

CREDIT OPINION

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Madison (City of) WI

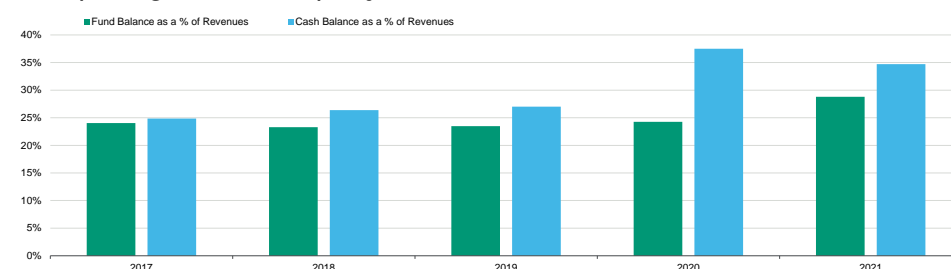
Update to credit analysis

Summary

[Madison](#) (Aaa stable) benefits from a sizeable tax base supported by a strong, diverse economy with significant institutional presence and above-average resident income. The financial position is solid, with a trend of fund balance growth (see Exhibit 1) due to strong budgetary management and financial planning practices. These positive attributes are balanced against limited revenue raising flexibility and elevated fixed costs.

Exhibit 1

Solid operating reserves and liquidity



Source: the city's audited financial statements

Credit strengths

- » Large tax base serves as the seat of government for the state, county and city, as well the state's flagship university
- » Solid socioeconomic and demographic profile
- » Stable financial position

Credit challenges

- » Elevated fixed costs
- » Limited revenue-raising flexibility because of state-imposed levy limits

Rating outlook

The stable outlook reflects the expectation that credit quality will remain sound, supported by continued economic growth and long-standing government and higher education presences within the city. It also reflects the expectation of financial stability due to conservative fiscal management.

Factors that could lead to an upgrade

- » Not applicable

Factors that could lead to a downgrade

- » Deterioration of the city's tax base and resident wealth and income
- » Material narrowing of operating reserves or liquidity
- » Increased leverage

Key indicators

Exhibit 2

Madison (City of) WI

	2017	2018	2019	2020	2021
Economy/Tax Base					
Total Full Value (\$000)	\$26,768,654	\$28,727,408	\$30,910,698	\$33,036,794	\$32,940,368
Population	248,856	252,086	254,977	258,366	258,366
Full Value Per Capita	\$107,567	\$113,959	\$121,229	\$127,868	\$127,495
Median Family Income (% of US Median)	120.0%	120.0%	120.9%	120.5%	120.5%
Finances					
Operating Revenue (\$000)	\$305,928	\$319,755	\$338,988	\$345,977	\$352,064
Fund Balance (\$000)	\$73,487	\$74,438	\$79,582	\$83,873	\$101,374
Cash Balance (\$000)	\$76,057	\$84,297	\$91,584	\$129,684	\$122,172
Fund Balance as a % of Revenues	24.0%	23.3%	23.5%	24.2%	28.8%
Cash Balance as a % of Revenues	24.9%	26.4%	27.0%	37.5%	34.7%
Debt/Pensions					
Net Direct Debt (\$000)	\$467,292	\$469,046	\$533,855	\$581,577	\$572,114
3-Year Average of Moody's ANPL (\$000)	\$529,245	\$544,818	\$538,752	\$575,066	\$684,357
Net Direct Debt / Full Value (%)	1.7%	1.6%	1.7%	1.8%	1.7%
Net Direct Debt / Operating Revenues (x)	1.5x	1.5x	1.6x	1.7x	1.6x
Moody's - ANPL (3-yr average) to Full Value (%)	2.0%	1.9%	1.7%	1.7%	2.1%
Moody's - ANPL (3-yr average) to Revenues (x)	1.7x	1.7x	1.6x	1.7x	1.9x

The 2020 cash balance includes \$29.4 million in restricted cash recorded in the debt service fund which is held in an escrow account for a crossover refunding. Net of restricted cash, the cash balance is 29% of revenues.

