
The Commonwealth of Massachusetts

November 15, 2013 Live Investor Conference Call: Bi-Monthly Credit Review & Review of 2013 Pension Actuarial Report

November 15, 2013



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Disclaimer

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Agenda

1. Economic Update
2. Fiscal 2014 Revenue Collection Update
3. Fiscal 2013 Budget Update
4. Fiscal 2014 and FY 2015 Budget Update
5. Big Topic: Review of 2013 Pension Actuarial Report
6. Debt / Capital
7. Questions



1. Economic Update



Economic Update

Wealth Measures:

- 2012 Per Capita Income in Massachusetts was \$54,687, or 128% of the US average
- Second highest measure in the country for 2012

Source: US Dept of Commerce, Bureau of Economic Analysis

Unemployment:

- The 2012 unemployment rate average was 6.7% for MA vs. 8.1% for US
- Massachusetts state unemployment rates for September and October scheduled to be released 11/22; most recent data is 7.2% rate for Massachusetts (August data) vs. the national average of 7.3% (October data)

Source: US Dept of Commerce, Bureau of Economic Analysis; MA Dept Labor & Workforce Development

Economic Output:

- 2012 GDP growth in MA of 2.6% versus 2.8% for the U.S.
- For the most recent quarter (Q3 of calendar year 2013), real MA GDP is estimated to have grown at an annualized rate of 3.5% vs. 2.8% for the US
- Q2: MA annualized growth of 1.7% vs 2.5% U.S. growth (revised)
- Q1: MA annualized growth of 3.4% vs 1.1% U.S. growth (revised)

Source: US Commerce Department, Bureau of Economic Analysis; and <http://www.MassBenchmarks.org>



Economic Update

Federal Reserve Bank of Philadelphia

State Coincident Indices

As of August 2013 Data (latest release)

