S&P Global Ratings

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Summary:

Lower Merion Township, Pennsylvania; General Obligation

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Summary:

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Credit Profile		
US$9.76 mil GO bnds ser 2019B due 07/15/2039		
Long Term Rating	AAA/Stable	New
US$9.04 mil GO bnds ser 2019A due 07/15/2034		
Long Term Rating	AAA/Stable	New
Lower Merion Twp GO		
Long Term Rating	AAA/Stable	Affirmed
Lower Merion Twp GO		
Long Term Rating	AAA/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AAA' rating to Lower Merion Township, Pa.'s $9.04 million series 2019A and $9.76 million series 2019B general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AAA' rating on the township's existing GO debt. The outlook is stable.

The township's full-faith-and-credit pledge secures the bonds.

Officials intend to use series 2019A bond proceeds to refund a portion of the township's series 2014A and series 2014B bonds for interest rate savings. Officials intend to use series 2019B bond proceeds to fund various capital improvement projects.

We rate the township higher than the nation because we believe Lower Merion 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 debt service on the bonds is at limited risk of negative sovereign intervention. In fiscal 2017, local property taxes generated 57% of township revenue, which demonstrated a lack of dependence on central government revenue.

Lower Merion's proximity to Philadelphia, coupled with consistent economic development, has led to its very strong economic indicators, which we expect will remain very strong. The township plans to gradually spend reserves down over the next few years to bring available reserves closer to its target of 18% of expenditures. However, it does not plan to bring reserves below very strong levels. The township continues to maintain practices and policies that we consider strong under our Financial Management Assessment (FMA) methodology. Over the next few years, Lower Merion plans to continue to issue debt, but will issue less debt than it has in previous years. This, coupled with above-average amortization of its debt, and a pension plan that is more than 100% funded, leads us to believe it will continue to maintain a strong debt profile.

The rating reflects our opinion of the township's:

- Very strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Very strong management, with strong financial policies and practices under our FMA methodology;
- Adequate budgetary performance, with balanced operating results in the general fund but an operating deficit at the total governmental fund level in fiscal 2017;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2017 of 35% of operating expenditures;
- Very strong liquidity, with total government available cash at 83.2% of total governmental fund expenditures and 6x governmental debt service, and access to external liquidity we consider strong;
- Strong debt and contingent liability profile, with debt service carrying charges at 13.9% of expenditures and net direct debt that is 126.6% of total governmental fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 71.3% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Very strong economy

We consider Lower Merion's economy very strong. The township has a projected per capita effective buying income of 236% of the national level, which we view as extremely high and a positive credit factor, and per capita market value of $259,076. Overall, the township's market value was stable over the past year at $15 billion in 2019. The county unemployment rate was 3.9% in 2017, below both commonwealth and national averages.

Lower Merion, with an estimated population of 57,837, is an affluent residential community in Montgomery County. The township benefits from convenient access to Philadelphia, 10 miles east, via a regional rail line with seven different stops in the township, as well as national rail service connecting to major northeast corridor business hubs. Assessed value (AV) has increased by 1.5% since fiscal 2016 to $7.6 billion in fiscal 2019. With continued economic development, which includes both residential and commercial development, officials report that the township expects an annual AV increase of 0.3%-0.6% over the next three years. The local economy is diverse and includes such leading employers as:

- Main Line Hospitals (4,168 employees),
- Lower Merion School District (1,779), and
- Susquehanna International Group LLP (1,270).

In addition, residents benefit from access to the broad and diverse Philadelphia-Camden-Wilmington MSA, which we consider a credit strength; this contributes to, what we view as, very strong wealth and income.

Very strong management

We view the township's management as very strong, with strong financial policies and practices under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

The township performs a five-year financial plan that includes a trend analysis for revenue and expenditures; it updates, and the township board reviews, this plan bi-annually. Management performs capital planning through a detailed six-year capital improvement plan (CIP) that it updates throughout the year, which the board approves as part of the annual budget process. The township's formal debt-management policy provides guidelines for financing its CIP, including the structure and term of debt financings.

Lower Merion also maintains formal board-adopted investment, cash-management, and reserve policies. The reserve policy requires the township to maintain a minimum fiscal year-end undesignated fund balance of no less than 12% of the year's general fund operating expenditures, coupled with guidelines for replenishment if township projections indicate fund balance falling below this minimum level.

Adequate budgetary performance

Lower Merion's budgetary performance is adequate, in our opinion. The township had balanced operating results in the general fund of 0.4% of expenditures, but a deficit result across all governmental funds of 7.5% in fiscal 2017. General fund operating results have been stable over the past three years, with a result of 1.9% in 2016 and a result of 2.2% in 2015.

We have taken into account recurring transfers into and out of the general fund, as well as moving significant one-time revenue and expenditures into the township's budgetary performance fund from governmental funds. Outside of using $1.4 million of reserves in fiscal 2016 due to a one-time $2.5 million transfer into the capital projects fund, the township has posted general fund surpluses annually since fiscal 2015. The township's governmental fund deficits have been driven by the capital fund spending down bond proceeds from previous years.

