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Ratings

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Summary:

Edmonds, Washington; General Obligation

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Credit Profile		
US$11.9 mil ltd tax GO imp and rfdg bnds (tax-exempt) ser 2021A due 12/01/2041		
Long Term Rating	AAA/Stable	New
US$2.695 mil ltd tax GO rfdg bnds (taxable) ser 2021B due 12/01/2041		
Long Term Rating	AAA/Stable	New
Edmonds ltd tax GO bnds		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to Edmonds, Wash.'s anticipated $11.9 million series 2021A limited-tax general obligation (GO) improvement and refunding bonds and anticipated $2.6 million series 2021B limited-tax GO refunding bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the city's limited-tax GO debt outstanding. The outlook is stable.

The city's limited-tax GO (LTGO) bonds are secured by the city's full faith and credit, including the obligation to levy ad valorem taxes subject to statutory limitations that include a maximum levy rate of $3.60 per $1,000 of assessed value (AV) under current conditions (the city's regular levy rate in 2021 is $0.906) and a limitation on property tax revenue growth to 1% per year, excluding new construction. The rating is equal to our view of the city's general creditworthiness, as obligor, because the limitations do not narrow the tax base or limit the fungibility of property tax revenue for different uses.

Edmonds intends to service debt for a portion of the 2021A bonds from net revenues from its water and sewer utility system. We rate to the strength of the LTGO pledge on the city's 2021 bonds as we lack the necessary information to assess the credit quality of the water and sewer pledge.

The series 2021B bonds are additionally secured from intergovernmental payments in the form of sales tax transferred from the Edmonds Public Facilities District (PFD) and Snohomish County PFD to the city and real estate excise tax receipts imposed by the city. We rate to the strength of the LTGO pledge on the city's 2021 bonds as we lack the necessary information to assess the credit quality of the sales tax and real estate excise pledge.

Proceeds from the sale of the 2021A bonds will fund various improvements to the city's Civic Park and facilities and refinance the city's series 2011 water and sewer improvement and refunding revenue bonds for debt service savings.

The 2021B bond proceeds will advance refund and restructure the portion attributable to Edmonds PFD with respect to the series 2012 limited tax general obligation refunding bonds to modify debt service requirements.

Credit overview

Edmonds' general credit characteristics reflect an affluent bedroom community supported by a wealthy property tax base and high household incomes, with access to the broad and diverse Seattle-Tacoma-Bellevue metropolitan statistical area (MSA) and the Puget Sound economy. Edmonds' favorable location within the Seattle MSA benefits the city by providing substantial employment opportunities to its residents, as well as improving home values throughout the area tied to strong economic growth in the region. Management reports the COVID-19 pandemic had a minimal impact on the local economy as residents shifted consumer spending towards e-commerce in combination with executing taxable transactions within the city's boundaries rather than surrounding employment areas during their work commute. The city has historically demonstrated strong financial performance, driven by conservative budgeting, revenue growth and prudent management practices and policies, which led to the building and maintenance of its very strong reserve position.

Due to several years of building its reserve position, management incorporated the budgeted use of available reserves to fund various capital-related expenditures and address a backlog of various maintenance projects. So, while reserves have decreased from historical highs, the drawdowns are intentional and current reserves remain at levels that we consider very strong and above its formalized reserve policy. Furthermore, the city's preference to cash fund capital outlay has tempered the need for substantial debt financing as reflected in the city's very strong debt profile. Although unlikely in the near term, downward pressure could emerge if the city's available fund balances decrease below its formal policy of 20% of operating expenditures.

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

- Very strong economy, highlighted by the city's optimal location near major transportation and shipping corridors in the broad and diverse Seattle-Tacoma-Bellevue MSA;
- Strong management, with realistic and well-grounded revenue and expenditure assumptions for budget building;
- Maintenance of its very strong reserve and liquidity position despite recent planned drawdowns; and
- Very strong debt and contingent liability profile supported by a low debt burden and manageable fixed costs.

Environmental, social, and governance (ESG) factors

We consider the city to have elevated environment risks given the city lies adjacent to Puget Sound and within the Cascadia subduction zone, exposing the city to storm-surges and other extreme events related to sea-level rise as well as seismic risks. We note, however, that these risks are somewhat mitigated by state building codes and the county-level emergency planning the city participates in. We consider the city's social and governance risk factors in line with our view of the sector broadly.

