

RatingsDirect®

Summary:

Dedham, Massachusetts; General Obligation; Note

Primary Credit Analyst:

Victor M Medeiros, Boston (1) 617-530-8305; victor.medeiros@spglobal.com

Secondary Contact:

Charlene P Butterfield, New York (1) 212-438-2741; charlene.butterfield@spglobal.com

Table Of Contents

Rating Action

Stable Outlook

Credit Opinion

Related Research

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Credit Profile

US\$7.665 mil GO mun purp loan of 2020 bnds dtd 06/22/2020 due 06/15/2050

| | | |
|-------------------------|------------|-----|
| <i>Long Term Rating</i> | AAA/Stable | New |
|-------------------------|------------|-----|

Dedham GO

| | | |
|-------------------------|------------|----------|
| <i>Long Term Rating</i> | AAA/Stable | Affirmed |
|-------------------------|------------|----------|

Rating Action

S&P Global Ratings assigned its 'AAA' long-term rating to Dedham, Mass.' series 2020 general obligation (GO) municipal-purpose loan bonds and affirmed its 'AAA' long-term rating on the town's existing GO debt. At the same time, S&P Global Ratings affirmed its 'SP-1+' short-term rating to the town's outstanding bond anticipation notes (BANs). The outlook, where applicable, is stable.

Dedham's full-faith-and-credit pledge, subject to Proposition 2-1/2 limitations, secures the bonds and BANs. We rate the limited-tax GO debt at the same level of our view of the town, reflected in the unlimited-tax GO bond rating, due to a lack of limitations on resource fungibility available for debt service.

The short-term rating reflects our criteria for evaluating and rating BANs. In our view, Dedham maintains a very strong capacity to pay principal and interest when BANs come due. The town has what we view as a low market-risk profile because it has strong legal authority to issue long-term debt to take out the BANs and it is a frequent issuer that regularly provides ongoing disclosure to market participants.

Officials intend to use series 2020 bond proceeds, totaling roughly \$7.665 million, to finance various capital projects townwide, including the construction of an early childhood education center, along with sewer infrastructure, road reconstruction, and sidewalk projects.

Credit overview

Dedham enters the national recession triggered by the outbreak of COVID-19 with strong budgetary flexibility and well-embedded financial management policies and practices, particularly in the areas of budgeting and planning.

Supporting the 'AAA' rating are Dedham's very high wealth and incomes, and its strong operations exhibited over several years. Prior to the pandemic, Dedham's strong and expanding tax base with employment participation in the broad and diverse Boston metropolitan statistical area (MSA) supported healthy reserves and generally good budgetary performance and operating flexibility.

While we note significant uncertainty around certain revenue shortfalls and potential state aid cuts that could weaken the town's performance as it heads into fiscal year 2021, we understand management has already taken measures to cushion the effects of potential revenue shortfalls and has additional measures at its disposal that it could implement should these cuts happen. Lending further stability to the rating and the outlook are the town's very strong liquidity

and stable revenue mix, with the predominant revenue stream of property taxes, with collections generally upward of 99% during the fiscal year payable.

While we recognize the reserves have come down over the past few years; they remain above average relative to 'AAA' rated communities in the commonwealth. Moreover, much of the decline reflects Dedham's proactive approach to funding its unfunded retirement liabilities, along with other major capital items, and not due to budgetary stress. Long-term fixed costs are manageable with this bond offering and are likely to grow over the near-to-immediate term with additional debt plans on the horizon. Nevertheless, we believe the town has the financial wherewithal to absorb any increases in required debt, pension contributions, and pay-as-you-go health care costs into the annual levy. Its tax rate remains affordable and in line to other similarly rated peers. In addition, the town maintains a sizable unused levy capacity, which will cater to gradual budgetary growth, and we note management has shown a willingness to increase the tax levy when necessary. That said, given that there is still much uncertainty related to the potential effects of COVID-19 and the ensuing economic recession on the town's finances, we will continue to monitor for any material adverse effects throughout the outlook period. (For more information on S&P Global Economics' latest forecast, see the article "An Already Historic U.S. Downturn Now Looks Even Worse," published April 16, 2020 on RatingsDirect.)

Dedham's GO bonds are eligible to be rated above the sovereign because we believe 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 roughly 75% of general fund revenue derived from property taxes with independent taxing authority and treasury management from the federal government.

