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CREDIT OPINION
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Framingham (City of) MA

Update following outlook revision to negative

Summary

Framingham (Aa2 stable) benefits from a large tax base with a significant commercial presence and above-average resident income and wealth. The city's financial operations have historically been very stable. However, draft unaudited fiscal 2021 results reflect a material decline in the financial position attributable to use of reserves to balance the operating budget, one-time use towards a school project and operating challenges in the utility enterprise fund. The city has begun to address the operating imbalance in the fiscal 2023 budget with conservative assumptions and a decline in the use of reserves. The debt burden is slightly elevated but expected to remain level over the next few years. The pension and OPEB liabilities should remain manageable over the long-term.

On May 26, we assigned a negative outlook and affirmed the Aa2 rating on the city's general obligation bonds.

Credit strengths

» Sizeable tax base with large commercial and industrial presence

» Above-average resident income and wealth

Credit challenges

» Recent reliance on reserves for operations and capital projects

» Ability to maintain balanced general fund operations

Rating outlook

The negative outlook reflects the recent decline in the financial position due to a greater use of reserves and limited property tax revenue increases that have resulted in a structural operating imbalance. The outlook also incorporates uncertainty around the city's large commercial sector that has been impacted by the coronavirus pandemic and the potential for it to limit the city's ability to stabilize its financial operations.

Factors that could lead to an upgrade

» Material growth in reserves

» Significant decline in leverage from debt, pension and OPEB liabilities

» Strengthening of resident income levels

Factors that could lead to a downgrade

» Further decline in general fund reserves beyond fiscal 2021 levels

» Inability to structurally balance the operating budget

» Material increase in leverage from debt, pension and OPEB liabilities

Key indicators

Exhibit 1

Framingham (City of) MA

	2016	2017	2018	2019	2020
Economy/Tax Base					
Total Full Value ($000)	$7,611,238	$8,446,149	$8,446,149	$9,773,588	$9,773,588
Population	70,743	71,232	71,649	72,308	72,308
Full Value Per Capita	$107,590	$118,572	$117,882	$135,166	$135,166
Median Family Income (% of US Median)	132.1%	130.7%	134.8%	131.1%	131.1%
Finances					
Operating Revenue ($000)	$262,756	$285,835	$294,708	$311,519	$319,255
Fund Balance ($000)	$46,669	$51,371	$53,234	$60,881	$59,250
Cash Balance ($000)	$65,898	$71,703	$72,002	$72,930	$76,502
Fund Balance as a % of Revenues	17.8%	18.0%	18.1%	19.5%	18.6%
Cash Balance as a % of Revenues	25.1%	25.1%	24.4%	23.4%	24.0%
Debt/Pensions					
Net Direct Debt ($000)	$219,990	$231,725	$257,219	$264,149	$294,322
3-Year Average of Moody's ANPL ($000)	$266,162	$286,067	$305,718	$299,243	$295,237
Net Direct Debt / Full Value (%)	2.9%	2.7%	3.0%	2.7%	3.0%
Net Direct Debt / Operating Revenues (x)	0.8x	0.8x	0.9x	0.8x	0.9x
Moody's - ANPL (3-yr average) to Full Value (%)	3.5%	3.4%	3.6%	3.1%	3.0%
Moody's - ANPL (3-yr average) to Revenues (x)	1.0x	1.0x	1.0x	1.0x	0.9x

As of June 30 fiscal year-end

Sources: US Census Bureau, Framingham (Town of) MA's financial statements and Moody's Investors Service

Profile

Framingham has a population of 72,308 (2019 American Community Survey) and is primarily residential with a large commercial and industrial presence acting as a regional economic center. The largest industry sectors that drive the local economy are professional, scientific, technical services, health services and retail trade. The city is located in Middlesex County approximately 20 miles west of Boston (Aaa stable).

