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Ratings

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Summary:

Danvers, Massachusetts; General Obligation

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Summary:

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Credit Profile		
US$20.275 mil GO muni purp loan bnds ser 2019A due 08/15/2039		
Long Term Rating	AAA/Stable	New
US$3.295 mil GO muni purp loan bnds ser 2019B due 08/15/2034		
Long Term Rating	AAA/Stable	New
Danvers Twn GO		
Long Term Rating	AAA/Stable	Upgraded
Danvers Twn GO		
Long Term Rating	AAA/Stable	Upgraded

Rationale

S&P Global Ratings raised its long-term rating one notch on the Town of Danvers, Mass' existing general obligation (GO) bonds to 'AAA' from 'AA+'. At the same time, S&P Global Ratings assigned its 'AAA' long-term rating to the town's series A and B 2019 GO bonds. The outlook on all ratings is stable.

The upgrade reflects our view of Danvers' consistently balanced financial results, which have led the town to maintain a strong reserve position over the past several years, and through various business and economic cycles. Also underpinning the rating is Danvers' very strong management conditions, with strong policies and plans that the town adheres to and updates accordingly. We believe these strong financial policies, combined with collaboration throughout all government departments, provide a robust budgeting and planning framework, further supporting the strong credit profile. Long term, the town's retirement liabilities could increasingly pressure the operating budget, although we understand officials are considering options to reduce the size of the liability and will likely begin meaningfully contributing toward Danvers's other postemployment benefit (OPEB) trust fund with new revenues streams, and once the pension system is fully funded. Therefore, absent a substantial reversal of budgetary performance and flexibility or a deterioration in its wealth and income conditions, we believe Danvers' credit quality will remain stable.

Danvers' full-faith-and-credit pledge, subject to Proposition 2 1/2 limitations, secures the bonds. We rate the limited-tax GO debt based on the application of our criteria "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness," published Jan. 22, 2018. We rate the obligation at the same level as our view of Danvers' general creditworthiness, as expressed in our rating on the town's unlimited-tax GO bonds.

Danvers' GO bonds are eligible to be rated above the sovereign because we believe the town can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria, "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013), Danvers has a predominately locally derived revenue source and we believe that pledged revenue supporting debt service on the bonds is at limited risk of negative sovereign intervention. In fiscal 2018, local property taxes generated 72.7% of town revenue, which demonstrated a lack of dependence on central government revenue.

Officials intend to use the bond proceeds, totaling about $23.57 million, for various municipal purposes including construction of the Smith Elementary School, Central and Engine 2 Fire Station Improvements, and new water mains, among other purposes.

The long-term rating further 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 (FMA) methodology;
- Strong budgetary performance, with balanced operating results in the general fund and at the total governmental fund level;
- Very strong liquidity, with total government available cash at 36.4% of total governmental fund expenditures and 7.9x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability profile, with debt service carrying charges at 4.6% of expenditures and net direct debt that is 69.3% of total governmental fund revenue, and a large pension and OPEB obligation and the lack of a plan to sufficiently address potential escalation of costs, but low overall net debt at less than 3.0% of market value; and
- Strong institutional framework score.

Very strong economy

We consider Danvers' economy very strong. The town, with an estimated population of 28,371, is located in Essex County in the Boston-Cambridge-Newton MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 130% of the national level and a per capita market value of $182,019. Overall, the town's market value has grown by 5.3% over the past year to $5.2 billion in 2019. The county unemployment rate was 3.4% in 2018.

A primarily residential community with a healthy commercial and industrial base, Danvers maintains a diverse economy with sectors in retail, manufacturing, health care, high technology, and higher education. Approximately 76.56% of the tax base is residential and 21.5% is commercial and industrial. Top employers include Medtronic Interventional Vascular, a biomedical research and development company (740 employees); IRA Motor Group (530 employees); and Hospice Care Dimensions (522 employees). The top 10 taxpayers constitute 6.6% of AV, which we consider very diverse.

