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CREDIT OPINION
18 April 2018

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Burlington (City of) VT

Update to credit analysis

Summary

Burlington (A2) is the economic center of Vermont (Aaa stable) and is anchored by the University of Vermont (Aa3 stable) and the affiliated medical center. Conservative management has strengthened the city's financial position, which somewhat mitigates rising fixed costs and a challenging revenue raising environment. The city's debt position is moderate while its pension liability is elevated.

Credit strengths

» Stable underlying economy and tax base serving as the economic center of the state

» Management team budgets conservatively and prudently manages expenditures, leading

» to recent operating surpluses and growth in reserves

» Low OPEB liability

Credit challenges

» Deferred maintenance will lead to increase in debt burden and debt service costs

» Somewhat challenged revenue raising environment

» Elevated pension liability

Rating outlook

Moody's typically does not assign outlooks to local government credits with this amount of debt outstanding.

Factors that could lead to an upgrade

» Continued surplus operations and material growth in reserves and liquidity

Factors that could lead to a downgrade

» Operating deficits reducing reserves and financial flexibility

» Renewed reliance on cash flow borrowing

» Material increase in the debt burden

» Retention of significant contingent liabilities resulting from sale of Burlington Telecom

Key indicators

Exhibit 1

Burlington (City of) VT	2013	2014	2015	2016	2017
Economy/Tax Base					
Total Full Value ($000)	$4,056,809	$4,019,395	$4,137,177	$4,267,608	$4,480,794
Population	42,331	42,342	42,570	42,556	42,452
Full Value Per Capita	$95,835	$94,927	$97,185	$100,282	$105,550
Median Family Income (% of US Median)	105.0%	106.6%	109.5%	112.8%	112.8%
Finances					
Operating Revenue ($000)	$115,842	$126,310	$56,762	$61,886	$63,288
Fund Balance ($000)	($3,509)	$4,358	$5,912	$9,300	$13,238
Cash Balance ($000)	$14,586	$9,974	$8,652	$10,017	$15,139
Fund Balance as a % of Revenues	-3.0%	3.5%	10.4%	15.0%	20.9%
Cash Balance as a % of Revenues	12.6%	7.9%	15.2%	16.2%	23.9%
Debt/Pensions					
Net Direct Debt ($000)	$68,040	$65,274	$80,903	$77,949	$84,289
3-Year Average of Moody's ANPL ($000)	$152,672	$172,735	$166,327	$172,846	$195,536
Net Direct Debt / Operating Revenues (x)	0.6x	0.5x	1.4x	1.3x	1.3x
Net Direct Debt / Full Value (%)	1.7%	1.6%	2.0%	1.8%	1.9%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	1.3x	1.4x	2.9x	2.8x	3.1x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	3.8%	4.3%	4.0%	4.1%	4.4%

Source: Moody's Investors Service; City audited financial statements

Profile

Burlington is located in northwestern Vermont along the coast of Lake Champlain. The population is approximately 42,200.

Detailed credit considerations

Economy and Tax Base: Strong healthcare and higher education institutions anchor stable tax base

The diverse $4.5 billion tax base (fiscal 2017) remains a strength of the city's credit profile, aided by the diversity of the local economy, the city's regional importance, and significant institutional presence. Education, health services, and government sector employment represent a large portion of the area's largest employers. The city's two largest employers are the University of Vermont Medical Center and the University of Vermont & State Agricultural College (Aa3 stable), which together employ approximately 8,000 people. In the private sector, GlobalFoundries' Essex Junction facility, which currently employs approximately 2,800 people, should remain stable over the near term following a $72 million investment.

Moderate growth in the tax base will continue over the medium term given planned development. The city's full value (estimated fair market value) increased 5% in fiscal 2017, bringing the five year compound average annual growth to 2.5%. Large-scale redevelopment plans for downtown, including the Burlington City Place, continue to progress. The city is currently working with a developer, and the estimated $70 million project will add over 270 residential units and office and retail space.

Income levels are average, with median family income equal to 107.1% of the state and 112.8% of the US. The city's unemployment rate of 1.8% (December 2017) is below the state (2.5%) and US (3.9%) rates.