Detailed credit considerations

Economy and tax base: sizeable and diverse tax base expected to remain stable although commercial sector poses some concern

Framingham's sizable $11.1 billion tax base (2021-22 equalized value) should experience moderate growth over the medium term driven by new residential developments and diverse commercial and industrial sectors. Over the short term, the city could experience more limited growth than seen in the last five years given the potential impact to the commercial and industrial sector due to the coronavirus pandemic. Located approximately 20 miles west of Boston on I-90, the city benefits from easy access to major transportation routes and has a large commercial and industrial presence. The 2021-22 equalized value increased by a healthy 13.6% since the last certification in 2019. Additionally, the 2022 assessed value increased by 5.5%, bringing the five year average annual growth rate to 6.8%. Importantly, the valuation growth has been driven by the strong residential sector and personal property.

While primarily residential in nature (79% of 2022 AV), the city benefits from a strong commercial component (14%) as well. Large employers in the city include Staples, Inc. (B3 stable), Bose Corporation, and TJX Companies Inc. (A2 stable), employing approximately 8,500 employees combined. The city reports that most of these companies are operating a hybrid return to work model for the near term. Additionally, four of the top ten taxpayers including Genzyme Corp., TJX and Bose have pending 2021 tax appeals. The city also reports that Genzyme and Bose have also had a material decline in jobs. Although, the reported job loss does not seem to have impacted the city's low unemployment rate of only 2.8% (March 2022).

Despite some weakness in the office space sector, the development pipeline remains strong driven by multiple residential projects, two hotels and some other retail and restaurants. The city has focused on redeveloping its central business district including creating a tax increment financing district that will focus on mixed use and transit oriented projects.

Wealth and income levels are above national medians with median family income equal to 131% of the US median and a 2022 equalized value per capita of $153,534.

Financial operations, reserves and liquidity: financial position challenged by recent use of reserves and limited tax increases

The city's financial position has declined recently due to greater use of reserves for operations and one-time capital contributions coupled with limited property tax levy increases over the last three years. Since the city form of government was established in fiscal 2019 the average annual tax levy increase has been 1.3% through fiscal 2022 (note fiscal 2021 budget was a decline from the prior year). The financial position has also been impacted by a decline in the utility enterprise fund in which revenues were materially impacted by the change in water and sewer usage related to the coronavirus pandemic. The utility also relied on reserves for capital needs with limited rate increases prior to the pandemic that limited the fund's operating flexibility.

The fiscal 2021 draft unaudited financials reflect a general fund operating deficit of $11.1 million equal to 3.4% of revenue. The financials reflect a $3 million deficiency in revenues over expenses and $8 million in net transfers out of the general fund. In total, the city transferred out just over $11 million including $6 million in reserves for the Fuller School Project, $2.3 million to support the utility enterprise fund budget, and the rest was dedicated to other one-time capital needs. The deficit reduced the available general fund reserves to $48.1 million representing 14.7% of revenue. The audit is expected to be released in June.

Fiscal 2022 year-to-date operations are mixed with revenues slightly off budget due to local receipts trending below budget. Although expenses are trending positive due to savings from open positions and tight controls over departmental spending. The city anticipates sufficient positive variance to offset $6.5 million in reserves used in the budget and end the year balanced to slightly positive.

The proposed fiscal 2023 budget reflects a first step in the city's goal of reducing its reliance on reserves. The proposal includes an overall budget increase of 5.8% driven by salaries, health insurance and retirement contributions. Inflationary impacts on fuel and supplies is also a growing factor. The budget is balanced with a plan to increase the tax levy to 2.0% plus new growth and use $4 million in reserves (down from $6.5 million in the prior year). There is no use of ARPA funding in the proposed budget. Additionally, the city will be increasing utility fund rates by 16% in July.

The unused levy capacity has increased to $37.2 million representing 11% of 2021 general fund revenue. The unused capacity provides the city additional operating flexibility to increase revenue in the future although the city is currently not contemplating raising the tax levy beyond the annual limit.

Liquidity

The cash position based on draft unaudited fiscal 2021 financials has declined to $69.4 million representing a satisfactory 21% of general fund revenue.

