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Summary:

Barnstable, Massachusetts; General Obligation

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Table Of Contents

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Credit Profile		
US$2.789 mil GO roadway imp bnds due 02/15/2036		
Long Term Rating	AAA/Stable	New
Barnstable GO		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' rating and stable outlook to the Town of Barnstable, Mass.' $2.8 million general obligation (GO) roadway improvement bonds and affirmed its 'AAA' rating, with a stable outlook, on the town's existing GO debt.

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.

We understand officials intend to use the current issuance to permanently finance some bond anticipation notes that come due in February as well as to fund various road improvement projects.

Credit overview

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 25% 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 believe that the town will likely manage these costs appropriately and that additional debt will likely remain relatively affordable due to Barnstable's size and wealthy tax base.

While we acknowledge the town could potentially face some challenges with a prolonged pandemic, in our view the impact of the COVID-19 pandemic on the town's finances has been limited, due in part to the town's residential tax base and a general fund revenue stream that is driven by stable property taxes. In addition, we expect officials will continue to make adequate budgetary adjustments to ensure budgetary balance. (For more information on the pandemic's effect on the U.S. public finance sector, see the articles "Staying Home For The Holidays," published Dec. 2, 2020, and "Outlook For U.S. Local Governments: Revenue Pressures Mount And Choices Get Harder," published Jan. 6, 2021, both on RatingsDirect.)

Under our criteria, titled "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And

Assumptions," published Nov. 19, 2013, 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 2020, local property taxes generated nearly 70% of revenue, which demonstrated a lack of dependence on central government revenue.

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 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 2020, as well as reflecting some continued risk associated with the pandemic on near-term operations;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2020 of 27% of operating expenditures;
- Very strong liquidity, with total government available cash at 23.3% of total governmental fund expenditures and 5.3x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability profile, with debt service carrying charges at 4.4% of expenditures and net direct debt that is 39.7% of total governmental fund revenue, as well as low overall net debt at less than 3.0% of market value and rapid amortization, with 74.9% 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.

Environmental, social, and governance factors

Our rating and analysis incorporate our view regarding the health and safety risk posed by the COVID-19 pandemic, which we believe could pressure budgets in the short term. Overall, we consider the town's social risks in line with that of the sector. We also analyzed Barnstable's governance risks relative to the town's credit factors and determined that these risks are in line with our view of the sector standard.

In addition, although we believe the town's environmental risks are somewhat above average given that Barnstable is a coastal community proximity along the Atlantic Ocean, we believe this risk is mitigated by the town's various coastal-resiliency initiatives and rising-sea-level mitigation projects. Specifically, to help mitigate rising sea levels and address coastal flooding, the town has placed sand barriers along its Sandy Neck area and has included in its five-year capital plan projects for access road relocation, which could be funded by fiscal 2023. In addition, Barnstable has various cybersecurity protections and maintains network and system backups and cybersecurity insurance.

Stable Outlook

Downside scenario

Although Barnstable has large long-term liabilities and increasing retirement costs, we think management will likely make the budgetary adjustments as necessary to maintain balanced financial operations. Nevertheless, while unlikely, we could lower the rating if a prolonged structural imbalance were to result in significantly deteriorated available reserves.

Credit Opinion

Very strong economy

We consider Barnstable's economy very strong. The town, with an estimated population of 43,860, is in Barnstable County in the Barnstable MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 124% of the national level and per capita market value of $364,307. Overall, the town's market value grew by 5.9% over the past year to $16.0 billion in 2021. The county unemployment rate was 3.9% in 2019, although we note unemployment increased significantly in 2020 because of the pandemic.

Barnstable is at the center of Cape Cod, with 100 miles of shoreline, and its population increases 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, the town itself, 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. We understand this project has added about 75 new jobs. Cape Town Plaza is also expanding with the developer, who has begun making ground-lease payments to the town totaling about $1 million annually. A new 340-unit senior citizen living center also came online within the last year. Management indicates these developments and others planned to come online should continue to expand the tax base at a good rate.

The county's unemployment rate has historically been in line with state and national averages. However, following the onset of the pandemic, the county's unemployment rate increased to a high of 21.5% in April 2020. Since then, the rate has steadily trended lower and stood at just 6.8% as of November 2020.

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 with consistent annual positive variances both in revenues and expenses. 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 reserve policies. The town's reserve policy includes a minimum unassigned reserve fund balance equal to 4% of expenditures. Finally, the town annually prepares and updates a robust five-year financial forecast and five-year capital improvement plan with funding sources identified.

Strong budgetary performance

Barnstable's budgetary performance is strong in our opinion. The town had operating surpluses of 3.6% of expenditures in the general fund and of 5.9% across all governmental funds in fiscal 2020.

Our assessment accounts for risks on budget performance related to the pandemic in fiscal 2021 as well as our expectation that the town will maintain at least balanced operations in fiscal 2021. Our assessment also adjusts for recurring transfers and one-time capital expenditures paid for with bond proceeds.

