

CREDIT OPINION

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Update

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Westerly (Town of) RI

Update - Moody's Downgrades Westerly, RI's GO to Aa3

Summary Rating Rationale

Moody's Investors Service has downgraded to Aa3 from Aa2 the rating on the Town of Westerly, RI's general obligation debt. Concurrently, we have downgraded to Aa3 the Rhode Island Health and Educational Building corporation's (RIHBEC) series 2011C secured solely by the town's general obligation pledge under its financing agreement.

The downgrade reflects the town's adequate but reduced financial position after several years of consecutive deficits. The rating also incorporates a sizeable and stable tax base near Providence, RI (Baa1 negative) and a slightly above-average and growing debt burden.

Credit Strengths

- » Sizeable and stable tax base with seasonal/tourism component
- » Strong full value per capita given the significant presence of seasonal residences
- » Sound funding of OPEB liability

Credit Challenges

- » Below-average reserve and liquidity levels
- » Slightly higher than average debt burden
- » Increasing costs for employee benefits

Rating Outlook

Outlooks are usually not assigned to local government credits with this amount of debt outstanding.

Factors that Could Lead to an Upgrade

- » Significant improvement in fund balance and liquidity
- » Material improvement in resident wealth levels

Factors that Could Lead to a Downgrade

- » Further reduction of liquidity
- » Continued use of reserve appropriations that result in further fund balance declines
- » Significant declines in the tax base or deterioration of the demographic profile

» Significant growth in debt burden

Key Indicators

Exhibit 1

Westerly (Town of) RI	2011	2012	2013	2014	2015
Economy/Tax Base					
Total Full Value (\$000)	\$ 6,145,010	\$ 6,187,004	\$ 6,223,505	\$ 5,887,246	\$ 5,936,881
Full Value Per Capita	\$ 269,826	\$ 269,398	\$ 273,116	\$ 258,496	\$ 271,835
Median Family Income (% of US Median)	N/A	117.9%	117.9%	117.9%	117.9%
Finances					
Operating Revenue (\$000)	\$ 77,660	\$ 81,303	\$ 87,986	\$ 89,920	\$ 89,734
Fund Balance as a % of Revenues	11.7%	10.0%	9.5%	10.3%	7.6%
Cash Balance as a % of Revenues	21.2%	13.6%	7.2%	5.8%	4.8%
Debt/Pensions					
Net Direct Debt (\$000)	\$ 75,937	\$ 90,472	\$ 87,017	\$ 81,854	\$ 82,114
Net Direct Debt / Operating Revenues (x)	1.0x	1.1x	1.0x	0.9x	0.9x
Net Direct Debt / Full Value (%)	1.2%	1.5%	1.4%	1.4%	1.4%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	N/A	1.2x	1.4x	1.4x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	N/A	1.7%	2.1%	2.1%

Source: Moody's Investors Service

Detailed Rating Considerations

Economy and Tax Base: Sizeable Coastal Community with a Significant Seasonal Component Will Remain Stable

Westerly's sizable \$5.9 billion tax base is expected to remain stable as it continues to benefit from its commutability to Providence (Baa1 negative) and parts of Connecticut (Aa3 negative). Additionally, the town has long been a popular summer home and vacation destination given its seaside location. The population increases to approximately 40,000 in the summer months, nearly doubling its year-round population. Over the last five years full valuation has declined at a 0.7% compound annual rate, a relatively manageable decline compared to that of many other Rhode Island communities. Favorably, the tax base increased 0.8% in fiscal 2015, and although the town is mostly built out, modest new growth is expected from several economic development projects in various areas of the town. Projects include a new medical facility, shopping center, and a coastal mixed-use development with a boutique hotel, condominiums, and restaurants.

Income levels slightly exceed state and national medians - median family income is 111.7% and 99.9% of the state and nation, respectively. Full value per capita is a very strong \$271,835 and reflects the significant presence of seasonal residences. The unemployment rate (6% in April 2015) lags the state (4.9%) and nation (4.7%).

