MOODY'S INVESTORS SERVICE

CREDIT OPINION
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Franklin (City of) WI

Update to credit analysis

Summary

Franklin, Wisconsin (Aa2) continues to experience tax base expansion, somewhat offsetting an above average debt burden due to borrowing for economic development. Financial reserves are healthy, and fixed costs will remain manageable given a modest pension burden.

Credit strengths

» Appreciating tax base with strong resident income indices

» Healthy operating reserves and liquidity

» Modest pension burden

Credit challenges

» Limited revenue raising flexibility due to state imposed levy limits

» Elevated debt burden for the rating category

Rating outlook

Outlooks are typically not assigned to issuers with this amount of debt.

Factors that could lead to an upgrade

» Significant growth in available operating reserves

» Continued expansion of the tax base and local economy

Factors that could lead to a downgrade

» Contraction of the city's tax base and/or weakening of resident income levels

» Draws on operating reserves or liquidity

» Material increases in the debt burden

Key indicators

Exhibit 1

Franklin (City of) WI	2014	2015	2016	2017	2018
Economy/Tax Base					
Total Full Value ($000)	$3,589,694	$3,649,186	$3,729,003	$3,888,926	$4,022,941
Population	35,920	36,103	36,155	36,295	35,779
Full Value Per Capita	$99,936	$101,077	$103,139	$107,148	$112,439
Median Family Income (% of US Median)	140.2%	140.1%	140.4%	144.2%	144.2%
Finances					
Operating Revenue ($000)	$28,721	$28,760	$27,713	$28,198	$30,683
Fund Balance ($000)	$5,065	$8,176	$8,579	$9,298	$8,125
Cash Balance ($000)	$11,281	$10,613	$9,722	$11,498	$22,598
Fund Balance as a % of Revenues	17.6%	28.4%	31.0%	33.0%	26.5%
Cash Balance as a % of Revenues	39.3%	36.9%	35.1%	40.8%	73.6%
Debt/Pensions					
Net Direct Debt ($000)	$37,712	$34,677	$31,445	$28,860	$48,810
3-Year Average of Moody's ANPL ($000)	$14,779	$21,100	$28,765	$32,398	$35,191
Net Direct Debt / Full Value (%)	1.1%	1.0%	0.8%	0.7%	1.2%
Net Direct Debt / Operating Revenues (x)	1.3x	1.2x	1.1x	1.0x	1.6x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	0.4%	0.6%	0.8%	0.8%	0.9%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	0.5x	0.7x	1.0x	1.1x	1.1x

The city's fiscal 2018 cash position is overstated due to unspent bond proceeds.
Sources: Moody's Investors Service, the city's audited financial statements, US Census Bureau

Profile

The city of Franklin encompasses 35 square miles in Milwaukee County (Aa2 stable), 10 miles south of the City of Milwaukee (A1 negative). It provides a full range of municipal services to roughly 36,000 residents.

Detailed credit considerations

Economy and tax base: Milwaukee area suburb continues to expand

Economic development within Franklin remains steady given its favorable location within the Milwaukee metropolitan area, and we anticipate values will continue to rise as a significant portion of the city remains available for development. The $4.4 billion tax base averaged 4% growth annually since 2014. Through September 2019, building permits for new single-family and multi-family homes have surpassed 2018 levels, with city officials anticipating over 900 new residential units will be completed within the next several years. Commercial developments continue within the city's tax increment districts (TID), with the completion of a 4,000 seat baseball stadium and mixed-use space, and current construction of additional mixed-use space and several restaurants in TID #5, known as Ballpark Commons. The city's newest TID, TID #7, will overlay TID #5 and include a 265-unit luxury apartment complex.

Franklin's demographic trends are strong. Population more than doubled between 1980 and 2010, but has remained relatively flat through 2018. As of September 2019, the city's unemployment rate was 2.9%, on par with the state (2.9%) but below the nation (3.3%). Median family income is strong, estimated at 144.3% of the nation.