Sources: US Census Bureau, Madison (City of) WI's financial statements and Moody's Investors Service

Profile

Madison is the state capital of [Wisconsin](#) (Aa1 stable) and is home to the flagship campus of the University of Wisconsin. It is the state's second largest city with an estimated population of just under 260,000.

Detailed credit considerations

Economy and tax base: strong regional economy supported by institutional presence

Madison's tax base continues to expand, with strong economic growth supported by its status as the state capital, a regional economic center and the institutional presence of the University of Wisconsin's flagship campus. The \$39 billion tax base averaged annual growth of 7% over the past five years driven by both appreciation of existing property and new construction. Residential development is strong, with 289 single-family and 3,331 multi-family units completed in 2021, which is up 66% from the previous year.

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Madison's Metro Transit is undergoing a redesign of its transit network to provide improved, equitable service to all areas of the city. Amongst its many goals, the redesign supports the city's goal of using 100% renewable energy sources and becoming carbon neutral by the year 2030. The expansion of the transit system is also expected to facilitate development along transit lines and increase access to areas of the city with available housing.

The city's diverse economy will remain a credit strength, with large governmental, health care, technology and insurance employers that city management notes have remained largely stable. As the state capital, Madison remains a major employment center, with the state employing over 44,000 employees, and the University of Wisconsin and its affiliated hospital and clinics (Aa3 stable) accounting for a combined employment of roughly 39,500. The Madison campus is the University of Wisconsin's largest campus, with roughly 47,936 students enrolled as of fall 2021. The university also provides a large, well-educated employment pool to support local businesses.

Financial operations and reserves: solid financial position

Continued development within the city has resulted in steadily growing property tax revenue, which will continue to support solid operating reserves. The fiscal 2022 executive operating budget is balanced and avoids use of fund balance by using \$13.1 million in federal funds from the state and local allocation of ARPA funds to support city services. The budget also includes almost \$3.1 million in expense reductions through cost saving reductions in personnel and other miscellaneous departments expenses. The fiscal 2022 budget also assumes balanced operations in the city's general fund, but year-to-date, management reports revenues are \$3 million above projections and expenditures are \$10 million under expectations, largely due to growing building permit revenue and staffing cost savings. The city also reports increases in the city's parking and room tax revenues; under Wisconsin law, 70% of room tax revenue must be utilized for tourism and tangible municipal development. The city has historically transferred the remaining 30% to the general fund and is budgeting for a \$4.2 million transfer in fiscal 2022.

Madison received \$47.2 million in American Rescue Plan Act (ARPA) funding, of which, roughly half has been spent. The city used the first half to address violence prevention and youth engagement, homelessness support, affordable housing, emerging and basic needs, and economic development. The remaining ARPA funds will be used for revenue replacement to continue core government operations and services.

Madison closed fiscal 2021 with an available operating fund (general, library, and debt service funds) balance of \$101.4 million, or 29% of operating revenue. The city's largest source of revenue is property taxes, which comprised almost 73% of fiscal 2021 operating revenue, followed by state aid at 12%. For the fiscal 2023 budget, which is currently in development, all agencies have been asked to cut their budgets and the city is expecting two tax incremental districts (TIDs) to close, which will add to the tax rolls and support further growth in property taxes and help alleviate any budgetary gaps.

Liquidity

The city closed fiscal 2021 with an unrestricted operating cash position of \$114.6 million, or a solid 33% of revenue. Madison also has \$7.6 million in restricted cash recorded in its debt service fund which is held in an escrow account for a crossover refunding.

