

RatingsDirect®

Summary:

Novi, Michigan; General Obligation; General Obligation Equivalent Security

Primary Credit Analyst:

Helen Samuelson, Chicago (1) 312-233-7011; helen.samuelson@standardandpoors.com

Secondary Contact:

Katelyn A Batesel, Centennial (303) 721-4683; katelyn.batesel@standardandpoors.com

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Summary:

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Credit Profile

Novi spl assess ltd tax bnds ser 2003 dtd 12/01/2003 due 10/01/2004-2017

Unenhanced Rating

AAA(SPUR)/Stable

Upgraded

Novi GO

Unenhanced Rating

AAA(SPUR)/Stable

Upgraded

Rationale

Standard & Poor's Ratings Services raised its long-term rating and underlying rating (SPUR) to 'AAA' from 'AA+' on Novi, Mich.'s general obligation (GO) debt outstanding. The outlook is stable.

The bonds are secured by city's full faith and credit and power to levy ad valorem taxes.

The upgrade reflects our assessment of the city's improved economy, with increasing market value and decreasing unemployment, as well as its passage of more formalized financial policies and procedures.

Novi's GO debt is 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. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions," U.S. local governments are considered to have moderate sensitivity to country risk. Novi has pledged its ad valorem full faith and credit GO to the debt, which is 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 city. 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, Novi has very strong financial flexibility, as demonstrated by its very strong budgetary flexibility and liquidity.

The ratings further reflect our view of the city's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with "strong" financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could deteriorate in the near term relative to fiscal 2014, which closed with a slight operating deficit in the general fund but a slight operating surplus at the total governmental fund level;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2014 of 41% of operating expenditures;
- Very strong liquidity, with total government available cash of 74.7% of total governmental fund expenditures and 8.2x governmental debt service, and access to external liquidity we consider strong;
- Very strong debt and contingent liability position, with debt service carrying charges of 9.1% of expenditures and

net direct debt that is 58.5% of total governmental fund revenue and low overall net debt at less than 3% of market value and rapid amortization with 88.6% of debt scheduled to be retired in 10 years; and

- Strong institutional framework score.

Very strong economy

We consider Novi's economy very strong. The city, with an estimated population of 58,980, is located in Oakland County in the Detroit-Warren-Dearborn, Mich. MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 147% of the national level and per capita market value of \$124,081. Overall, the city's market value fell by 1.5% over the past year to \$7.3 billion in 2016. The county unemployment rate was 6.8% in 2014.

Due to continued residential and commercial development, the city's market value and assessed value (AV) have increased by approximately 20% and 9%, respectively. Novi is home to a number of sizable retail centers, hotels, a convention center, and the regional and global headquarters of several enterprises. Some of the area's top employers include St. John's Health, Novi Community Schools, Fox Run Retirement Community, and Ryder Systems Inc. In addition, as the city is located between Detroit and Ann Arbor, residents have easy access to a broad and diverse economic base with numerous employment opportunities.

Very strong management

We view the city's management as very strong, with "strong" financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

Management consults the city assessor, the state of Michigan, its departments heads, and historical trend data to develop revenue and expenditure forecasts for both the upcoming budget and its long term financial plan.

Budget-to-actual reports are presented to the board monthly, while investments are reported quarterly. Also, the city maintains a formal debt management policy, a rolling six-year capital improvement plan, an investment policy, and a formal reserve policy that stipulates that the city must keep at least 18% of expenditures on hand.

Adequate budgetary performance

Novi's budgetary performance is adequate in our opinion. The city had slight deficit operating results in the general fund of 0.9% of expenditures, but a slight surplus result across all governmental funds of 1.4% in fiscal 2014. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from 2014 results in the near term.

We have elected to make a number of adjustments to the city's financial data in order to better analyze its typical operations as well as compare its performance to that of its peers. For instance, we have moved recurring transfers to and from the general fund above the line to appear as revenues and expenditures, respectively, and combined the city's public safety fund with its general fund.

