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Summary:

Scarborough, Maine; General Obligation

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US$7.48 mil 2020 GO		
Long Term Rating	AA+/Stable	New
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Long Term Rating	AA+/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AA+' rating to Scarborough, Maine's series 2020 general obligation (GO) bonds and affirmed its 'AA+' rating on the town's existing GO debt. The outlook on all ratings 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. We rate the limited-tax GO debt on par with our view of Scarborough's general creditworthiness, since the ad valorem tax is not derived from a measurably narrower tax base and there are no limitations on the fungibility of resources, which supports our view of the town's overall ability and willingness to pay debt service.

Officials intend to use series 2020 bond proceeds for various capital improvement projects.

Credit overview

The rating reflects our opinion of the town's historically balanced operations, which have led to the continued maintenance of its strong reserve position. Although the full impact of the COVID-19 pandemic remains to be seen, we believe the town's reserve positon, conservative budgeting practices, low retirement costs, and strong management conditions should provide it with cushion to absorb any unanticipated declines in revenues or unexpected stagnation in its economy as a result of recessionary pressures or events related to COVID-19. Therefore, the stable outlook reflects our view that the town's economy should remain stable, including its retirement costs and liabilities, and our expectation that management will continue to make the budgetary adjustments necessary to maintain balanced operations, with no current plans to draw down on its fund balance.

The rating reflects our opinion of Scarborough's:

- 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;
- Adequate budgetary performance, with balanced operating results in the general fund and at the total governmental fund level in fiscal 2019;
- Strong budgetary flexibility, with an available fund balance in fiscal 2019 of 11.7% of operating expenditures;

- Very strong liquidity, with total government available cash at 20.8% of total governmental fund expenditures and 3.7x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability profile, with debt service carrying charges at 5.6% of expenditures and net direct debt that is 111.5% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value; and
- Strong institutional framework score.

Stable Outlook

Downside scenario

If financial performance deteriorates, leading to a continuous reduction of reserves and weakening of budgetary flexibility, or if the debt profile weakens, we could lower the rating.

Upside scenario

Although unlikely, if the town increases reserves to levels comparable with those of higher-rated peers, consistently with strong budgetary performance while sustaining a strong debt and contingent liability profile, coupled with a very strong economy, we could raise the rating.

Credit Opinion

Very strong economy

We consider Scarborough's economy very strong. The town, with an estimated population of 20,352, is located in Cumberland County in the Portland-South Portland, ME MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 147% of the national level and per capita market value of $230,762. Overall, the town's market value grew by 17.1% over the past year, to $4.7 billion in 2020. The county unemployment rate was 2.7% in 2018.

The town enjoys direct access to Maine's major arteries (Interstate 95 and I-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 includes small commercial and industrial businesses. There is no taxpayer concentration, with the 10 leading taxpayers accounting for 7.2% of assessed value (AV). The town has recently completed a full revaluation which increased its AV in fiscal 2020 by 17% over the previous year to $4.7 billion. Officials report that Maine Life Care, the town's largest taxpayer at about 1.7% of total AV, is currently appealing its AV. Officials estimate the town's exposure, on a worst-case scenario, at about $350,000 in total for fiscal years 2019 and 2020 combined. The town is disputing this appeal and expects its case to go before the Maine Supreme Judicial Court in the near future.

While we expect the town's economy will likely remain relatively stable, we believe its economic metrics could potentially weaken during the next few years as a result of regional and national economic trends and recessionary pressures related to COVID-19. (For more information, please see "An Already Historic U.S. Downturn Now Looks Even Worse," published April 16, 2020). Officials indicate that although the town experiences an uptick in economic activity during the summer months from visitors and tourists, they do not expect a significant impact on its commercial sector, given that the town's tourism-related businesses are limited in number. Additionally, many of the town's smaller businesses, such as restaurants, have remained opened, albeit operating on a limited basis.

Scarborough's leading employers include Hannaford Bros.' corporate headquarters, a U.S. Postal Service distribution center, and Maine Health. According to management, there are various developments underway across the town, including a new mixed-use development that will include an office building at a former horse racetrack property, a new facility being built by Maine Medical Center, ongoing expansion at Maine Life Care (a retirement community), and new car dealerships, as well as six new commercial units. Officials also indicate a 288-unit apartment complex along Haigis Parkway is nearly complete, with the last phase of the project expected to generate about $15 million in additional value when done.

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 management's strong focus on financial and capital planning, evidenced by Scarborough's five-year capital improvement plan (CIP), which sets parameters and outlines debt and non-debt financing for all capital projects. The town adheres to its formal investment policy, with annual reporting of investments to the town council. Finance officials present monthly variance reports to the town manager and quarterly reports to council. Management budgets conservatively, coupled with at least a four-year historical trend analysis.

Scarborough manages reserves in accordance with its stated policy. Management also maintains, and follows, a formal debt management policy. The formal reserve policy targets an unassigned fund balance at 10.0% of the budget but not less than 8.3%, which the town has adhered to over the past two years.

The town has cyber-security protections in place and maintains various backups of its networks and systems. The town also maintains cyber-security insurance.

Adequate budgetary performance

Scarborough's budgetary performance is adequate, in our opinion. The town had balanced operating results of 0.1% of expenditures in the general fund and of negative 0.3% across all governmental funds in fiscal 2019. Although the town's budgetary performance has been stable in the past few years, our assessment considers our view that the town's future budgetary results over the next two years could differentiate from previous years because of recessionary pressures and economic and financial uncertainty related to COVID-19.

