S&P Global Ratings

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Summary:

Barnstable, Massachusetts; General Obligation

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Credit Profile		
US$12.13 mil GO muni purpose bnds ser 2020 due 02/15/2040		
Long Term Rating	AAA/Stable	New
Barnstable GO		
Long Term Rating	AAA/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' rating and stable outlook to Barnstable, Mass.' series 2020 general obligation (GO) municipal-purpose loan bonds and affirmed its 'AAA' rating, with a stable outlook, on the town's existing GO debt.

We understand the town is also concurrently issuing $2 million of bond anticipation notes we will not rate.

Under our criteria, titled "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions," published Nov. 19, 2013, on RatingsDirect, we rate Barnstable higher than the nation because we think the town can maintain better credit characteristics than the nation in a stress scenario based on its predominantly locally derived revenue base and our view that pledged revenue supporting bond debt service is at limited risk of negative sovereign intervention. In 2019, local property taxes generated 69% of revenue, which demonstrated a lack of dependence on central government revenue.

Security and the use of proceeds

We understand officials intend to use series 2020 bond proceeds to fund various capital improvement projects.

The town's full-faith-and-credit pledge, subject to Proposition 2 1/2 limitations, secures the bonds. We rate the limited-tax GO debt on par with our view of Barnstable's general creditworthiness because the ad valorem tax is not derived from a measurably narrower property tax base and there are no resource-fungibility limitations, supporting our view of its overall ability and willingness to pay debt service.

Credit summary

The rating reflects our opinion of Barnstable's very strong economy, supported by a wealthy tax base and high income. In addition, we think the town's continued maintenance of very strong budgetary flexibility, with available reserves averaging about 24% of expenditures during the past three fiscal years, due to positive financial performance and very strong management further support our view of the rating. Although we think long-term retirement liabilities and costs and potential additional debt could pressure the budget, we posit that the town will likely manage these costs appropriately and that additional debt will likely remain relatively affordable due to its size and wealthy tax base. Furthermore, due to its location, the town has also undertaken various coastal-resiliency initiatives; it is currently planning for additional rising-sea-level-mitigation projects.

The town's general creditworthiness reflects our opinion of its:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong financial management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with a slight operating surplus in the general fund and an operating surplus at the total governmental-fund level in fiscal 2019;
- Very strong budgetary flexibility, with available fund balance in fiscal 2019 at 24% of operating expenditures;
- Very strong liquidity, with total government available cash at 19.7% of total governmental-fund expenditures and 3.2x governmental debt service, and access to external liquidity we consider strong;
- Strong debt-and-contingent-liability position, with debt service carrying charges at 6.2% of expenditures and net direct debt that is 48.3% of total governmental-fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 75% of debt scheduled to be retired within 10 years, but a large pension and other-postemployment-benefit (OPEB) obligation and the lack of a plan to sufficiently address the obligation; and
- Strong institutional framework score.

Very strong economy

We consider Barnstable's economy very strong. The town, with a population estimate of 44,331, is in Barnstable County in the Barnstable Town MSA, which we consider broad and diverse. The town has a projected per capita effective buying income at 117% of the national level and per capita market value of $340,294. Overall, market value has grown by 5.8% during the past year to $15.1 billion in fiscal 2020. County unemployment was 4.3% in 2017.

At the center of Cape Cod, with 100 miles of shoreline, Barnstable's population grows to more than 120,000 during the summer. About 89% of the tax base is residential, followed by commercial properties at 10%. Barnstable serves as a retail, transportation, and services hub for the entire Cape and islands. Leading employers include Cape Cod Health Care, Barnstable, and Cape Cod Community College.

Various developments will continue to expand the economy, including a new $45 million corporate headquarters for Cape Cod Five Cent Savings Bank that is nearly complete; town officials expect this project to relocate about 150 employees and add 60-90 new jobs. Cape Town Plaza is also expanding; the developer is assembling tenants. The developer has begun making ground-lease payments to the town, totaling about $1 million annually. Other developments underway include:

- The expansion of Cape Cod Potato Chips' current facilities;
- The construction of an underground conduit-and-transmission station by Vineyard Wind, which the town has entered into a host agreement for with the company;
- The Cape Cod Mall's renovations with new entertainment options being built and several new retails shops opening; and
- A $120-million expansion to Cape Cod Hospital, which should create additional employment opportunities.

