

Summary:

**Fitchburg, Massachusetts; General
Obligation; Non-School State
Programs; Note**

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Credit Profile

US\$14.7 mil GO BANs dtd 06/21/2019 due 06/19/2020

<i>Short Term Rating</i>	SP-1+	New
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US\$5.15 mil GO st qual mun purp loan 2019 bnds due 06/01/2039

<i>Long Term Rating</i>	AA/Stable	New
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<i>Underlying Rating for Credit Program</i>	A+/Positive	New
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Fitchburg GO state qualified muni purp loan of 2016 bnds ser 2016 due 09/01/2027

<i>Long Term Rating</i>	AA/Stable	Current
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<i>Underlying Rating for Credit Program</i>	A+/Positive	Outlook Revised
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Rationale

S&P Global Ratings revised its outlook to positive from stable and affirmed its 'A+' underlying rating on Fitchburg, Mass.' outstanding general obligation (GO) debt. At the same time, we assigned our 'A+' underlying rating to the city's 2019 GO state qualified municipal purpose bonds. The outlook is positive.

Furthermore, we assigned our 'AA' long-term rating to the 2019 GO bonds. The long-term rating reflects the state program rating. Additionally, we assigned our 'SP-1+' short-term rating to the city's GO bond anticipation notes (BANs) dated June 21, 2019 and payable June 19, 2020.

The positive outlook reflects our belief that there is at least a one-in-three chance we will raise the underlying rating during the two-year outlook period. The city's economic growth and consistent, conservative budgeting has led to a material increase in reserve levels. Over the next two years, should management continue to produce year-end results similar to what it has over the past few years, along with continued economic growth, we could raise the rating.

The short-term rating on the notes reflects our criteria for evaluating and rating BANs. In our view, Fitchburg maintains a very strong capacity to pay principal and interest when the notes come due. We view the city's market risk profile as low because it has strong legal authority to issue long-term debt to take out the notes and is a frequent debt issuer that regularly provides ongoing disclosure to market participants. We understand officials intend to use proceeds from the notes to temporarily finance various citywide capital projects, including updates to utility system infrastructure, airport and municipal parking garage improvements, and school building repairs.

The long-term rating reflects our assessment of the security provided by the Massachusetts Qualified Bond Act. Under the Qualified Bond Act (Massachusetts General Law, Chapter 44A), approval by the Municipal Finance Oversight Board, which oversees and monitors the program, is required. Once a participant is approved, the state treasurer pays debt service directly to the paying agent from money withheld from the borrower's annual state aid appropriation. If

necessary, the state treasurer advances debt service from legally available funds and withholds the amount paid from aid payable to the municipality. There is no appropriation risk related to the debt service payment. Given the law's provisions, we view the state's obligation to pay debt service identical to the commonwealth's unconditional debt obligation, and therefore we rate the program on par with Massachusetts' GO debt. Therefore, the long-term rating will move in tandem with the state GO rating. (For more information on the creditworthiness of the commonwealth, please refer to the full analysis on Massachusetts, published April 9, 2018, on RatingsDirect.)

The underlying rating reflects the application of our criteria, titled "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness" (published Jan. 22, 2018). The city's full faith and credit pledge, subject to limitations of Proposition 2-1/2, secures the series 2019 BANs and bonds and the city's outstanding GO debt. Despite limitations imposed by the commonwealth levy limit law, we did not make a rating distinction between the limited-tax GO pledge and Fitchburg's general creditworthiness because the tax limitation imposed on the city's ability to raise revenue is already embedded in our analysis of the city's financial and economic conditions.

The underlying rating further reflects our view of the following factors for the city:

- Adequate economy, with projected per capita effective buying income (EBI) at 78.1% and market value per capita of \$62,819, though that benefits from access to a broad and diverse metropolitan statistical area (MSA);
- Adequate management, with standard financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2018;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2018 of 16% of operating expenditures;
- Very strong liquidity, with total government available cash at 32.5% of total governmental fund expenditures and 12.0x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability position, with debt service carrying charges at 2.7% of expenditures and net direct debt that is 44.3% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value, but a large pension and other postemployment benefit (OPEB) obligation and the lack of a plan to sufficiently address it; and
- Strong institutional framework score.

