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## Summary:

# Mahwah Township, New Jersey; General Obligation

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### Credit Profile

US\$32.0 mil GO bnds ser 2020 due 01/15/2045

*Long Term Rating* AAA/Stable New

Mahwah Twp GO

*Long Term Rating* AAA/Stable Affirmed

## Rating Action

S&P Global Ratings assigned its 'AAA' rating to Mahwah Township, N.J.'s series 2020 public-improvement serial general obligation (GO) bonds, totaling \$32.85 million, consisting of general improvement bonds (\$26.55 million), water utility bonds (\$4.5 million), and sewer utility bonds (\$1.8 million). At the same time, S&P Global Ratings affirmed its 'AAA' rating on the township's existing GO debt. The outlook is stable.

Securing debt service on the bonds is the township's full faith and credit, including the requirement to levy ad valorem taxes on all taxable property within its borders without limitation as to rate or amount. Proceeds from the sale of the bonds will fund a variety of capital projects, including road improvements as well as water and sewer improvements.

### Credit overview

Mahwah's general credit characteristics are characterized by a strong residential economy that in our view has helped the township maintain its solid financial position, in addition to well-embedded financial policies and proactive planning. Continued residential and some new commercial development will provide additional support to the growing tax base.

We understand the impacts of COVID-19 have been fairly limited on the township, primarily because of the township's revenue mix, as well as a management team that is conservative in its budgeting and proactive in making expenditure adjustments as needed. Nevertheless, in our view, there still remains some uncertainty related to the potential effects of the pandemic and the ensuing recession on the budget, which we will continue to monitor throughout the outlook period. (For more information on S&P Global Economics' latest economic forecast, see "The U.S. Faces a Longer and Slower Climb from the Bottom," published June 25, 2020, on RatingsDirect.)

Mahwah's GO bonds are eligible to be rated above the sovereign because we believe the township can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions" (published Nov. 19, 2013), the township has a predominantly locally derived revenue source, with independent taxing authority and independent treasury management from the federal government.

The long-term rating reflects our assessment of Mahwah Township'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 a slight operating deficit in the current fund in fiscal 2018 according to audited results and a slight operating surplus in fiscal 2019 according to unaudited results;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2018 of 19% of operating expenditures;
- Very strong liquidity, with total government available cash at 66.3% of current fund expenditures and 5.4x governmental debt service, and access to external liquidity we consider strong;
- Adequate debt and contingent liability profile, with debt service carrying charges at 12.2% of expenditures and net direct debt that is 97.6% of current fund revenue, as well as low overall net debt at less than 3% of market value and rapid amortization, with 69.8% of debt scheduled to be retired in 10 years, but a large pension and other postemployment benefit (OPEB) obligation; and
- Strong institutional framework score.

Our stable outlook reflects our opinion that the township's strong, stable local economy and very strong reserves will continue to help cushion the economic and financial effects of the pandemic. We understand current fund reserves should remain very strong. As a result, we expect the township's rating will remain unchanged during the outlook period. Although our outlook is generally for two years, we note the significant downside risks associated with the COVID-19 pandemic and recession over the next six to 12 months.

### **Environmental, social, and governance factors**

Our rating incorporates our view regarding the indirect risks posed by the COVID-19 pandemic. Absent the implications of COVID-19, we consider the township's social risks in line with those of the sector. We view the state's governance of its pension plans and lack of mechanism to prefund OPEBs as a weakness for New Jersey local governments, as with Mahwah. We view the township's environmental risks as in line with our view of the sector standard.

## **Stable Outlook**

The township's very strong wealth and income levels, access to the New York City employment base, and good management practices and policies should enable officials to maintain strong budgetary performance in the next two years. Nevertheless, should revenue streams significantly weaken as a result of the COVID-19 pandemic or some other unforeseen reason, or expenditures significantly increase resulting in drawdowns that reduce reserves to a level no longer commensurate with the current rating, we could lower the rating.

