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Summary:

Scarborough, Maine; General Obligation

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Credit Profile

US\$2.945 mil GO Bnds ser 2017 due 11/01/2036

Long Term Rating AA+/Stable New

Scarborough Twn GO

Long Term Rating AA+/Stable Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to the town of Scarborough, Maine's series 2017 general obligation (GO) bonds, and affirmed its 'AA+' long-term ratings on the town's existing GO debt. The outlook is stable.

The town's full-faith-and-credit pledge secures the bonds. Scarborough can levy ad valorem property taxes for bond repayment, subject to limitations of the state's LD-1 legislation. Despite state limitations on levy limits, we did not make a rating distinction for the limited-tax GO pledge due to the town's flexibility under the levy limit. Officials plan to use bond proceeds for various capital improvement projects.

The rating reflects our opinion of the following factors for Scarborough, specifically its:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong management, with "good" 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 2016;
- Strong budgetary flexibility, with an available fund balance in fiscal 2016 of 11.0% of operating expenditures;
- Very strong liquidity, with total government available cash at 20.4% of total governmental fund expenditures and 3.5x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability position, with debt service carrying charges at 5.8% of expenditures and net direct debt that is 114.1% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

Very strong economy

We consider Scarborough's economy very strong. The town, a primarily residential community with an estimated population of 19,885, is approximately seven miles south of Portland in southeastern Cumberland County. It is in the Portland-South Portland MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 133% of the national level and per capita market value of \$189,910. Overall, market value grew by 0.8% over the past year to \$3.8 billion in 2017. The county unemployment rate was 2.9% in 2016.

The town enjoys direct access to Maine's major arteries (Interstates 95 and 295 and U.S. Route 1), connecting it to

larger employment centers throughout Cumberland County. In addition to access to major markets in the region, Scarborough has a sizable employment base that consists of small commercial and industrial businesses. There is no taxpayer concentration as the ten leading payers account for 7.2% of assessed value.

Some of the largest employers include the town itself, Hannaford Bros. (corporate headquarters), U.S. Postal Service Distribution Center, and Maine Medical Center. Officials indicate the town's real estate market continues to see growth as some of the largest taxpayers are expanding local operations. Piper Shores, a senior retirement center, continues to expand and is completing new additions to its campus while evaluating additional growth and expansion plans. Martin Point Health Care has also opened a new facility in Scarborough this year and added more than 50 jobs. Ongoing and future projects include a 288-unit multifamily apartment complex along the Haigis Parkway which has received preliminary approval and is expected to add \$30 million-\$40 million in new valuation for the town in the next two-to-three years. In addition, Nonesuch River Brewing is constructing a 10,000-square-foot building that will house a local brewery and restaurant. As such, we expect the local area economy to remain very strong from now on.

Strong management

We view the town's management as strong, with "good" financial policies and practices under our FMA methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis.

Highlights include a strong focus on financial and capital planning, evidenced by Scarborough's five-year capital improvement plan, which sets the parameters and outlines the debt and nondebt financing of all the capital projects. The town adheres to its formal investment policy with annual reporting of investments to the council. Finance officials present monthly variance reports to the town manager and quarterly reports to the town council. Budget assumptions are done conservatively, along with at least a four-year historical trend analysis. Reserves are managed in accordance with Scarborough's stated policy. Management also maintains and follows a formal debt management policy. The formal reserve policy targets an unassigned fund balance at 10% of budget, but not less than 8.3%, to which the town currently does not adhere.

Strong budgetary performance

Scarborough's budgetary performance is strong, in our opinion. The town had operating surpluses of 3.1% of expenditures in the general fund and 2.0% across all governmental funds in fiscal 2016. General fund operating results of the town have been stable over the last three years, with results of 2.3% in 2015 and 1.3% in 2014.

We adjusted fiscal 2016 performance for recurring transfers and nonrecurring revenues and expenditures. According to officials, the town was able to achieve a general fund surplus mainly due to expenditures coming in under budget. Specifically, the town saw cost savings in relation to its capital project for the Wentworth school project. It also saw higher-than-expected revenues of about \$936,000 compared to the budget due to increases in excise taxes, licenses and permits, and other items. For fiscal 2017, management reports budget-to-actuals are on target, with excise revenues continuing to outperforming revenue projections and expenditures tracking below target. As such, the town currently expects to end the year with a general fund surplus.