Additional rating factors include our opinion of Dedham's:

- Very strong economy, with access to a broad and diverse MSA;
- Very strong management, with strong financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could improve in the near term relative to fiscal 2019, which closed with an operating deficit in the general fund and a slight operating deficit at the total governmental fund level in fiscal 2019;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2019 of 23% of operating expenditures;
- Very strong liquidity, with total government available cash at 27.8% of total governmental fund expenditures and 3.3x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability position, with debt service carrying charges at 8.5% of expenditures and net direct debt that is 74.4% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

Environmental, social, and governance (ESG) factors

Our rating incorporates our view regarding the indirect risks posed by the COVID-19 pandemic. Absent the implications of COVID-19, we consider the city's social risks in line with those of the sector. In addition, we view the

town's governance risks as being generally in line with those of peers, although we note management's pension funding discipline and proactive approach to managing its other postemployment benefit (OPEB) liabilities have led to funding levels above that of state peers. Dedham is land-locked with no significant bodies of water that pose an abnormal risk for the community. We view environmental risks as being generally in line with the sector standard.

Stable Outlook

Downside scenario

We could lower the rating if financial performance were to deteriorate significantly, leading to a sharp draw on reserves, or if costs related to long-term liabilities increase at a faster pace and squeeze out other expenditures, pressuring operations and reserves over a sustained period.

Credit Opinion

Very strong economy

We consider Dedham's economy very strong. The town, with an estimated population of 25,813, is in Norfolk County in the Boston-Cambridge-Newton MSA, which we consider broad and diverse. It has a projected per capita effective buying income of 163% of the national level and per capita market value of \$212,230. Overall, market value grew by 7.7% over the past year to \$5.5 billion in 2020.

Despite the recessionary economic effects stemming from the pandemic, we believe the town's sizable tax base is poised for additional growth, in our view, due to ongoing developments in the pipeline, albeit at a more muted pace. Since 2016, assessed valuation (AV) grew 26%. In addition, we note the strength of Dedham's tax base and general economic make-up, do not fully account for the presence of some wealthy tax-exempt private schools and a sizable not-for-profit assisted-living center. The tax base is very diverse, in our opinion. Roughly, 80% of the tax base is residential with the 10 leading taxpayers accounting for about 10.5% of AV.

The county unemployment rate was 2.5% in 2019. Despite this very low figure, rapidly evolving economic conditions due to the pandemic have already affected the labor market (see "U.S. Jobs Market Buckles Under The Coronavirus Pandemic," published April 2, 2020). While the economy showed resilience in the past recession, high unemployment, particularly if it exceeds 10%, is a risk. We will monitor the long-term effects of the current downturn on the labor market and the economy overall.

Very strong management

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

Assessment strengths include management's:

- Regular budget monitoring with formal monthly reports on budget-to-actual results to the town manager and council;
- Formal, five-year financial plan based on revenue and expenditure assumptions from past performance;

- Annually updated, five-year capital improvement plan with identified projects and funding sources and budgetary costs linked to the town's five-year financial plan;
- Formal investment-management policy stipulated in the town's charter;
- Debt management policy of maintaining debt service at a 10% operating budget ceiling; and
- Formal operating reserve policy of maintaining stabilization reserves equal to 5%-10% of the operating budget.

Adequate budgetary performance

Due to the sudden rapid economic deterioration, our assessment incorporates heightened near-term uncertainty that exists due to the recessionary pressures related to the COVID-19 pandemic and resulting financial pressures.

Dedham's budgetary performance assessment as it enters fiscal 2021 is adequate, in our opinion. The town had deficit operating results in the general fund of negative 1.8% of expenditures, and slight deficit results across all governmental funds of negative 0.8% in fiscal 2019.

Budgetary performance metrics include adjustments for recurring transfers and one-time capital expenditures paid for with bond proceeds. In general, over the last several years, operating performance has been stable, although reserves have come down from previous highs. The town has been using its fund balance to support ongoing capital planning initiatives, and has electively made payments to the retirement system above annual requirements to reduce the unfunded liability. While this has lowered overall reserves, they remain healthy and above those of similarly rated peers.

On a budgetary basis, revenues have generally outperformed the budget and management has done well managing costs. Throughout the pandemic, Dedham has implemented a hiring and discretionary spending freeze, with any savings rolled into any potential shortfalls in fiscal 2021 should there be reductions in state aid, which we believe is likely. As a result, despite some anticipated revenue declines, the town is realizing expenditure savings across several departments that should cushion its operations without dipping deeply into reserves. Currently, it is estimating balanced operations as it plans for the fiscal 2021 budget, but current projections again suggest a roughly \$2.9 million reduction in overall reserve balances, due to the town having budgeted for the use of reserves to support capital expenditures.