Adequate economy

We consider Fitchburg's economy adequate. The city, with an estimated population of 41,000, is in Worcester County, approximately 46 miles west of Boston and 25 miles north of Worcester. It is in the Worcester MSA, which we consider to be broad and diverse. The city has a projected per capita EBI of 78.1% of the national level and per capita market value of \$62,819. Overall, market value grew by 8.9% over the past year to \$2.6 billion in 2019. The county unemployment rate was 3.5% in 2018.

Fitchburg is a primarily residential and historically industrial community that benefits from access to regional employment opportunities in Worcester, where many residents commute for employment. Major employers include Fitchburg State University (500 employees), Demoulas Supermarket (460), Great Wolf Lodge (445), the Montachusett

Opportunity Council (280), and Highlands Long-Term Care Center (268).

The city continues to see growth in its commercial and residential base. Officials report several housing developments have recently been occupied, with additional residential projects in the pipeline. Marijuana businesses have applied for licenses in the city, with three growing operations currently open and with additional applications for retail and growing operations working through the permitting process. Officials continue to work to spur development in the city's downtown through streetscaping and quality of life improvements. Recent downtown projects include Fitchburg State's video game lab and entrepreneur center, along with an artists' community, which includes 60 live and work spaces.

We believe officials will continue to leverage state grants, along with local investment to promote private development. We expect further growth in the tax base and income levels, but expect that the city's economy will remain adequate throughout the outlook period.

Adequate management

We view the city's management as adequate, with standard financial policies and practices under our FMA methodology, indicating the finance department maintains adequate policies in some, but not all, key areas.

In development of its annual budget, the city analyzes three-to-five years of historical trends to form its revenue and expenditure assumptions. When available, the city consults outside sources, such as the governor's proposed municipal aid budget, which typically provides a more conservative estimate of state revenue for the upcoming budget year. In addition, management reviews budget requests submitted by city department heads and prioritizes expenditures that will be incorporated in the mayor's proposal to the city council.

During the fiscal year, management reviews performance trends regularly and shares monthly budget-to-actuals to the mayor, city council, and all department heads. The council can make adjustments and amend the budget on the mayor's recommendation, as required by ordinance. Fitchburg also maintains an informal five-year capital improvement plan and has a formal investment policy with monthly reporting on earnings and holdings to the council. There is no debt management policy outside of state guidelines, and management does not perform formal revenue and expenditure forecasting. The city does not have a formal reserve policy outside of an informal 5% target for stabilization.

Strong budgetary performance

Fitchburg's budgetary performance is strong, in our opinion. The city had operating surpluses of 2.2% of expenditures in the general fund and 3.3% across all governmental funds in fiscal 2018. General fund operating results of the city have been stable over the last three years, with results of 0.9% in 2017 and 2.5% in 2016.

We adjusted budgetary performance to account for recurring transfers and expenditure of bond proceeds. The city has consistently produced positive operating results over the past few years. We believe management's use of conservative revenue projections and budget monitoring have yielded historically stable financial operations. The general fund surplus for the fiscal 2018 was mainly due to conservative budgeting, which led to better-than-budgeted revenue and departments not fully expending budgeted appropriations. The city also recognized savings due to retirements and health insurance cost savings.

Management reports that fiscal 2019 budget-to-actual variances are favorable, with revenues exceeding budget by approximately \$2.5 million, and with expenditures at least break even. The adopted 2020 budget totals \$129.6 million, a 4.4% increase over fiscal 2018. The increase primarily reflects additional staffing, although generally the budget is consistent with prior years. Management continues to make capital investments in the 2020 budget, noting that as debt service declines it expects to increase pay-as-you-go capital by the amount of the decline.