We adjusted fiscal 2019 performance for recurring transfers and nonrecurring revenue and expenditures under the general fund and total governmental fund.

For fiscal 2020, officials indicate it has not experienced any major disruptions to its revenues or expenditures so far. The town has collected about 98% of property taxes so far this fiscal year and excise taxes are on target with historical averages, with a majority already collected. The town expects to receive the remainder of its excise taxes by the end of the year. On the expense side, officials indicate budget-to-actuals are tracking favorably as it has reduced employees' schedules and furloughed some part-time staff as a result of COVID-19. The town expects this will result in cost savings for fiscal 2020. As a result, the town currently expects to end the year with balanced operations. Property taxes account for 81% of general fund revenue, followed by intergovernmental revenue at 11%. The fiscal 2019 surplus was primarily the result of conservative budgeting, which led to savings in expenses, including education, and overall higher-than-budgeted revenues.

The town has not yet adopted its fiscal 2021 budget, but is reviewing its revenue and expenditure assumptions, given the events related to COVID-19. According to management, the town is currently planning for a reduction in state aid for education and decreases in revenue sharing for fiscal 2021. Management is budgeting for a 20% decrease in revenue sharing, compared with the latest projections provided by the state, as a conservative measure. The town is also exploring a potential 0% increase in taxes, or a very minimal one, for next year.

Therefore, although we think the town should maintain stable finances during the next two fiscal years, we imagine the unprecedented widespread effects of COVID-19 will have an effect on state revenue and many local economies, including Scarborough's, and could potentially result in weaker budgetary performance for fiscal 2021 and beyond. If management were to maintain balanced financial results during the next two fiscal years, or until we think the threat of stagnating or decreasing revenue as a result of negative economic shocks has subsided, we could revise our view of the town's budgetary performance to strong.

Strong budgetary flexibility

Scarborough's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2019 of 11.7% of operating expenditures, or $10.7 million.

The town has consistently maintained what we consider strong budgetary flexibility over the past three fiscal years. Management expects to end fiscal 2020 with balanced operations and has no plans to draw down on reserves in the short term. While the full economic and financial impact of COVID-19 remains unknown at this time, based on management's expectation that the town will maintain at least balanced operations for fiscal 2020 and not draw down on reserves in fiscal 2021, we currently expect its budgetary flexibility to remain very strong. The town also a formal reserve policy that targets maintaining unassigned fund balance at 10.0% of the budget but no less than 8.3%, to which it currently adheres.

Scarborough also has an interfund loan receivable of about $2.5 million in the general fund due from the Haigis Parkway assessment fund. The town holds a restricted fund balance of $2.9 million to cover current shortfalls in receivables from the assessment fund. Officials indicate the general fund has not experienced any shortfalls in payments, and they expect to repay the remaining balance over time.

Very strong liquidity

In our opinion, Scarborough's liquidity is very strong, with total government available cash at 20.8% of total governmental fund expenditures and 3.7x governmental debt service in 2019. In our view, the town has strong access to external liquidity, if necessary.

Scarborough has issued GO bonds every year for the past 20 years, supporting its strong access to external liquidity. The town does not currently have investments that we consider permissive or aggressive, because its investments are mainly in governmental funds, including money market funds with maturities of less than one year. Additionally, it does not have any contingent liquidity risks from financial instruments with payment provisions that change upon the occurrence of certain events. The town also does not expect any liquidity issues or the need to issue cash flow notes over the next few months. Therefore, we expect liquidity to remain stable.

Strong debt and contingent liability profile

In our view, Scarborough's debt and contingent liability profile is strong. Total governmental fund debt service is 5.6% of total governmental fund expenditures and net direct debt is 111.5% of total governmental fund revenue. Overall net debt is low at 2.6% of market value, which is in our view a positive credit factor.

With this issuance, Scarborough will have about $110 million of total direct debt outstanding. The town currently does not plan to issue any additional debt over the next two years.

Pension and other postemployment benefits

- We do not view pension costs as a long-term credit concern because of the town's high funding, manageable liabilities, and overall low costs.
- We expect contribution increases will likely remain affordable because of the town's revenue strength, strong reserves, and conservative budgeting.

As of June 30, 2019, Scarborough participates in:

- Maine Public Employees' Retirement System's (MPERS) consolidated plan for local participating districts, which is 91.1% funded with a proportionate share of the town's net pension liability of $4.5 million, assuming a 6.75% discount rate as of fiscal 2019;
- MPERS' state employees' and teachers' plan, which is 83% funded with a proportionate share of the town's net pension liability of $495,178, assuming a 6.75% discount rate as of fiscal 2019;
- International City Manager's Assn. (ICMA) money-purchase plan, a defined-contribution plan; and
- Scarborough also provides other postemployment benefits as an implicit rate subsidy to retirees.

Scarborough's pension contributions totaled 2.1% of total governmental fund expenditures in 2019. The town continues to fund 100% of its actuarially determined contribution. In addition, fiscal 2019 contributions exceeded static and minimum funding progress. In general, we expect plan contributions to meet or exceed our view of minimum funding progress, in part because of the plan's closed, 11-year amortization that should result in timely funding progress. However, we believe the plans 'static mortality projections and level percent amortization could lead to some contribution volatility. Nonetheless, we expect costs to remain manageable for the town.

Strong institutional framework

The institutional framework score for Maine municipalities is strong.

Related Research

- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013

- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019