Due in large part to the city's aggressive capital improvement plan, it ran deficits in both its general fund and its total governmental funds in fiscal years 2012 and 2013, and it projects that it will continue to draw down on its combined general and public safety funds in fiscal years 2016 and 2017. Management currently estimates that it ended fiscal 2015 with an adjusted general fund surplus of over \$2 million, which it attributes primarily to increased property tax revenue (from AV growth) and building permit revenue. Given that the city has established minimum reserve

requirements for both its general fund and special revenues fund, and that it has historically outperformed its budgets, we believe that the city's budgetary performance will remain at least adequate for the foreseeable future.

Very strong budgetary flexibility

Novi's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2014 of 41% of operating expenditures, or \$12.0 million. We expect the available fund balance will remain above 30% of expenditures for the current and next fiscal years, which we view as a positive credit factor.

As we have combined the city's public safety funds with the general fund, we have included the latter's reserves in our analysis of Novi's budgetary flexibility. Consequently, we note that management estimates that its combined reserves increased to nearly \$14 million in fiscal 2015, which equates to 40.8% of expenditures. As a result of the deficits projected for fiscal years 2016 and 2017, management currently estimates that its combined fund balance will fall to \$12.7 million at the end of fiscal 2017, which we would still consider very strong, at 39.8% of expenditures. As the city has a formal policy of keeping at least 18% to 22% of expenditures on hand, and as management seems resolved to maintain this policy, we believe that the city's budgetary flexibility should remain very strong for the foreseeable future.

Very strong liquidity

In our opinion, Novi's liquidity is very strong, with total government available cash of 74.7% of total governmental fund expenditures and 8.2x governmental debt service in 2014. In our view, the city has strong access to external liquidity if necessary.

We have based our assessment of the city's access to external liquidity on its recent history of debt issuances, which include a variety of different types of debt. Also, the city's 2014 audit reported over \$36 million in cash and cash equivalents at the end of the fiscal year.

Very strong debt and contingent liability profile

In our view, Novi's debt and contingent liability profile is very strong. Total governmental fund debt service is 9.1% of total governmental fund expenditures, and net direct debt is 58.5% of total governmental fund revenue. Overall net debt is low at 2.9% of market value and approximately 88.6% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

The city has no plans to issue additional debt, and it recently adopted a conservative debt management policy that limits its net direct debt to no more than \$2,500 per capita and its debt service payments to less than 20% of combined operating and debt-service funds expenditures.

Novi's combined pension and other postemployment benefits (OPEB) contributions totaled nearly 8.3% of total governmental fund expenditures in 2014. Of that amount, 5.1% represented contributions to pension obligations and 3.1% represented OPEB payments. The city made its full annual required pension contribution in 2014.

Novi contributes to the Michigan Employees Retirement System, a defined-benefit, state-administered pension plan, to which it pays its full required employer contribution each year. In addition, the city also provides health care benefits to most of its full-time employees upon their retirement. In order to fund these benefits, the city paid nearly \$678,000 for retirees' health premiums in 2014 while also contributing approximately \$1.5 million toward its Retiree Health Care Benefits Trust (106% of its actuarially required contribution), which is currently 83% funded.

Strong institutional framework

The institutional framework score for Michigan municipalities with a population between 4,000 and 600,000 is strong.

Outlook

The stable outlook reflects our expectation that the city will maintain very strong budgetary flexibility and at least adequate budgetary performance for the next two years.

Downside scenario

Should the city's economy weaken significantly, or should its budgetary performance deteriorate to such a degree that its reserves fell below its stated policy, we could consider lowering the ratings.

Related Criteria And Research

Related Criteria

- USPF Criteria: Local Government GO Ratings Methodology And Assumptions, Sept. 12, 2013
- USPF Criteria: Financial Management Assessment, June 27, 2006
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Limited-Tax GO Debt, Jan. 10, 2002
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Institutional Framework Overview: Michigan Local Governments

Ratings Detail (As Of November 23, 2015)

Novi Bldg Auth, Michigan

Novi, Michigan

Novi Bldg Auth bldg auth rfdg bnds (GO - ltd tax)

Unenhanced Rating NR(SPUR) Current

Novi Bldg Auth bldg auth (sr complex) bnds ser 1999 dtd 09/01/1999 due 10/01/2002-2014 2016 2019 2025

Unenhanced Rating NR(SPUR) Current

Many issues are enhanced by bond insurance.

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