Fitchburg derives a majority of its general fund revenue from historically stable sources, the largest of which is intergovernmental revenue. For fiscal 2018, state aid made up 52% of the city's general fund revenue, followed by property taxes (38%). Over the past five years, its in-year property tax collection rate has averaged approximately 97%. Although Fitchburg is more dependent on intergovernmental aid relative to other peers in the state—making it more susceptible to fluctuations in this revenue source due to adverse state fiscal conditions—we expect it to maintain an overall predictable revenue profile that will support, at least, stable budgetary performance over the two-year outlook period.

Very strong budgetary flexibility

Fitchburg's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2018 of 16% of operating expenditures, or \$20.7 million.

Over the past several years, the city has consistently added to available reserves due to positive operating performance. Management is currently projecting positive performance and another increase in reserves by fiscal year-end 2019. As we expect at least balanced operations over the next few years, we expect the city's budgetary flexibility to remain very strong throughout the outlook period.

Very strong liquidity

In our opinion, Fitchburg's liquidity is very strong, with total government available cash at 32.5% of total governmental fund expenditures and 12.0x governmental debt service in 2018. In our view, the city has strong access to external liquidity if necessary.

Fitchburg is a regular market participant that has issued debt frequently over the past 20 years, including GO bonds and short-term BANs. The city has no variable-rate or direct-purchase debt, and management has confirmed it has no contingent liquidity risks from financial instruments with payment provisions that change on the occurrence of certain events. City investments are subject to state guidelines, and Fitchburg invests its cash in low-risk assets with original maturities of three months or less, including the Massachusetts Municipal Depository Trust, money markets, and short-term certificates of deposit. For these reasons, the city's available cash position remains strong and stable, and we expect its liquidity profile to remain very strong over the next two years.

Adequate debt and contingent liability profile

In our view, Fitchburg's debt and contingent liability profile is adequate. Total governmental fund debt service is 2.7% of total governmental fund expenditures, and net direct debt is 44.3% of total governmental fund revenue. Overall net debt is low at 2.8% of market value, which is, in our view, a positive credit factor.

Following this issuance, Fitchburg will have approximately \$82 million in total direct debt, including capital leases. We consider a portion of the city's enterprise debt to be self supporting through user charges. It may undertake projects

that require borrowing, including at schools and city hall, the library, for wastewater projects and at the airport. We have incorporated these debt plans as we currently understand them into our analysis and do not anticipate they will materially change the debt profile.

In our opinion, a credit weakness is Fitchburg's large pension and OPEB obligation, without a plan in place that we think will sufficiently address it. Fitchburg's combined required pension and actual OPEB contributions totaled 10.6% of total governmental fund expenditures in 2018. Of that amount, 7.0% represented required contributions to pension obligations, and 3.6% represented OPEB payments. The city made 100% of its annual required pension contribution in 2018. The funded ratio of the largest pension plan is 45.9%.

The city participates in the Fitchburg Contributory Retirement System, a cost-sharing, multiple employer, defined-benefit pension plan. As of June 30, 2018, its net pension liability was approximately \$137.5 million. The plan uses a 7.25% discount rate, which we believe is somewhat higher than average. Fitchburg expects to fully amortize the unfunded actuarial accrued liability by 2032, if all assumptions are met.

The city also provides OPEBs. As of June 30, 2018, the net OPEB liability totaled nearly \$164 million. Fitchburg established an OPEB trust fund, with a balance of \$915,000. It has worked with its collective bargaining units to share costs by increasing employee co-pays and premiums to reduce the overall liability, but intends to focus on addressing its OPEB liability after the pension is fully funded. We believe the city's retirement costs will continue to represent a credit weakness based on high carrying costs, elevated unfunded liabilities, and aggressive assumptions.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Outlook

The positive outlook reflects our view that there is at least a one-in-three chance we could raise the rating within the next two years. Should the city continue to produce positive results, leading to stable or increasing reserve levels, particularly if it were to formalize financial management policies and practices, along with continued economic growth and without material negative changes in other metrics, we could raise the rating. However, should reserves decline or economic growth stagnate, or if there is a material growth in debt or debt carrying charges, we could revise the outlook to stable.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015
- Local Government Pension And Other Postemployment Benefits Analysis: A Closer Look, Nov.8, 2017

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed

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to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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