Debt, pension and OPEB: elevated fixed costs

The city's fixed costs will remain above average due to regular borrowing for capital projects and rapid principal amortization. Madison is in the process of issuing \$103 million of general obligation unlimited tax (GOULT) bonds and notes for capital projects, community development and affordable housing projects, and metro transit facilities projects. Following the sale, the city's debt burden will be 1.7% of full value and 1.6x operating revenue. The city has plans to issue approximately \$15 million of Sewer Revenue Bonds this year. Fixed costs, inclusive of debt service and pension contributions, were 34% of operating revenue in fiscal 2020 (see Exhibit 3).

Exhibit 3

Fixed costs consist largely of debt service payments

2021	\$\$\$ (000)	% of Operating Revenues	Discount Rate
Operating Revenue	352,064	n/a	n/a
Reported Unfunded Pension Liability	(92,528)	-26%	7.00%
Moody's Adjusted Net Pension Liability	876,616	249%	2.52%
Reported Net OPEB Liability	85,257	24%	2.25%
Moody's Adjusted Net OPEB Liability	81,263	23%	2.83%
Net Direct Debt	572,114	163%	n/a
Debt & unfunded retirement benefits (Moody's adjusted)	1,529,993	434.58%	
Pension Contribution	17,481	4.97%	n/a
OPEB Contribution	3,265	0.93%	n/a
Debt Service	98,991	28.12%	n/a
Total Fixed Costs	119,737	34.01%	n/a
Tread Water Gap	n/a	n/a	n/a
Moody's Adjusted Fixed Costs	n/a	n/a	n/a

Source: the city's audited financial statements and Moody's Investors Service

Legal security

The city's outstanding GOULT debt is backed by the city's full faith and credit pledge. Debt service is payable from a designated property tax levy that is unlimited as to rate or amount.

The city also has approximately \$820,000 in lease revenue bonds outstanding issued through its Community Development Authority (CDA), which is rated Aa2. Debt service is payable from rental payments by the city to the CDA. Per the lease agreement, the city is required to make semiannual rental payments sufficient to pay debt service on the outstanding lease revenue bonds, subject to annual appropriation.

Debt structure

All of the city's debt is fixed rate. Principal amortization is rapid with 92% of debt retired within 10 years.

Debt-related derivatives

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

Pensions and OPEB

Madison participates in the Wisconsin Retirement System (WRS), a statewide cost-sharing plan. 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.

The city's three-year adjusted net pension liability (ANPL) is \$684 million, equivalent to 1.9x operating revenue and 1.8% 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. In comparison, the reported net pension liability (NPL), based on the plan's reported 7% discount rate, was negative \$92.5 million in fiscal 2021, reflecting a net pension asset. The city's ANPL is much higher than reported pension liabilities because the market interest rates that we use to value pension liabilities are far lower than reported discount rates (see Exhibit 4).

Exhibit 4

Adjusted pension liabilities notably higher than reported pension liabilities because of Moody's adjustments

\$ thousands	2019	2020	2021
Net direct debt	\$533,855	\$581,577	\$572,114
Net pension liability, reported basis	\$49,669	(\$46,356)	(\$92,528)
Discount rate	7.00%	7.00%	7.00%
Net OPEB liability, reported basis	\$71,257	\$82,996	\$85,257
Adj. net pension liability	\$498,586	\$677,870	\$876,616
Discount rate	4.22%	3.22%	2.52%
Adj. net OPEB liability	\$71,453	\$80,211	\$81,263
Pension asset shock indicator	14%	15%	19%
Pension assets, % of revenue	398%	466%	526%
Shock return level	-6%	-5%	-5%
Expected investment return volatility	12%	12%	13%

Sources: the city's audited financial statements and Moody's Investors Service

Madison's other post-employment benefits (OPEB) obligations do not pose a material cost. The OPEB liability reflects an implicit rate subsidy for retirees who pay to remain on the city's health care plan. These liabilities are funded on a pay-as-you-go basis, with contributions of \$3.3 million in fiscal 2021. The city's reported net OPEB liability at the close of fiscal 2021 was \$85 million. Moody's adjusted net OPEB liability, which is adjusted similarly to our adjustments to pension liabilities, is slightly lower at \$81 million, equivalent to 0.2% of full value and 0.2x operating revenue.