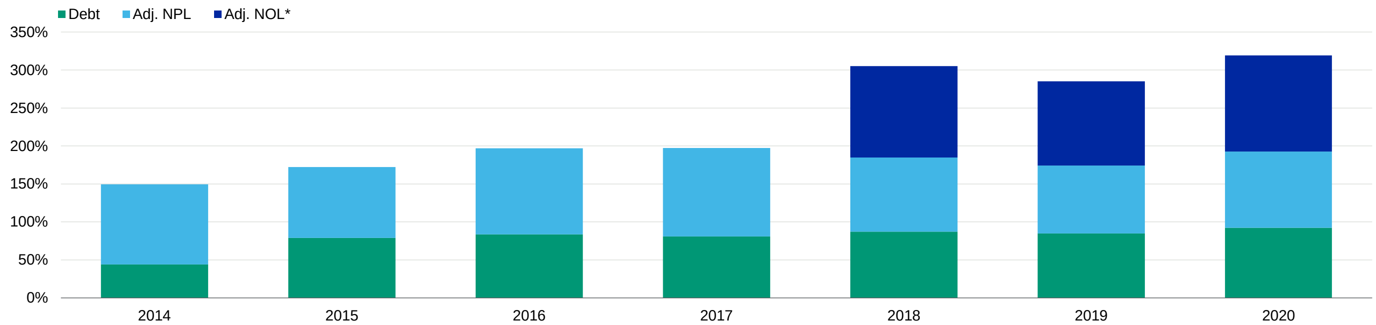
Debt, pension and OPEB liabilities: above-average debt burden and modest pension and OPEB liabilities expected to remain manageable

The city's debt and long term liabilities are expected to remain manageable over the near term (see exhibit) given the city's debt policy and conservative budgeting towards long-term liabilities. Including the current issuances the net direct debt burden of $303.7 million represents 2.8% of equalized value and 0.9 times general fund revenue which is above average for the rating category but is manageable given the city's debt policy, amortization of principal and debt exclusions. The city's debt policy limits the amount of debt service paid within the tax levy to no more than 5% of the budget. The city expects annual debt issuance of $10 million to $15 million.

Exhibit 2

Framingham's leverage is likely to remain manageable given the city's debt policy and budgeting towards long-term liabilities

Leverage as a % of revenue



Adj. NOL not available pre-GASB 75

Sources: Moody's Investors Service and Framingham's financial statements

Legal security

The bonds and notes are backed by the city's full faith and credit general obligation limited tax pledge given that debt service has not been voted by the city as excluded from the tax levy limit under Proposition 2 ½.

Debt structure

The entire debt portfolio is fixed rate with 73% of principal retired in 10 years.

Debt-related derivatives

Framingham does not have any debt-related derivatives.

Pensions and OPEB

Framingham's pension and OPEB liabilities are significantly larger than its debt burden and, though manageable at this time, represent a potential future credit challenge. The city participates in the Framingham Contributory Retirement System, a multi-employer defined benefit plan and makes annual required contributions based on at least its proportional share. The retirement plan expects to be fully funded by 2030 and currently uses a 7.25% discount rate. The city's teachers participate in the Massachusetts Teachers Retirement System in which the city receives on-behalf payments toward the liability that is covered by the Commonwealth. The city also funds its OPEB liability on a pay-go basis plus annual budgeted deposits into an OPEB trust, although the city did not make a deposit in fiscal 2021 or 2021 given financial concerns related to the pandemic. The table below summarizes the city's 2020 debt, pension and OPEB unfunded liabilities and contributions.

