Summary:

Missoula, Montana; Appropriations; General Obligation

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Rationale

S&P Global Ratings affirmed its 'AA+' underlying rating (SPUR) on Missoula, Mont.'s outstanding unlimited tax general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AA' rating on the city's limited tax GO bonds. The outlook on all ratings is stable.

The unlimited-tax GO bonds outstanding are general obligations of the city payable from proceeds of an ad valorem tax, which the city covenants to levy annually on all taxable property within the city other than certain exclusions, without limitation as to rate or amount.

The limited-tax GO bonds are limited obligations of the city and are payable from funds appropriated during the budget process, including ad valorem property taxes and other legally available money of the city. The city covenants in the resolution to appropriate principal and interest payments each fiscal year from its general fund. The limited-tax GO bonds are rated one notch below the unlimited-tax GO bonds due to the additional appropriation risk associated with the security structure, as stated in our criteria "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" (published Jan. 22, 2018, on RatingsDirect).

The rating reflects our view of the city's:

- Strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong management, with "good" financial policies and practices under our Financial Management Assessment methodology;
- Adequate budgetary performance, with balanced operating results in the general fund but an operating deficit at the total governmental fund level in fiscal 2017;
- Very strong liquidity, with total government available cash at 11.4% of total governmental fund expenditures and
144.7% of governmental debt service, and access to external liquidity that we consider strong;

- Very strong debt and contingent liability position, with debt service carrying charges at 7.9% of expenditures and net direct debt that is 36.5% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 94.1% of debt scheduled to be retired in 10 years; and

- Strong institutional framework score.

**Strong economy**

We consider Missoula's economy strong. The city, with an estimated population of 70,333, is located in Missoula County in the Missoula, MT MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 93.2% of the national level and per capita market value of $117,081. Overall, the city's market value grew by 0.7% over the past year to $8.2 billion in 2019. The county's unemployment rate was 3.6% in 2017.

Missoula is the second-largest city in Montana and serves as a regional trade and service center for an 11-county area with a population estimate of more than 350,000. The area economy is diverse, with ties to health care, retail, and tourism. The city is also home to the University of Montana, which serves approximately 11,000 students or roughly 15% of the city's population. Property values in Montana are assessed every two years to reflect an 18-month lag in market activity. The appraisal period had previously spanned six years, so the jump in market value in 2017 to 2018 from $7.3 billion to $8.1 billion is reflective of significant growth that wasn't property captured in the previous cycle. As such, assessed value (AV) grew from $113.13 million to $121.75 million. This rapid increase in AV resulted in taxpayers appealing their AV and having those appeals granted. Due to these appeals, AV in 2019 has slightly decreased to $121.73 million, which will have an effect on the city's mill value and tax collections. City management has noted ongoing commercial and residential developments, including an expansion of the airport and new conference center, will likely have a positive effect on market value and AV. City management further expects less taxpayers will appeal in the near future as the two-year appraisal cycle will become more familiar.

**Strong management**

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.

Highlights include:

- The city uses historical data to budget for revenue and expenditures. It uses in-house software to collaborate with all departments throughout the year;
- The city council reviews its budget to actuals on a monthly basis;
- The city budgets for the current year only, rather than a formal long-term projection;
- The city maintains a five-year capital improvement plan, which lists project and funding sources, with updates on an annual basis;
- The city has a formal investment policy, with holding and earnings reported to city council on a monthly basis;
- The city has a formal debt policy, which provides qualitative restrictions and robust reporting mechanisms; and
• The city has a formal reserve policy to maintain a total general fund reserve minimum 7% of general fund expenditures.

Adequate budgetary performance
Missoula's budgetary performance is adequate in our opinion. The city had balanced operating results in the general fund of 0.1% of expenditures, but a deficit result across all governmental funds of negative 5.1% in fiscal 2017.

