

## CREDIT OPINION

19 January 2017

New Issue

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## Newton (City of) MA

New Issue - Moody's Assigns Aaa to Newton MA's GOLT Bonds; Outlook Stable

### Summary Rating Rationale

Moody's Investors Service has assigned an Aaa rating to the City of Newton, MA's \$39.5 million General Obligation Municipal Purpose Loan of 2017 Bonds. Moody's maintains a Aaa rating on the city's outstanding general obligation bonds. The outlook is stable.

The Aaa rating reflects the wealthy tax base and diverse, strong regional economy, manageable debt profile and aggressive funding of it's pension liability. The rating also incorporates a long trend of conservative fiscal management with a stable financial position and improving reserves.

### Credit Strengths

- » Sizeable, wealthy and diverse tax base with favorable location and institutional presence
- » Formal financial policies and conservative, multi-year budgeting approach
- » Strong fiscal management including plans to aggressively fund it's pension liability in 2029

### Credit Challenges

- » Limited ability to raise property taxes under Proposition 2 ½
- » Large liabilities for pension and OPEB

### Rating Outlook

The stable outlook indicates our expectation of continued financial stability due to conservative budget forecasting including five year operating and capital plans as well as adherence to comprehensive financial and debt policies. The outlook also incorporates the strength of both the city and regional economies.

### Factors that Could Lead to a Downgrade

- » A multi-year trend of declines in available General Fund balance
- » Increased reliance on free cash appropriations to balance operating budgets
- » Material increase in the debt burden
- » Failure to improve the funding status for long-term liabilities over the medium term

## Key Indicators

Exhibit 1

<b>Newton (City of) MA</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>
<b>Economy/Tax Base</b>					
Total Full Value (\$000)	\$ 22,520,035	\$ 21,757,018	\$ 21,757,018	\$ 22,305,254	\$ 22,305,254
Full Value Per Capita	\$ 264,391	\$ 252,282	\$ 250,239	\$ 252,645	\$ 251,137
Median Family Income (% of US Median)	230.5%	239.2%	239.0%	239.0%	239.0%
<b>Finances</b>					
Operating Revenue (\$000)	\$ 326,882	\$ 347,238	\$ 366,056	\$ 347,913	\$ 373,457
Fund Balance as a % of Revenues	8.3%	8.5%	9.2%	10.2%	14.6%
Cash Balance as a % of Revenues	15.4%	15.6%	17.0%	19.9%	21.7%
<b>Debt/Pensions</b>					
Net Direct Debt (\$000)	\$ 188,320	\$ 189,298	\$ 199,866	\$ 216,517	\$ 260,150
Net Direct Debt / Operating Revenues (x)	0.6x	0.5x	0.5x	0.6x	0.7x
Net Direct Debt / Full Value (%)	0.8%	0.9%	0.9%	1.0%	1.2%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.2x	1.3x	1.4x	1.5x	1.4x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	1.7%	2.1%	2.3%	2.4%	2.4%

As of June 30, fiscal year-end

Full Value = Equalized Value (2017 Equalized Value (\$000) = \$26,223,774)

Source: Moody's Investors Service, City audited financials

## Recent Developments

Since our last report dated [July 14, 2016](#), the fiscal 2016 audit has been finalized and reflects a positive operating position with a \$15 million surplus. The 2017 assessed and equalized values also represent continued growth and strength in the tax base and economy. The debt burden has experienced a modest increase and the pension liability remains relatively unchanged compared to annual revenues. The city has also adopted a formal debt management policy.

## Detailed Rating Considerations

### Economy and Tax Base: City Benefits From Strong Valuation Growth and High Wealth and Income Levels

The \$26.2 billion tax base is the third largest in the commonwealth and includes a diverse residential and commercial composition. We expect it to remain stable over the medium term, benefiting from strong residential growth and a healthy commercial sector. The city has experienced six consecutive years of assessed value growth including 7.5% in 2017. The positive trend increases the five-year compound annual growth rate to 4.4%. Additionally, the two year equalized value increased 17.6% from 2015, marking the largest increase in over ten years. The city has experienced recent commercial expansion and improvement around the Chestnut Hill Mall and Route 9 corridor. Currently, commercial and mixed-use redevelopment is under construction on Needham Street and Wells Ave. Additionally, Rockport Group is the latest footwear company to open a new headquarters in the greater Boston area. Annual new growth revenue in 2017 was healthy at \$4.8 million but down slightly from the historic highs of over \$5 million in 2015 and 2016.

Newton benefits from its prime location just seven miles west of Boston (Aaa stable). The local economy is bolstered by favorable access to public transportation and major regional roadways, as well as the institutional presence of [Boston College](#) (Aa3 stable) and Lasell College. There is also a large healthcare presence in the city, including Newton-Wellesley Hospital, a member of [Partners HealthCare System](#) (Aa3 stable). Wealth and income levels, as indicated by the very strong \$295,256 2017 equalized value per capita and \$156,411 median family income, far exceed commonwealth and national medians. In addition, the city's unemployment rate of 2% (November 2016) continues to trend below the commonwealth (2.6%) and US (4.4%).