Exhibit 3

Framingham's fiscal 2020 debt, pension and OPEB liabilities and contributions

2020	$$$ (000)	% of Operating Revenues	Discount Rate
Operating Revenue	319,255	n/a	n/a
Reported Unfunded Pension Liability	99,479	31%	7.25%
Moody's Adjusted Net Pension Liability	320,355	100%	3.22%
Reported Net OPEB Liability	407,802	128%	2.66%
Moody's Adjusted Net OPEB Liability	404,957	127%	2.70%
Net Direct Debt	294,322	92%	n/a
Debt & unfunded retirement benefits (Moody's adjusted)	1,019,634	319.38%	
Pension Contribution	15,847	4.96%	n/a
OPEB Contribution	13,652	4.28%	n/a
Debt Service	14,584	4.57%	n/a
Total Fixed Costs	44,082	13.81%	n/a
Tread Water Gap	(4,102)	-1.28%	n/a
Moody's Adjusted Fixed Costs	39,980	12.52%	n/a

Sources: Moody's Investors Service and Framingham's financial statements

The city's annual pension contributions over the past five years (2016-2020) have averaged a strong $3.5 million over the tread water indicator which is the amount required to keep the unfunded liability from increasing if all actuarial assumptions are realized. Failure to realize the assumed return on pension assets could result in larger required increases to meet the funding schedule. Fixed costs for debt service, pension and OPEB liabilities is a low, just under 14% of general fund revenue.

ESG considerations

Environmental

Environmental risks are not a material risk to the city at this time. The city continues to actively manage its environmental resiliency and sustainability through a new sustainability officer that started at the city in recent years. The city has previously participated in the Commonwealth's municipal vulnerability preparedness program and is currently working on its green community designation. The capital plan includes green projects like stormwater improvements and fleet electrification. Moody's ESG Solutions assesses the city's climate risks based on county level data as having high risk for hurricanes, medium risk for water stress, extreme rainfall and sea level rise and low risk for heat stress.

Social

Social considerations such as demographics, labor force, income and education are material considerations that influence the city's economy, demographic, financial and leverage trends. Population in the city is slightly increasing and median age is equal to the US. The coronavirus pandemic is a social consideration under our ESG framework. The city's property tax base is diverse with mostly residential composition that has been resilient throughout the pandemic.

Governance

The city practices conservative fiscal management including formal policies and capital planning although recent budgets have included an increasing use of reserves for operations. The city also recently elected a new mayor that took office in January 2022.

Massachusetts cities have an institutional framework score [1] of "Aa", which is strong. The sector's major revenue source of property taxes, are subject to the Proposition 2 1/2 tax levy cap which can be overridden with voter approval only. However, the cap of 2.5% still allows for moderate revenue-raising ability. Expenditures primarily consist of personnel costs, as well as education costs for cities that manage school operations, and are highly predictable given state-mandated school spending guidelines and employee contracts. Unpredictable revenue fluctuations tend to be minor, or under 5% annually. Across the sector, fixed costs are generally less than 25% of expenditures. Fixed costs are driven mainly by debt service and pension costs. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 4

Framingham (City of) MA

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Scorecard Factors and Subfactors	Measure	Score
Economy/Tax Base (30%) [1]		
Tax Base Size: Full Value (in 000s)	$11,101,739	Aa
Full Value Per Capita	$153,534	Aaa
Median Family Income (% of US Median)	188.2%	Aaa
Notching Adjustments:[2]		
Regional Economic Center		Up
Finances (30%)		
Fund Balance as a % of Revenues	14.7%	A
5-Year Dollar Change in Fund Balance as % of Revenues	0.4%	A
Cash Balance as a % of Revenues	21.2%	Aa
5-Year Dollar Change in Cash Balance as % of Revenues	1.1%	A
Management (20%)		
Institutional Framework	Aa	Aa
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures (x)	1.0x	A
Debt and Pensions (20%)		
Net Direct Debt / Full Value (%)	2.6%	A
Net Direct Debt / Operating Revenues (x)	0.9x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	2.7%	A
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	0.9x	A
	Scorecard-Indicated Outcome	Aa2
	Assigned Rating	Aa2

[1] Economy measures are based on data from the most recent year available.
[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.
[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.
Sources: US Census Bureau, Framingham's financial statements and Moody's Investors Service

Endnotes

1 The institutional framework score assesses a municipality's legal ability to match revenues with expenditures based on its constitutionally and legislatively conferred powers and responsibilities. See US Local Government General Obligation Debt (July 2020) methodology report for more details.

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