditures and 8.9x governmental debt service in 2019. In our view, the village has strong access to external liquidity if necessary.

We believe the village has strong access to external liquidity based on its approximately annual issuance of GO bonds. The village does not have any direct purchase or privately placed debt that we would view as a contingent liability risk.

Very weak debt and contingent liability profile

In our view, Northbrook's debt and contingent liability profile is very weak. Total governmental fund debt service is 12.2% of total governmental fund expenditures, and net direct debt is 232.1% of total governmental fund revenue.

The village does not have additional debt planned within the next two years.

In our opinion, a credit weakness is Northbrook's large pension and OPEB obligation, without a plan in place that we think will sufficiently address the obligation. Northbrook's combined required pension and actual OPEB contributions totaled 15.7% of total governmental fund expenditures in 2019. Of that amount, 14.4% represented required contributions to pension obligations, and 1.3% represented OPEB payments. The village made 110% of its annual required pension contribution in 2019.

Although pension contributions remain a long-term credit consideration, we believe the liability is manageable. Northbrook contributes to three defined benefit pension plans. The Illinois Municipal Retirement Fund (IMRF) is a defined benefit agent multiple-employer public employee retirement system. The police and fire pension plans are both single-employer pension plans.

The IMRF plan has a net liability of $17 million and is 86.9% funded. The village's net pension liability as of April 30, 2019, for its police and firefighters plans was a combined $93.4 million. The police plan maintained a funded level of 52.8% and the fire plan maintained a funded level of 53.4%, using the plan's fiduciary net position as a percent of the total pension liability. The police and fire plans funding level decreased since the 2015 audit due to reduced return assumptions to 7% from 8%, which we view as a positive step toward fully funding the pension system. In addition, the village uses actuarially determined contributions (ADCs) that assume 100% funding by 2040, which will lead to higher funding levels compared with other Illinois municipalities that only strive for 90% funded levels (as required by state law).

Beginning in fiscal 2018, Northbrook contributed 110% of the ADC, using incremental increases in ambulance fees to help improve the police and fire pensions. Furthermore, the state requires the funding based on projected unit cost, but the village used the assumption of entry age normal; this increased the funding for fiscal 2019.

Although, we do not anticipate any significant increases in contributions during the next several years that would cause greater budgetary pressure, we do not believe the village has a credible plan to address the severely low funding levels.

Northbrook allows retirees to buy health insurance at their own cost under its plan for employees, so it has only an implicit rate subsidy for OPEBs.

Strong institutional framework

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

Outlook

The stable outlook reflects our opinion that we will likely not change the rating during the two-year outlook period.

The outlook also reflects our opinion of the village's very strong economy, which benefits from its participation in the Chicago MSA, and strong management.

Downside scenario

We could lower the rating if Northbrook's budgetary performance weakens in a way that we believe compromises the village's financial flexibility or liquidity profile. We could also lower the rating if the village's fixed costs, including debt and pensions, increases significantly compared with expenditures and began to affect the village's ability to produce balanced financial results.

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
- 2018 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.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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