Favorably, property taxes generate nearly three-fourths of general fund revenue, and collections remain very strong. Other local receipts, such as motor-vehicle excise taxes and building permits will be under pressure due to the pandemic, however. State aid will also be under pressure, although this revenue accounts for roughly 8% of the general fund. While the budget is not yet adopted, management has taken up several measures that will likely result in budgetary performance remaining, at least, adequate, over the next year. Notably, pensions, OPEBs, and other fixed costs, are well contained and manageable, in our opinion.

Very strong budgetary flexibility

Dedham's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2019 of 23% of operating expenditures, or \$27.6 million. When factoring in a \$2.9 million total fund balance decline in fiscal 2020, available reserves remain very strong at approximately 20% of operating expenditures.

Management is anticipating maintaining reserves at very strong levels. While not currently factored into our

assessment, the town also maintains a growing unused levy capacity that exceeds \$9.1 million for fiscal 2019, allowing management to raise the levy above levy limitations without electorate approval. This provides additional revenue enhancement support in future town budgets should economically sensitive revenues remain weak.

Very strong liquidity

In our opinion, Dedham's liquidity is very strong, with total government available cash at 27.8% of total governmental fund expenditures and 3.3x governmental debt service in 2019. In our view, the town has strong access to external liquidity if necessary.

We believe liquidity will likely remain very strong because there is no expectation of significantly deteriorated cash balances. The town also maintains strong access to external liquidity by frequently issuing debt for capital projects. In addition, we note Dedham is not aggressive with its investments. The town does not currently have any variable-rate or direct-purchase debt, reducing its contingent liquidity risk exposure.

Adequate debt and contingent liability profile

In our view, Dedham's debt and contingent liability profile is adequate. Total governmental fund debt service is 8.5% of total governmental fund expenditures, and net direct debt is 74.4% of total governmental fund revenue. Overall net debt is low at 1.8% of market value, which is, in our view, a positive credit factor.

Following this issuance, the town will have \$96.9 million of debt outstanding. Our debt assessment includes \$28 million medium-term debt plans for a public safety building during the next few fiscal years.

Pension and other postemployment benefits

- We do not view pension and OPEB liabilities as a source of credit pressure for Dedham, given that that costs are manageable and affordable given the strength of the town's revenue base.
- Because of changes to Dedham's underlying assumptions to a more conservative posture, unfunded ratios have come down as a result. Nevertheless, we believe, the underlying changes limit the chance of unexpected contribution escalations.
- Furthermore, OPEB liabilities are generally funded on a pay-as-you-go basis, which, given claims volatility as well as medical cost and demographic trends, is likely to lead to escalating costs. The town, however, has established a trust, fully funds it, and currently maintains a healthy OPEB balance.

Dedham's combined required pension and actual OPEB contributions totaled 8.3% of total governmental fund expenditures in 2019. Of that amount, 3.9% represented required contributions to pension obligations, and 4.3% represented OPEB payments. The town made 100% of its annual required pension and OPEB contribution in 2019.

Dedham contributes to a cost-sharing, multiple-employer, defined-benefit pension plan administered by Dedham Contributory Retirement Board. The plan had a net fiduciary position of 78.9%, as of the measurement date of Dec. 31, 2018, and a net pension liability of \$35.4 million. Notably, the town revised several assumptions that reduced funded ratios. It reduced the investment rate of return from 7.5% to 7.25%. In addition, changes to the valuation report reflected revised mortality assumption, and investment losses. These changes resulted in the town pushing back its plan for fully funding the plan through 2030.

While Massachusetts requires all pension systems to achieve full funding no later than 2040, Dedham remains well

ahead of schedule, and maintains a reasonably well-funded ratio. We generally view closed amortization schedules as positive, and note that the town has been meeting our static funding metric in the most recent year, and our minimum funding progress calculation, indicating that the system's funded ratios may dramatically improve over time.

In addition, Dedham maintains an OPEB liability of \$52 million, assuming a 7.5% discount rate. At June 30, 2018, the OPEB plan was 27% funded. Notably, the town has been funding 100% of its required contribution. We expect the plans' annual cost to remain level.

Strong institutional framework

The institutional framework score for 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

| Ratings Detail (As Of June 5, 2020) | | |
|---|------------------|----------|
| Dedham GO BANs ser 2019 dtd 04/04/2019 due 06/04/2020 | | |
| <i>Short Term Rating</i> | NR | Affirmed |
| Dedham GO (AMBAC) | | |
| <i>Unenhanced Rating</i> | AAA(SPUR)/Stable | Affirmed |
| Dedham GO (MBIA) (National) | | |
| <i>Unenhanced Rating</i> | AAA(SPUR)/Stable | Affirmed |

Many issues are enhanced by bond insurance.

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