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Ratings

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Summary:

Andover, Massachusetts; General Obligation

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Summary:

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Credit Profile		
US$11.58 mil GO mun purp loan bnds ser 2020 due 11/15/2050		
Long Term Rating	AAA/Stable	New
Andover GO		
Long Term Rating	AAA/Stable	Affirmed
Andover GO mun purp ln		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' rating to Andover, Mass.' series 2020 general obligation (GO) municipal-purpose loan bonds (approximately $11.6 million) and affirmed its 'AAA' rating on the town's existing GO debt. The outlook on all ratings is stable.

The town's full-faith-and credit pledge, subject to Proposition 2 1/2 limitations, secures the bonds and outstanding GO debt. We rate this issuance based on the application of our criteria "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness," published Nov. 20, 2019. Despite limitations imposed by the commonwealth's levy limit law, we did not make a rating distinction between the town's limited- and unlimited-tax GO pledges.

Andover's GO bonds are eligible for a rating above the sovereign because we think the town can maintain better credit characteristics than the nation in a stress scenario. Under our criteria, titled "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions," published Nov. 19, 2013, the town has a predominately locally derived revenue source with property taxes generating 75% of general fund revenue. The town also has independent taxing authority and treasury management from the federal government.

Officials plan to use series 2020 bond proceeds to fund various capital items and to permanently finance existing short-term debt.

Credit summary

The rating reflects our view that Andover's local economy remains very strong, including its very high wealth levels and overall robust employers, despite the recent regional and national economic recession. The town has historically maintained its reserve levels at about 10% while also adhering to a comprehensive capital improvement plan, funded largely on a pay-go basis. We expect management, with well-embedded financial management policies and practices, will likely continue to produce at least break-even results. We view the town's large pension and other postemployment liabilities as credit factor that is currently manageable, but could present budgetary pressure over the medium-term. Overall, the town has demonstrated a strong trend of stability in key credit factors, which we believe will persist through the slow recovery of the recession. For more information, see "The U.S. Economy Reboots, With

Obstacles Ahead" published Sept. 24, 2020, on RatingsDirect.

The rating also 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 methodology;
- Adequate budgetary performance, with balanced operating results in the general fund and a slight operating surplus at the total governmental fund level in fiscal 2019;
- Strong budgetary flexibility, with an available fund balance in fiscal 2019 of 10.2% of operating expenditures;
- Very strong liquidity, with total government available cash at 30.2% of total governmental fund expenditures and 6.4x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 4.7% of expenditures and net direct debt that is 46.9% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 68.5% of debt scheduled to be retired in 10 years, but a large pension and other postemployment benefit (OPEB) obligation and the lack of a plan to sufficiently address the obligation; and
- Strong institutional framework score.

Environmental, social, and governance factors

The rating incorporates our view regarding the health and safety risks posed by the COVID-19 pandemic. Absent the implications of COVID-19, we consider the town's social risks in line with those of the sector. We analyzed Andover's environmental and governance risks relative to its economy, management, financial measures, and debt and liability profile and determined that all are in line with our view of the sector standard.

Stable Outlook

Downside scenario

Should budgetary performance and flexibility see sustained and significant deterioration, we could lower the rating.

Very strong economy

We consider Andover's economy very strong. The town, with an estimated population of 35,782, is located in Essex County in the Boston-Cambridge-Newton, Mass.-N.H. MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 201% of the national level and per capita market value of $245,906. Overall, the town's market value grew by 5.7% over the past year to $8.8 billion in 2020. While the county unemployment rate was 3.0% in 2019, it has increased as of late due to the COVID-19 pandemic economic closures; the county unemployment was 10.7% in September 2020.

Andover is a primarily residential town, accounting for approximately 81% of total assessed value (AV). The town's location, approximately 25 miles north of Boston, on Interstates 93 and 495, provides residents with access to a broad range of employment opportunities across the deep and diverse MSA economy, with commuter rail stations facilitating travel to Boston and the region.

The town maintains a sizable and diverse high-end economic base; large employers include Raytheon Co. (4,500 employees); the Internal Revenue Service (1,975), which operates a regional service center; Pfizer (1,200); and Putnam Investments (900). Phillips Medical, a previous large employer within the town, relocated elsewhere in 2019; the 140-acre property was sold to Atlantic Management Corp. for $36 million. License and permitting has remained strong, with investment in commercial and residential development demonstrating stability throughout the recession and nascent recovery. The planning and business development office of the town is facilitating strategies to help local restaurants and hotels adjust to the current restrictions resulting from the pandemic, including allocating parking for outdoor dining and assisting with ramping up curbside pickup capacity. In partnership with the Andover Community Trust, the town has also implemented a rental/mortgage assistance program to assist low to middle-income residents financially affected by the pandemic with up to one month (and maximum of $5,000) of overdue or future mortgage costs. The town has dedicated $200,000 of its CARES Act funding to this program.

While we expect some potential softening in the local economy due to the pandemic, overall we expect Andover's economy to remain very strong.

Very strong management

We view the town's management as very strong, with strong financial policies and practices under our Financial Management Assessment methodology, indicating financial practices are strong, well embedded, and likely sustainable.

The town uses identified trends and commonwealth estimates to develop annual revenue and expenditure assumptions, which it then uses to update its five-year budget forecast for complementing capital and budgetary planning. Management regularly monitors its budget, tracks revenue and expenditures, and reports budget-to-actual results to the finance committee at a minimum on a monthly basis. The town is permitted to make midyear budget adjustments, if needed, during special town meetings. It also has a five-year CIP and a capital budget that management approves and reprioritizes annually. The town adheres to a formal debt management policy when planning and addressing capital needs, including a policy that limits debt service in any one year to 10% of budgeted general expenditures, and targets principal amortization at 20 years. It has a formal reserve policy of maintaining reserves between 3% and 7% of expenditures, which it has exceeded recently.