Financial operations and reserves: healthy operating reserves and liquidity

The city's financial position is expected to remain healthy given a history of conservative budgeting and positive variances. Franklin closed fiscal 2018 with an available operating fund (general, tax increment financing (TIF) districts and debt service funds) balance of $8.1 million, equivalent to 26.5% of operating revenue. Projections for fiscal 2019 reflect a $592,000 general fund surplus due to an uptick in property taxes as recent developments come online. The fiscal 2020 budget projects a $764,000 deficit, inclusive of a $524,000 transfer out for capital outlay and a $1.3 million contingency.

Like many Wisconsin (Aa1 stable) cities, Franklin manages and finances development through TIDs that could pose operating pressure if revenues were to fall short of projections. The city had four active TIDs at the end of 2018, three of which are collecting incremental revenues. The city created an additional TID in 2019.

LIQUIDITY

The city closed fiscal 2018 with a net operating cash position of $22.6 million, or 73.6% of operating revenue. This figure is overstated, however, as it includes unspent bond proceeds. Net of these restricted funds, cash is a still healthy $13.8 million, or 45% of revenue.

Debt and pensions: fixed costs to remain manageable

The city's debt burden is expected to remain above average given regular borrowing for capital projects, though fixed costs should remain stable given its modest pension burden. Following an upcoming issue, net direct debt will be 1.5% of full value and 2.2x operating revenue, net of $1 million of GOULT debt supported by the city's water system. Management reports potentially borrowing up to $9.5 million in additional general obligation debt for TID projects in 2020, and plans to resume its practice of biennial borrowing for general capital projects in 2021.

Fixed costs, inclusive of debt service and pension contributions, were 14.9% of operating revenue in fiscal 2018.

DEBT STRUCTURE

All of the city's long-term debt is fixed rate. Principal amortization is average with 72.8% of debt retired within ten years.

Approximately $9.5 million, or 14% of outstanding debt, consists of short-term note anticipation notes (NANs) which mature on March 1, 2023. The city plans to ultimately issue long-term debt to refinance the NANs.

DEBT-RELATED DERIVATIVES

The city has no exposure to any debt-related derivatives.

PENSIONS AND OPEB

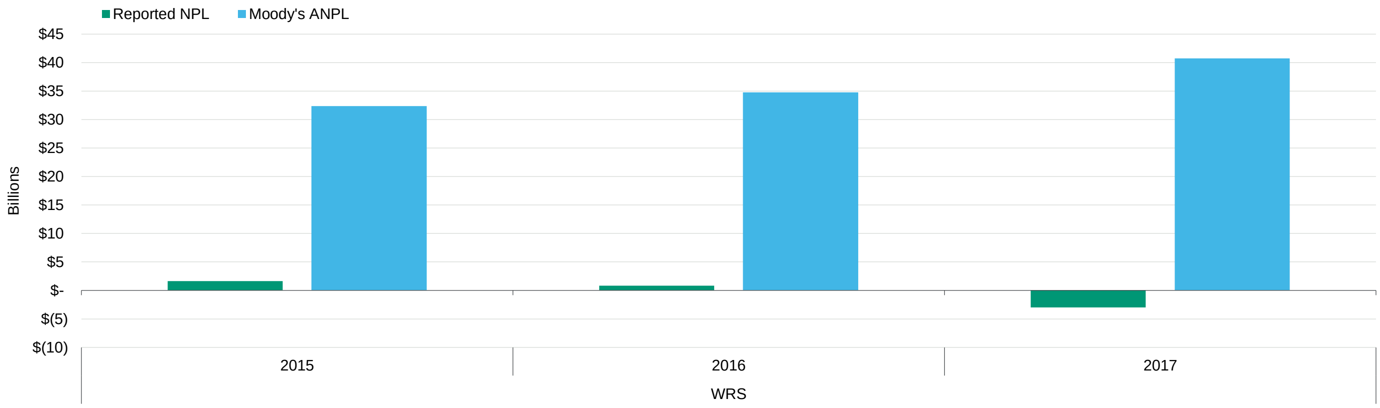
Eligible public works employees participates in the City of Franklin Defined Benefit Retirement Income Plan, a single-employer defined benefit pension plan, and all other eligible city employees participate in the City of Franklin Defined Contribution Plan, both of which are administered by the Principal Life Insurance Company (A1 stable). All eligible public safety employees and all city employees hired after January 1, 2019 participate in the Wisconsin Retirement System (WRS), a statewide cost-sharing plan. Existing employees were given the option of making an irrevocable election to join WRS as of January 1, 2019 or to remain in the supplemental pension plans.

