

## CREDIT OPINION

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## New Bedford (City of) MA

### Update to credit analysis

#### Summary

New Bedford (A1 stable) has a large tax base that continues to grow after significant declines incurred during the recession. The resident income levels are below average while poverty and unemployment are elevated compared to state and US levels. The financial position will remain stable with limited change to reserves and liquidity. Additionally, overall city management is strong, having formal and multi-year financial, capital and debt plans. While the debt burden will likely remain manageable, the pension and OPEB liabilities are significant and will remain a drag on the overall credit profile.

#### Credit strengths

- » Sizeable tax base
- » Strong fiscal management
- » Continued trend of positive economic development

#### Credit challenges

- » Significant pension and OPEB liabilities
- » Below average wealth and income levels with an elevated poverty rate
- » Limited operating flexibility under Proposition 2½

#### Rating outlook

The outlook on the underlying rating reflects continued stability in the city's overall financial operations that is expected to continue over the near term. The city is bolstered by strong management which adheres to comprehensive policies that, if coupled with a trend of improved reserves and continued tax base growth could help mitigate the large long term liabilities and lead to positive rating pressure.

#### Factors that could lead to an upgrade

- » Continued trend of stability in financial operations
- » Growth in general fund reserves and liquidity
- » Continued growth trend in the tax base
- » Maintenance of current debt burden
- » Material decline in the pension liability

## Factors that could lead to a downgrade

- » Increase in the debt burden or pension liability
- » Trend of general fund operating deficits
- » Stagnant tax base valuation

## Key indicators

Exhibit 1

<b>New Bedford (City of) MA</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
<b>Economy/Tax Base</b>					
Total Full Value (\$000)	\$5,818,718	\$5,818,718	\$5,366,954	\$5,366,954	\$5,618,295
Population	94,927	94,873	94,909	94,988	95,032
Full Value Per Capita	\$61,297	\$61,332	\$56,548	\$56,501	\$59,120
Median Family Income (% of US Median)	68.9%	69.5%	69.9%	70.3%	70.3%
<b>Finances</b>					
Operating Revenue (\$000)	\$299,935	\$306,140	\$295,463	\$318,243	\$339,063
Fund Balance (\$000)	\$26,735	\$26,127	\$21,340	\$26,359	\$26,477
Cash Balance (\$000)	\$25,252	\$29,071	\$27,838	\$31,611	\$36,289
Fund Balance as a % of Revenues	8.9%	8.5%	7.2%	8.3%	7.8%
Cash Balance as a % of Revenues	8.4%	9.5%	9.4%	9.9%	10.7%
<b>Debt/Pensions</b>					
Net Direct Debt (\$000)	\$102,699	\$108,196	\$117,503	\$134,069	\$140,176
3-Year Average of Moody's ANPL (\$000)	\$384,223	\$557,953	\$542,923	\$572,809	\$621,617
Net Direct Debt / Operating Revenues (x)	0.3x	0.4x	0.4x	0.4x	0.4x
Net Direct Debt / Full Value (%)	1.8%	1.9%	2.2%	2.5%	2.5%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.3x	1.8x	1.8x	1.8x	1.8x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	6.6%	9.6%	10.1%	10.7%	11.1%

As of June 30 fiscal year end; Net direct debt does not include self supporting wastewater and water fund related debt service

Source: Moody's Investors Service and New Bedford's audited financial statements

## Profile

New Bedford is one of Massachusetts is a major fishing port. The tax base is predominantly residential with a diverse commercial and industrial presence. The city has a population of 94,988 and is located on the southcoast, approximately 56 miles south of Boston.

## Detailed credit considerations

### Massachusetts Qualified Bond Program Enhancement

The enhanced Aa2 rating and stable outlook on the city's bonds reflect the credit enhancement provided by the QBP. The program is a direct payment system whereby the Commissioner of Revenue authorizes the State Treasurer to deduct from the city's monthly state aid payments an amount sufficient to meet the city's debt service on qualified securities.

The State Treasurer acts as the paying agent on the bonds and makes debt service payments directly to DTC. The city is expected to receive aid from the commonwealth totaling more than 13 times total state qualified debt service (based on fiscal 2018 state aid and maximum annual debt service assumptions). We believe the commonwealth's strong commitment to state aid for municipalities and the program's sound payment mechanisms, which do not rely on the trigger of a notice of potential default, enhance the likelihood of full and timely debt service payment.

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The programmatic rating is linked to the Commonwealth of Massachusetts' general obligation rating of Aa1 with a stable outlook.

#### **Economy and tax base: Sizeable tax base with growing economy; below average wealth and income**

New Bedford, located on Buzzards Bay on the southeast shore of Massachusetts, is a local industrial center and a major national fishing port with a deep water harbor. The \$5.6 billion tax base (2017-18 equalized value) is very large compared to the median size for the rating category. Equalized valuation increased 4.7% in 2017, the first positive gain since the recession. Additionally, the 2017 assessed value jumped 6.3%, marking four years of positive growth. Valuations will likely continue to trend upward with modest growth over the near-term, since the housing market is improving and a long-term plan for economic development is now taking root.

New-growth revenue in 2018 was over \$2 million, the strongest year in over ten years. New development is underway across the city from north to south and ranges from smaller entrepreneurial opportunities, downtown redevelopment including a second, new 67 room hotel, and continued redevelopment of old mills into market-rate condos and apartments.

New Bedford's historic identity as a port city will continue to play a critical role in its overall economic health. The city is home to the nation's largest commercial fishing workforce, which contributes to roughly 2% of the commonwealth's GDP. While the fishing industry continues to have its challenges, New Bedford's industry is relatively diverse and stable.

