

RatingsDirect®

Summary:

Barnstable, Massachusetts; General Obligation

Primary Credit Analyst:

Christina Marin, Boston 617-530-8312; christina.marin@spglobal.com

Secondary Contact:

Anthony Polanco, Boston 617-530-8234; anthony.polanco@spglobal.com

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Credit Profile

US\$11.259 mil GO mun purp loan bnds ser 2017 due 02/15/2037

Long Term Rating AAA/Stable New

Barnstable GO

Long Term Rating AAA/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' long-term rating to Barnstable, Mass.' series 2017 general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AAA' long-term rating on Barnstable's previously issued GO debt. The outlook is stable.

We understand the town is concurrently issuing bond anticipation notes, which we do not rate.

We rate Barnstable higher than the sovereign because we believe the town can maintain better credit characteristics than the U.S. in a stress scenario, based on its predominantly locally derived revenue base and our view that pledged revenue supporting debt service on the bonds is at limited risk of negative sovereign intervention. In 2016, local property taxes generated 71% of revenue, demonstrating a lack of dependence on central government revenue.

The town's full-faith-and-credit pledge, subject to the limits of Proposition 2 1/2, secures the bonds. Despite the limitations imposed by the state levy limit law, we did not make a rating distinction for the limited-tax GO pledge given the town's flexibility under the levy limit. We understand bond proceeds will pay for capital improvements to the town's schools, wastewater system, and sidewalks, among other capital projects.

The 'AAA' long-term rating reflects our assessment of the following factors for the town:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with "strong" financial policies and practices under our Financial Management Assessment 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 2016;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2016 of 23% of operating expenditures;
- Very strong liquidity, with total government available cash at 24.0% of total governmental fund expenditures and 3.7x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability profile, with debt service carrying charges at 6.4% of expenditures and net direct debt that is 48.9% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 78.1% of debt scheduled to be retired in 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

Since our last review, our assessment of Barnstable's economy improved to very strong from strong, due to the strengthening of the Barnstable metropolitan statistical area. The town, with an estimated population of 44,629, has a projected per capita effective buying income of 120% of the national level and per capita market value of \$296,453. Overall, the town's market value grew by 0.7% over the past year to \$13.2 billion in 2017. The county unemployment rate was 6.3% in 2015.

Located in the center of Cape Cod, and with 100 miles of shoreline, Barnstable's population grows to over 120,000 during the summer months. The town's assessed value (AV) was revalued in fiscal 2016, resulting in a 3.5% increase. We understand the revaluation prompted no major taxpayer appeals. The property tax base is primarily residential, with 88% of AV classified as such. Building permits in calendar year 2016 were at a five-year high with an estimated value of \$213.7 million. Barnstable serves as a retail, transportation, and services hub for the entire Cape and the islands. Its largest employers include Cape Cod Health Care (2,548), the town itself (1,331), and Cape Cod Community College (514). We expect our evaluation of Barnstable's economy to remain at least strong due to the town's property wealth and above-average per capita incomes.

Very strong management

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

Barnstable's budgets are prepared based on 10 years of historical information as well as an evaluation of economic indicators. We believe that budgetary assumptions have been conservative. The town recently launched an open budget website that provides real-time budget-to-actual information, and quarterly investment reports are shared with the finance director. Written policies include a comprehensive debt policy, investment policy, and a 4% reserve policy. Finally, the town annually prepares and updates a robust 10-year financial forecast and five-year capital improvement plan.

Strong budgetary performance

Barnstable's budgetary performance is strong in our opinion. The town had slight surplus operating results in the general fund of 0.9% of expenditures, and surplus results across all governmental funds of 4.6% in fiscal 2016.

In our analysis of budgetary performance, we adjusted expenditures for recurring transfers and one-time capital projects. The principal sources of general fund revenue in fiscal 2016 were real estate and personal property taxes (71% of the total) and intergovernmental (17%). Current-year property tax collection rates are healthy, averaging 97.7% over the past three fiscal years.

The positive operating result in 2016 is a result of better-than-budgeted revenues from motor vehicle excise taxes and beach fees. Also, town officials report that expenditures came in nearly \$1 million lower than budget due to turnbacks across departments.