WRS contributions are determined using a level contribution actuarial method in an effort to keep employer and employee contribution rates at a level percentage of payroll over time, and are set at 100% of the plan's funding requirement. As a result, WRS remains one of the best-funded public employee retirement systems in the country, with statewide employer contributions to WRS in 2017 totaling 107.7% of the amount needed to tread water[1].

The city's adjusted net pension liability (ANPL) was $40.1 million in 2018, up from $30.9 million in 2016, bringing the three-year average to $35.1 million, or 1.2x operating revenue and 0.9% of full value. Moody's ANPL reflects the use of a market-based discount rate to value pension liabilities rather than the assumed rate of investment return on plan assets.

Growth in the Moody's ANPL has been driven largely by falling market discount rates, however the plan's NPL has benefited from strong investment performance in recent years, with WRS reported a net pension asset as of fiscal 2017. (See Exhibit 2.)

Exhibit 2
Wisconsin Retirement System remains well-funded on a reported basis



Source: State of Wisconsin

The city's other post-employment benefits (OPEB) obligations do not pose a material credit risk. The OPEB liability reflects an implicit rate subsidy for retirees who pay to remain on the city's health plan. Franklin's net OPEB liability at the close of fiscal 2018 was $2.5 million. Moody's adjusted net OPEB liability, which is similar to our adjustments to pension liabilities, is $4.3 million, equivalent to a low 0.1% of full value and 0.1x operating revenue.

Management and governance: moderate institutional framework

City management is strong, employing reserve policies and long-term capital planning. Franklin's formal policy to maintain governmental fund balances between 20% and 30% and maintain at least 15% of the succeeding year's budgeted expenditures in working capital.

Wisconsin cities have an Institutional Framework score of A, which is moderate. The sector's major revenue source, property tax revenue, is subject to a cap that restricts cities from increasing their operating property tax levies except to capture amounts represented by net new construction growth. Revenues and expenditures tend to be predictable. Across the sector, fixed and mandated costs are generally high. Expenditures are somewhat flexible, as collective bargaining is allowed for public safety employees but is curbed for non-public safety employees.

Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 3

Franklin (City of) WI

Rating Factors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$4,360,269	Aa
Full Value Per Capita	$121,867	Aa
Median Family Income (% of US Median)	144.3%	Aa
Finances (30%)		
Fund Balance as a % of Revenues	26.5%	Aa
5-Year Dollar Change in Fund Balance as % of Revenues	17.8%	Aa
Cash Balance as a % of Revenues	73.6%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	47.3%	Aaa
Management (20%)		
Institutional Framework	A	A
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	0.9x	Ba
Notching Factors:[2]		
Other Analyst Adjustment to Management Factor (specify): overly punative operating history due to bond issuances		Up
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	1.5%	Aa
Net Direct Debt / Operating Revenues (x)	2.2x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	0.8%	Aaa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.1x	A
	Scorecard-Indicated Outcome	Aa2
	Assigned Rating	Aa2

[1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.
Sources: Moody's Investors Service, the city's audited financial statements, US Census Bureau

Endnotes

1 Employer contributions that tread water equal the sum of current year service cost and interest on reported net pension liabilities at the start of the year, using reported actuarial assumptions. If plan assumptions are met exactly, contributions equal to the tread water indicator will prevent the reported net pension liabilities from growing. Net liabilities may decrease or increase in a given year due to factors other than the contribution amount, such as investment performance that exceeds or falls short of a plan's assumed rate of return.

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