

RatingsDirect®

Summary:

Natick, Massachusetts; General Obligation

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Credit Profile

US\$9.3 mil GO mun purp loan bnds ser 2017 due 07/15/2042

Long Term Rating AAA/Stable New

Town of Natick GO

Long Term Rating AAA/Stable Affirmed

Town of Natick GO mun purp ln of bnds

Long Term Rating AAA/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' rating and stable outlook to the town of Natick, Mass.' series 2017 general obligation (GO) municipal purpose loan bonds and affirmed its 'AAA' rating, with a stable outlook, on the town's existing GO debt.

We rate the town higher than the nation because we believe it 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. (Please see our criteria article, titled "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions," published Nov. 19, 2013, on RatingsDirect.) In fiscal 2016, local property taxes generated 73% of general fund revenue, which demonstrated a lack of dependence on central government revenue.

Natick's full-faith-and-credit-GO pledge, subject to the limitations of Proposition 2 1/2, secures the bonds. Despite limitations imposed by the commonwealth's 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.

Officials intend to use series 2017 bond proceeds to fund a variety of municipal purposes.

The rating reflects our opinion of the town'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 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 32.4% of total-governmental-fund expenditures and 4.9x 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 53.2% of total-governmental-fund revenue, as well as low overall net debt at less than 3% of

- market value and rapid amortization, with 76% of debt scheduled to be retired within 10 years, but significant medium-term debt plans and a large pension and other-postemployment-benefit (OPEB) obligation; and
- Strong institutional framework score.

Very strong economy

We consider Natick's economy very strong. The town, with an estimated population of 35,864, is located in Middlesex County in the Boston-Cambridge-Newton MSA, which we consider broad and diverse. The town has a projected per capita effective buying income of 177% of the national level and per capita market value of \$214,802. Overall, the town's market value grew by 4.7% over the past year to \$7.7 billion in fiscal 2017. The county unemployment rate was 3% in 2016.

Natick, a primarily residential community, approximately 18 miles from Boston, is part of the Greater Boston area. The town has an established local economy that has experienced steady growth over the years. The property tax base is 77.9% residential and 19.6% commercial and industrial. Assessed value (AV) has reached \$7.7 billion in fiscal 2017, and officials are projecting AV will continue to grow. Mathworks, the town's leading employer, is a software developer that has recently expanded its Lakeside campus; the company expects to add an estimated 700-1,000 jobs.

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.

Natick's management highlights include its:

- Conservative budgeting,
- Strong budgetary monitoring, and
- Long-term financial and capital plans.

Management submits quarterly reports on budget-to-actual results to the board of selectmen with adjustments made when needed. The town performs a five-year forecast for all long-term financial needs. Management maintains a five-year, annually updated capital improvement plan that identifies funding sources for each project. The town has adopted commonwealth guidelines for its investment policy. Management reports holdings, prepared quarterly by the treasurer, to the board through an annual audit.

Natick maintains its own formal debt and reserve policies under its financial management principles. The reserve policy calls for the town to maintain a general-stabilization-fund balance at a minimum of 2% of revenue with a target of 5%.

Strong budgetary performance

Natick's budgetary performance is strong, in our opinion. The town had operating surpluses of 3.2% of expenditures in the general fund and 2.7% of expenditures across all governmental funds in fiscal 2016. General fund operating results of the town have been stable over the past three fiscal years, with a result of 3% of expenditures in fiscal 2015 and 2.2% of expenditures in fiscal 2014.

We adjusted fiscal 2016 audited general fund and total-governmental-funds operating results for recurring transfers, one-time transfers, and bond proceed usage. In fiscal 2016, revenue exceeded budgeted expectations by roughly \$3.4

million; management attributes this to its underbudgeting of the local meals and hotel tax and licenses and permit fees, coupled with strong tax title collections.

Management is projecting a surplus between \$4 million and \$7 million at fiscal year-end 2017 due to increased revenue and strong collections. The adopted fiscal 2018 budget totals \$153.8 million, a 5.1% increase over fiscal 2017. We expect Natick's budgetary performance will likely remain strong due to historical performance and management's consistent conservative budgeting.

Very strong budgetary flexibility

Natick's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 23% of operating expenditures, or \$30.6 million.

Available funds include assigned and unassigned fund balances, as well as a variety of stabilization funds within and outside the general fund that management could make available for general operational use. The town expects to maintain, if not grow, available reserves and refrain from using stabilization funds. With conservative financial practices and a practical maintenance of reserves, we believe budgetary flexibility will likely remain very strong.

Very strong liquidity

In our opinion, Natick's liquidity is very strong, with total government available cash at 32.4% of total-governmental-fund expenditures and 4.9x governmental debt service in fiscal 2016. In our view, the town has strong access to external liquidity if necessary.

Natick regularly accesses the bond market by frequently issuing debt, supporting its strong access to external liquidity. We also believe Natick's liquidity profile is conservative with no high exposure to refinancing risk, debt, or other potential obligations that could pose a risk to liquidity. Therefore, we expect the liquidity profile will likely remain very strong over the next two fiscal years.

Strong debt-and-contingent-liability profile

In our view, Natick'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 53.2% of total-governmental-fund revenue. Overall net debt is low at 1.1% of market value and approximately 76% of direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors. Negatively affecting our view of the town's debt profile is its significant medium-term debt plans.

Subsequent to this issue, Natick will have \$93 million of direct debt outstanding. Within the next two years to three years, the town plans to issue between \$68 million and \$73 million in debt as part of its upcoming middle school, fire station, and new parking garage construction projects. The estimated school project cost is \$95 million-\$100 million. Management expects about 50% of aid from Massachusetts School Building Authority for the projects. While the timing and final amounts could vary, based on these plans, we expect Natick's net direct debt to increase; we have incorporated this into our view of the town's debt profile.

In our opinion, Natick's large pension and OPEB obligation is a credit weakness. Natick's combined required pension and actual OPEB contribution totaled 8.2% of total-governmental-fund expenditures in fiscal 2016. Of that amount, 5.2% represented required contributions to pension obligations and 2.9% represented OPEB payments. The town

made its full annual required pension contribution in fiscal 2016. The funded ratio of the largest pension plan is 56.5%.

Natick contributes to the Natick Contributory Retirement System, a cost-sharing, multiemployer, defined-benefit pension 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 \$88.1 million with 56.5% funding as of fiscal 2016 based on an assumed rate of return of 7.5%. Due to the low funded ratio, we believe contributions will likely continue to rise over the next few fiscal years.

Natick also provides OPEB to retirees. As of July 1, 2014, the most recent actuarial valuation, it reported a \$125 million OPEB liability. Natick has traditionally funded OPEB through pay-as-you-go financing. It paid \$4.4 million, or 2.9% of expenditures, which was 34% of the annual required contribution, in fiscal 2016. The town established an OPEB trust fund in fiscal 2011 to finance this liability. As of Feb. 28, 2017, the trust fund balance was \$2.1 million.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion that Natick will likely maintain its very strong reserves, supported by very strong management. We believe the town's participation in the broad and diverse Boston MSA provides additional rating stability. Therefore, we do not expect to change the rating within the outlook's two-year period.

However, we note rising pension costs related to the weak funded status of the pension plan could pressure the town's debt-and-contingent-liability profile. For now, budgetary performance and flexibility remain unaffected by those long-term liabilities due largely to the town's very strong management and budgetary flexibility. Should these pressures require management to draw down reserves over time to maintain balanced operations, we could lower the rating.

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
- 2016 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.globalcreditportal.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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