

## CREDIT OPINION

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 Rate this Research

### Contacts

Douglas Goldmacher +1.212.553.1477  
 VP-Senior Analyst  
 douglas.goldmacher@moodys.com

Nicole Serrano +1.212.553.4143  
 VP-Senior Analyst  
 nicole.serrano@moodys.com

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# Princeton (Municipality of) NJ

## Update to credit analysis

### Summary

The [Municipality of Princeton](#), NJ (Aaa stable) benefits from its high wealth, strong finances, and modest debt. In addition, the municipality has extraordinary institutional presence; it is home to [Princeton University](#) (Aaa stable), the [Princeton Theological Seminary](#) (Aa1 stable), and the [Institute for Advanced Study](#) (Aaa stable).

Princeton has seen only a modest negative impact from the pandemic. Property taxes came in without issue and, although the parking utility saw a large decrease in revenue, the overall financial impact was not material.

### Credit strengths

- » Above-average resident wealth and income
- » Strong reserve position
- » Institutional presence of multiple institutions of higher education

### Credit challenges

- » Above-average fixed costs

### Rating outlook

The stable outlook reflects the expectation that, despite the pandemic, the municipality's tax base and finances will remain strong in the near to medium term.

### Factors that could lead to an upgrade

- » Not applicable

### Factors that could lead to a downgrade

- » Material deterioration of the tax base and resident wealth and income
- » Sustained declines in reserves and liquidity

### Key indicators

Exhibit 1

Fund balance figures reflect Moody's adjustments.

Sources: Princeton audited financial statements, US Census Bureau, & Moody's Investors Service

## Profile

Princeton is a high wealth community located in central [New Jersey](#) (A3 positive) anchored by Princeton University. It has a population of approximately 31,000.

## Detailed credit considerations

### Economy and tax base: Substantial tax base with above-average income levels

The municipality's tax base will remain strong given its high wealth and the stabilizing presence of the university and other institutions of higher education, all of which are major employers in the region. Princeton is also in long commuting distance of both [New York City](#) (Aa2 stable) and [Philadelphia](#) (A2 stable). Princeton is approximately 87% residential and has a modest commercial base. Wealth and income in the \$8.7 billion tax base are above-average, with equalized value per capita of just over \$282,000 and median family income equal to 275.5% of the national median or 254% of the state median. The tax base is, however, dramatically understated as it does not include the 34% of the base which is tax exempt.

Although Princeton is, in some ways, a mature, developed community, there is modest ongoing redevelopment, which will likely contribute to tax base growth. Some of this development is associated with the university, such as new residential colleges and an art museum, and some is not, including a new hotel and a medical office and retail space.

Princeton has seen only modest negative impact from the pandemic. Unemployment in the county spiked sharply but has since recovered. At 5% for September, the unemployment rate is above the national (4.6%) and below the state (6.2%) rates.

### Financial and liquidity: Strong financial position with positive trend

The municipality's financial position will remain strong in the medium term as management continues to budget conservatively. Current Fund balance increased in 2020 to just under \$19 million, or 31% of current fund revenues from \$16.8 million, or 27.6% of current fund revenues in 2019. Moody's makes [certain adjustments](#) to New Jersey local governments' fund balances to include receivables and reserves that would be eligible to be included in fund balance under GAAP accounting but are excluded under state statutory accounting regulations. The municipality's Moody's-adjusted Current Fund Balance increased in 2020 to \$26.8 million, or a very healthy 43.8% of revenues from \$24.1 million, or a very healthy 39.6% of revenues in 2019. On an adjusted basis, the municipality has been generally stable with a modest upward trend.

While the municipality's finances are strong, its flexibility is somewhat restrained on the revenue side by the 2% statutory tax levy cap. On the expenditure side, the municipality's flexibility is also limited by its fixed costs. In 2020, fixed costs for debt service, required pension contributions and OPEB came to \$13.2 million, or 21.5% of revenues. This is high compared to both state and national medians, largely due to rapid principal repayment.

Although 2021 is not yet over, year to date results have been generally strong. Management reports that property taxes were barely impacted by the pandemic. The strong tax collections are noteworthy since property taxes are the municipality's largest source of revenue; they accounted for 58.5% of revenues in 2020. State aid contributed another 4%. While court fines, fees, and hotel taxes have all taken a hit, they are relatively modest. Parking revenues took a more substantial hit in 2020 and, though they are recovering, are not yet back to normal in 2021. Fortunately, the municipality's general finances are strong enough that, in order to help the parking utility, the annual transfer from the utility to the general budget was skipped. Between the eliminated transfer and reduced operational expenditures, the utility actually ran a surplus in 2020 and is in good shape in 2021.

The other major source of revenue is the contribution from the university, which has held steady. Between PILOTs, voluntary contributions, and other programs, the university contributes approximately \$8.5 million to the municipality, or 14% of current fund revenues. The relationship between the university and the municipality remains strong.

Direct pandemic-related expenditures have been modest and are expected to be covered by CARES Act and other extraordinary aid.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on [www.moody's.com](http://www.moody's.com) for the most updated credit rating action information and rating history.

### Liquidity

Liquidity will remain strong in the near to medium term. The municipality ended 2020 with cash of \$30.7 million, representing 50.1% of revenues.

### Debt and pensions: Low debt burden with above-average pension liabilities

Princeton's debt burden will remain modest during the near to medium term. Including the current issuance, the municipality's net direct debt burden will be 1% of equalized value. Management intends to issue small amounts of debt to pay for annual capital projects over the next few years.

### Legal security

Debt service on the municipality's bonds is secured by its pledge of its full faith and credit backed by its legal obligation to levy ad valorem tax on all taxable property for the payment of debt service without limit as to rate or amount.

