

RatingsDirect®

Summary:

Canton, Massachusetts; General Obligation

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US\$8.27 mil GO mun purp loan of 2021 bnds due 05/15/2033

Long Term Rating AAA/Stable New

Canton GO

Long Term Rating AAA/Stable Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' rating to Canton, Mass.' \$8.270 million series 2021 general obligation (GO) municipal-purpose loan bonds and affirmed its 'AAA' rating on the town's existing GO debt. The outlook is stable.

Canton's full-faith-and-credit pledge, subject to Proposition 2-1/2 limitations, secures the bonds. We rate the limited-tax GO debt based on the application of our criteria, titled "Issue Credit Ratings Linked To U.S. Public Finance Obligors' Creditworthiness," published Jan. 22, 2018, on RatingsDirect. Despite the commonwealth's levy-limit-law-imposed limitations, we did not make a rating distinction between the limited- and unlimited-tax GO pledges. We rate the limited-tax GO debt on par with our view of Canton's general creditworthiness because the ad valorem tax is not derived from a measurably narrower property tax base and there are no resource-fungibility limitations, supporting our view of its overall ability and willingness to pay debt service. Proceeds from the series 2021 bonds will fund various capital projects.

Credit overview

The rating reflects our view of the town's very strong economy, supported by a wealthy property tax base and high income. In addition, Canton's maintenance of very strong budgetary flexibility supports our view of its credit quality. Strong long-term planning and historically consistent positive results lead us to expect management will make necessary budgetary adjustments to maintain balanced operations despite potential cost escalation from retirement liabilities.

Although we are optimistic that the economic recovery is starting to accelerate in the U.S., top-line growth and labor market developments could be uneven, and we will continue to monitor the town for material economic and financial changes. (For more information on COVID-19 and the federal stimulus' effect on the U.S. public finance sector, see "State, Local Government, School District, And Charter School Sector Views Revised Back To Stable," March 24, 2021.) The town anticipates that conservative budgeting will help produce approximately break-even results in fiscal 2021, and we expect federal funding and new payment-in-lieu-of-taxes (PILOT) revenue should help Canton maintain stability in the short run. Therefore, we do not expect to change the rating within the outlook period.

Under our criteria, "Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions" (Nov. 19, 2013), we rate Canton higher than the sovereign because we believe the town can maintain better credit characteristics than the nation in a stress scenario based on its predominantly locally derived revenue

base and our view that pledged revenue supporting bond debt service is at limited risk of negative sovereign intervention.

The rating further reflects our opinion of the town'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;
- Strong budgetary performance, with operating surpluses in the general fund and at the total governmental fund level in fiscal 2020;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2020 of 19% of operating expenditures;
- Very strong liquidity, with total government available cash at 23.2% of total governmental fund expenditures and 5.7x governmental debt service, and access to external liquidity we consider strong;
- Very strong debt and contingent liability profile, with debt service carrying charges at 4.0% of expenditures and net direct debt that is 30.0% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 80.2% of debt scheduled to be retired in 10 years, but significant medium-term debt plans and a large pension and other postemployment benefit (OPEB) obligation; and
- Strong institutional framework score.

Environmental, social, and governance risks

We consider the town's socioeconomic profile to be a social factor opportunity as high incomes and population growth have helped Canton maintain its strong financial position while continuing to bring new businesses to the area. We analyzed the issuer's environmental and governance risks relative to its economy, management, financial measures, and debt and liability profile and determined that they are in line with our view of the sector standard.

Stable Outlook

Downside scenario

We could lower the rating if finances were to deteriorate significantly or the town were to experience budgetary pressure due to increasing retirement benefit contributions, leading to a drawdown on reserves.

Credit Opinion

Very strong economy

We consider Canton's economy very strong. The town is a suburban, primarily residential community 15 miles south of Boston, with a population of 23,258. It is in Norfolk County in the Boston-Cambridge-Newton MSA, which we consider to be broad and diverse. The town has a projected per capita effective buying income of 159% of the national level and per capita market value of \$240,562. Overall, market value grew by 6.9% over the past year to \$5.6 billion in 2021. The county unemployment rate was 2.5% in 2019 and climbed to 8.3% in 2020 because of the pandemic and national recession. Rapidly evolving economic conditions as a result of COVID-19 affected the labor market in uneven

ways (see "Economic Outlook U.S. Q2 2021: Let The Good Times Roll," March 24, 2021).

The town's location along Route 128 and Interstate 95 and two commuter-rail train stations provide local residents with easy access to numerous employment centers, including downtown Boston; the Route 128 high-technology corridor; and Providence, R.I. Assessed value (AV) continues to grow due to a healthy real estate market and ongoing development. Management reports that AV increased in total by 6.8% in fiscal 2021, whereas equalized values grew by 11.8%. Although residential values rose by approximately 5.0%, commercial value growth led the way, with 12.8% year over year.