Danvers is 20 miles north of Boston on Interstate 95 and Route 1, which provide easy access to employment centers in and around the town. New growth has remained steady at about 1% of the tax levy since 2016. In addition, local officials are seeing a strong demand in the housing market with an increase in home prices and housing starts. We expect market value to continue to grow due to numerous ongoing commercial and residential developments. Furthermore, in December 2017, Danvers adjusted its zoning bylaws to encourage additional mixed-use development. As a result of this rezoning, the town has identified 1,000 units of potential development in the downtown area. The former municipal hospital, which was once one of the largest employers with 300 Town employees before closing in 1990, recently reopened as a substance abuse facility with 180 beds and 220 new jobs and now generate roughly $300,000 per year in tax revenue. Other projects include the redevelopment of a former EconoLodge site to create 200 units of housing and the addition of a medical marijuana facility in the town's business park. With the marijuana facility, the town of Danvers has a host agreement in which the town will realize greater than $250,000 or 3% of gross revenue annually.

Due to many of these projects and a growing real estate market, AV remains strong and poised for further growth. We anticipate that Danvers' economy will remain steady throughout our two-year outlook period.

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.

We revised our view of Danvers' fiscal management environment to very strong. Namely, we revised our view of the town's long-term financial plan and debt management policy. In March 2016, Danvers introduced a debt management policy that caps debt service at 10% of expenditures and requires the board of selectmen to annually review the proposed capital improvements' financial impact. In addition, the town developed a rolling five-year, long-term financial plan that identifies budgetary pressures in out-years and prioritizes structural balance. Since its adoption, town officials have demonstrated that these policies are embedded and institutionalized in the budget making process.

In developing the budget, Danvers uses conservative assumptions grounded in a historical trend analysis and an understanding of current economic conditions. It maintains strong practices in the areas of budgetary control, with quarterly budget-to-actual reports and investment reports presented to the board of selectmen. The town also has a rolling five-year, long-term financial plan that identifies budgetary pressures in out-years and prioritizes structural balance. Complementing this plan is a five-year capital improvement plan that officials update annually and that identifies funding sources for specified capital projects. Along with the debt policy, the town approved a fund balance policy that targets an unassigned general fund balance of 8%-12% of its annual operating expenditures. If unassigned fund balance drops below 5%, the policy directs officials to restore the balance above that level as soon as possible. The town has been in compliance with these policies since 2016. Danvers maintains a written investment policy that mirrors state guidelines. Finally, in fiscal 2019 the board of selectmen adopted financial policy guidelines to cover remaining policy areas such as funding the OPEB trust fund.

Strong budgetary performance

Danvers' budgetary performance is strong in our opinion. The town had balanced operating results of 0.4% of expenditures in the general fund and of 0.1% across all governmental funds in fiscal 2018. General fund operating results of the town have been stable over the last three years, with a result of 1.7% in 2017 and a result of 2.3% in 2016.

In our assessment of budgetary performance, we made adjustments for recurring interfund transfers and one-time expenditures.

Management attributes the surplus in fiscal 2017 to departmental turnbacks. In addition, management also reported that economically sensitive revenue (such as hotel tax, excise tax, and permits) came in higher than conservative assumptions. In fiscal 2018, after adjusting for transfers and one-time revenues and expenditures, Danvers achieved almost break-even results in the general fund and across all governmental funds for similar reasons.

For fiscal 2019, officials anticipate that revenues will be approximately $1.5 million above projections and expenditures will be below by $2.0 million. These results are due to snow and ice surplus because of a mild winter, school department turnbacks, and conservative estimates in major local receipts. Furthermore, town officials indicated that $1.5 million was added to the general stabilization fund, $750,000 to the school construction and stabilization fund, $600,000 was used for investments in capital, and $350,000 was added to OPEB via free cash ($832,000 was added to OPEB in total).

The town recently adopted a budget for fiscal 2020. This budget assumes a 2.5% tax rate increase and $600,000 in new growth based on Danvers' current trends. In addition, it includes planned use of the school stabilization fund as the town phases in debt service payments for construction of the Smith School and an anticipated retirement contribution increase of 7.1%. Overall there are no significant changes compared to previous budgets.

We anticipate the town's budgetary performance will be stable despite high long-term costs associated with Danvers' pension and OPEB liabilities. Management is generally conservative in its budget assumptions, which has historically led to positive budgetary variances, as well as the ability regenerate appropriated free cash. Consequently, over the next two fiscal years, we expect management will continue to align recurring revenues with recurring expenditures as it has historically done.