Stable Outlook

Downside scenario

We could lower the rating if the city experiences material financial deterioration due to softening of key revenue streams or prolonged capital spending without taking any corresponding budgetary adjustments, resulting in a material decrease in available reserves that are no longer comparable with those of similarly rated peers.

Credit Opinion

Mature bedroom community rooted in the dynamic and diverse Puget Sound economy supported by very strong wealth and income metrics

Encompassing approximately 10 square miles, Edmonds functions as a thriving bedroom community with a population of roughly 42,780 residents. The city is less than 20 miles north of downtown Seattle, and it participates in the Puget Sound economy, which provides residents with ample employment opportunities throughout Snohomish and King counties, bolstering local income levels. The city is known as a daytime destination, with its economy primarily driven by retail, services, and health care. Edmonds has several car dealerships and a Swedish Hospital (217 bed capacity) off highway 99, in addition to various retail and restaurants in the city's downtown business district. Further anchoring the city's economy is its waterfront access, which provides residents access to the Washington State Ferries, a public fishing pier, and underwater park. The Port of Edmonds is within the city, which consists of approximately 662 moorage slips and has the storage capacity for 232 dry boats. Finally, the city has a very active arts community, including several galleries in the business district and a performing arts center.

After contracting in fiscal 2010 due to the national economic downturn, the city's property tax base demonstrated strong growth, surpassing its previous 2009 peak in 2017. The city's property tax base consists predominantly of residential and some commercial parcels, adding a degree of stability to its tax base. Due to appreciation and light economic development, the city's annual AV growth averaged 9.6% the past five years. In aggregate, the city's property tax base grew by $4.2 billion, or 58%, to $11.6 billion during 2016-2021.

Despite the fully built-out characteristics, officials anticipate continued modest growth in taxable value (TV) in the near term, which will likely be spurred by positive reappraisals and development projects already in the pipeline. Some examples of projects already in the pipeline include expansion to its medical campus, the addition of several apartment and assisted living complexes, and the expected addition of a light rail to the area (expected to come online in nearby Lynnwood in 2024) from Seattle that will likely spur further development. Although the Seattle-Tacoma-Bellevue economic area was one of the first major metropolitan areas affected by the COVID-19 pandemic, economic activity in the city continues to strengthen, as reflected in numerous economic indicators such as property tax growth, consumer spending resilience, and steady output of economic developments, which we expect will continue to support the city's very strong economy. For more information on the effect of the pandemic on U.S. public finance, see "Economic Outlook U.S. Q4 2021: The Rocket Is Leveling Off," published Sept. 23, 2021, on RatingsDirect.

Strong managerial practices using conservative budgetary assumptions and detailed long-term planning

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

When formulating the subsequent year's budget, management uses several years of historical trend analysis. Additionally, management works with various outside sources, including local developers and auto dealerships for revenue projections. Monthly budget-to-actual financial reporting is provided to the city council and budgetary amendments are generally made on a quarterly basis. A formalized five-year financial forecast is conducted for the general fund, inclusive of conservative projections, and is updated on an annual basis. Furthermore, the city has a formalized comprehensive five-year capital improvement plan (CIP) across multiple funds, which is also updated annually.

The city has a formal investment policy in place and it provides council with monthly investment holdings and performance reports. The city also has a formalized unassigned reserve fund policy to maintain a minimum of 16% of operations, in addition to a contingency reserve policy to maintain 4% of operations, in place for financial stabilization and emergencies. Lastly, the city does not have a formalized debt policy.

Despite recent uses of reserves for planned projects, Edmond's operational performance is balanced

In assessing the city's budgetary performance, we adjusted for annually recurring transfers into and out of the general fund and eliminated what we consider one-time capital outlay. Historically, Edmonds maintained stable budgetary performance resulting from a combination of conservative budgeting and strong revenue growth. The budget is monitored regularly throughout the year, and final results are often better than budgeted. The city plans to maintain elevated levels of cash-funded capital as part of the annual operating budget, resulting in budgeted uses of fund balance in excess of its formal reserve policy. Absent elevated capital spending to address various capital related projects, the city's operations remain structurally sound given Edmonds' stable historical performance, strong revenue growth, and consistent budget monitoring.

