

07 Jul 2020 | New Issue

Fitch Rates Hingham, MA's \$104 Million GO Water Bonds 'AAA'; Outlook Stable

Fitch Ratings-New York-07 July 2020:

Fitch Ratings has assigned an 'AAA' rating to the following Town of Hingham, MA general obligation (GO) bonds:

--\$104,095,000 GO Water Bonds, Series 2020.

In addition, Fitch has affirmed the following Town of Hingham ratings:

--Issuer Default Rating (IDR) at 'AAA';

--\$48 million outstanding GO bonds at 'AAA'.

The Rating Outlook is Stable.

The bonds are expected to sell via negotiated sale the week of July 13. Proceeds will be used to purchase the assets of the Hingham Water Company for supplying the town with water.

SECURITY

The bonds are general obligations of Hingham backed by its full faith and credit. Property taxes levied by the town are subject to limitation by the Proposition 2 1/2 statute, unless voters approve the exclusion of debt service on the bonds from the limitation. A portion of the town's outstanding bonds are exempt from the limitations of Proposition 2 1/2.

ANALYTICAL CONCLUSION

The 'AAA' IDR and general obligation bond ratings reflect Fitch's expectation for the town of Hingham to maintain healthy financial flexibility through both the current downturn and future economic cycles, consistent with a history of strong operating performance and sound reserves. The town's robust financial profile reflects a wealthy property tax base, modest expenditure

growth and a demonstrated ability to reduce expenditures during economic downturns. Hingham's long-term liability burden as a percentage of the resource base is low, even when incorporating the series 2020 bonds, which Fitch considers self-supporting from water system user fees.

Economic Resource Base

Hingham is a wealthy residential suburb of Boston located in Plymouth County about 15 miles south of Boston on the Atlantic coast. The estimated 2019 census population of 24,679 is up over 11% since 2010. The town's proximity to Boston has helped to support tax base and population growth over the last decade.

KEY RATING DRIVERS

Revenue Framework::'aaa'

Fitch expects Hingham to realize continued strong revenue growth based on anticipated appreciation of its existing tax base and expansion driven by new investment. The town's independent legal ability to raise revenues within the statutory cap is substantial in comparison to the very low level of historical revenue volatility.

Expenditure Framework::'aa'

Fitch expects the natural pace of spending growth to be in line with revenue growth over time. Carrying costs for long-term liabilities claim a moderate proportion of governmental spending. The town has demonstrated the flexibility and willingness to cut spending during economic downturns.

Long-Term Liability Burden::'aaa'

Hingham's long-term liability burden for debt and Fitch-adjusted net pension liabilities is low at 5% of personal income. Fitch's long-term liability burden analysis excludes the current bond issuance as self-supporting debt. The agency views the town's plan to support debt service entirely from water system operations as achievable. The long-term liability burden would remain consistent with a 'aaa' assessment even if the current issuance were included. Fitch anticipates that the

burden will remain low with modest expected future debt offsetting the risk of growth in the pension liability.

Operating Performance: 'aaa'

The town's high inherent budget flexibility and strong general fund balance position it to manage through downturns with a robust level of fundamental financial flexibility. Management's conservative budgeting practices have helped to support the town's favorable operating performance and strengthening of reserves through the recent recovery period positioning it well to withstand the current downturn.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Not applicable for issuers with a 'AAA' rating.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A sustained increase in the town's long-term liability burden to greater than 10% of personal income due to changes in the town's NPLs, or debt issuance beyond Fitch expectations combined with the charging of insufficient water system rates to fully cover system related debt service costs from operations;

--A sustained decline in unrestricted general fund balance to levels that provide more limited gap closing capacity with an expectation for slow recovery.

Best/Worst Case Rating Scenario

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit

[<https://www.fitchratings.com/site/re/10111579>].

CURRENT DEVELOPMENTS

The ongoing outbreak of coronavirus and related government containment measures worldwide create an uncertain global environment for U.S. state and local governments and related entities in the near term. While Hingham's most recently available fiscal and economic data may not fully reflect impairment, material changes in revenues and expenditures are occurring across the country and are likely to worsen in the coming weeks and months as economic activity suffers and public health spending increases. Fitch's ratings are forward-looking in nature, and Fitch will monitor developments in state and local governments as a result of the virus outbreak as it relates to severity and duration, and incorporate revised expectations for future performance and assessment of key risks.

In its baseline scenario, Fitch assumes sharp economic contractions hit major economies in the first half of 2020 at a speed and depth that is unprecedented since World War II. Sequential recovery is projected to begin from 3Q20 onwards as the health crisis subsides after a short but severe global recession. GDP is projected to remain below its fourth quarter 2019 level until mid-2022. Additional details, including key assumptions and implications of the baseline scenario and a downside scenario, are described in the April 2020 reports titled, "Fitch Ratings Coronavirus Scenarios: Baseline and Downside Cases - Update" (<https://www.fitchratings.com/site/re/10120570>) and "Fitch Ratings Updates Coronavirus Scenarios for U.S. State and Local Tax-Supported Issuers" on www.fitchratings.com.

