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Ratings

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Summary:

Northbrook Village, Illinois; General Obligation

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Credit Profile		
US$10.495 mil GO bnds ser 2021 due 12/01/2040		
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

One or more of the Credit Ratings referenced within this article was assigned by deviating from S&P Global Ratings' published Criteria.

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to the Village of Northbrook, Ill.'s series 2021 general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on the village's previously issued GO debt. The outlook is stable.

We assessed Northbrook's general creditworthiness using our criteria "U.S. Local Governments General Obligation Ratings: Methodology And Assumptions," published Sept. 12, 2013. Under the criteria (table 8), a county unemployment rate of greater than 10% for the past calendar year is reflected as a one-point downward adjustment to the economy factor score. Social distancing and shutdown measures designed to slow the spread of COVID-19 resulted in a spike in unemployment rates across the U.S. during the middle of 2020; in some cases, extreme spikes led to annual rates in excess of 10%. However, in our opinion, this period of significantly elevated unemployment was due to public health policy and may not reflect fundamental weakness in the local economy. This is demonstrated by the rapid decline in monthly unemployment rates following the relaxation of social distancing and other measures. To assess the local economy under these circumstances, we have made an exception to our criteria and are evaluating the village ratings using the average unemployment rate for Cook County excluding the months of April through July 2020, when federal stimulus funding provided the most significant support. This adjusts the unemployment rate to 8.5% instead of using the full-year 2020 average unemployment rate of 11.1%. As a result, we did not apply this one-point downward adjustment to the economic score.

Northbrook's unlimited-tax GO pledge secures the series 2021 bonds. The village will use the bond proceeds to fund capital improvements throughout the village.

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 moderately sensitive to country risk. Northbrook has pledged its general obligation ad valorem unlimited tax revenue as 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 overview

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, a very desirable and growing residential sector, and 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 given our opinion of the village's stable financial performance and management continuing to balance 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 partly offsets volatility risk given economic fluctuations related to the village's sales tax--the major tax revenue source.

The 'AAA' rating further reflects our assessment of the village's:

- Very strong economy, with access to a broad and diverse MSA;
- Strong management, with good financial policies and practices under our financial management assessment 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 2020;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2020 of 53% of operating expenditures;
- Very strong liquidity, with total government available cash at 100% of total governmental fund expenditures and 8.2x governmental debt service, and access to external liquidity 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 181.8% of total governmental fund revenue, as well as a large pension and other postemployment benefit (OPEB) obligation and the lack of a plan to sufficiently address the obligation; and
- Strong institutional framework score.

Environmental, social, and governance (ESG) factors

The village proactively manages its cybersecurity risk with training and infrastructure improvements that are incorporated into its capital planning, and the village has developed a climate action plan, which we view as positive governance and environmental factors. We view the village's social risks as in line with the sector standard.

Stable Outlook

Downside scenario

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

Credit Opinion

Very strong economy

We consider Northbrook's economy very strong. The village, with an estimated population of 32,454, is located in Cook County in the Chicago-Naperville-Elgin MSA, which we consider broad and diverse. The village has a projected per capita effective buying income of 191% of the national level and per capita market value of $265,007. Overall, the village's market value grew by 13.2% over the past year to $8.6 billion in 2021.

With access to the broad and diverse Chicago, MSA, the village has seen consistent growth. We expect this growth to continue given ongoing and planned developments throughout the village, which include mixed-use developments, townhomes, apartments, single-family homes, and a number of commercial enterprises. For S&P Global Economics' latest U.S. economic forecast, see the report "Economic Outlook U.S. Q3 2021: Sun, Sun, Sun, Here It Comes," published June 24, 2021. Overall, we anticipate that the village's economic base will remain very strong for the foreseeable future.

Strong management

We view the village's management as strong, with good financial policies and practices under our financial management assessment methodology, indicating our view that 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% of revenue, which provides a cushion against fluctuations in economically sensitive revenue, a debt policy (which do not view as materially more restrictive than state statutes), and an investment policy. The board receives monthly and quarterly financial reports, a two-year budget document (although it 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 monthly economic reports that help monitor and project sales tax collections.