We understand the pandemic did not materially affect fiscal 2020 results. Officials attribute the fiscal 2020 general fund surplus primarily to higher-than-expected revenue, particularly from real estate and personal property tax, as well as from motor-vehicle excise taxes. Revenues came in about $4.0 million above budget. In addition, the town realized some expense savings due to conservative budget estimates as well to some cost reductions in the fourth quarter following the onset of the pandemic.

The fiscal 2021 budget was being finalized at the start of the pandemic. Town management notes that it immediately froze all vacant positions and cut discretionary spending beginning in the fourth quarter of fiscal 2020. As a result, the budget for fiscal 2021 was held flat relative to the previous year, totaling $168.2 million. Included in the budget was a $2.8 million fund-balance appropriation, which was consistent with prior years' appropriations. Officials report fiscal 2021 budget-to-actual results continue to track well despite the pandemic, and that the town should end the year with at least breakeven operations. This is due in part to a very strong residential market, with property taxes generating nearly 69% of general fund revenue, followed by intergovernmental aid at 19%. Property tax collections have averaged 99% during the past three fiscal years, and we understand there has not been a change in collections as a result of the pandemic. Furthermore, we note the town received nearly $24 million in coronavirus relief funds (from the federal Coronavirus Aid Relief and Economic Security Act funding) that have and will continue to offset pandemic-related expenses.

Although we expect budgetary performance will likely remain adequate to 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 an available fund balance in fiscal 2020 of 27% of operating expenditures, or $48.4 million.

The town has consistently maintained available reserves well above 20% of expenditures during the past three fiscal years. The fiscal 2021 budget includes a fund-balance appropriation of $2.8 million. Management, however, does not currently expect to realize any actual reserve drawdowns by fiscal year-end.

Due to the fiscal 2021 budget's current performance, management expects to end fiscal 2021 with at least breakeven operations. Barnstable's formal reserve policy calls for maintaining an unassigned fund balance at a minimum 4% of expenditures, which it has been well above historically. The unassigned fund balance totaled $41.8 million, or 19.5% of expenditures, in fiscal 2020.

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 5.3x governmental debt service in 2020. 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 on 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 4.4% of total governmental fund expenditures, and net direct debt is 39.7% of total governmental fund revenue. Overall net debt is low at 0.8% of market value, and approximately 74.9% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

We anticipate the town could issue an additional $20 million-$30 million annually during the next three years for various capital improvements, most notably for a major sewer-related project that will eventually convert town residents from septic to a municipal sewer system.

We understand that Barnstable, similar to 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 adequate to strong, we believe debt metrics could potentially weaken, depending on future sewer-related debt. Management intends to finance these strategies through debt exclusion overrides, sewer assessments, sewer-and-tax rate increases, and commonwealth or federal funding.

Pension and other postemployment benefits

A credit weakness is Barnstable's large pension and OPEB obligation, particularly given the pension systems' low funded ratio. While the town is currently managing these costs, we believe it has a limited ability to control future pension liability growth.

Pension and OPEB highlights include:

- While the town is managing these costs, we believe pension and OPEB liabilities will likely remain a long-term credit pressure 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 believe unexpected-contribution-escalation risk will likely increase and could add some pressure to the budget. However, we 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 also maintains an irrevocable OPEB trust fund, which has a current balance of about $5.8 million as of fiscal 2020, equal to 2.7% funding.

At June 30, 2020, the town participates in:

- Barnstable County Retirement Association, which is 62.3% funded, with a proportionate share of the town's net pension liability at $117.7 million, assuming a 7.15% discount rate as of fiscal 2020; and
- Barnstable's defined-benefit, postretirement, health care plan, which is 2.7% funded as of fiscal 2020, with an OPEB liability of about $210.4 million.

Barnstable's combined required pension and actual OPEB contributions totaled 7.7% of total governmental fund expenditures in 2020. Of that amount, 5.0% represented required contributions to pension obligations, and 2.7% represented OPEB payments. The town made its full annual required pension contribution in 2020. The funded ratio of the largest pension plan is 62.3%.

The town makes its actuarially determined contribution annually. Contributions are expected to increase by 5.28% per year on a level percentage-of-pay amortization basis. While the retirement system recently extended the amortization period by two years, to account for a revision of the discount rate to 7.15%, the adopted funding schedule achieves full funding in 2037. We view the period as a positive as it is less than 20 years, but continue to view the discount rate as elevated, potentially leading to cost escalation. The retirement system did not meet either our static or minimum funding progress metrics in the most recent year. (For more information on the plan, see "Pension Spotlight: Massachusetts," Oct. 14, 2020.)

Barnstable created an OPEB trust fund in 2011 that had about a $5.8 million balance at June 30, 2020. Management contributed $628,000 to this OPEB fund in fiscal 2020, and plans to increase the base contribution by $50,000 annually, which it incorporated into long-term financial planning. We view prefunding OPEB liabilities positively, and we expect retirement costs will likely remain manageable during the next few fiscal years, although we believe Barnstable's large and growing pension and OPEB liabilities could add some pressure to the budget over the long term.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 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
- 2020 Update Of Institutional Framework For U.S. Local Governments