Financial Operations and Reserves: Adequate but Reduced Financial Flexibility

The town's financial flexibility will improve, albeit slowly, as management is committed to eliminating its reliance on fund balance appropriations. The town ended fiscal 2015 with its fifth consecutive drawdown, reducing General Fund balance to \$11.4 million (12.7% of revenues) from \$14.2 million (18.4% of revenues) in fiscal 2011. The drawdown of \$1.3 million largely stems from management's reliance on budgeted reserve appropriations to fund both operating and capital costs. Positively, budgeted reserve appropriations have been declining from \$1 million in 2015 to \$200,000 in the fiscal 2017 budget. Management's ability to produce structurally balanced budgets will remain an important factor in the rating given that current reserve levels are below the median for the rating.

In fiscal 2016 the town has shown progress in stabilizing operations as management estimates a \$250,000 surplus. While helpful, it will take several years of these modest surpluses to rebuild fund balance to levels more consistent with the rating category. The estimated surplus was achieved despite a reserve appropriation of \$675,000 across school and town budgets.

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The fiscal 2017 budget increased 2% and was balanced with a 2.6% levy increase. The property levy remains Westerly's primary revenue source (75.4% in fiscal 2015) and collections remain strong at approximately 98%. State aid, including aid for education, comprised 20.9% of 2015 revenues. The largest expenditures are education (62.6% of 2015 operating expenditures), debt service (11.4%) and public safety (8.8%).

LIQUIDITY

Liquidity is narrow, but likely to modestly improve in the near term. The net cash position at the close of fiscal 2015 was \$4.3 million, or 4.8% of General Fund revenues. The town benefits from supplemental liquidity in its health insurance reserve of \$2 million and is expected to receive \$975,000 FEMA reimbursement this year.

Debt and Pensions: Slightly Above Average Debt Burden; Manageable Pension Liability

Westerly's debt position will potentially grow by \$38.5 million over the next few years to finance renovations in its elementary schools. The renovations will accommodate the consolidation of its four elementary schools down to three. Voter's are expected to approve the consolidation in November with construction to follow shortly thereafter. The direct debt burden, is currently slightly above average at 1.4% of full valuation while debt service comprises an above-average 11.4% of operating expenditures. The town has no overlapping debt.

DEBT STRUCTURE

All debt is fixed rate and amortization of principal is average, with 82.2% repaid within ten years.

DEBT-RELATED DERIVATIVES

Westerly has no derivatives.

PENSIONS AND OPEB

The town maintains various defined benefit pension plans and a defined contribution plan. The total combined ARC for all pension plans was \$6.3 million or 6.9% of expenditures in fiscal 2015. The combined adjusted net pension liability for all plans, under Moody's methodology for adjusting reported pension data, for the State administered ERS teachers plan, the MERS plan and the locally administered police plan is \$106 million, which represents 1.8% of full value or 1.2 times General Fund revenues. Moody's uses the adjusted net pension liability to improve comparability of reported pension liabilities. The adjustments are not intended to replace the town's reported liability information, but to improve comparability with other rated entities. We determined the town's share of liability for the state-run plans in proportion to its contributions to the plans.

The total unfunded OPEB liability is \$11.1 million as of July 1, 2014, the most recent valuation report, and the plan's funded ratio is a strong 22.4%. The town contributed \$429,000 in fiscal 2015, which represents 46.3% of the ARC and less than 1% of expenditures.

Total fixed costs for fiscal 2015, including debt service, required pension contributions and retiree health care payments, represented \$17.2 million or 18.9% of the town's operating expenditures.

Management and Governance

Rhode Island towns and cities have an institutional framework score of "A," or moderate. Revenues, consisting mostly of property taxes and state aid, are moderately predictable with economically sensitive revenues accounting for a fairly small portion. Revenue raising flexibility is moderate; although there is a limit on annual property tax levy increases, the cap is a fairly generous 4%. Expenditures mostly consist of personnel costs which are moderately predictable. Expenditure reduction ability is also moderate given the presence of public sector unions in the state. Pension costs will continue to rise despite reform on the state level.

Legal Security

The bonds are secured by an unlimited tax general obligation pledge of the town.

Use of Proceeds

Not applicable.

Obligor Profile

Westerly has a population of approximately 21,840 and is located on the southwestern coast of Rhode Island, approximately 40 miles from Providence.

Methodology

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Ratings Methodologies page on www.moodys.com for a copy of this methodology.

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