On the whole, property taxes constitute 72.7% of revenues and state aid about 14.9%. We believe tax collections are strong and stable, with the town typically receiving 99% on a current basis.

Very strong budgetary flexibility

Calculation for available reserves includes assigned, unassigned, and committed stabilization reserves. The town has maintained reserves above the policy target of 15% of expenditures for the past several fiscal years and above 20% for the past four fiscal years. Management expressed a commitment to maintaining fund balance level in fiscal years 2019 and 2020.

We expect our assessment of budgetary flexibility to remain at least strong if not very strong, based on the town's fund balance policy that calls for the unassigned fund balance to remain at 8%-12% of expenditures.

Very strong liquidity

In our opinion, Danvers' liquidity is very strong, with total government available cash at 36.4% of total governmental fund expenditures and 7.9x governmental debt service in 2018. In our view, the town has strong access to external liquidity if necessary.

Danvers retains strong access to external liquidity as a regular market participant. Over the past several years, the town has frequently issued debt to support its capital project endeavors. Danvers has no variable-rate or direct-purchase debt. We expect the town's liquidity profile to remain very strong.

Weak debt and contingent liability profile

In our view, Danvers' debt and contingent liability profile is weak. Total governmental fund debt service is 4.6% of total governmental fund expenditures, and net direct debt is 69.3% of total governmental fund revenue. Overall net debt is low at 2.0% of market value, which is in our view a positive credit factor.

The town has $104.4 million in total direct debt outstanding, of which $1.4 million is BANs. It plans to issue $2.6 million over the next two-to-three years for school roof replacements and Haybarn renovations in Endicott Park. We do not expect this additional debt to materially impact the debt profile.

In our opinion, a credit weakness is Danvers' large pension and OPEB obligation, without a plan in place that we think will sufficiently address potential escalation of costs. Danvers' combined required pension and actual OPEB contributions including the town, electric, water, and sewer divisions totaled 11.1% of total governmental fund expenditures in 2018. Of that amount, 6.0% represented required contributions to pension obligations, and 5.1% represented OPEB payments. For just the town division, Danvers' combined required pension and actual OPEB contributions totaled 9.3%. Of that amount, 5.1% represented required contributions to pension obligations, and 4.2% represented OPEB payments. The town made its full annual required pension contribution in 2018. The funded ratio of the largest pension plan is 54.8%.

The town participates in the Danvers Contributory Retirement System, and covers substantially all employees of the town except for teachers and school administrators, which are covered under the Massachusetts Teachers Retirement System. Danvers contributed its full actuarially required contribution in 2018, which amounted to $5.7 million. As of Jan. 1, 2018, the town's net pension liability including the enterprise division was $75.6 million. Excluding the enterprise divisions, the town's net pension liability was $58.6 million. In addition to the pension benefits, Danvers also provides OPEBs. As of Jan. 1, 2018, the town had a net OPEB liability including the enterprise divisions of $192.3 million. Excluding the enterprise divisions the town had a net OPEB liability of $177.6 million.

Danvers has adopted a funding schedule for its pension liability, aiming to fully fund its liability by 2035. It has also adopted a more conservative plan by revising its projected rate of return downward again to 7.50% from 7.75%, although we still consider this elevated compared to peers. In regard to the OPEB obligation, the town is committed to increasing its contribution amount, as well as establishing an OPEB trust fund in place of the OPEB stabilization fund. At the end of fiscal 2018, the trust fund had a balance of $5.5 million. In addition, the town plans to begin meaningfully contributing toward the OPEB trust fund with new revenues streams, and redirect annual pension contributions to OPEB when the pension plan is fully funded.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Outlook

The stable outlook reflects our view of Danvers' strong budgetary performance and very strong budgetary flexibility, enhanced by a secure and diverse economy. We believe the town's predictable operating profile, strong management team, and conservative management practices should allow available reserves to remain strong. Therefore, we do not expect a rating change over our two-year outlook horizon.

However, if declining budgetary performance led to a material reserve reduction over several years, 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
- 2018 Update Of Institutional Framework For U.S. Local Governments