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Summary:

Grosse Pointe Shores, Michigan; General Obligation

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Summary:

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Credit Profile		
US$8.055 mil cap imp bnds (ltd tax GO) ser 2022 due 10/01/2051		
Long Term Rating	AAA/Stable	New
Grosse Pointe Shores		
Long Term Rating	AAA/Stable	Affirmed
Village of Grosse Pointe Shores, A Michigan City ltd tax GO rfdg bnds		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' rating, with a stable outlook, to Village of Grosse Pointe Shores, A Michigan City, Mich.'s roughly $8 million series 2022 limited-tax general obligation (GO) capital improvement bonds and affirmed its 'AAA' rating, with a stable outlook, on its existing GO debt.

The city's limited full-faith-and-credit pledge and agreement to levy ad valorem property taxes, within statutory and constitutional tax limitations, secure the series 2022 bonds. We rate the limited-tax GO debt on par with the city's general creditworthiness (i.e., unlimited-tax GO pledge) because it collects ad valorem taxes from the entire property tax base and there are few limitations on the fungibility of resources available for debt service.

The city's GO debt is eligible for a rating above the sovereign because we believe it can maintain better credit characteristics than the U.S. in a stress scenario. Based on our criteria, titled "Ratings Above The Sovereign: Corporate and Government Ratings--Methodology and Assumptions" (published Nov. 19, 2013, on RatingsDirect), the city has predominantly locally derived revenue sources, with independent taxing authority and treasury management from the federal government.

Officials will use series 2022 bond proceeds to fund improvement and replacement of various water and sewer lines.

Credit overview

The city is a small, affluent Detroit suburb with multimillion-dollar properties and a stable tax base producing annual property tax revenue growth. Economic strength is further bolstered by strong management, who produced neutral or positive operating results since fiscal 2009, except for fiscal 2019 due to one-time capital outlays. Series 2022 bonds and the possibility for additional new-money debt within the next several years weigh on our view of the debt profile; however, debt and carrying charges are manageable, especially when factoring in the city's revenue raising flexibility because the property millage rate is significantly lower than the Headlee limit. The city's pension plan posted large investment returns in fiscal 2021 that reduced the liability to about $2.6 million, from $10.4 million, a credit positive. The city's other postemployment benefits (OPEB) liability has marginally decreased over the last several years, despite contributions less than the actuarially determined contribution (ADC); retirement costs are currently not a pressure, but this could change depending on assumption changes and market volatility.

The stable outlook reflects S&P Global Ratings' expectation for operations to remain structurally sound, considering management's performance history and no plans to significantly draw down reserves. We expect a limited change to other credit fundamentals; therefore, we do not expect to change the rating within the two-year outlook.

The rating reflects our view of the city's:

- Status as an affluent northeast Detroit suburb, with wealth and income metrics considerably higher than peers;
- Consistently balanced or positive operations and maintenance of very strong reserves, with expectations for limited near-term change;
- Increasing, but manageable debt due to series 2022 bonds, and pension funding progress that materially improved in fiscal 2021 from notable investment performance; and
- Strong management with good risk-mitigating financial management policies and practices under our Financial Management Assessment (FMA) methodology, combined with a strong institutional framework.

Environmental, social, and governance

We do not currently identify any outsized social or governance risks affecting the city's credit quality; we view them as in line with sector standards. Environmental risks are heightened because the city borders Lake St. Claire and, without base elevation, is prone to "100-year" flooding. Management is proactively managing flood risk through plans to replace its water pump station.

Stable Outlook

Downside scenario

We could lower the rating or issue a negative outlook if budgetary performance deteriorates, whether due to operating pressure or one-time spending, causing available reserves to decrease and hold below 25% of operating expenditures. While not expected, we could also change the rating or outlook if the debt and retirement-liabilities profile significantly weakens, or if management's financial policies and practices become less formalized.

Credit Opinion

Wealthy Detroit suburb with wealth and income levels providing broad rating strength

The small, one-square-mile residential city borders Lake St. Claire, about 20 minutes northeast of downtown Detroit, in Wayne and Macomb counties. As it is home to multimillionaires, income and wealth levels are significantly higher than peers, providing broad support for the rating. We typically characterize the stable local economy as very strong; however, we currently consider it strong due to county unemployment above 10% in 2020 as a result of COVID-19. Unemployment is likely to fall below 10% in 2021, and we think the community is comparatively more insulated from recessions than others, considering its demographics.

The city's tax base is nearly 100% residential, with market value and taxable value increasing by over 28% and 23%, respectively, between fiscal years 2017 and 2022. The 10 leading taxpayers include a yacht club and Martha Ford, and there is little taxpayer concentration, with concentration typically 7% or less over the last decade. Management reports no significant recently settled or outstanding tax appeals.

Wayne County's average unemployment was 13.8% in 2020 due to COVID-19. It increased to a high of 27.4% in May 2020, then decreased to 6.4% in January 2022. Countywide unemployment does not accurately represent labor market conditions for most city residents because it captures cyclicality from automotive manufacturing.

Strong management with good risk-mitigating financial management policies and practices

Highlights include management's:

- Budgeting based upon three years of trends, conservative assumptions, and information from various sources, such as the Michigan Treasury, Department of Labor, and professional associations;
- Monthly budget-to-actual reporting to the city council and as-needed budget amendments;
- Multiyear financial projections with reasonable assumptions that look five years beyond the current budget year for each governmental fund line item;
- Lack of a rolling five-year capital-improvement plan, though officials maintain planning documents that assess needs for over five years, with updates made intermittently;
- Formal investment management policy that mirrors state guidelines, with investment earnings reported quarterly to the council through informal discussions;
- Lack of a comprehensive debt management policy, though state limits are followed; and
- Formal reserve policy requiring maintenance of unrestricted general fund reserves of at least 25% of expenditures, which is followed.

