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Summary:

Norfolk, Massachusetts; General Obligation

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Credit Profile		
US$8.125 mil GO rfdg bnds dtd 08/05/2019 due 03/15/2031		
Long Term Rating	AA+/Stable	New

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to Norfolk, Mass.' series 2019 general obligation (GO) refunding bonds. The outlook is stable.

Bond proceeds will be used to refund the series 2011 municipal purpose loan to lower overall debt service requirements. Securing debt service on the bonds is with the town's full faith and credit subject to limitations under Proposition 2 1/2. Despite limitations imposed by the Commonwealth levy limit law, we do not make a rating distinction for the limited-tax GO pledge due to Norfolk's flexibility under the levy limit.

Norfolk is a residential town that benefits from access to the Boston metropolitan statistical area (MSA). Management has consistently produced at least balanced operating results, and despite a small draw of reserves in fiscal 2018, we expect continued balanced operations. While we expect retirement-related costs to rise, we believe management is working to incorporate new financial management tools to ensure continued financial stability.

The long-term rating reflects our opinion of the following factors for the town:

- Very strong economy, with access to a broad and diverse MSA;
- Adequate management, with standard financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with a slight operating deficit in the general fund but break-even operating results at the total governmental fund level in fiscal 2018;
- Adequate budgetary flexibility, with an available fund balance in fiscal 2018 of 7.0% of operating expenditures;
- Very strong liquidity, with total government available cash at 14.2% of total governmental fund expenditures and 3.2x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 4.5% of expenditures and net direct debt that is 68.0% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

Very strong economy

We consider Norfolk's economy very strong. The town, with an estimated population of 11,859, is a primarily residential community approximately 20 miles southwest of Boston in Norfolk 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 159% of the national level and per capita market value of $151,265. Overall, the town's market value grew by 7.7% over the past year to $1.8 billion in 2019. The county unemployment rate was 3% in 2018.

Norfolk is on a Massachusetts Bay Transportation Authority commuter rail line, with Route 1A also providing access to the surrounding areas. While most residents commute to Boston for work, some commute to Providence, approximately 30 miles to the south, and town management reported an increase in the number of permanent telecommuters.

Within Norfolk, the largest employer is the Massachusetts Correctional Institution at Norfolk (about 500 employees). Other large employers include W.T. Holmes Transportation Co. Inc. (150 employees) and Jofran Sales (74). Residential property has historically accounted for the majority of Norfolk's total assessed valuation (AV), with residential AV accounting for 93% of the fiscal 2019 total valuation. Management reports that several new housing developments are either underway or in early discussions, and we expect they will help grow the local tax base. Additionally, management is exploring longer-term options regarding improving water and sewer connections downtown, which could spur new commercial development. We expect Norfolk to maintain a very strong economic base over the next several years, due to its proximity to Boston and stable residential base.

Adequate management

We view the town's management as adequate, with standard financial policies and practices under our FMA methodology, indicating the finance department maintains adequate policies in some, but not all, key areas.

We understand that management is in the latter stages of implementing a new capital improvement plan, along with revised revenue and expenditure forecasting. It has worked with the state's Department of Revenue, Division of Local Services, to develop and implement the revised plans. As the town adopts these new plans and policies, and as they are integrated into the budgeting process, we will continue to re-evaluate the town's policies under our FMA.

While the town has debt and reserve policies, and has been adhering to them, it is not clear that they were incorporated into the decision-making process in the recent past. The debt policy has a minimum principal amount, limits the financing term to the useful life of the asset, limits the ratio of net debt to total AV to 1.5%, limits general fund non-exempt debt to 10% of general fund revenues, and requires 50% of outstanding principal to be repaid within 10 years. The reserve policy requires reserves to be maintained between 5%-10% of general fund revenues, as well as how funds may be used.

The town maintains a formal investment management policy, which mirrors state law. Town management uses several years of revenue data when projecting revenues, and incorporates three years' worth of budget-to-actuals when projecting expenditures. The forward-looking budget process includes the next budgeted year, as well as projections for the following two fiscal years. Budget-to-actuals are reported quarterly to the board, while amendments are permitted only during the twice yearly town meeting days.

The town does not currently have a five-year CIP, but does maintain a 20-year vehicle replacement plan, which management notes represents the majority of the town's capital costs. There is no long-term financial plan. We will continue to revisit our view of management policies as they are revised.

Strong budgetary performance

Norfolk's budgetary performance is strong, in our opinion. The town had slight deficit operating results in the general fund of negative 1.0% of expenditures, but a balanced result across all governmental funds of 0.5% in fiscal 2018.

We adjusted budgetary performance to account for annually recurring transfers into and out of the general fund. Additionally, we adjusted for revenues and expenditures in the elementary school construction fund and the police/dispatch center fund when assessing total governmental funds performance.