Hingham Coronavirus Implications

Prior to the pandemic, the town was experiencing surplus operations due to positive variances in snow removal costs and a reorganization of the town's engineering department. Following state and local emergency declarations in March, the town transitioned to remote operations and instituted expenditure controls for both municipal and school operations. The town deferred non-essential hiring and some capital purchases. Management does not report any material revenue reductions since the implementation of stay at home orders, and estimates ending its June 30, 2020 fiscal year with a \$1.5 million net-operating surplus. Fitch considers the town's liquidity position as strong, with Hingham reporting about \$40 million in cash in the general fund and an additional \$15.1 million available from non-major funds. These levels are similar to fiscal end 2019, when general fund unrestricted fund balances were \$37 million or 32% of spending.

The adopted budget for fiscal 2021 shows modest property tax and other revenue declines, and conservative assumptions for reductions in state aid. The budget includes a plan to implement

cost reduction measures should annualized revenues materially underperform expectations. In addition to spending controls, the budget provides for the utilization of about \$3.3 million in fund balance to help offset projected revenue declines. Should revenues decline beyond budgeted expectations and threaten operational balance, the town would impose additional spending cuts to school and municipal departments.

Water System Purchase

Since 2012, the town of Hingham has been engaged in the process of evaluating the feasibility of the acquisition of the privately held water company servicing the town residents of Hingham, Hull and a portion of North Cohasset. The feasibility study was prompted by a series of water main breaks and resident critiques of the relatively high rates compared with other Massachusetts towns. Management reports they had the fifth highest water rates in the state in 2012. An 1879 statute from the initial creation of the private town water company provided the town with the option to purchase the system at any time subject to a two-thirds affirmative vote by town meeting. Following a year of study, which indicated that town ownership was feasible, they were engaged in litigation with the water company for about five years to determine the purchase price, which is set at \$107.7 million plus a \$3.2 million reimbursement for capex that occurred during the good husbandry period.

The acquisition of the water system is expected to be completed on or about July 31, 2020. The town has signed a five year contract with a water system operator (Suez Water Services) with a five-year renewal option. Following the acquisition, the town plans to complete a rate structure study and a capital study. The Hingham Board of Selectmen will serve as the town's water commissioners, and are permitted to set rates at any time without limit or additional state or regulatory approval. Annual capital spending for the system has initially been budgeted at \$2.7 million a year, an increase from an estimated \$1.4 million in annual capital spending incurred by the private water company over the last decade. As part of the acquisition, the town will create an enterprise fund for the system with system-related debt service expected to be paid from net-operating revenues but backstopped by a general obligation commitment. The town has stated its intention to fully support the debt service on the series 2020 bonds from water system user fees, and Fitch views this commitment as reasonable given the recent positive operating history of the private water system and the town's financial projections following the acquisition. In addition to the town of Hingham, the water system will continue to service a portion of the towns of Hull and Cohasset as well.

CREDIT PROFILE

The town's market value per capita is a very high \$322,000, highlighting the desirable geographic location in the greater Boston metro-area. Healthcare, retail and service-related industries employ the largest percentage of people, with Blue Cross & Blue Shield the largest employer, followed by the town, the retirement/senior living community of Linden Ponds and the retailer Talbots.

Revenue Framework

Real and personal property taxes are the largest revenue source and made up roughly 70% of the fiscal 2019 general fund revenues. Intergovernmental revenues, primarily for education, account for about 10% of revenues. Motor vehicle and boat registration excise taxes represent another 4% of revenues.

Over the last decade, general fund revenues have increased at over a 4% CAGR, exceeding U.S. GDP growth for the same period. The strong growth is due to a combination of solid tax base appreciation and new investment. Fitch expects this trend of strong growth to continue due to the strong regional economy and housing market as evidenced by 3%-5% annual home price growth in recent years.

Pursuant to state law, Proposition 2 1/2 limits the town's ability to levy property taxes by a "levy ceiling," an absolute cap on the level of property taxation, set at 2.5% of the overall property tax valuation, and a levy limit that restricts the annual growth in taxation by a 2.5% increase over the previous year's levy plus the value of new growth. Taxation in excess of the levy limit requires voter approval. Declines in equalized value lower the "levy ceiling" and vice versa. The town levy ceiling (currently \$187 million) is very high compared with its fiscal 2020 tax levy (\$86 million) due to continued growth in value over the years.

Management has historically levied close to the full 2.5% levy increase each year. Any excess in levy capacity is carried forward and available for use at any time. The town's excess capacity available for the fiscal 2021 budget is \$549,725, less than 1% of fiscal 2020 budgeted revenues. Additionally, the town's debt service on its voted debt can be excluded from Proposition 2 1/2 limits.