The town is active in its development efforts, occasionally considering special tax agreements or direct property development if the economic development committee feels it is warranted. As one new development of the past year, ProDrive Technologies expanded its manufacturing capabilities with a new property in Canton. Additionally, a building permit has been issued for a new substance abuse treatment center. The combined Tufts Health Plan and Harvard Pilgrim Health Care organization recently announced it would acquire the currently vacant property that was the former Reebok headquarters. As part of this move, the health group will also consolidate its headquarters in Canton, which management projects could add 2,000 jobs to the town. Canton also negotiated a new 30-year PILOT agreement for the property. Beginning in fiscal 2021, the town is slated to receive a \$1.6 million annual PILOT payment with 3% annual increases.

The town is seeking to expand development along its Route 138 corridor. It was awarded a \$75,000 economic development grant to study a large area of the corridor, the conclusion of which points to the town targeting the creation of a zone with destination stores, restaurants, and community resources. Massachusetts Department of Transportation has committed more than \$20 million to rehabilitate Route 138 from Stoughton to Milton in 2022. In addition, Canton has been actively improving and expanding infrastructure to support new developments and the expansion of its commercial and industrial sectors. Therefore, we expect the town's economy to remain very strong.

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:

- In developing the budget, the town uses conservative assumptions grounded in historical trend analysis and careful state-aid and local-tax-revenue tracking.
- Management regularly monitors budgetary performance and presents monthly reports to department heads and the town administrator.
- Management also performs a five-year budget forecast and communicates the results to department heads.
- Canton maintains a five-year capital improvement program (CIP) that identifies funding sources, as well as a reserve target to keep the unassigned fund balance above 15% of budgeted expenditures, which the town has adhered to since fiscal 2017.
- Canton follows the commonwealth's investment restrictions and monitors and reports investments monthly.
- It does not have a formal debt policy.

Furthermore, the town has taken steps to mitigate exposure to cyber-related risks, and it has been addressing concerns related to climate change that could directly affect taxable properties. In addition to adopting an energy reduction plan, a fuel-efficient vehicle policy, and a municipal vulnerability preparedness plan, it has also made several changes to zoning bylaws and subdivision rules and regulations to enable and encourage low-impact development and "green" infrastructure storm water solutions. Canton has also been awarded a grant from the Municipal Vulnerability Preparedness grant program to do a hydrological study of the town's storm water infrastructure and flood-prone areas to come up with targeted solutions and public outreach and education programs. Finally, Canton is home to the Southern Sky Renewable solar facility, one of the largest solar photovoltaic facilities in Massachusetts. It was installed in 2012 and currently a minimum of 31% of the town's electrical consumption is offset by this facility.

Strong budgetary performance

Canton's budgetary performance is strong, in our opinion. The town had operating surpluses of 1.9% of expenditures in the general fund and 2.0% across all governmental funds in fiscal 2020. General fund operating results have been stable, at 0.4% in 2019 and 1.9% in 2018. Our assessment of operating results adjusts for recurring transfers and bond-financed capital spending.

Canton continued its streak of steady operating performance, with a \$2.0 million net positive result in its general fund. This marks its sixth consecutive surplus result. The town had planned to support higher expenditures using operating transfers into the general fund. However, it experienced approximately \$1.5 million in cost savings during the year in ways both related and unrelated to COVID-19. Fee- and nonproperty tax-based revenues also came in above budgeted figures. These factors helped the town overcome a \$1.5 million decline in property tax revenue, which we attribute to its payment date extension for 2020. We expect that the lower collection rate for that year will likely revert back to its higher levels.

The town's fiscal 2021 operating budget totals \$103.4 million and is balanced using approximately \$874,000 of reserves. The budget represents a 3.2% increase over the previous year. The town is projecting an approximately 8% year-over-year decline in gross local receipts revenue (i.e., local nonproperty revenue) related to COVID-19. However, its conservative revenue budget should support approximately breakeven results for the fiscal year. This projection is also supported by higher-than-anticipated state aid receipts.

Canton is currently in the process of adopting its fiscal year 2022 budget, although the Finance Committee introduced a recommended budget totaling \$106.7 million. This budget is designed to fund contractual increases to public employees and address rising special education costs. Fiscal 2022 will be the first year the town receives PILOT revenue from the Tufts Associated Health Plan/Harvard Pilgrim Health Care Organization combined group, with \$1.6 million set to come in. Although the new PILOT revenue does not affect the town's Proposition 2-1/2 tax levy limit, Canton has elected to leave \$1.6 million in space under the cap. Over time, this ability to increase property taxes by more than normal annual cap increases could provide some extra flexibility. The town's revenue profile is generally stable, with property taxes accounting for 72% of general fund revenue, followed by intergovernmental revenue at 19% in fiscal 2020. We expect budgetary performance will likely remain strong.

Very strong budgetary flexibility

Canton's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2020 of 19% of operating expenditures, or \$21.0 million. Over the past three years, the total available fund balance has remained at a consistent level overall, totaling 19% of expenditures in 2019 and 19% in 2018.