Strong budgetary performance

Northbrook's budgetary performance is strong, in our opinion. The village had a surplus operating result in the general fund of 2.3% of expenditures and a slight surplus results across all governmental funds of 1.4% in fiscal 2020.

We note that we have made a number of adjustments to the village's operating data to better analyze its typical operations and facilitate comparisons with peers. For instance, we have removed expenditures that were funded by bond proceeds.

The village's largest sources of tax revenue are home rule and state share sales taxes, which accounted for 38.3% of total general fund revenue in fiscal 2020. Property taxes (18.5%) and state income taxes (7.7%) were the next leading sources of tax revenue.

Despite challenges posed by the pandemic, officials project that the village finished fiscal 2021 with a modest general fund drawdown of $2.2 million, which it primarily attributes to one-time costs associated with a voluntary separation incentive that it provided to employees (totaling roughly $1.5 million). The fiscal 2020 budget features a modest surplus of $31,000, which officials report is conservative. The village is expecting $4.5 million in American Rescue Plan Act funds, and officials report that a number of revenue items are coming in better than budgeted given the economic recovery. In light of the village's historically stable operations as well as official projections, we anticipate that the village will maintain adequate-to-strong operations for the foreseeable future.

Very strong budgetary flexibility

Northbrook's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2020 of 53% of operating expenditures, or $21.6 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. Over the past three years, the total available fund balance has been consistent, totaling 54% of expenditures in 2019 and 51% in 2018.

Given our expectations for budgetary performance, we anticipate that reserves will remain very strong and in line with the village's reserve policy of 40% of revenue for the foreseeable future.

Very strong liquidity

In our opinion, Northbrook's liquidity is very strong, with total government available cash at 100% of total governmental fund expenditures and 8.2x governmental debt service in 2020.

We believe the village has strong access to external liquidity based on regular issuance of GO bonds. The village is party to a privately placed GO bond, but we do not view any of its terms as posing a risk to either the village's liquidity or operations. Overall, given our expectations for the village's operations, we anticipate that its liquidity position will remain very strong for the foreseeable future.

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 181.8% of total governmental fund revenue.

The village has no additional debt planned within the next two years, and thus we do not anticipate that its debt burden will change materially.

Pension and OPEB liabilities

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 required pension and actual OPEB contributions totaled 16.6% of total governmental fund expenditures in 2020, with 15.3% representing required contributions to pension obligations and 1.3% representing OPEB payments. The village made 112% of its required pension contribution.

Although pension contributions remain a long-term credit consideration, we believe the liability is manageable.

Northbrook contributes to three defined benefit pension plans as of April 30, 2020:

- The Illinois Municipal Retirement Fund (IMRF), a defined benefit agent multiple-employer public employee retirement system that is 93.8% funded for the village portion with a proportionate share of the net pension liability equal to nearly $5 million and 93.2% funded for the library portion with a liability of $1.3.
- A single-employer police pension plan that is 51.5% funded with a net liability of $50.8 million.
- A single-employer firefighter pension plan that is 51.7% funded with a net liability of $49.9 million.
- Northbrook allows retirees to buy health insurance at their own cost under its plan for employees, until the age of 65 or until they are eligible for Medicare. The OPEB liability totals $9.4 million.

The IMRF assumes a discount rate of 7.25% while the police and fire plans assume a rate of 7%. Required contribution in the State of Illinois are designed to meet only 90% funding by 2040. For several years, the village has been contributing more than the ADC for its police and firefighter plans, using incremental increases in ambulance fees to help improve funding. Although we anticipate no 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. Although we believe the village's excess contributions somewhat mitigate rising pension pressures, we note that said contributions have fallen short of our view of both static and minimum funding progress. For more information on our view of Illinois pensions, see "Pension Brief: Single-Employer Pension Plans Are Straining Illinois Municipalities' Credit Quality," published July 27, 2021.

Strong institutional framework

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

Related Research

- 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