The town's fiscal 2018 budget, while not final yet, is expected to be balanced. It expects the budget to include a 3.5% estimated tax increase and a decrease in state school aid of about \$1.4 million, which management indicates is

conservative and based on the governor's budget, for which the town is mitigating through a mixture of increase in revenues and limiting education expenditures in fiscal 2018. Property taxes account for 74% for general fund revenues, followed by intergovernmental at 12%. Tax collections remain strong, averaging 99% over the past three years. As such, we expect budgetary performance to remain strong.

Strong budgetary flexibility

Scarborough's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2016 of 11.0% of operating expenditures, or \$8.7 million.

The town has consistently maintained strong budgetary flexibility over the past three-years. For fiscal 2017, it expects to end the year with another increase in available reserves. The town has updated its formal reserve policy, which now targets its unassigned fund balance to be maintained at 10% of budget but no less than 8.3%, to which it currently does not adhere.

The town also has an interfund loan receivable of about \$2.6 million in the general fund due from the Haigis Parkway Assessment fund. The town holds a restricted fund balance of \$2.7 million to cover current shortfalls in receivables from the district. Officials indicate the general fund has not experienced any shortfalls in payments. They expect the remaining balance to be fully repaid within the next two-to-three years. As such, we expect the town's budgetary flexibility to remain, at least, strong.

Very strong liquidity

In our opinion, Scarborough's liquidity is very strong, with total government available cash at 20.4% of total governmental fund expenditures and 3.5x governmental debt service in 2016. In our view, the town has strong access to external liquidity if necessary.

Scarborough has issued GO bonds every year for the past 15 years, supporting its strong access to external liquidity. The town does not currently have investments we consider permissive or aggressive because they are in governmental funds mainly, including money-market funds with maturities of less than one year. In addition, it does not have any contingent liquidity risks from financial instruments with payment provisions that change on the occurrence of certain events. Therefore, we expect the town's liquidity profile to remain very strong.

Strong debt and contingent liability profile

In our view, Scarborough's debt and contingent liability profile is strong. Total governmental fund debt service is 5.8% of total governmental fund expenditures, and net direct debt is 114.1% of total governmental fund revenue. Overall net debt is low at 2.9% of market value, which is, in our view, a positive credit factor.

With this issuance, the town will have about \$99 million in total direct debt. Officials plan to issue about \$9 million of debt over the next two years for various capital improvement projects as existing debt expires. Even with this additional debt, we expect the town's debt profile to remain strong. However, should overall net debt increase above 3% of market value and cause debt ratios to weaken, we could view the debt profile as adequate.

Scarborough's combined required pension and actual other postemployment benefit (OPEB) contributions totaled 0.9% of total governmental fund expenditures in 2016. The town made its full annual required pension contribution in 2016.

The town contributes to the Maine Public Employees Retirement System, a defined-benefit plan, for pensions, and the International City Manager's Assn. (ICMA) Money Purchase Plan, a defined-contribution plan. The town's share of the net pension liability for the defined-benefit plan for town and school department employees a combined \$5.4 million, with an 88% funded ratio. Scarborough has made its full contractually required contribution into the plan in the past three years and expects to continue to do so from now on. It matches up to 6% of the contributions employees make to the ICMA plan and also provides OPEBs as an implicit rate subsidy to retirees.

Strong institutional framework

The institutional framework score for Maine municipalities is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion of Scarborough's very strong economy and liquidity. The town's strong budgetary performance and flexibility, strong management conditions, and debt profile further support the rating. Given its historical fiscal performance and our view that management will likely maintain its strong budgetary flexibility and, at least, an adequate debt profile, we do not expect to change the rating within the two-year outlook period.

Upside scenario

Over time, if the town were to increase reserves comparable with those of higher rated peers, consistently through strong budgetary performance while sustaining a strong debt and contingent liability profile, coupled with a very strong economy, we could raise the rating.

Downside scenario

If financial performance were to deteriorate, leading to a continuous reduction of reserves and weakening of budgetary flexibility to levels comparable to that of lower rated peers, or if the debt profile were to weaken, we could lower the rating.

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

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