Norfolk's management has produced four consecutive strong budgetary results, in our view, with at least balanced operating results over that period. We believe the town's stable revenue profile, with 74% of 2018 general fund revenues derived from local property taxes, aids in revenue predictability. Intergovernmental aid was 18% of general fund revenues, approximately one-third of which was the state's on-behalf payment to the teachers' retirement system. We further believe that management carefully budgets its expenditures and monitors throughout the year, leading to the consistent results.

Management reports that revenues and expenditures are tracking on budget for fiscal 2019 and will likely result in positive operations given expenditure turnbacks. Although the town absorbed an approximately 5% assessment increase from its regional high school, collaboration and coordination with the school district has improved recently, leading to predictable variations in assessments. At this time, management does not expect a major deviation from the budget. We expect at least balanced operations on a GAAP basis, given management's track record and current projections. Consequently, we expect Norfolk to maintain strong budgetary performance over the outlook period.

Adequate budgetary flexibility

Norfolk's budgetary flexibility is adequate, in our view, with an available fund balance in fiscal 2018 of 7.0% of operating expenditures, or $3.0 million.

Due to the draw on reserves in fiscal 2018, along with increasing expenditures, we revised our view of the town's budgetary flexibility to adequate from strong, as available reserves dropped below 8% of general fund expenditures. Given projections for fiscal 2019, we do not anticipate revising our view during the outlook period, as we expect reserves as a percentage of expenditures to remain relatively consistent.

Very strong liquidity

In our opinion, Norfolk's liquidity is very strong, with total government available cash at 14.2% of total governmental fund expenditures and 3.2x governmental debt service in 2018. In our view, the town has strong access to external liquidity if necessary.

Norfolk has demonstrated strong access to external liquidity by issuing GO debt frequently within the past 20 years. The town does not have any variable-rate or direct-purchase debt, nor does it have any contingent liquidity risks from financial instruments with payment provisions that change on the occurrence of certain events. The town's investments are primarily in short-term instruments that mature in less than one year. Therefore, we believe its liquidity profile will likely remain very strong over the next two fiscal years.

Strong debt and contingent liability profile

In our view, Norfolk's debt and contingent liability profile is strong. Total governmental fund debt service is 4.5% of total governmental fund expenditures, and net direct debt is 68.0% 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 issuance, Norfolk will have approximately $32 million in outstanding debt, which includes $935,000 in bond anticipation notes issued for vehicle procurement that it expects to pay off within the next several years. Additionally, it has approximately $1.9 million in self-supporting debt related to the water enterprise fund. We do not expect any material new-money debt issuances within the next few years.

Norfolk's combined required pension and actual other postemployment benefit (OPEB) contributions totaled 5.4% of total governmental fund expenditures in 2018. Of that amount, 4.3% represented required contributions to pension obligations, and 1.1% represented OPEB payments. The town made its full annual required pension contribution in 2018.

Eligible town employees participate in the Norfolk County Retirement System, a cost-sharing, multiple-employer, defined-benefit pension plan. The town has a proportionate net pension liability of $16.8 million. We note that the retirement system lowered its discount rate to 7.75% from 8.0%, but we continue to view this as higher than average. We also view the system's funded ratio of 63.5% as low funded. Given the high discount rate, low funded ratio, and other actuarial assumptions that may be optimistic, we believe pension costs are likely to rise. Should pension costs rise significantly, this could pressure the town's finances. The town has paid its full required contribution each of the last three fiscal years and expects to continue doing so.

The town provides OPEB benefits and historically paid costs on a pay-as-you-go basis. Management reports that it is establishing an irrevocable OPEB trust fund, to which it expects the town will contribute at least $50,000 annually. We generally view a trust fund as a credit positive, but depending on the town's contributions, it remains to be seen if this will materially reduce Norfolk's net OPEB liability in the near term. As of June 30, 2018, the town's net OPEB liability was approximately $21.3 million.

While total fixed costs, including pension and OPEB costs, remain manageable, we believe they will continue to increase, possibly rapidly. If retirement costs as a percentage of expenditures were to rise significantly, we could revise our view of the town's liability and plan for addressing both the liability and annual costs.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Outlook

The stable outlook reflects our view of Norfolk's very strong economy, with access to a broad and diverse MSA, strong budgetary performance, and limited additional capital needs. We do not expect to raise or lower the rating over our two-year outlook horizon.

Downside scenario

Recurring or substantial negative budgetary performance, leading to weakened budgetary flexibility and an available fund balance not in line with similarly rated peers, could result in a lower rating.

Upside scenario

A positive rating change would depend on adoption of formal financial management policies and maintenance of at least strong budgetary flexibility, coupled with the town's wealth and income indicators rising to levels on par with other 'AAA' rated entities.

Related Research

2018 Update Of Institutional Framework For U.S. Local Governments