The fiscal 2017 general fund budget increased 3.5% from 2016 to \$152 million. Operating results are currently trending on target. Officials expect the water enterprise account to show negative variances at fiscal year-end due to several

unexpected capital expenditures relating to contamination of one of the town's wells. However, they indicated the account is likely to return to balanced operations through a 9% rate increase in fiscal 2018.

Management expects rising benefit expenses to pressure the budget in future years. Also, there may be changes associated with contract settlements as negotiations are currently being conducted in 2017 for the 2018 fiscal year. Despite future budgetary challenges, we expect operating performance to remain at least adequate given Barnstable's history of stable operating performance.

Very strong budgetary flexibility

Barnstable's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 23% of operating expenditures, or \$35.0 million.

The town's reserves declined in 2016 due to a reclassification of sewer construction funds to "restricted" from "available". However, based on careful planning and conservative budgeting, Barnstable has maintained reserve levels in excess of 20% for the last three years. We do not expect our assessment of budgetary flexibility to weaken during our outlook period, as town officials have not indicated plans to draw on reserves.

Very strong liquidity

In our opinion, Barnstable's liquidity is very strong, with total government available cash at 24.0% of total governmental fund expenditures and 3.7x governmental debt service in 2016. In our view, the town has strong access to external liquidity if necessary.

Barnstable is a regular market participant, having issued GO bonds frequently over 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. It has consistently had very strong liquidity and we do not anticipate a change to these ratios, consistent with our view of the town's strong 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 6.4% of total governmental fund expenditures, and net direct debt is 48.9% of total governmental fund revenue. Overall net debt is low at 0.7% of market value, and approximately 78.1% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

Barnstable has \$124 million in direct debt outstanding as well as \$1.3 million in short-term bond anticipation notes. For our calculation of debt scores, we remove self-supporting debt from the town's various enterprise accounts as well as state aid reimbursement. Barnstable expects to issue an additional \$20 million over the next two years for various capital projects.

Although this requirement is outside of our outlook horizon, we understand that Barnstable, like other Cape communities, is under pressure to comply with federal regulation to reduce nitrogen levels in area waterways. The town has just begun mitigation planning, and expects to release a report this summer. However, given other Cape municipalities' experiences, we expect costs associated with compliance to materially affect Barnstable's debt profile. Mitigation strategies include sewer expansion, effluent mitigation, and nitrogen management, and will likely be paid for

through betterments, sewer rates, tax rates, and state or federal funding.

In our opinion, a credit weakness is Barnstable's large pension and OPEB obligation, without a plan in place that we think will sufficiently address the obligation. Barnstable's combined required pension and actual OPEB contributions totaled 8.0% of total governmental fund expenditures in 2017. Of that amount, 4.9% represented required contributions to pension obligations, and 3.0% represented OPEB payments. The town made 100% of its actuarial determined pension contribution in 2016. The funded ratio of the largest pension plan is 58.1%.

The town is a member of the Barnstable County Retirement Association pension plan, which was approximately 57% funded as of Jan. 1, 2014. Barnstable's proportionate share of the net pension liability is about 15%, or \$94 million.

The town provides eligible retirees with lifetime health care insurance. The actuarial accrued liability was \$130 million as of June 30, 2014. Barnstable created a trust fund in 2011 to begin accumulating assets to fund its OPEB liability and had a balance of approximately \$2.7 million as of June 30, 2016. It made a contribution to this fund of \$478,000 in 2017 and a plan to increase the base contribution by \$50,000 per year has been incorporated into the town's long-term financial planning.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Outlook

The stable outlook reflects our view of the town's very strong budgetary flexibility and liquidity, further supported by a very strong economy. As such, we do not expect to change the rating in the next two years. Although Barnstable maintains a strong debt and liability profile, and despite pension and OPEB costs that are expected to continue rising through the medium term, we do not anticipate weakened performance or liquidity measures, due to the town's very strong management practices. Steady economic development in recent years should aid tax base stability and provide additional tax revenue.

Downside scenario

While unlikely, a prolonged period of structural imbalance resulting in significant deterioration of available reserves could result in a lower rating.

Related Research

2016 Update Of Institutional Framework For U.S. Local Governments

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