Unaudited fiscal 2018 general fund results show the township posted a $175,983 general fund surplus. This is after a one-time transfer of $1 million from the general fund to the capital projects fund to help build up its capital fund balance so the township didn't have to issue debt in 2018. This also includes a $2 million refund from its health insurance carrier, which is much higher than the $800,000 refund it will typically expect to see in the future.

Fiscal 2019 budgeted expenditures totaled $68.2 million; officials used $3.96 million of fund balance appropriation to balance the budget, which is part of the township's conservative budgeting. Officials report that Lower Merion plans to gradually spend down its fund balance over the next few years, as it remains well over its fund balance policy. However, officials report that most line items are coming in close to or better than budget. This includes a one-time $2 million payment in accordance with a development agreement, as well as saving a little less than $200,000 in overtime expenses as a result of a mild winter. At this time, officials report the township expects to finish with close to a $2 million use of general fund reserves at year-end. Lower Merion's governmental funds are tracking close to budget and we do not expect a deviating trend in those funds. Therefore, we expect budgetary performance to remain adequate.

Very strong budgetary flexibility

Lower Merion's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2017 of 35% of operating expenditures, or $21.1 million. Over the past three years, the total available fund balance has remained at a consistent level overall, totaling 33% of expenditures in 2016 and 36% in 2015.

The township is currently levying 4.19 mills for general purposes, which remains well below its 30-mill levy maximum. Lower Merion has not raised taxes since 2011, and it wants to delay the need for any tax increase. If it were to raise taxes, one levied mill would provide about $7.65 million of general fund revenue annually, which we believe gives the township additional flexibility if needed. With small drawdowns planned over the next few years, we expect available fund balance to remain very strong, as the township plans to eventually bring available reserves close to 18% of expenditures.

Very strong liquidity

In our opinion, Lower Merion's liquidity is very strong, with total government available cash at 83.2% of total governmental fund expenditures and 6x governmental debt service in 2017. In our view, the township has strong access to external liquidity if necessary.

We believe Lower Merion's regular issuance of GO debt since fiscal 2005 supports its strong access to external liquidity. The township does not have any contingent liabilities. In addition, it does not have investments we consider permissive or aggressive; its investments mainly include certificates of deposit and money-market funds.

Strong debt and contingent liability profile

In our view, Lower Merion's debt and contingent liability profile is strong. Total governmental fund debt service is 13.9% of total governmental fund expenditures, and the township's $103 million of net direct debt is 126.6% of total governmental fund revenue. Overall net debt is low at 2.3% of market value, and approximately 71.3% of the direct debt is scheduled to be repaid within 10 years, which are, in our view, positive credit factors.

All debt is fixed-rate debt to maturity, and there is no direct-purchase debt outstanding. Over the next two years, Lower Merion expects to issue additional bonds to finance portions of its CIP. However, the township will issue less than its usual $8 million-$10 million of annual debt issuance. Management indicates a desire to improve the overall debt profile, and it plans to issue less debt than it retires over the next few years in an attempt to reduce total debt.

Lower Merion's combined required pension and actual other postemployment benefits (OPEB) contributions totaled 4.6% of total governmental fund expenditures in 2017. Of that amount, 2.7% represented required contributions to pension obligations, and 1.8% represented OPEB payments. The township made 106% of its annual required pension contribution in 2017.

Lower Merion maintains two pension plans for police and other employees, which it has funded at, or more than, 100% of the annual required contribution (ARC). Contributions in fiscal 2017 totaled $2 million, or 105.5% of the ARC. As of Dec. 31, 2017, the last actuarial date, the police retirement plan and the employees' retirement plan were both over 100% funded. The township funds the pension plans through two separate pension trust funds it has established. Lower Merion also provides OPEB through a single-employer, defined-benefit plan it funds through pay-as-you-go financing; fiscal 2017 contributions of $998,658 represented 32.4% of the ARC. As of Jan. 1, 2017, its unfunded actuarial accrued liability totaled $26.3 million.

Strong institutional framework

The institutional framework score for Pennsylvania municipalities is strong.

Outlook

The stable outlook reflects S&P Global Ratings' opinion of Lower Merion's very strong economy, budgetary flexibility, and liquidity. We believe that the township's location and desirability will likely sustain its very strong economic indicators and that extensive management and financial policies are likely to preserve its very strong budgetary flexibility and liquidity.

If budgetary performance were to deteriorate, resulting in a significant decrease in reserves where budgetary flexibility or liquidity falls below levels we consider very strong, or if the debt profile were to weaken significantly, we could lower the rating; however, we consider this unlikely. We do not expect to change the rating over the two-year outlook period.

Related Research

- 2018 Update Of Institutional Framework For U.S. Local Governments
- 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