Expenditure Framework

The bulk of general fund spending is associated with education at roughly 46% of total

expenditures followed by public safety spending at 12%. School spending is above the minimum level required by the Commonwealth.

General fund expenditure growth has historically been in line with revenue growth and the town has flexibility to reduce expenditures if necessary. Growth is expected by Fitch to continue at this same pace.

Total fixed carrying costs for debt, pensions and OPEB were a manageable 15% of fiscal 2019 governmental spending. Principal on governmental debt amortizes at a rapid pace of 78% over ten years. Modest growth in future pension and OPEB contributions has occurred the past five fiscal years will likely continue with changes to be offset by overall growth in the expenditure base and should not materially affect the metric.

The town's workforce environment contributes to its solid level of expenditure flexibility. Employee labor contracts are expected to be favorable to management in a fiscal downturn and are not subject to binding arbitration. Union contracts are flexible with no minimum manning requirements and management has the ability to reduce staff at any time if necessary.

Long-Term Liability Burden

The town's long-term liability burden for net-debt and Fitch-adjusted NPLs represents a low 5% of residents' personal income. The town, while small, maintains a significant resource base as measured by the elevated personal income levels at greater than \$100,000 per capita, as estimated by Fitch. Debt (including a small portion of overlapping debt) makes up about half of the overall liability burden.

Inclusion of the series 2020 GO water bonds would increase the metric to 8%, a level that supports an 'aaa' assessment. Fitch typically excludes self-supporting debt from user fees from the long-term liability burden assessment. While the town manages its own public power and sewer, Hingham management does not have experience managing a water system and Fitch notes potential risks regarding the outcome of the completion of a capital study and a rate study that will follow the acquisition of the system. If study outcomes materially differ from expectations and require significant additional debt issuance, Fitch expects management will take appropriate action to adjust user rates to support all system debt from operations. Actions contrary to this expectation could lead to Fitch considering the water system debt as not self-supporting and

incorporate it more directly into the town's long-term liability burden assessment.

The Fitch-adjusted NPLs are about 3% of personal income. The town is the primary member of the Hingham Contributory Retirement System (HCRS), a cost-sharing multiple-employer defined benefit plan. All town employees participate in HCRS, except teachers who participate in the Commonwealth-administered Teachers' Retirement System for which the town has no liability or contribution requirements. The HCRS ratio of assets to liabilities is 68% based on the system's 7.5% rate of return assumption but drops to a relatively weak 58% using Fitch's 6% discount rate assumption. The small size of the NPL compared to the resource base and the town's consistent full actuarial contributions mitigate this concern.

The town's net OPEB liability is roughly 3% of personal income. Fitch views positively the town's efforts to manage its future OPEB liability costs through the establishment of a trust. As of fiscal 2019 the trust contains \$15.9 million compared to the \$85.8 million total liability.

Operating Performance

Fitch believes Hingham is well-positioned to manage the challenges associated with the current economic downturn while maintaining a high level of fundamental financial flexibility. The town's robust reserves, solid revenue raising ability and demonstrated willingness to utilize it, moderate fixed carrying costs and strong control over other expenditures afford the town substantial gap-closing capacity. Fitch's FAST model suggests Hingham's revenues appear less susceptible to economic downturns than most other local governments, suggesting a lower likelihood of significant revenue declines in the near term that would materially weaken the town's financial flexibility.

The town implemented a revised general fund balance policy in 2013 of 16%-20% of expenditures and has consistently exceeded that level every year since. At fiscal year-end 2019, a general fund net operating surplus after transfers of about \$2.8 million improved the unrestricted fund balance to \$37 million or a healthy 32% of general fund spending. Management uses conservative budgeting practices and has previously reduced departmental expenses during periods of economic stress. Fitch expects similar actions to occur if necessary during the current and future economic downturns.

In addition to the sources of information identified in Fitch's applicable criteria specified below,

this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

The highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Contacts:

Primary Rating Analyst

Patrick Goggins,

Analyst

+1 646 582 4695

Fitch Ratings, Inc.

Hearst Tower 300 W. 57th Street

New York 10019

Secondary Rating Analyst

Kevin Dolan,

Director

+1 212 908 0538

Committee Chairperson

Eric Kim,

Senior Director

+1 212 908 0241

Media Relations: Sandro Scenga, New York, Tel: +1 212 908 0278, Email:

sandro.scenga@thefitchgroup.com

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Applicable Criteria

[U.S. Public Finance Tax-Supported Rating Criteria \(pub. 27 Mar 2020\) \(including rating assumption sensitivity\)](#)

Applicable Model

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST States & Locals - Fitch Analytical Stress Test Model, v2.4.0 (1)

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