Expanding the use of the port with the recent creation of the southcoast terminal has positioned the city to benefit from offshore wind energy. The site will be used for deployment, operations and training for offshore wind in the coming years. The state has a mandate to develop 1,600 megawatts of wind energy by 2027, and this first procurement could allow for up to 800 megawatts. There are currently three companies that have wind leases south of Martha's Vineyard.

Wealth levels are below average with median family income equal to 70% of the US median. The unemployment rate has improved over the years but still elevated at 5.5% (December 2017) compared to 3.1% of the state and 3.9% of the nation. Additionally, the labor force continues to see year over year growth. The poverty rate of 23% of population below the poverty line and a still elevated unemployment rate continue to dampen the improving economic condition of the city.

#### **Financial operations, reserves and coverage: Stable position expected to continue due to strong fiscal management**

The city's financial position will likely remain stable, subject to improvements in reserves from positive variance in revenues and more volatile expenses like snow and ice and health insurance.

Fiscal 2017 audited results reflect balanced operations in the general fund with a slight \$68,000 operating surplus. The balanced operating result reflects positive variance in both revenues and expenses that offset minimal use of free cash for operating and capital needs. The available general fund balance remained relatively unchanged at \$26.5 million or 7.8% of revenues, below the median for A1 and Aa3 rated municipalities across Massachusetts.

The fiscal 2018 general fund budget increased 3.2% from the prior year driven by pension contributions, health insurance and assessments. The budget was balanced with a tax levy increase to the 2.5% limit plus new growth and a 3.6% increase in state aid. No reserves were used to balance operations. Year-to-date revenues and expenditures are marginally positive compared to budget and the city expects to end the year with around a \$700,000 surplus in the general fund.

The primary revenue source is state aid, representing 55% of 2017 revenues followed by property taxes at 33%. In fiscal 2018, the city had \$4 million in unused levy capacity or 1.2% of revenues, providing some additional operating flexibility under Proposition 2 ½. The city has shown an ability to tap the unused levy capacity; having used around \$5.7 million since 2014. The long range financial forecast (2018-2022) projects balanced operations while maintaining reserves at just over 8% of revenues in 2022.

#### **LIQUIDITY**

Cash and investments at the end of fiscal 2017 were \$36.3 million, or 10.7% of revenues. The cash position covers a limited 89% of the outstanding BANs being issued should market access be an issue at maturity in May 2018. Mitigating the liquidity position is consistent market access over the last five years.

#### **Debt and pensions: Manageable debt burden with large pension and OPEB liabilities**

The direct net debt burden of 2.8% of 2017-18 equalized value and 0.5 times 2017 general fund revenues will remain manageable over the near term given a formal debt policy that will ensure affordability for the city's limited flexibility for capital funding. The net direct

debt remains manageable because of the self supporting nature of the wastewater fund and water fund for which we subtract \$109 million from the total amount outstanding. The gross direct debt, which includes all the self-supporting debt, materially increases to 5.2%. The self-supporting nature of the wastewater and water funds are a key credit factor.

The five-year capital improvement plan (2018-2022) totals \$93.6 million, a material increase from last year largely attributable to more comprehensive project planning and rise in costs. The plan funding sources include \$83.5 million of projects financed through debt issuance. The tax supported debt is expected to keep annual General Fund debt service around 3.5% of expenditures through 2022.

#### DEBT STRUCTURE

The entire debt portfolio is fixed rate with 63% of principal retired in ten years. Fiscal 2017 general fund debt service represented \$11.4 million or a limited 3.4% of general fund expenditures.

#### DEBT-RELATED DERIVATIVES

New Bedford is not subject to any swap agreements or other derivative products.

#### PENSIONS AND OPEB

New Bedford is a member of the City of New Bedford Retirement System, a multi-employer cost-sharing plan for all employees other than teachers and certain administrators who are covered by the state teachers plan through on behalf payments made to the city. The city paid its 2017 actuary determined contribution of \$26.7 million representing 7.9% of expenditures. The 2017 three-year average Moody's Adjusted Net Pension Liability (ANPL), under Moody's methodology for adjusting reported pension data, is \$539 million or an average, 1.6 times revenues but elevated 9.6% of equalized value. The plan funding date is currently 2034.

The city is funding its OPEB liability on a pay-as-you-go basis plus deposits into an OPEB trust. In 2017, the city funded 54% of the ARC, representing \$17.4 million. The total Unfunded Actuarially Accrued Liability is \$485.5 million as of the valuation report dated July 1, 2016. In fiscal 2017 the city adopted a funding policy to make annual contributions equal to 10% of free cash. As of the last valuation, the liability was 0.17% funded.

Total fixed costs in 2017, including debt service, required pension contributions and retiree healthcare payments, represented \$55.5 million or 16.3% of expenditures.

#### Management and governance: Strong city management helps bolster weaker credit constraints of tax base and limited reserves

The city's management team is very strong. The city adheres to comprehensive fiscal policies that have stabilized operations over the last five years and positioned the city to implement a manageable capital plan and project balanced operations over the near term.

Massachusetts cities have an Institutional Framework score of Aa, which is high compared to the nation. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. Massachusetts cities major revenue source, property taxes, are subject to the Proposition 2 1/2 cap which can be overridden with voter approval only. However, the cap of 2.5% still allows for moderate revenue-raising ability. Unpredictable revenue fluctuations tend to be minor, or under 5% annually. Across the sector, fixed and mandated costs are generally greater than 25% of expenditures. However, Massachusetts has public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

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