In addition, Barnstable expects to generate about $2 million in new revenue annually from short-term room taxes enacted by the Massachusetts Legislature in late 2018, including an additional tax on services for water protection and management exclusive for Cape Cod communities. Due to these and other developments and increasing building-permit activity, officials expect the economy to continue to grow. Therefore, we expect Barnstable's economy will likely remain very strong.

Very strong management

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

Barnstable prepares its budgets based on 10 years of historical information and an evaluation of economic indicators. In our opinion, budgetary assumptions have been conservative. The town also has an open-budget website that provides real-time budget-to-actual information, and it shares quarterly investment reports with the finance director. Barnstable has written comprehensive debt, investment, and 4%-unassigned-reserve policies. Finally, the town annually prepares and updates a robust five-year financial forecast and five-year capital improvement plan.

The town has cybersecurity protections. The town maintains various network and system backups and cybersecurity insurance.

Barnstable has also undertaken several initiatives to help mitigate rising sea levels, including placing sand barriers along its Sandy Neck area and moving some infrastructure, such as accessibility roads, away from impact areas. The town is also performing additional planning and expanding its coastal-resiliency efforts.

Strong budgetary performance

Barnstable's budgetary performance is strong, in our opinion. The town had slight surplus operating results in the general fund at 1.4% of expenditures and surplus results across all governmental funds at 5.6% of expenditures in fiscal 2019. General fund operating results have been stable during the past three fiscal years at 0.2% of expenditures in fiscal 2018 and 2.2% in fiscal 2017.

Fiscal 2019 results include adjustments for recurring transfers and one-time capital expenditures paid for with bond proceeds. Officials attribute the fiscal 2019 general fund surplus primarily to higher-than-expected revenue, including motor-vehicle excise taxes, licenses and permits, and investment income. In addition, the town experienced significant savings in health-insurance costs as more employees moved to high-deductible plans. The town also had other budget savings, including public safety and administrative services.

The fiscal 2020 budget totals $168.2 million, a 3% increase over fiscal 2019. The fiscal 2020 budget also includes a $2.4 million fund-balance appropriation the town historically performs through conservative budgeting. Officials report fiscal 2020 budget-to-actual results are tracking favorably, and they currently expect to end fiscal 2020 with another general fund surplus. Property taxes generate 69% of general fund revenue, followed by intergovernmental aid at 18%; collections have averaged 99% during the past three fiscal years. In addition, the town expects to generate about $2 million in new revenue from short-term room taxes, which we expect will likely support consistently positive financial operations.

Although we expect budgetary performance will likely remain strong, we posit future pension and OPEB costs could become a budgetary pressure due to below-average funding. We also think adjustments to more-conservative assumptions could materially affect annual contributions, pressuring the bottom line, particularly if economic or business conditions worsen.

Very strong budgetary flexibility

Barnstable's budgetary flexibility is very strong, in our view, with available fund balance in fiscal 2019 at 24% of operating expenditures, or $41.8 million. During the past three fiscal years, total available fund balance remained consistent overall, which totaled 23% of expenditures in fiscal 2018 and 24% in fiscal 2017.

The town has consistently maintained available reserves above 20% of expenditures during the past three fiscal years. The fiscal 2020 budget includes a fund-balance appropriation of $2.4 million. Management, however, does not currently expect to realize any actual reserve drawdowns by fiscal year-end 2020.

Due to the fiscal 2020 budget's current performance, management expects to end fiscal 2020 with another reserve increase. Barnstable's formal reserve policy calls for maintaining unassigned fund balance at a minimum 4% of expenditures, which it has adhered to historically. Unassigned fund balance totaled $36 million, or 21% of expenditures, in fiscal 2019.

Very strong liquidity

In our opinion, Barnstable's liquidity is very strong, with total government available cash at 19.7% of total governmental-fund expenditures and 3.2x governmental debt service in fiscal 2019. In our view, the town has strong access to external liquidity if necessary.

Barnstable is a regular market participant that has issued GO bonds frequently during the past several years. We understand it has not entered into any bank loans, direct-purchase debt, or contingent-liquidity risks from financial instruments with payment provisions that change upon the occurrence of certain events. The town has consistently had, what we consider, very strong liquidity; we do not expect these ratios to change, which is consistent with our view of its strong budgetary performance.

