

RatingsDirect®

Summary:

Middleborough, Massachusetts; General Obligation

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Credit Profile

US\$45.945 mil GO municipal purp loan ser 2021 dtd 10/01/2021 due 10/01/2049

Long Term Rating AA/Stable New

Middleborough Twn GO

Long Term Rating AA/Stable Affirmed

Rating Action

S&P Global Ratings assigned its 'AA' long-term rating to Middleborough, Mass.' 2021 general obligation (GO) municipal-purpose loan bonds. At the same time, S&P Global Ratings affirmed its 'AA' rating on the town's long-term debt outstanding. The outlook is stable.

The town's full-faith-and-credit pledge, subject to the limitations of Proposition 2-1/2, secures the GO bonds. The bond proceeds (\$45.9 million) will permanently finance outstanding bond anticipation notes issued for the construction costs of a new high school, a public works facility, and the acquisition of a fire tower water storage tank. This issuance also includes the refunding of approximately \$2.8 million of the town's 2009 bonds. The town is concurrently issuing \$6.7 million in bond anticipation notes, which we were asked not to rate; however, this debt is included in our analysis.

The electorate voted to exempt debt service costs of the high school construction project from Proposition 2-1/2 limitations. We rate the limited-tax GO debt based on the application of our "Issue Credit Ratings Linked To U.S. Public Finance Obligor's Creditworthiness" criteria (published Nov. 20, 2019, on RatingsDirect). We are rating the obligation at the same level with our view of Middleborough's general creditworthiness. Any limitation imposed on the obligor's ability to raise revenue is already embedded in the rating. Therefore, we are not making a rating distinction. The town has approximately \$117 million in total direct debt outstanding.

Credit overview

The town has consistently produced at least balanced operating results over the past several years, reflecting consistent and conservative budgeting practices. Accordingly, the town demonstrated financial and economic resilience vis a vis the risks caused by the pandemic in fiscal years 2020 and 2021, solidifying its solid financial profile. The town also expects to receive a total of \$2.6 million in American Rescue Plan Act funds, which will be allocated to replace lead water pipes throughout the town. The town's economic development is also steady, including a recently created a cannabis district, which has attracted 17 cannabis companies to Middleborough for retail, cultivation, manufacturing, and processing. We expect Middleborough to continue its trajectory of steady and positive financial and economic profile, facilitated by prudent financial management.

The long-term rating further reflects our view of the following factors, including Middleborough's:

- Strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with slight operating surpluses in the general fund and at the total governmental fund level in fiscal 2020;
- Strong budgetary flexibility, with an available fund balance in fiscal 2020 of 10.9% of operating expenditures;
- Very strong liquidity, with total government available cash at 59.1% of total governmental fund expenditures and 14.5x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability profile, with debt service carrying charges at 4.1% of expenditures and net direct debt that is 77.8% of total governmental fund revenue, and a large pension and other postemployment benefit (OPEB) obligation and the lack of a plan to sufficiently address the obligation, but low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

Environmental, social, and governance (ESG) factors

We evaluated the town's environmental, social, and governance (ESG) factors relative to its economy, financial measures, management, and debt and long-term liability profile. We consider the town's social, environmental, and governmental risks as in line with those of the sector. The town participates in the Municipal Vulnerability Preparedness program, which provides state support to identify climate hazards, assess vulnerabilities, and develop action plans to improve resilience to climate change.

Stable Outlook

Downside scenario

Should the town experience revenue shortfalls beyond what management can absorb into the budget, resulting in a reduction in reserves, or if rising fixed costs pressure fiscal balance over time, we could lower the rating.

Upside scenario

If the town were to achieve stronger income and market value metrics comparable with higher rated communities within the state, as well as maintain strong budgetary performance, while addressing rising costs associated with retirement liabilities, we could raise the rating.

Credit Opinion

Strong economy

We consider Middleborough's economy strong. The town, with an estimated population of 25,093, is in Plymouth County in the Boston-Cambridge-Newton, Mass.-N.H. MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 101.5% of the national level and per capita market value of \$118,617. Overall, the town's market value grew by 3.8% over the past year to \$3.0 billion in 2021. The county unemployment rate was 9.5% in 2020, which spiked at 18.3% in April 2020. The county 2019 unemployment rate was 3.0%.