Adequate budgetary performance

We have revised our view of Andover's budgetary performance to adequate from strong, largely due to what we view as uncertainty in the revenue environment during the economic recovery. The town had balanced operating results in the general fund of negative 0.2% of expenditures, and slight surplus results across all governmental funds of 1.1% in fiscal 2019.

The town's fiscal year end is June 30. Its primary revenue source is property tax (75%), followed by intergovernmental revenues (6.9%), and local tax and fee revenues (6.4%).

We adjusted fiscal 2019 budgetary performance to account for recurring transfers and the expenditure of bond proceeds. The town's operational results for fiscal 2019 were positive, resulting in adding approximately $3.8 million to reserves, attributed to conservative budgeting, in particular with positive variances in hotel/motel tax and motor vehicle tax revenues compared to budget.

Fiscal 2020 year-end estimates indicate the town produced another year of positive operational results, adding approximately $3.4 million to reserves. In response to the COVID-19 pandemic stay-at-home mandates, the town implemented a mandatory spending freeze as it anticipated reduced revenues from hotel/motel and motor vehicle taxes. Of the $3.4 million in surplus, $1.8 million of it derived from unspent appropriations. While the town had some unbudgeted expenses related to the pandemic, the operating budget was not affected. The bulk of its COVID-19-related expenses (primarily for personal protection equipment) was funded via grants, however the town has applied for reimbursement from the state for about $380,000 in COVID-19-related expenses. The state has allocated $3.2 million in CARES Act funding to the town for expenses between March 1, 2020 and Dec. 30, 2020.

The town's fiscal 2021 budget is a level services budget, approved by the town at $202 million, an increase of 4% over the fiscal 2020 budget. State officials have committed to level state aid funding in line with fiscal 2020. The balanced budget includes increases in funding for major obligations, including pensions, education and debt service, as well as significantly modified revenues assumptions compared to 2019 estimates for license, meals and hotel/motel tax revenues (reduced by 25%), and motor vehicle tax revenues (reduced by 15%). Despite this, the town maintains its commitment to fund its capital improvement program, which is largely funded on a pay-go basis by dedicating approximately 5% of its budget to cash fund projects.

Given 2020 estimates and management's track record of producing at least balanced results, we believe that general fund and total governmental fund performance should remain stable. However, we believe future pension and OPEB costs could become a budgetary pressure due to the respective funding ratios and closed amortization schedule. Management is actively making budgetary adjustments when needed for these costs and is actively working to reduce the unfunded liability. The town is funding the actuarially determined contribution for pensions and has begun to prefund OPEBs. Nevertheless, we believe these liabilities could strain future operations, particularly if economic conditions worsen and actuary assumptions are not met.

Strong budgetary flexibility

Andover's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2019 of 10.2% of operating expenditures, or $19.7 million.

The town has consistently maintained a strong budgetary flexibility. For fiscal 2020, unaudited results show available reserves at about $21 million, or 10.3% of expenditures. We anticipate Andover's available reserves will remain stable and at levels we consider strong, given the expectation for continued strong budgetary performance and the stable credit environment.

Very strong liquidity

In our opinion, Andover's liquidity is very strong, with total government available cash at 30.2% of total governmental fund expenditures and 6.4x governmental debt service in 2019. In our view, the town has strong access to external liquidity if necessary.

Andover has maintained very strong cash balances over the past three fiscal years. The town does not have any contingent liquidity risk from financial instruments with payment provisions that change on the occurrence of certain events. We do not consider any of the town's investments risky. Additionally, we believe it demonstrated its strong access to external liquidity through its issuance of GO bonds over the past 20 years. We expect Andover's liquidity profile to remain very strong throughout the outlook period.

Strong debt and contingent liability profile

In our view, Andover's debt and contingent liability profile is strong. Total governmental fund debt service is 4.7% of total governmental fund expenditures, and net direct debt is 46.9% of total governmental fund revenue. Overall net debt is low at 1.1% of market value, and approximately 68.5% of the direct debt is scheduled to be repaid within 10 years, which are in our view positive credit factors.

Following this issuance, Andover has approximately $118.6 million of total direct debt. Of that amount, we consider roughly $18.8 million of enterprise-related GO debt self-supporting, based on three years of evidence that user charges have provided partial coverage to support the obligations. The town expects to issue about $115 million over the next two to three years to construct a new school, which has the potential of negatively affecting our view of the town's debt profile.

Pension and other postemployment benefits

- In our opinion, a credit weakness is Andover's large pension and OPEB obligation that is currently manageable but may pressure the rating over the medium to long term.
- In fiscal 2019, Andover's pension contributions did not meet our actual static funding progress or our actual minimum funding progress, indicating the growth of the liability was larger than the pension contribution amount for that year.

Andover participates in the following plans as of June 30, 2019:

- Andover Contributory Retirement System: 43.2% funded, $179.3 million net pension liability.

The town made its full annual required pension contribution in 2019. Andover's combined required pension and actual OPEB contributions totaled 8.2% of total governmental fund expenditures in 2019. Of that amount, 4.9% represented required contributions to pension obligations, and 3.2% represented OPEB payments. The town's net OPEB liability was $127.8 million at the end of fiscal 2019. In 2017, the town began funding an OPEB trust, which was valued at $12.5 million at the end of fiscal 2019, or about 9% of the liability. While we acknowledge the town is actively working to moderate its pension and OPEB liability, we continue to see a potential medium-term risk of increased budgetary pressure from such fixed costs, which could translate to rating pressure over the long-term, in particular if the liability continues to grow.

Strong institutional framework

The institutional framework scorefor Massachusetts municipalities is strong.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019