The town has consistently maintained very strong reserves over the past three years. Management anticipates unassigned fund balance will remain in excess of its 15% policy limit at the end of fiscal 2021. When general fund revenues outpace expenditures, the town typically takes the portion of undesignated reserves and transfers it to dedicated reserves or considers one-time expense uses for the funds. We understand officials do not currently plan to spend down fund balance in the near future. Therefore, we expect flexibility will remain very strong. Additionally, the town's anticipated new PILOT revenue for fiscal 2022 has provided it with some taxing space under the limits of Proposition 2-1/2. Management intends to maintain the levy under the limit unless extraordinary circumstances require raising it. We believe this arrangement provides a small amount of extra flexibility.

Very strong liquidity

In our opinion, Canton's liquidity is very strong, with total government available cash at 23.2% of total governmental fund expenditures and 5.7x governmental debt service in 2020.

We believe the town has strong access to external liquidity, as evidenced by regular GO debt issuances. Canton does not have any variable-rate or direct-purchase debt. Most of the town's investments are in certificates of deposit, U.S. treasury obligations, and government agencies. We expect liquidity to remain very strong.

Very strong debt and contingent liability profile

In our view, Canton's debt and contingent liability profile is very strong. Total governmental fund debt service is 4.0% of total governmental fund expenditures, and net direct debt is 30.0% of total governmental fund revenue. Overall net debt is low at 0.7% of market value, and approximately 80.2% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors. Negatively affecting our view of the town's debt profile are its significant medium-term debt plans. In our opinion, a credit weakness is Canton's large pension and OPEB obligation.

We calculate that the town will have approximately \$49 million in total direct debt, approximately \$13 million of which we consider adequately covered by enterprise rates and charges based on historical coverage ratios. The town's five-year CIP includes approximately \$78 million of debt-financed capital projects. The additional expected issuance over the next two years is incorporated in our view of the town's debt. Therefore, we do not expect additional issuance will have a material effect on our view of Canton's debt profile.

Pension and other postemployment benefit obligations

- In our opinion, a credit weakness is Canton's large pension and OPEB obligation. We believe the low pension funded ratio, permissive assumptions, and large OPEB liability collectively result in a liability profile likely to pressure the operating budget, particularly if assumptions are not met.
- While the use of an actuarially determined contribution (ADC) is a positive, we believe some of the assumptions used to build the pension ADC reflect what we view as slightly weak assumptions and methodologies, which we believe increases the risk of unexpected contribution escalations.
- The town funds OPEB liabilities on a pay-as-you-go basis, although it is prefunding the obligation.

Canton participated in the following pension and OPEB plans as of June 30, 2019:

- Norfolk County Retirement System (NCRS), a cost-sharing, multiple-employer defined-benefit pension plan, which is 64.6% funded, with the town's net pension liability at \$44.2 million.
- Town of Canton OPEB plan, a single-employer, defined-benefit health care plan that provides medical, dental, and life insurance to current and future retirees and their dependents and beneficiaries. The OPEB plan is funded on a pay-as-you-go basis, and at fiscal-year-end had a funded ratio of 7.2% and a net OPEB liability of \$82.6 million.

Canton's combined required pension and actual OPEB contributions totaled 8.8% of total governmental fund expenditures in 2020. Of that amount, 4.7% represented required contributions to pension obligations, and 4.1% represented OPEB payments. The town made its full required pension contribution in 2020. The funded ratio of the largest pension plan is 64.6%. We believe the discount rate remains high at 7.75%, along with permissible mortality tables, and optimistic payroll growth assumptions. The system made progress in both our static and minimum funding progress calculations, indicating it addressed both the current costs and unfunded liabilities. The system's closed, nine-year amortization schedule is a positive, leading to full funding ahead of the state's 2040 pension funding deadline. However, we believe that to meet this timeline, the system maintains assumptions we view as more likely to lead to contribution volatility.

Canton also provides OPEB to retirees. It has set up an OPEB trust to prefund the liability, which we view as positive. The OPEB trust has a \$6.4 million balance. The town made a \$914,000 transfer to the OPEB trust for fiscal 2021 and expects to transfer \$1.05 million in fiscal 2022. In addition, when the NCRS plan is fully funded in 2029, the town will shift those pension assessment savings to OPEB funding. Although we recognize that management is attempting to mitigate the risks associated with the large pension and OPEB obligation and that costs are currently manageable, we believe unfunded liabilities will likely remain a challenge since costs continue to grow and pressure the long-term budget.

Strong institutional framework

The institutional framework score for Massachusetts municipalities is strong.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- 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

Ratings Detail (As Of April 28, 2021)

Canton Twn st qual go rfdg bnds		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Canton Twn GO mun purp loan bnds ser 2017 dtd 03/16/2017 due 06/15/2037		
<i>Long Term Rating</i>	AAA/Stable	Affirmed

Ratings Detail (As Of April 28, 2021) (cont.)

Canton Twn GO mun purp loan bnds (Tax-exempt)

Long Term Rating

AAA/Stable

Affirmed

Canton Twn GO (MBIA) (National)

Unenhanced Rating

NR(SPUR)

Many issues are enhanced by bond insurance.

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