

RatingsDirect®

Summary:

Barnstable, Massachusetts; General Obligation

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Credit Profile

US\$10.601 mil GO mun purp loan ser 2018 due 02/15/2038

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 2018 general obligation (GO) bonds and affirmed its 'AAA' rating, with a stable outlook, on Barnstable's existing GO debt.

We understand the town is concurrently issuing \$2.6 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 sovereign because we believe 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 debt service on the bonds is at limited risk of negative sovereign intervention. In 2017, local property taxes generated 70% of revenue, which demonstrated a lack of dependence on central government revenue.

The town's full-faith-and-credit pledge, subject to Proposition 2 1/2 limits, secures the bonds. Despite limitations imposed by the commonwealth-levy-limit law, we did not make a rating distinction for the limited-tax-GO pledge due to the town's flexibility under the levy limit.

We understand officials intend to use series 2018 bond proceeds to fund various capital improvement projects.

The rating reflects our opinion of Barnstable's:

- 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 (FMA) methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total-governmental-fund level in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 24% of operating expenditures;
- Very strong liquidity, with total government available cash at 23.3% of total-governmental-fund expenditures and 3.5x governmental debt service, and access to external liquidity we consider strong;
- Strong debt-and-contingent-liability position, with debt service carrying charges at 6.6% of expenditures and net direct debt that is 48.7% of total-governmental-fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 77.9% 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 an estimated population of 44,487, 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 of 120% of the national level and per capita market value of \$305,984. Overall, market value has grown by 2.9% over the past year to \$13.6 billion in fiscal 2018. The county unemployment rate was 4.7% in 2016.

Located at the center of Cape Cod, and with 100 miles of shoreline, Barnstable's population grows to more than 120,000 during the summer. About 88% of the town's property tax base is residential, followed by commercial properties at 10%. Barnstable serves as a retail, transportation, and services hub for the entire Cape and the islands. Leading employers include Cape Cod Health Care, Barnstable, and Cape Cod Community College.

There are also various developments taking place in the town that will continue to expand the economy, including building a new \$45-million corporate headquarters for Cape Cod Five Cent Savings Bank that will relocate about 170 employees and add 60-90 new jobs. In addition, Total Athletic is constructing a \$12-million athletic-training-and-recreational-sports complex. Other developments underway include renovations and expansions of current facilities owned by Cape Cod Potato Chips; the construction of an assisted-living residential complex, a new Courtyard-Marriott hotel, and new multifamily condominium units; and the proposed \$120-million expansion to Cape Cod Hospital, which should create additional employment opportunities. Due to these and other developments and increasing building-permit activity, officials expect the town's economy to continue to grow. Therefore, we believe Barnstable's economy will likely remain very strong.

Very strong management

We view the town's 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. We believe budgetary assumptions have been conservative. The town recently launched 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 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 operating surpluses of 2.2% of expenditures in the general fund and 5.9% of expenditures across all governmental funds in fiscal 2017. General fund operating results have been stable over the past three fiscal years, with a result of 0.9% of expenditures in fiscal 2016 and 0.5% in fiscal 2015.

Fiscal 2017 results include adjustments for recurring transfers and one-time capital expenditures paid for with bond proceeds. Officials attribute the fiscal 2017 positive performance primarily to a conservative approach to budgeting that led to revenue exceeding the budget and lower-than-expected expenditures. Specifically, major revenue factors

came in better than budgeted, including building permit fees, motor vehicle taxes, property taxes, and intergovernmental revenue. The town also saw cost savings due to departmental turnbacks in appropriations and lower-than-budgeted expenditures for employee benefits.

The fiscal 2018 budget totals \$160.2 million, a 4.3% increase over fiscal 2017. The fiscal 2018 budget also includes a \$2.9 million fund balance appropriation that the town historically does through conservative budgeting. Officials report budget-to-actual results are tracking the budget favorably with revenue--including building-permit fees and motor-vehicle excise taxes--currently exceeding projections and expenditures remaining on target. Therefore, the town currently expects to end fiscal 2018 with balanced operations. Property taxes account for 70% of general fund revenue followed by intergovernmental aid at 19%. Collections have averaged 99% over the past three fiscal years.

Although we expect budgetary performance to remain strong, we believe future pension and OPEB costs could become a budgetary pressure due to below-average funding ratios. 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 an available fund balance in fiscal 2017 of 24% of operating expenditures, or \$38.8 million.

The town has consistently maintained available reserves above 20% of expenditures over the past three fiscal years. Although the fiscal 2018 budget includes a fund balance appropriation of \$2.9 million, officials do not expect to realize drawdowns in reserves by fiscal year-end. Due to the fiscal 2018 budget's current performance, management expects to end fiscal 2018 with another reserve increase. Barnstable also has a formal reserve policy of maintaining unassigned fund balance at a minimum of 4% of expenditures, which it has adhered to historically.

Very strong liquidity

In our opinion, Barnstable's liquidity is very strong, with total government available cash at 23.3% of total-governmental-fund expenditures and 3.5x governmental debt service in fiscal 2017. 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 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; we do not expect these ratios to change, which is consistent with our view of the town's 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 6.6% of total-governmental-fund expenditures, and net direct debt is 48.7% of total-governmental-fund revenue. Overall net debt is low at 0.7% of market value and approximately 77.9% 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 \$119 million in total direct debt outstanding. Officials expect to issue \$10

million-\$20 million annually over the next three years for various capital improvement projects, including a sewer-related project.

We understand 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. However, due to other Cape municipalities' experiences, we believe costs associated with compliance could materially affect Barnstable's debt profile. Mitigation strategies include sewer expansion, effluent mitigation, and nitrogen management; 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. Barnstable's combined required pension and actual OPEB contribution totaled 11.2% of total-governmental-fund expenditures in fiscal 2017. Of that amount, 4.8% represented required contributions to pension obligations and 6.4% represented OPEB payments. The town made its full annual required pension contribution in fiscal 2017. The funded ratio of the largest pension plan is 57.3%.

Barnstable contributes to the Barnstable County Retirement Assn. pension plan, a cost-sharing, multiemployer, defined-benefit plan. Using updated reporting standards in accordance with Governmental Accounting Standards Board Statement Nos. 67 and 68, the town's proportionate share of the net pension liability was about \$103.9 million with a 57% funded ratio at Dec. 31, 2016, based on an assumed rate of return of 7.6%. We believe this weak funding ratio is due to numerous years of underfunding, aggressive assumptions, and weak market performance. Due to the funded ratio, we believe contributions will likely continue to rise over the next few fiscal years. While the town is currently managing these costs, we believe it has a limited ability to control future pension-liability growth.

Barnstable provides eligible retirees with lifetime health-care insurance. The actuarial accrued liability was \$184 million at June 30, 2016. Barnstable created an OPEB trust fund in 2011 that had a balance of approximately \$3.3 million as of June 30, 2017. Management contributed \$478,000 to this OPEB fund in 2017; management plans to increase the base contribution by \$50,000 per year, which it has incorporated into the town's long-term financial planning. While we view the practice of prefunding the OPEB liability positively, we believe Barnstable's large and growing pension and OPEB liabilities could pressure the budget over the long term.

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. We believe the town's very strong management and liquidity further support the rating. Although the town has large long-term liabilities and increasing retirement costs, we believe 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 period.

However, while unlikely, we could lower the rating if a prolonged period of structural imbalance were to result in

significant available reserve deterioration.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- Local Government Pension And Other Postemployment Benefits Analysis: A Closer Look, Nov. 8, 2017
- 2017 Update Of Institutional Framework For U.S. Local Governments

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 the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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