The commonwealth's second-largest municipality by area, Middleborough has capitalized on its capacity for new development in both residential and commercial sectors, facilitating increases to its tax base.

The town is primarily residential, with residential properties making up 82% of total assessed value (AV), with total AV continuing to grow annually. Leading taxpayers are a mixture of commercial, industrial, and residential properties, resulting in a low taxpayer concentration. The town created a cannabis district in 2019 and is currently negotiating 17 host agreements with cannabis companies for retail, manufacturing, cultivation, and processing of cannabis. Currently, one retail is already operating, while the remaining 16 are anticipated to open by the summer/fall of 2022. The town estimates such enterprise activity to yield between \$1.5 million to \$2 million in annual revenue from sales and excise taxes. Additionally, Amazon recently opened a 30,000 square foot distribution center, and a new train station stop on the South Coast Rail will be completed by the end of calendar year 2022/spring 2023, which will be coupled with mixed-use development in the vicinity.

Strong management

We view the town's management as strong, with good financial policies and practices under our FMA methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis.

Management performs a three-year trend analysis when budgeting for revenue and expenditures. It has a multiyear capital improvement plan, which is updated occasionally and drafted by a capital planning committee in consultation with department heads. The reserve policy aims to maintain a minimum stabilization fund at 3% of general fund revenue, which it currently exceeds.

Management maintains a debt policy that establishes parameters for the types of projects it can fund with bonds and caps debt service at 10% of operating expenditures. Middleborough follows commonwealth guidelines when managing investments and frequently reviews investment performance. In addition, management maintains strong budget surveillance with frequent reports on budget-to-actual results to the town council, coupled with the flexibility to adjust the budget when needed. The town maintains a long-term financial plan, which incorporates level growth rates for outyear budget assumptions. We believe the town generally uses conservative budget assumptions and expect management will continue to adjust the budget based on new information.

Strong budgetary performance

Middleborough's budgetary performance is strong in our opinion. The town had slight operating surpluses of 1.3% of expenditures in the general fund and 1.4% across all governmental funds in fiscal 2020. General fund operating results have been stable, at 0.8% in 2019 and 0.9% in 2018.

For analytical consistency, we adjusted for one-time capital expenditures out of the high school building and police station funds. Property taxes generated about 57% of general fund revenue in fiscal 2020. Intergovernmental aid accounted for about 35% and local excise taxes about 6% of general fund revenues.

The town continues to produce positive operations, largely due to conservative budgeting practices. The town's budgets allow for some unpredictable revenue and expenditure variance, including unknown new growth revenues. We believe this demonstrated practice somewhat insulates it from variances in the current environment.

The town's 2021 budget totaled \$80.2 million and actuals are expected to have outperformed expectations in the positive. The town general fund revenues are expected to be more than budgeted revenues by \$1.6 million. While the town's meals and rooms tax came up slightly short relative to budget, its excise tax revenue exceeded budgetary estimates, which was the primary driver of the year-end surplus. Additionally, the town has been allocated \$4.1 million in CARES Act funding; it has submitted a reimbursement claim for \$2.4 million and has received \$1.4 million of these funds. It has until Dec. 31, 2021, to utilize these funds. The town has also been allocated \$2.6 million in ARP Act funds, of which it received \$1.3 million in fiscal 2021. It expects to receive the remainder of the ARP Act funds, in addition to possibly several million dollars from the county, in fiscal 2022; these monies are not included in the budget.

Actuals for fiscal 2022 are trending in line with budget. The town's preliminary fiscal 2022 budget is currently estimated at \$85.2 million, a 6.2% increase over the fiscal 2021 budget. The town is negotiating five union contracts, which are not expected to pressure the budget.

Strong budgetary flexibility

Middleborough's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2020 of 10.9% of operating expenditures, or \$8.7 million.

Positive operating results during the previous several fiscal years has resulted in reserves increasing to levels we consider strong. The town's reserve policy sets a minimum stabilization fund balance at 3% of general fund revenue. The fund balance has exceeded the minimum threshold over the past few years, and, given recent operating results, we expect reserves to remain at least at their current levels if not increase over the next one to two years.

Very strong liquidity

In our opinion, Middleborough's liquidity is very strong, with total government available cash at 59.1% of total governmental fund expenditures and 14.5x governmental debt service in 2020. In our view, the town has strong access to external liquidity if necessary.

