

# RatingsDirect®

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## Summary:

# Chatham, Massachusetts; General Obligation

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## Summary:

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### Credit Profile

US\$7.365 mil GO rfdg bn ds due 08/01/2028

*Long Term Rating*

AAA/Stable

New

Chatham GO

*Long Term Rating*

AAA/Stable

Affirmed

## Rationale

S&P Global Ratings assigned its 'AAA' long-term rating to the Town of Chatham, Mass.' general obligation (GO) refunding bonds. S&P Global Ratings also affirmed its 'AAA' long-term rating on the town's GO debt outstanding. The outlook is stable.

The bonds are GOs of the town, for which it has pledged its full faith and credit, a portion of which is subject to Proposition 2 1/2 levy limits. Because Chatham is highly rated and has very strong flexibility under the cap, we do not consider the levy limit a credit negative. Bond proceeds will be used to refund 2005 and 2008 bonds for an estimated \$646,000 in net present value savings.

We rate the town above the sovereign because we believe it can maintain better credit characteristics than the U.S. 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. The rating above the sovereign is based on our criteria, "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect).

In our opinion, our rating on Chatham reflects the town's:

- Very strong economy, with market value per capita of \$1.0 million and projected per capita effective buying income at 170% of the national level;
- Strong management, with "good" financial policies and practices under our financial management assessment (FMA) methodology;
- Strong budgetary performance, with an operating surplus in the general fund but a slight operating deficit at the total governmental fund level in fiscal 2015;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2015 of 18% of operating expenditures;
- Very strong liquidity, with total government available cash at 33.5% of total governmental fund expenditures and 2.1x governmental debt service, and access to external liquidity we consider strong;
- Weak debt and contingent liability position, with debt service carrying charges at 16.3% of expenditures and net direct debt that is 256.1% of total governmental fund revenue, but low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

### **Very strong economy**

We consider Chatham's economy very strong. The town, with an estimated population of 5,988, is located in Barnstable County. The town has a projected per capita effective buying income of 170% of the national level and per capita market value of \$1.0 million. Overall, the town's market value grew by 4.3% over the past year to \$6.2 billion in 2016. The county unemployment rate was 6.3% in 2015.

Chatham is about 90 miles south of Boston, at the elbow of Cape Cod. The town contains beachfront property on both the ocean and the bay and is primarily an affluent summer resort and second-home community. Chatham's population multiplies in the summer to approximately 30,000. Due to its 67 miles of coastline and desirable location, Chatham continues to experience high-end residential waterfront development. While selling prices for individual residential properties did decrease in the recession, total market value has remained high.

Looking ahead, based on our regional forecasts, we expect the regional economy to remain stable, but with lower growth compared with that of the nation. Still, recent data indicate that the region's median home prices will continue to improve, and that housing starts will remain positive. This is important because Chatham, along with other local governments in the region, largely look to property taxes to meet rising expenditure demands.

### **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.

Highlights of management policies include a strong focus on financial and capital planning evidenced by its five-year, annually updated capital needs budget and 10-year facilities replacement plan. The town conducts financial forecasting to identify future revenue and expenditure trends and to complement the capital budget. In building the budget, Chatham does a trend analysis, looking back at five years of historical data. Budget assumptions are conservative and budget performance is monitored monthly. The town's reserve policy sets 5% as the minimum balance in the stabilization account with a mandate to replenish the account within five years if reserves track lower than 5%. Although Chatham is currently in compliance, the balance in the stabilization account is exactly 5%. We also note that the town has a basic debt management policy, which stipulates that all new debt must be issued through a debt exclusion, requiring voter approval.

### **Strong budgetary performance**

Chatham's budgetary performance is strong in our opinion. The town had surplus operating results in the general fund of 2.8% of expenditures, but a slight deficit result across all governmental funds of 0.6% in fiscal 2015. General fund operating results of the town have been stable over the past three years, with a result of 4.7% in 2014 and a result of 3.0% in 2013.

In our analysis of budgetary performance, we net out \$3.5 million in one-time capital spent from bond proceeds for wastewater purposes. We also account for recurring transfers from the general fund to the water fund. The surplus in 2015 is a result of strong collections and turnbacks of \$473,000.

For fiscal 2016, management expects similar results with unspent expenditures totaling \$485,000 and revenue coming

in higher than budget. The 2017 budget includes expenditure increases relating to rising health insurance costs and the addition of a firefighter.