We have adjusted out one-time expenditures from costs associated from the city's road project from total governmental expenditures in 2017. Unaudited actuals for fiscal 2018 indicate a deficit of $2.8 million, or 5% of general fund expenditures, however city management indicates a surplus will be reflected when audited actuals are released in September of 2018 due to a 75-day revenue recognition period and grant funding accruals. For fiscal 2019, the city faced budgeting difficulties due to the decrease in property tax collections, but resolved to raise the property tax rates to offset this loss. The city resolved to raise property taxes by 3.67% for the 2019 budget, which contributed to a budgeted surplus operating result. City management has indicated they intend to continue build general fund reserves in coming years.

Adequate budgetary flexibility
The city has maintained good fund balances in recent years, most recently in fiscal 2017 with an assigned and unassigned available fund balance of 4.1% of general fund expenditures. Management projects that these fund balances are likely to increase at the end of fiscals 2018 and 2019. Management maintains a formal reserve policy of 7% of general fund expenditures, which the city has been in compliance in its calculated total general fund balance. (Inclusive of committed fund balance). We note that the general fund balance is composed primarily of amounts due from other funds, which we understand is for the water fund and capital projects fund, the latter having a negative fund. The city additionally intends both allocate expenditures to other departments with equipment, and issue capital leases to manage the capital fund, which management expects will bring the capital fund back into positive fund balance within two years.

The city recently acquired the municipal water system and utilized an interfund transfer from the general fund to inject working capital into the system. The city issued water revenue debt for this water fund and intends to refund these bonds within the fiscal year to bring funds back into the general fund. We currently rate these bonds 'A/Stable'. (For more information, please see the article "Missoula, Montana," published Jan. 31, 2017.)

Very strong liquidity
In our opinion, Missoula's liquidity is very strong, with total government available cash at 11.4% of total governmental fund expenditures and 144.7% of governmental debt service in 2017. In our view, the city has strong access to external liquidity if necessary.

The city has shown evidence of issuing different forms of debt within the past 20 years. We note the city has a private placement loan with a current outstanding balance of $200,183. The loan agreement has no provisions for acceleration, and we note that the principal remaining is less than 1% of fiscal 2017 revenue. We believe this issuance possesses no contingent liquidity risk.
Very strong debt and contingent liability profile

In our view, Missoula's debt and contingent liability profile is very strong. Total governmental fund debt service is 7.9% of total governmental fund expenditures, and net direct debt is 36.5% of total governmental fund revenue. Overall net debt is low at 1.3% of market value, and approximately 94.1% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors. The city does not anticipate issuing any significant medium-term debt.

Missoula's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 4.9% of total governmental fund expenditures in 2017. The city made its full annual required pension contribution in 2017. Missoula's pension contributions totaled 4.6% of total governmental fund expenditures in 2017. The city made its full annual required pension contribution in 2017. The city participates in the Public Employees Retirement Plan (PERS), the Firefighters' Unified Retirement System (FURS), and Municipal Police Officers' Retirement System (MPORS). Based on the new Governmental Accounting Standards Board reporting standards, the city's net pension liability across all plans was $33.5 million as of June 30, 2017 based on the current discount rates, and the largest plan, PERS, maintained a funded ratio of 73.8%.

Strong institutional framework

The institutional framework score for Montana municipalities is strong.

Outlook

The stable outlook reflects our view of the city's strong economy and status as an MSA. The stable outlook also reflects our expectation that the city will be able to manage its budget despite its declining mill value and maintain a performance that we would consider at least adequate. We do not anticipate changing the rating during the outlook's two-year horizon.

Upside scenario

Should the city perform better than expected for a sustained time and exhibit sustained operational balance, improving our view of the city's performance and resulting in stronger flexibility, and should the city establish stronger policies and procedures, improving our view of the city's management, we could raise the rating.

Downside scenario

Should AV appeals continue to apply budgetary pressure and the city is unable to manage the potential loss of revenue, resulting in a structural imbalance, weakening our view of the city's budgetary performance, or should the water fund and capital projects fund continue to draw from the available fund balance, weakening our view of the city's flexibility, we could lower the rating.

Related Research

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

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.