Strong debt-and-contingent-liability profile

In our view, Barnstable's debt-and-contingent-liability profile is strong. Total governmental-fund debt service is 6.2% of total governmental-fund expenditures, and net direct debt is 48.3% of total governmental-fund revenue. Overall net debt is low at 1.1% of market value and about 75% of direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

With this issuance, the town will have about $113 million of total direct debt outstanding. Officials currently expect to issue an additional $10 million-$20 million annually during the next three years for various capital improvements, including a sewer-related project and the construction of a school field.

We understand Barnstable, like other Cape communities, is under pressure to comply with federal regulation to reduce nitrogen levels in area waterways. Mitigation strategies include sewer expansion, effluent mitigation, dredging, abandoned cranberry bog conversion, aquaculture, alternative-septic systems, permeable reactive barriers, and stormwater treatment.

While we expect the town's debt profile will likely remain, at least, adequate, we imagine debt metrics could potentially weaken, depending on its final-financing strategy and amounts for future sewer-related debt. Management intends to finance these strategies through betterments, sewer-and-tax rates, and commonwealth or federal funding

In our opinion, Barnstable's large pension and OPEB obligation, without a plan in place we think will sufficiently address the obligation, is a credit weakness.

Pension and OPEB highlights include:

- While the town is managing these costs, we think pension and OPEB liabilities will likely remain a long-term credit concern due to lower funding and our expectation costs will likely increase.
- The plan's actuarially determined pension contribution reflects, what we view as, somewhat weak assumptions and methodologies; we imagine unexpected-contribution-escalation risk will likely increase and potentially pressure the budget. We, however, expect the town will likely continue to manage these costs and maintain stable finances due to conservative budgeting and financial planning that has led to consecutive positive financial operations during the past few fiscal years.
- Barnstable funds OPEB on a pay-as-you-go basis, which, due to claims volatility and medical-cost and demographic trends, is likely to lead to escalating costs. Management, however, also maintains an irrevocable OPEB trust fund, which has a current balance of about $5.6 million as of fiscal 2020, according to the town, or 3.3% funding.

At June 30, 2019, Barnstable participates in:

- Barnstable County Retirement Assn., which is 57.6% funded, with a proportionate share of the town's net pension liability at $117 million, assuming a 7.375% discount rate as of fiscal 2019; and
- Barnstable's defined-benefit, postretirement, health-care plan, which is 3.3% funded as of fiscal 2020, with an OPEB liability of about $167.9 million.

Barnstable's combined required pension and actual OPEB contribution totaled 8.2% of total governmental-fund expenditures in fiscal 2019: 4.8% represented required contributions to pension obligations and 3.4% represented OPEB payments. The town made its full annual required pension contribution in fiscal 2019.

Barnstable did not make funding progress in fiscal 2020, as contributions fell short of static funding. There is an actuarial plan to reach full funding, and contributions should increase by roughly 5.28% due to the appropriation schedule. The plan's schedule calls for full funding within a closed 17 years. With a 7.375% discount rate, we see some market-volatility risk. Management primarily attributes cost-escalation risk due to an increasing faster-than-payroll contribution schedule that aggressively defers contributions.

Barnstable created an OPEB trust fund in 2011 that had a roughly $4.9 million balance at June 30, 2019. Management contributed $660,000 to this OPEB fund in fiscal 2020; management plans to increase the base contribution by $50,000 annually, which it incorporated into long-term financial planning. While we view prefunding OPEB liabilities positively, and we expect retirement costs will likely remain manageable during the next few fiscal years, we think Barnstable's large and growing pension and OPEB liabilities could pressure the long-term budget.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion of the town's very strong economy and budgetary flexibility, supported by strong budgetary performance. In our opinion, very strong management and liquidity further support the rating. Although Barnstable has large long-term liabilities and increasing retirement costs, we think management will likely make the necessary budgetary adjustments to maintain balanced financial operations. Therefore, we do not expect to change the rating within the two-year outlook.

However, while unlikely, we could lower the rating if a prolonged structural imbalance were to result in significantly deteriorated available reserves.

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
- 2019 Update Of Institutional Framework For U.S. Local Governments