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### Financial Operations and Reserves: Stable Financial Position Expected To Continue Over Near Term

We expect the financial position to remain stable over the near term due to conservative budgeting and sound fiscal management. Of note, the reserve position has improved over the last five years to a more appropriate level for the highest rating category. Fiscal 2016 available General Fund balance equaled \$54.6 million or 14.6% of revenues a marked improvement from the very slim levels at the end of fiscal 2012 of \$27.3 million or 8.3% of revenues. The fiscal 2016 audited financials reflect an operating surplus for the fourth year in a row, in the amount of \$15 million (net of bond premium) attributable to a positive variance in revenues primarily improved collection rates of over 100% and strong license and permit fees.

The fiscal 2017 budget increased by 4.7% driven by education, salaries and employee benefits. The budget is balanced with a 4.15% tax levy increase and conservative estimate on local receipts. The budget also includes \$3.9 million in Free Cash appropriations towards capital and equipment needs. Revenues and expenditures through the end of November 2016 are trending on budget with no major variances.

The five-year budget forecast (FY18-22) includes small budget gaps of 0.3% of revenues in fiscal 2018 rising to 3.6% (\$16 million) in 2022. We expect the city to address the minor budget gaps, as they have historically, through operating efficiencies and tight budget controls as the fiscal years approach.

#### LIQUIDITY

The liquidity position is healthy with fiscal 2016 cash and investments totaling \$81.2 million or 21.7% of revenues.

### Debt and Pensions: Manageable Debt Burden; Large But Well-Planned For Pension Liability

The direct debt burden of 1.2% of equalized value will remain manageable due to a comprehensive capital plan, debt exclusions and a recently adopted debt management policy. The overall debt burden increases to 2.3% when incorporating the considerable overlapping debt of the regional transportation, water and wastewater systems. The capital improvement plan (FY18-22) totals \$672.5 million up from \$604 million last year. Bond financing represents \$179.6 million or 27% of project costs not counting mixed financing sources. Currently, the authorized unissued amount is \$63.6 million.

#### DEBT STRUCTURE

All debt is fixed rate and amortization of principal is below average with 49% retired in ten years. Fiscal 2016 debt service represented \$18.6 million or 5.2% of expenditures. At this level the city is in compliance with its new debt policy to maintain debt service between 4% and 7.5% of the annual budget.

#### DEBT-RELATED DERIVATIVES

Newton is not subject to any derivative agreements or interest rate swaps.

#### PENSIONS AND OPEB

The city participates in the Newton Contributory Retirement System, a multi-employer, defined benefit retirement plan. The city's annual contribution for the plan was \$21.7 million in fiscal 2016, or 6% of General Fund expenditures. The city's 2016 three-year average Moody's Adjusted Net Pension Liability, under Moody's methodology for adjusting reported pension data, is \$527.3 million, or an average 1.41 times General Fund revenues. Additionally, the city is committed to an aggressive funding strategy that includes a pension funding date of 2029. While this strategy is a credit positive and a reflection of strong management, the funding will be a challenge given that it requires a 9.6% annual increase in retirement contributions.

Newton also contributed 40% of its annual Other Post Employment Benefit costs in 2016, representing \$19.7 million plus an annual contribution to its OPEB trust. The OPEB UAAL as of July 30, 2016 is a large \$719 million with a current funded ratio of 0.5%. Based on the city's pension funding strategy, the city anticipates eliminating the OPEB liability by 2042.

Total fixed costs for fiscal 2016, including debt service, required pension contributions and retiree healthcare payments, represented \$60 million or 16% of General Fund expenditures.

### Management and Governance: Strong Management; Formal Policies

The city maintains strong fiscal management and governance through conservative budgeting and proactive, long-term financial planning including a five year budget forecast and capital plan as well as formal financial and reserve policies. In December, the city adopted a debt management policy that limits annual debt service in the General Fund to between 4% and 7.5% of the budget.

Massachusetts cities have an institutional framework score of "Aa," or strong. Revenues are highly predictable due to a heavy reliance on property taxes. Cities have a moderate revenue-raising ability given the Proposition 2 ½ levy limit. Expenditures primarily consist of personnel costs, as well as education costs for cities that manage school operations, and are highly predictable given state-mandated school spending guidelines and employee contracts. Cities have a moderate expenditure reduction ability given the high presence of collective bargaining contracts, offset by low fixed costs in most cases.

### Legal Security

The bonds are secured by a general obligation limited tax pledge of the city as all debt service has not been excluded from the levy limitations of Proposition 2 ½.

### Use of Proceeds

Bond proceeds will fund various city capital projects.

### Obligor Profile

Newton is located seven miles west of Boston, MA with a population of 87,000.

### Methodology

The principal methodology used in this rating was US Local Government General Obligation Debt published in December 2016. Please see the Rating Methodologies page on [www.moody.com](http://www.moody.com) for a copy of this methodology.

### Ratings

Exhibit 2

#### Newton (City of) MA

Issue	Rating
General Obligation Municipal Purpose Loan of 2017 Bonds	Aaa
Rating Type	Underlying LT
Sale Amount	\$39,541,000
Expected Sale Date	01/25/2017
Rating Description	General Obligation Limited Tax

Source: Moody's Investors Service

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