## **Credit Opinion**

### **Very strong economy**

We consider Mahwah's economy very strong. The township, with an estimated population of 27,051, is in Bergen County in the New York-Newark-Jersey City MSA, which we consider to be broad and diverse. It has a projected per capita effective buying income of 177% of the national level and per capita market value of \$242,174. Overall, market value grew by 3.8% in 2018 to \$6.3 billion in 2019. The county unemployment rate was 2.9% in 2019, although we note unemployment has spiked throughout the country, including Bergen County, within the last few months.

Mahwah's economy is buttressed by its access to Manhattan and North New Jersey employment markets. It is approximately 25 miles from New York City and is served by multiple bus lines, New Jersey Transit, Interstate 287, NJ Route 17, the New York State Thruway, and U.S. Route 202. Approximately 78% of the township's tax base is residential, while 20% is commercial and industrial. Most of the commercial development is along the junction of highways and the Route 17 corridor.

The township continues to see modest residential and project projects that continue to add some growth to the tax base over the last five years. We understand officials anticipate a similar level of modest residential and commercial growth over the next year. As a result, we expect that the economy will continue to grow at a moderate pace.

Nevertheless, rapidly evolving economic conditions as a result of COVID-19 have significantly affected the labor market. We note the county unemployment rate of 14.9% as of May 2020 already far surpasses the peak during the Great Recession, when Bergen County's unemployment rate approached 8.0% in late 2010 and early 2011. Furthermore, the effects of social distancing and other decisions made to safeguard the community from the spread of COVID-19 support our view of an economic contraction in 2020. As a result, we will monitor the longer-term effects of the current downturn on the labor market and the economy overall.

### **Strong management**

We view the township'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.

The budget is drafted using five years of historical data and is conservative, as indicated by results that typically outperform the budget each year. Budget-to-actual reports are presented to the board quarterly, and officials make transfers as needed. The township prepares a two-year current fund projection and six-year capital improvement plan. It has adopted a formal investment and cash management policy that mirrors state guidelines, which are restrictive. Additionally, management reports performance and holdings to the board monthly in the treasurer's report. The debt policy includes a debt limit at 1.0% of equalized value in addition to a debt service ceiling at 15% of the township's expenditures. Lastly, Mahwah adheres to an informal target of at least \$6 million of unreserved funds in addition to adopting a formal surplus policy that outlines that budgetary surplus used cannot exceed 10% of the succeeding year's adopted budget, that the township must maintain an ending surplus of 15%-20% of the succeeding year's adopted budget, and that the ending surplus balance should be 5%-8% of the succeeding year's projected tax levy.

### **Adequate budgetary performance**

Mahwah's budgetary performance is adequate, in our opinion. The township had slight deficit operating results in the current fund of 0.9% of expenditures in fiscal 2018, according to audited results, and a slight operating surplus in fiscal 2019, according to unaudited results. Our assessment accounts for our expectation that fiscal 2020 could experience some budgetary challenges and some deterioration relative to fiscal 2018 and 2019 results, primarily because of risks associated with the COVID-19 pandemic and the national recession.

In fiscal year 2018, the township appropriated \$5.3 million of fund balance in the budget for property tax relief and some one-time expenditures. During the fiscal year, the township replenished nearly the full amount appropriated, primarily as a result of conservative budgeting. Therefore, the township ended the year with the maintenance of very strong reserves, following a slight drawdown of \$197,000.

The fiscal 2019 budget similarly included the use of \$5.1 million in fund balance. Unaudited results for the year indicate better-than-expected revenues as well as expenditure savings in most departments. As a result, the township ended the year with break-even results and the maintenance of \$7.5 million in current fund reserves. We understand delinquent taxes came in better than expected, as did construction and court fees, which helped bolster results.

Management indicates revenues and expenses for the first six months of fiscal 2020 are tracking well relative to budget. Furthermore, we understand the COVID-19 pandemic has not significantly affected finances for the year. In terms of revenues, management indicates it is currently planning for a revenue shortfall of \$1.0 million, even though management expects the actual decline in revenues to be closer to \$200,000-\$300,000. The stability in revenues despite the pandemic is due in part to a revenue mix dominated by property taxes. On the expense side, management indicates COVID-19-related expenses for the year have been limited, currently totaling less than \$100,000.