Our view of the town's available cash excludes certain funds we believe are unavailable for general operations or debt service. Net of these funds, the town has maintained very high cash balances. We believe Middleborough's frequent debt issuance, including GO bonds and BANs, demonstrates its strong access to external liquidity and further supports the liquidity profile.

Middleborough does not currently have any contingent liquidity risk from financial instruments with payment provisions that change on the occurrence of certain events. In addition, it does not currently have investments we view as aggressive. Given the high cash balances, we do not expect deterioration in the town's liquidity profile, despite potential variability in property tax collections and other revenues due to the uncertain economic environment.

Weak debt and contingent liability profile

In our view, Middleborough's debt and contingent liability profile is weak. Total governmental fund debt service is 4.1% of total governmental fund expenditures, and net direct debt is 77.8% of total governmental fund revenue. Overall net debt is low at 3.0% of market value, which is in our view a positive credit factor.

The town has about \$117 million in total direct debt outstanding, including BANs and self-supporting enterprise debt. We understand the town may issue up to \$650,000 in new-money debt over the next one-to-two years for a fire engine

pumper truck. Our view of the town's debt profile could change should its overall net debt increase as a percentage of market value.

Pension and OPEB liabilities

In our opinion, a credit weakness is Middleborough's large pension and OPEB obligation, with a plan we believe does not sufficiently address the obligation.

- In our opinion, a credit weakness is Middleborough's large pension and OPEB obligation, particularly given the low funded ratios of the pension system and OPEB trust fund, without a credible plan in place to meaningfully address the liabilities.
- While the use of an actuarially determined contribution (ADC) is a positive, we believe some of the assumptions used to build the pension ADC reflect what we view as slightly weak assumptions and methodologies, which we believe increases the risk of unexpected contribution escalations.
- Although OPEB liabilities are funded on a pay-as-you-go basis, costs remain low despite the large liability, and we expect the town will continue adding to its OPEB trust fund.

As of June 30, 2019, the town participated in the following pension plan:

- Plymouth County Contributory Retirement System (PCCRS): 61.1% funded with a \$62 million proportionate share of the net pension liability

Middleborough's combined required pension and actual OPEB contributions totaled 9.4% of total governmental fund expenditures in 2020. Of that amount, 6.1% represented required contributions to pension obligations, and 3.4% represented OPEB payments. The town made its full required pension contribution in 2020.

The PCCRS is a cost-sharing, multiple-employer, defined-benefit pension plan. The system uses a 7.875% discount rate. We believe this discount rate is high for municipal systems and could lead to volatile contributions should market performance not meet expectations. The system has recently lowered the discount rate from 8% and will continue to explore further reductions, which we view positively. While Massachusetts requires all pension systems to achieve full funding no later than 2040, PCCRS has planned to do so by 2029. We generally view closed, short amortization schedules as positive, but for PCCRS to meet its adopted funding schedule to achieve full funding in 2029 costs must rise, given the low funded ratio and short funding schedule. Positively, PCCRS met both our static funding metric in the most recent year as well as our minimum funding progress calculation, indicating that the system is addressing current costs and making headway addressing its unfunded liabilities. The adopted schedule for the plan shows contributions increasing by 5% annually, which we believe, given current costs, will remain manageable. However, should Middleborough face budgetary pressures due to the rising fixed costs, our view of the debt and liability profile could weaken. For more on our view of the state's pension plans and recent reforms, see "Pension Spotlight: Massachusetts," Oct. 14, 2020.

Middleborough also provides OPEBs to retirees. As of June 30, 2020, it reported a \$107.2 million net OPEB liability. The town has traditionally paid OPEB costs on a pay-as-you-go basis, although it has begun prefunding the liability. Middleborough participates in a regional OPEB trust, into which it allocates \$200,000 annually. As of fiscal year-end 2020, the town's assets within the trust fund totaled \$1.8 million. We understand its formal policy is to contribute

\$200,000 to the trust annually and that it will shift pension payments to OPEBs once the pension plan is fully funded. We believe retirement costs are likely to continue growing, particularly if pension plan assumptions are not met.

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
- Credit Conditions: U.S. Regions' Economies Perk Up As The Pandemic's Impact Ebbs, April 16, 2021
- 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

Ratings Detail (As Of September 10, 2021)		
Middleborough Twn GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Middleborough Twn GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Middleborough Twn GO (AGM)		
<i>Unenhanced Rating</i>	AA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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