Financial Operations and Reserves: Stable financial position

The city remains committed to improving its financial position and has generated five consecutive surpluses (audited 2013-2017). Management adheres to the fund balance policy adopted by the Council in 2015 which targets an unassigned fund balance of 10-15%. The city achieved its fund balance policy goal in fiscal 2016, well ahead of schedule.

Audited fiscal 2017 results reflect a $3.9 million surplus driven by strong performance in licenses and permit revenues and conservative budgeting of information technology expenses, police payroll and the benefits of a mild winter. Available reserves are $13.2 million or a sound 20.9% of revenue. Of this amount, $8.4 million (13.3%) is unassigned.

While the city expects a smaller surplus (in excess of $300,000) for fiscal 2018 (June 30th year-end) on a preliminary basis, future reserve growth will moderate given rising fixed costs. Specifically, costs for debt service, salaries and employee benefits will outpace growth for the city's largest revenue source, property taxes. Evidence of some budgetary tightening is seen in the fiscal 2018 budget which projects adding $100,000 to unassigned fund balance, notably less than $1 million surpluses in each of the two prior fiscal years. The budget increased 6% over the prior year.

ENTERPRISE RISK

Current city management has significantly improved the health of its various enterprise funds which were, for many years, a drain on the General Fund. The city will further reduce enterprise exposure with the pending sale of Burlington Telecom. The city has agreed to terms with a private buyer and is now seeking approval by the state's Public Utility Commission.

LIQUIDITY

The 2017 General Fund cash position improved to $15 million, or 23.9% of revenues.

Debt and Pensions: Growing debt burden; Elevated pension liability

Exclusive of the revenue bonds supported by the city's airport, electric and wastewater enterprise funds, the city's General Fund-supported net direct debt burden is currently 2.0% of full value. The city's debt burden includes general obligation debt issued on behalf of the school department, although debt service is paid by the school department. The debt burden will increase over the near term due to annual issuance of approximately $7 million for annual capital needs for the city and the school and electric departments. In addition, the city plans to issue (pending voter approval) approximately $25 million over the next four years to address deferred maintenance.

DEBT STRUCTURE

All debt is fixed rate and amortization of principal is below average, with 57.3% retired within ten years. Fiscal 2017 debt service costs of $3.7 million (net of GO debt service issued for school purposes and paid by the school department) comprised 6.1% of expenditures.

DEBT-RELATED DERIVATIVES

Burlington has no interest rate swaps or derivative agreements

PENSIONS AND OPEB

The city participates in the Burlington Employee Retirement System, a single-employer, defined benefit retirement plan. The city contributed $9.3 million to the plan in fiscal 2017, representing 15.1% of General Fund expenditures. The city's adjusted net pension liability under Moody's methodology for adjusting reported pension data, is $245.6 million, or an above average 3.9 times General Fund revenues. This is inclusive of the pension burden across all governmental and enterprise funds. When including only the general fund's portion, the adjusted net pension liability is more moderate, but still an above-average 2.4 times revenues. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities.

The city contributed $137 towards its annual OPEB cost in fiscal 2017, representing less than 1% of expenditures. The total unfunded liability is $3.8 million as of June 30, 2015.

Total fixed costs for fiscal 2017, including debt service, required pension contributions and retiree healthcare payments, represented $12.9 million, or 21.4% of expenditures.

Management and Governance

The management team, in place since 2012, remains committed to improving the city's financial position. The city adopted a fund balance policy in 2015 with which it reached compliance well ahead of schedule. In fiscal 2016, the city eliminated the material weaknesses found in prior audits. In addition, the city is adhering to a recently adopted ten year capital plan that will address deferred maintenance.

Vermont Cities have an Institutional Framework score of Aa, which is high. Institutional Framework scores measure a sector's legal ability to increase revenues and decrease expenditures. Property taxes, Vermont Cities' major revenue source, are not subject to a cap. Unpredictable revenue fluctuations tend to be minor, or under 5% annually. Across the sector, fixed and mandated costs are generally less than 25% of expenditures. However, Vermont has public sector unions, which can limit the ability to cut expenditures. Unpredictable expenditure fluctuations tend to be minor, under 5% annually.

REPORT NUMBER 1121375

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