Financial strength from revenue autonomy and capacity to generate revenue

Fiscal 2021 ended with a $463,000 surplus, or 7.5% of general fund expenditures, increasing reserves to about $2.4 million, or 36.1%. We adjusted fiscal 2019-2021 results for one-time expenditures, and we treat recurring transfers into the general fund from the water and sewer fund, as well as recurring transfers into other governmental funds from the general fund, as regular operating revenue/expenditures. Positive operating results reflect a 3.8% increase in property tax revenue and park program revenue that rebounded after decreasing in fiscal 2020 due to the pandemic. Additionally, operations were aided by new city leadership that was conservative with spending.

The fiscal 2022 adopted general fund budget forecasts balanced operating results; management still expects this, though it reports the possibility of a small surplus. The budget includes about $50,000 in American Rescue Plan Act (ARPA) funds, equating to less than 1% of budgeted revenue. The city has received half of its estimated $274,000 in total ARPA funding, which must be spent by 2026.

For fiscal 2023, management has no major inflationary concerns and is developing a conservative and balanced budget. Three labor contracts were recently extended by three to five years, helping to manage personnel costs over the next several years.

Overall, we expect finances to remain largely the same over the near term because:

- Operating results are consistently neutral or positive;
- Management has no plans to significantly draw down reserves; and
- Operations are 81% funded via property taxes and there is significant revenue raising flexibility, since it only levies about 13 mills and may go up to about 19 mills, under the Headlee limit.

The city has a master equipment lease with a local bank that allows for payment acceleration triggered by default. There is less than $830,000 outstanding, or 16.7% of available cash and equivalents: liquidity would likely remain very strong in the unlikely event of default.

Manageable debt and carrying charges, limited change expected despite possibility of additional debt

Following the series 2022 bond issuance, net direct debt will total about $11.1 million, or 148% of budgeted fiscal 2022 total governmental fund revenue, including about $2.2 million outstanding on two lease-purchase agreements for various equipment. Series 2022 bonds are 30-year bonds, which will slow the pace of debt retirement, although most (80%) of its other debt matures within 10 years. We consider $2.85 million, or 86% of the city's series 2013 and 2016 bonds as self-supporting: they are only backed by the city's GO pledge; however, about 57% of series 2013 bonds are paid from the water and sewer fund, while the marina fund fully pays series 2016 bonds. Because of this, debt service is typically less than 6% of total governmental fund expenditures.

Overall, we view the debt profile as weak due to increasing debt levels from series 2022 bonds and the possibility that up to $8 million in additional new-money debt could be issued within the next several years for construction of a water pump station replacement. The new-money debt plans are preliminary; they could happen beyond two years and the issuance amount could be less because management is exploring grant funding opportunities. Nonetheless, we expected debt to remain manageable and not create budgetary pressure.

Manageable retirement costs, recently significant funding progress from investment earnings

The city administers two single-employer, defined-benefit plans, providing pension and OPEB for general and public safety employees. It also has a defined contribution (DC) plan administered by an insurance company for general nonunion employees.

As of June 30, 2021, the city's retirement liabilities were:

- Pension, which was 91.5% funded, with a $2.6 million liability when using a 6.72% discount; and
- OPEB, which was 18.1% funded, with a $8.5 million liability when using a 7% discount.

Fiscal 2021 retirement costs totaled about $730,000, or 11.4% of total governmental fund expenditures, reflecting:

- $405,000 to pension;
- $200,000 to OPEB; and
- $125,000 to DC.

Pension contributions have equaled or been slightly more than the ADC since fiscal 2012. OPEB contributions have been below the ADC since first reporting in fiscal 2017, although the liability has marginally decreased.

Fiscal 2021 pension contributions were less than our minimum funding progress metric; however, funding progress significantly improved (91.5% from 68%) due to money-weighted investment returns exceeding 30%, net of expenses. An actuarial plan exists to reach full funding within 18 years and contributions should increase by approximately 3.2% annually due to level-percent-of-pay amortization. Considering the plan had a 79% equity allocation target in fiscal 2021, we identify some cost-escalation risk depending on market volatility and portfolio strategies.

Strong institutional framework

The institutional framework score for Michigan municipalities is strong.

Grosse Pointe Shores--Key Credit Metrics

	Most recent	Historical information		
		2021	2020	2019
Strong economy				
Projected per capita EBI % of U.S.	212			
Market value per capita ($)	267,219			
Population			3,064	3,059
County unemployment rate(%)			13.8	
Market value ($000)	818,758	796,906	735,790	
Ten largest taxpayers % of taxable value	6.6			
Very strong budgetary performance				
Operating fund result % of expenditures		7.5	0.9	(1.9)
Total governmental fund result % of expenditures		10.9	2.0	(3.2)
Very strong budgetary flexibility				
Available reserves % of operating expenditures		36.1	29.0	26.6
Total available reserves ($000)		2,240	1,776	1,685
Very strong liquidity				
Total government cash % of governmental fund expenditures		78	68	62
Total government cash % of governmental fund debt service		1,387	1,279	1,215
Strong management				
Financial Management Assessment	Good			
Weak debt & long-term liabilities				
Debt service % of governmental fund expenditures		5.6	5.3	5.1
Net direct debt % of governmental fund revenue	148			
Overall net debt % of market value	3.1			
Direct debt 10-year amortization (%)	44			
Required pension contribution % of governmental fund expenditures		6.3		
OPEB actual contribution % of governmental fund expenditures		3.1		
Strong 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
- 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
- 2021 Update Of Institutional Framework For U.S. Local Governments
- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022
- Alternative Financing: Disclosure Is Critical To Credit Analysis In Public Finance, Feb. 18, 2014