Despite COVID-19-related pressures and planned drawdowns, Edmonds was adequately positioned to withstand the economic shock and its lingering effects and maintain its overall sound financial profile. While tax collections initially softened during the onset of the pandemic due to travel restrictions and stay-at-home orders, collections rebounded by August 2020 allowing the city's total tax collections to avoid any material decreases and mirror fiscal 2019 figures. Because of the city's financial durability, it did not have to lay off or furlough any employees to maintain structural balance during the pandemic and year-to-date tax collections estimates are trending higher than pre-pandemic levels.

The city received approximately $2 million in CARES Act funding which helped fund pandemic-related expenditures and provide community assistance in the form of grants. The city expects to receive approximately $11.9 million from the federal America Rescue Plan (ARP) stimulus and plans to exhaust the fund annually through 2024. Management anticipates allocating the federal funding toward pandemic- and capital-related expenditures and several community betterment initiatives. We expect ARP funding will support credit quality of issuers across the U.S. public finance sectors as detailed in our report, "Across U.S. Public Finance, All Sectors Stand to Benefit From the American Rescue Plan," published March 18, 2021.

The city's primary sources of general fund revenue in fiscal 2020 were property taxes (41%), sales taxes (26%), and utility taxes (19%). Despite COVID-19 pressures, sales tax revenues experienced an aggregate increase, with the city reporting that year-over-year collections were stronger than budget estimates. Management attributes the growth in sales collection to residents shifting consumer spending towards e-commerce in combination with executing taxable transactions within the city's boundaries rather than surrounding employment areas during their work commute. Property tax revenues have generally increased in line with the city's expanding economy and management believes this trend will continue in tandem with TV growth. We also note that the city is not levying at its maximum rates, which provides the city with additional revenue-raising flexibility if needed.

The city's 2021 adopted budget anticipated $42.5 million in general fund revenues and year-to-date estimates show $43.8 million resulting in a positive variance of approximately 3%. On the expenditure side, the city's year-to-date estimates are approximately $708,000 less than adopted budgeted figures and the city forecasts it will produce a small operating deficit of approximately $613,451 or roughly 1% of expenditures. Given Edmonds' established track record producing positive variances at year-end, it is likely the city will reduce the magnitude of its estimated deficit and maintain balanced operations.

The city has a general fund receivable of $3.8 million from the Edmonds PFD that is a discreetly presented component unit but legally separate entity. The receivable consists of the remaining balance of the series 2012 LTGO bonds and prior loans to the PFD from the city that accumulated between fiscal years 2011-2017. The city guaranteed repayment of the Edmonds PFD's Sales Tax Obligation and Refunding Bonds, 2008 (subsequently refinanced in 2018) through a contingent loan agreement (CLA) with the PFD and it is required to advance funds necessary to assist with debt service. The debt service on the portion of the city-issued 2012 LTGO bonds attributable to the Edmonds PFD are payable by the PFD based on an interlocal agreement. We have not adjusted our view of the city's available fund to exclude this receivable as the 2012 LTGO bonds are being refinanced with the series 2021B bonds. Furthermore, Edmonds expects to recover the total balance of all past advancements made under CLA (on or before FYE 2027) due to the debt restructuring coupled with the extension of a dedicated sales tax that is expected to generate sufficient revenue for the PFD to service future debt payments. However, in subsequent reviews, if we do not see any progress from the PFD toward paying the balance owed to the city, we will consider the receivable uncollectable and adjust our view of the city's available fund balance, which could have negative implications.

As Edmonds intends to address future capital outlay and a backlog of various maintenance projects, we anticipate fluctuation in the city's budgetary flexibility as reserves built up in prior years are disbursed in subsequent years, but we do not view this as a material credit weakness given the city's discretion in the timing and amounts for pay-as-you-go capital expenditures. Although unlikely in the near term, downward pressure could emerge if the city's available fund balances decrease below its formal policy of 20% of operating expenditures.

Low debt burden and relatively minimal debt service costs support a very strong debt and contingent liability profile

Including the pro forma effect of these issuances, our ratios are based on an overall net direct debt of roughly $104.5 million. We note that a sizable portion of Edmonds overall net direct debt is due to overlapping taxing entities, which accounts for 87% or $90.9 million of city's net direct debt burden. We expect the city's debt and contingent liability profile will remain at least strong over the two-year horizon given the absence of additional debt plans. Edmonds adopted five-year CIP serves as a blueprint to address subsequent growth and development in a prudent manner. The general fund CIP totals about $16.2 million for fiscal years 2021-2026. All projects included in the CIP have identified funding sources that are determined with consideration of the city's financial capacity.