We expect operating performance to remain strong and in line with performance in years past. Through careful planning and prudent budgetary practices, we believe Chatham officials are well-prepared to manage increasing fixed costs associated with long-term liabilities, leading to stable operations in the future.

We also believe Chatham maintains a stable and predictable revenue profile that is largely independent from state or federal funds. On the whole, the town benefits from its high property tax base, which makes up more than 76% of total revenues. In addition, it maintains one of the lowest tax rates in the commonwealth, which again reflects the strong level of property wealth relative to the costs of services the town provides. Tax collections have historically remained strong despite the large number of second-home properties. Current collections have averaged 99% in the past five years. State aid represents a limited share of the town's general fund revenue, at 10%, which we view as a credit strength given the ongoing risk of state aid reductions.

### **Very strong budgetary flexibility**

Chatham's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2015 of 18% of operating expenditures, or \$6.7 million.

The town has continued to increase available reserves in the past three fiscal years, leading to improved budgetary flexibility and, according to management, it does not plan to spend down reserves. Management projects fiscal 2016 will close with another surplus that would raise available reserves further. We anticipate Chatham will maintain reserves at very strong levels over the next several years as credit conditions are stable and the town is careful in planning its capital outlay spending. The town has additional flexibility in unused levy capacity, which was \$1.985 million in 2016.

### **Very strong liquidity**

In our opinion, Chatham's liquidity is very strong, with total government available cash at 33.5% of total governmental fund expenditures and 2.1x governmental debt service in 2015. In our view, the town has strong access to external liquidity if necessary.

Our opinion is that liquidity will remain very strong because there is no significant deterioration of cash balances planned or anticipated. Furthermore, we note Chatham does not have any contingent liquidity risk from financial instruments with payment provisions that change on the occurrence of certain events.

### **Weak debt and contingent liability profile**

In our view, Chatham's debt and contingent liability profile is weak. Total governmental fund debt service is 16.3% of total governmental fund expenditures, and net direct debt is 238% of total governmental fund revenue. Overall net debt is low at 1.9% of market value, which is in our view a positive credit factor.

Following this issue, Chatham will have roughly \$111.8 million of total direct debt outstanding. Of that amount, \$28.7 million is related to short-term financing through the Massachusetts Clean Water Trust.

Chatham's debt profile is elevated based on debt issued under its wastewater management plan. As with all

communities on Cape Cod, Chatham was facing pressure from the state and the Environmental Protection Agency to replace existing private septic systems with a public wastewater system to reduce nitrogen levels in the ecosystem. In 2009, the town embarked on a \$210 million plan to install sewer lines throughout the community and expand its treatment plan. Chatham frontloaded much of the debt to take advantage of financing options under recent economic stimulus packages. In the future, the town plans to issue \$10 million-\$15 million every two years until the project is complete in 2040. All of the debt for the wastewater project is being done through debt exclusions, which requires a majority vote of Chatham residents.

Other capital needs are limited as the town has recently completed updates on all of its major public buildings.

Chatham's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 6.2% of total governmental fund expenditures in 2015. Of that amount, 4.1% represented required contributions to pension obligations, and 2.1% represented OPEB payments.

For pensions, the town participates in the Barnstable County Retirement System, a cost-sharing, multi-employer defined-benefit pension plan, which is 60% of the total pension liability. Chatham's proportionate share is \$18.67 million, or 41% of expenditures. While pension costs are manageable, due to the county retirement system's below-average funded ratio, we believe this will likely remain a growing cost over the next few years. An additional long-term credit consideration is the town's long-term OPEB liabilities. As per the most recent information available, the town's OPEB unfunded actuarial accrued liability was \$16.7 million. Chatham recently established a trust to help defray costs associated with rising OPEB expenses. The trust currently has a balance of \$573,000.

### **Strong institutional framework**

The institutional framework score for Massachusetts municipalities is strong.

## **Outlook**

The stable outlook reflects our expectation that Chatham will likely maintain strong reserves. In our view, the town's extremely strong, highly desirable, and diverse property tax base lends stability to property tax revenue, which is its main revenue source. In addition, we expect the town's debt service payments as a percent of general fund expenditures to remain moderate and the overall net debt burden to remain low relative to the market value. For these reasons, we do not expect to change the rating within the two-year parameter of the outlook. Over time, credit factors that could lead toward a negative rating action would be sustained operating deficits and a weaker financial position.

## **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
- 2015 Update Of Institutional Framework For U.S. Local Governments

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