### Debt structure

All of Princeton's long-term debt is fixed rate. The municipality periodically issues bond anticipation notes.

### Debt-related derivatives

The municipality is not party to any interest rate swaps or other derivatives.

### Pensions and OPEB

The municipality's pension liabilities larger than its debt and, though manageable at this time, represent a potential future credit challenge. The municipality participates in two state-sponsored multiple employer cost-sharing pension plans and funds retiree healthcare (OPEB) on a pay-go basis. The table below summarizes the total 2020 pension and OPEB contributions and unfunded liabilities.

Exhibit 2

2020	(000)	% of Operating Revenues	Discount Rate
Operating Revenue	61,218	n/a	n/a
Reported Unfunded Pension Liability	46,340	76%	7.00%
Moody's Adjusted Net Pension Liability	118,073	193%	2.70%
Reported Net OPEB Liability	28,663	47%	3.48%
Moody's Adjusted Net OPEB Liability	28,734	47%	3.43%
Net Direct Debt	83,349	136%	n/a
Debt & unfunded retirement benefits (Moody's adjusted)	230,157	375.96%	
Pension Contribution	3,251	5.31%	n/a
OPEB Contribution	909	1.48%	n/a
Debt Service	9,010	14.72%	n/a
Total Fixed Costs	13,170	21.51%	n/a
Tread Water Gap	846	1.38%	n/a
Moody's Adjusted Fixed Costs	14,016	22.90%	n/a

Sources: Princeton audited financial statements & Moody's Investors Service

The state-sponsored boards, which control the pension funds, have historically set contribution rates at a level insufficient to allow the plans to tread water. In addition, the tread water gap does not take into account the very aggressive assumptions underpinning the actuarial analysis, which likely would make the gap even larger. To the extent that the multiple-employer pension plans in which Princeton participates experience returns on assets that fall short of their assumptions, the municipality's required pension contribution will increase. Because it is not pre-funding OPEB benefits as they accrue, the municipality's currently modest OPEB costs and liabilities will likely escalate as the number of retirees it covers grows and retirees age.

## ESG considerations

### Environmental

Environmental risk is [generally low for the local government sector](#) and does not factor materially into the municipality's credit profile as responsibilities for environmental risk mitigation fall to other overlapping government entities. According to data from Moody's affiliate Four Twenty Seven, based on county-level data, the municipality is at high risk from hurricanes and water stress and medium risk from extreme rainfall.

### Social

[Social considerations](#) such as wealth, income, and employment are major factors in the municipality's credit quality and are discussed in the economy section.

### Governance

Governance is a [key credit consideration](#) for all local government issuers. The municipality has a formal fund balance policy to maintain an unadjusted fund balance equal to a minimum of 15%-20% of the operating budget. Conservative budgeting and expenditure controls contribute to the municipality's consistently strong operating results.

New Jersey municipalities have an Institutional Framework score <sup>1</sup> of "Aa," or strong. Revenues are moderately predictable and mostly consist of property taxes; however, cities are required to make county and school district tax levies whole in the event of tax appeals. Revenue-raising ability is moderate as cities are constrained by a 2% cap on the property tax levy. Cities can raise the levy above the cap for debt service, pensions and certain qualified expenses. Expenditures, which primarily consist of personnel and public safety, are highly predictable. Cities have a moderate ability to adjust costs given the presence of collective bargaining and high fixed costs.

## Rating methodology and scorecard factors

The US Local Government General Obligation Debt methodology includes a scorecard, a tool providing a composite score of a local government's credit profile based on the weighted factors we consider most important, universal and measurable, as well as possible notching factors dependent on individual credit strengths and weaknesses. Its purpose is not to determine the final rating, but rather to provide a standard platform from which to analyze and compare local government credits.

Exhibit 3

### Princeton (Municipality of) NJ

Scorecard Factors and Subfactors	Measure	Score
<b>Economy/Tax Base (30%)</b> <sup>[1]</sup>		
Tax Base Size: Full Value (in 000s)	\$8,747,532	Aa
Full Value Per Capita	\$282,178	Aaa
Median Family Income (% of US Median)	269.8%	Aaa
<b>Notching Factors:</b> <sup>[2]</sup>		
Institutional Presence		Up
<b>Finances (30%)</b>		
Fund Balance as a % of Revenues	43.8%	Aaa
5-Year Dollar Change in Fund Balance as % of Revenues	11.2%	Aa
Cash Balance as a % of Revenues	50.1%	Aaa
5-Year Dollar Change in Cash Balance as % of Revenues	13.4%	Aa
<b>Management (20%)</b>		
Institutional Framework	Aa	Aa
Operating History: 5-Year Average of Operating Revenues / Operating Expenditures	1.0x	A
<b>Debt and Pensions (20%)</b>		
Net Direct Debt / Full Value (%)	1.0%	Aa
Net Direct Debt / Operating Revenues (x)	1.4x	A
3-Year Average of Moody's Adjusted Net Pension Liability / Full Value (%)	1.2%	Aa
3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues (x)	1.7x	A
	Scorecard-Indicated Outcome	Aaa
	Assigned Rating	Aaa

[1] Economy measures are based on data from the most recent year available.

[2] Notching Factors are specifically defined in the US Local Government General Obligation Debt methodology.

[3] Standardized adjustments are outlined in the GO Methodology Scorecard Inputs publication.

Fund balance figures reflect Moody's adjustments.

Sources: Princeton audited financial statements, US Census Bureau, & Moody's Investors Service

## Endnotes

**1** The institutional framework score assesses a municipality's legal ability to match revenues with expenditures based on its constitutionally and legislatively conferred powers and responsibilities. See [US Local Government General Obligation Debt \(July 2020\)](#) methodology report for more details.

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