The city has one bank loan with approximately $521,122 outstanding, however, the legal documents associated with the loan do not include any permissive events of default or acceleration provisions that would cause potential threat to the city's liquidity profile.

Pension and other postemployment benefits highlights:

- We do not consider pensions or other postemployment benefits (OPEB) a source of credit pressure for the city; carrying charges are low and the city participates mostly in adequately-funded-to-overfunded pooled multiple-employer plans, with contributions approximating actuarially determined contributions (ADCs).
- The city's pension plans show funding progress that we don't expect will lead to material liability increases for plan participants.
- We consider the city's OPEB, which it funds on a pay-as-you-go basis, manageable.

The city participates in the following plans as of June. 30, 2020:

- Public Employees' Retirement System (PERS) 1, a cost-sharing multi-employer plan, with a funded ratio of 69% and proportionate net pension liability of $3.4 million;
- PERS 2/3, a cost-sharing multi-employer plan, with a funded ratio of 97% and proportionate net pension liability of $1.5 million;
- Public Safety Employees' Retirement System (PSERS), with a funded ratio of 116% and net pension asset of about $35,000;
- Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plan 1, with a funded ratio of 147% and proportionate net pension asset of $7.1 million;
- LEOFF Plan 2, with a funded ratio of 116% and proportionate net pension asset of $3.6 million;
- Single-employer Firemen Pension Plan, with a funded ratio of 19% and net pension liability of $507,497; and
- LEOFF 1 Retiree Medical and Long-Term Benefit Plan, with a funded ratio of 0% and total OPEB liability of $8.3 million.

The contractually required contributions (CRCs) of the PERS plans exceeded both static funding and minimum funding progress in fiscal 2020, indicating our view of timely progress in reducing pension liabilities. The city makes its full required contributions. The contributions, which are developed using the same approach as the ADCs, are set for each biennium and can therefore diverge from the annually updated ADCs. However, because they determine funding requirements using an approach that approximates 10- to 15-year level-percentage open amortization, timely progress on reducing liabilities is still made even when ADCs increase above their CRCs, so we believe costs will likely remain stable. However, we note the plans' 7.4% discount rates are above our baseline of 6.0%, which we believe increases potential contribution volatility in the future.

Adequate institutional framework

The institutional framework score for Washington municipalities is adequate, in our view, partly because of statutory discretion regarding the quality and timeliness of annual financial reporting.

Local ratings' relationship with U.S. sovereign

Edmond's LTGO bonds are eligible to be rated above the sovereign because we believe the city can maintain better credit characteristics than the U.S. in a stress scenario. We do not expect the city to default in a stress scenario likely to accompany a sovereign default given autonomy from sovereign intervention. 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. We view the city as exhibiting relatively low funding interdependency with the federal government, as local derived revenues represent most total governmental funds revenue. However, consistent with our view that U.S. state and local governments are moderately sensitive to country risk, we would be unlikely to set ratings on the city's LTGO-backed debt more than two notches above the U.S. sovereign rating.

Edmonds, Wash.: Key Credit Metrics				
	Most recent	**--Historical information--**		
		2020	**2019**	**2018**
Very strong economy				
Projected per capita EBI % of U.S.	177			
Market value per capita ($)	272,295			
Population		43,145	42,821	42,012
County unemployment rate(%)		8.5		
Assessed value ($000)	11,648,793	11,011,221	10,223,134	9,107,285
Ten largest taxpayers % of taxable value	1.4			
Adequate budgetary performance				
Operating fund result % of expenditures		(3.8)	(0.0)	4.5
Total governmental fund result % of expenditures		0.5	3.1	8.7
Very strong budgetary flexibility				
Available reserves % of operating expenditures		38.9	42.3	45.5
Total available reserves ($000)		16,415	17,913	18,284
Very strong liquidity				
Total government cash % of governmental fund expenditures		100	118	119
Total government cash % of governmental fund debt service		4417	5322	5627
Strong management				
Financial Management Assessment	Good			
Very strong debt & long-term liabilities				
Debt service % of governmental fund expenditures		2.3	2.2	2.1
Net direct debt % of governmental fund revenue	26			
Overall net debt % of market value	0.9			
Direct debt 10-year amortization (%)	37			
Required pension contribution % of governmental fund expenditures		4.6		
OPEB actual contribution % of governmental fund expenditures		0.9		
Adequate institutional framework				

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

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014

- 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
- 2020 Update Of Institutional Framework For U.S. Local Governments