Furthermore, we understand that much of this increase in expense could be reimbursed either through the Federal Emergency Management Agency (FEMA) or the county. As a result of the limited effect of the pandemic expected for the year, management expects to end the year with a manageable drawdown in reserves. Specifically, management estimates that at worst, it could use between \$500,000 and \$1.0 million in reserves for the year.

Although the township may continue appropriating much of its reserves in the budget, we expect budgetary performance will remain adequate to strong. Conservative budgetary practices, such as budgeting for 97% property tax collections despite averaging over 99%, provide some cushion.

### **Very strong budgetary flexibility**

Mahwah's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2018 of 19% of operating expenditures, or \$7.4 million.

The township has historically maintained its target of at least a nominal fund balance well above its \$6 million target. Management indicates it expects to maintain relatively stable reserves despite the pandemic, given the stability of the township's revenue mix. Specifically, if the township were to use \$1.0 million of reserves in fiscal 2020, the year-end fund balance would remain very strong in our view, at an estimated 17% of expenses.

Additionally, the township maintains banked levy capacity equal to \$599,458, as well as excess surplus in the sewer utility, and open space funds provide additional flexibility if needed.

### **Very strong liquidity**

In our opinion, Mahwah's liquidity is very strong, with total government available cash at 66.5% of current fund expenditures and 5.4x governmental debt service in 2018. In our view, the township has strong access to external liquidity, if necessary.

The township does not report any direct-purchase debt or contingent liabilities with tender options or immediate acceleration risk. Its investments are not what we consider aggressive, as they consist of certificates of deposit, money market funds, and cash.

### **Adequate debt and contingent liability profile**

In our view, Mahwah's debt and contingent liability profile is adequate. Debt service is 12.2% of current fund expenditures and net direct debt is 89.8% of current fund revenue. Overall net debt is low at 0.7% of market value, and approximately 82.0% of the direct debt is scheduled to be repaid within 10 years; in our view, these are positive credit factors. In our opinion, a credit weakness is Mahwah's large pension and OPEB obligation.

Following this issuance, we understand the township's primary capital needs consist of a new Department of Public Works building that management estimates will cost \$24 million. Management expects to issue at least a portion of this amount within the year. Despite this, we do not expect to change our view of the township's debt position.

### **Pension and other postemployment benefits**

- We view pension and OPEB liabilities as a source of credit pressure for Mahwah, as with most New Jersey local governments.
- While it is currently managing pension costs, we believe the township has limited ability to control future growth of these liabilities.

Mahwah participates in the following state-administered pension plans:

- Police and Firemen's Retirement System: 60.20% funded with a crossover date in 2076, with a proportional share of the net pension liability equal to \$27.3 million.
- Public Employees' Retirement System: 42.04% funded with a crossover date in 2057, with a proportional share of the net pension liability equal to \$17.7 million.

Mahwah's combined required pension and actual OPEB contributions totaled 11.8% of current fund expenditures in 2018. Of that amount, 6.8% represented required contributions to pension obligations and 5.0% represented OPEB payments.

Although the township funds 100% of its actuarially determined contributions (ADCs), contributions fell short of both static and minimum funding progress, in part because of poor assumptions and methodologies, but also because of the state's continued underfunding of its portion of the ADC. The plans' 30-year, level-dollar open amortization schedule will result in slow funding progress. (For more details and information on these risks, see "New Jersey Pension Funding: State Actions Reverberate At The Local Level," published Dec. 12, 2018.) We also believe there is a significant possibility the state will reduce annual pension contributions or delay scheduled contribution increases because of the current recession, which could result in higher required contributions for the township.

OPEB liabilities are funded on a pay-as-you-go basis, which, given claims volatility as well as medical cost and demographic trends, could lead to escalating costs in the short term. The total OPEB liability stands at \$69.3 million.

### **Strong institutional framework**

The institutional framework score for New Jersey 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
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020

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