ESG considerations**Madison (City of) WI's ESG Credit Impact Score is Neutral-to-Low CIS-2**

Exhibit 5

ESG Credit Impact Score**CIS-2****Neutral-to-Low**

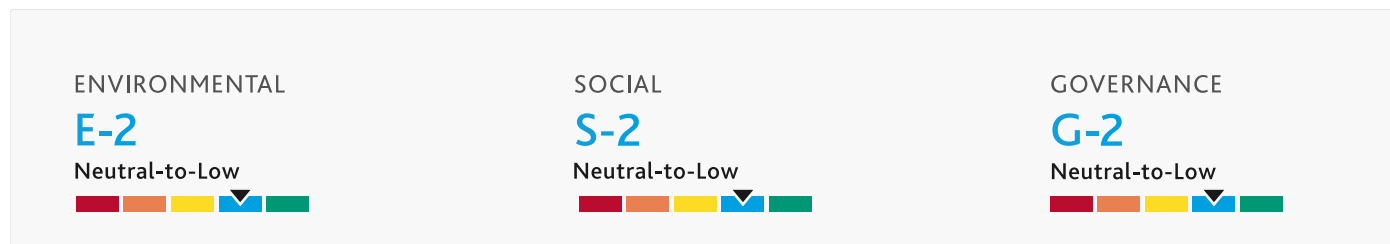
For an issuer scored CIS-2 (Neutral-to-Low), its ESG attributes are overall considered as having a neutral-to-low impact on the current rating; i.e., the overall influence of these attributes on the rating is non-material.

Source: Moody's Investors Service

Madison's ESG Credit Impact Score is neutral-to-low (**CIS-2**), reflecting neutral to low exposure to environmental, social, and governance risks.

Exhibit 6

ESG Issuer Profile Scores



Source: Moody's Investors Service

Environmental

The city's E issuer profile score is neutral-to-low (**E-2**), reflecting low exposure to environmental risks, including heat stress, water stress, and extreme rainfall. Madison maintains a comprehensive sustainability plan to adapt to changing environmental, social and economic conditions over time. Initiatives include improving water quality, reducing waste, and increasing the use renewable energy.

Social

The S issuer profile score is neutral-to-low (**S-2**), reflecting population growth, a diverse labor market, and strong educational attainment. Health metrics are also favorable: nearly 96% of the city's population has health insurance compared to the national rate of 91%. Overall demographics and educational attainment are strengths. Residents have easy access to basic services and the county scores favorably in health and safety.

Governance

Madison's G issuer profile score is neutral-to-low (**G-2**). The city is limited in its ability to raise revenue, however management utilizes a conservative budgetary approach and multi-year capital planning to maintain operating reserves in compliance with its formal fund balance policy.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

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 7

Madison (City of) WI

Rating Factors	Measure	Score
Economy/Tax Base (30%)[1]		
Tax Base Size: Full Value (in 000s)	\$38,606,699	Aaa
Full Value Per Capita	\$149,426	Aa
Median Family Income (% of US Median)	120.5%	Aa
Notching Factors:[2]		
Institutional Presence		Up
Regional Economic Center		Up
Finances (30%)		
Fund Balance as a % of Revenues	28.8%	Aa
5-Year Dollar Change in Fund Balance as % of Revenues	9.0%	A
Cash Balance as a % of Revenues	34.7%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	12.9%	Aa
Management (20%)		
Institutional Framework	A	A
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	1.0x	Baa
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	1.5%	Aa
Net Direct Debt / Operating Revenues (x)	1.6x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	1.8%	A
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.9x	A
	Scorecard-Indicated	
	Outcome	Aaa
	Assigned Rating	Aaa

[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: US Census Bureau, Madison's financial statements and Moody's Investors Service

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