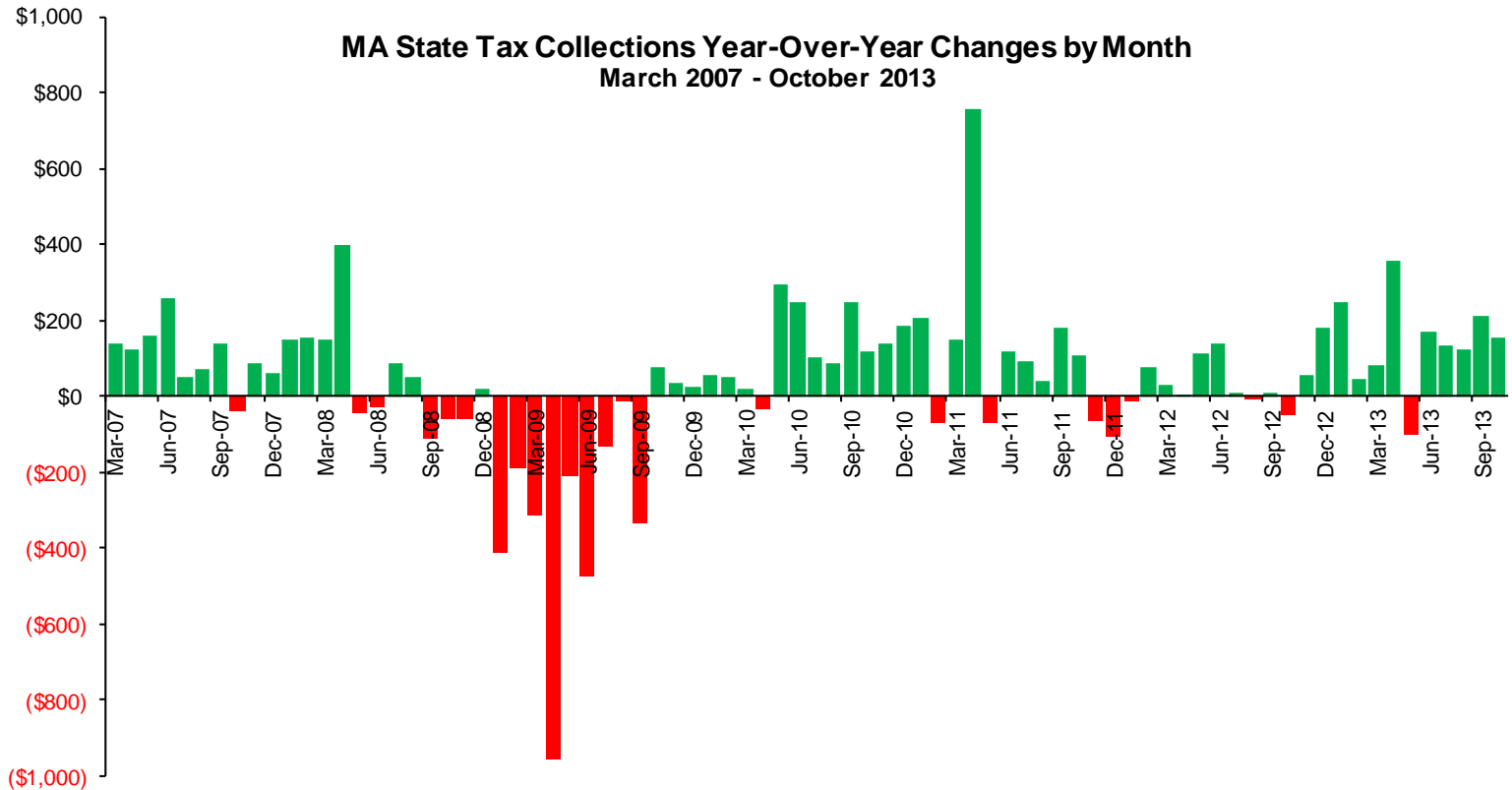
State	Current Level	(Sept 2012 - August 2013)	(Sept 2008 - August 2013)	State	Current Level	(Sept 2012 - August 2013)	(Sept 2008 - August 2013)
		12-month % Change	5-Year % Change			12-Month % Change	5-Year % Change
Alabama	134.1%	1.65%	-2.93%	Montana	167.9%	2.12%	0.11%
Alaska	116.8%	-2.63%	-1.17%	Nebraska	162.9%	1.57%	1.30%
Arizona	182.4%	2.13%	-4.84%	Nevada	181.6%	1.04%	-14.20%
Arkansas	141.8%	0.82%	-1.27%	New Hampshire	196.0%	3.79%	5.15%
California	156.5%	2.54%	3.97%	New Jersey	154.8%	3.92%	2.93%
Colorado	183.8%	3.84%	2.95%	New Mexico	159.1%	0.88%	-6.31%
Connecticut	156.6%	3.13%	3.31%	New York	152.6%	3.07%	7.21%
Delaware	145.2%	2.52%	-2.92%	North Carolina	162.3%	2.81%	0.77%
Florida	146.5%	2.03%	-1.79%	North Dakota	196.9%	4.04%	34.89%
Georgia	168.7%	3.44%	1.44%	Ohio	143.9%	2.28%	3.66%
Hawaii	109.8%	1.70%	-1.61%	Oklahoma	152.9%	0.94%	0.24%
Idaho	198.0%	2.75%	-3.13%	Oregon	208.3%	3.59%	3.32%
Illinois	146.5%	2.16%	0.44%	Pennsylvania	144.0%	2.18%	1.85%
Indiana	149.3%	3.13%	4.65%	Rhode Island	149.8%	1.93%	0.74%
Iowa	145.1%	1.81%	3.74%	South Carolina	155.2%	2.57%	0.09%
Kansas	145.9%	1.68%	-1.13%	South Dakota	165.0%	3.14%	5.96%
Kentucky	143.4%	1.53%	1.27%	Tennessee	153.5%	2.17%	4.07%
Louisiana	127.4%	2.19%	1.28%	Texas	190.5%	3.31%	8.80%
Maine	138.5%	2.44%	-4.89%	Utah	200.0%	3.30%	6.04%
Maryland	151.6%	2.04%	0.40%	Vermont	151.2%	2.87%	2.73%
Massachusetts	180.1%	2.66%	9.30%	Virginia	151.2%	1.37%	0.63%
Michigan	129.5%	2.94%	1.75%	Washington	161.7%	3.47%	1.66%
Minnesota	158.1%	3.39%	5.68%	West Virginia	159.1%	1.71%	0.32%
Mississippi	144.4%	2.94%	1.73%	Wisconsin	143.4%	2.93%	1.33%
Missouri	136.7%	1.86%	-2.42%	Wyoming	166.0%	1.99%	-1.10%
				United States	156.0%	2.66%	5.34%

2. Fiscal 2014 Revenue Collections Update



Fiscal 2014 Revenue Collections Update

- Monthly year-over-year changes in collections have mostly been on the positive side since October 2009, albeit the pace of revenue growth was slow most of 2012. The growth picked up recently (December 2012/January 2013 through October 2013).



Fiscal 2014 Revenue Collections Update

- **FY2013 recap:** Preliminary fiscal 2013 tax revenues totaled approximately \$22.123 bn, an increase of approximately \$1.009 bn, or 4.8%, over fiscal 2012, \$627 mm above the benchmark. Surge in investment-related incomes (cap gains, dividends), one-time payments partly contributed to this growth
- **FY2014:** Strong revenue performance continued during the first four months of fiscal 2014.

October 2013 Tax Collection Summary (in \$ millions) (Preliminary as of November 5, 2013)

	----- Month of October -----					----- FY14 Year-to-Date -----				
	10/13 Collections	10/13 v. 10/12 \$ Change	10/13 v. 10/12 Actual % Change	10/13 v. 10/12 Baseline % Change	10/13 \$ Above/(Below) Benchmark Based on FY14 Estimate of \$22.797 Billion	10/13 FY14 YTD Collections	10/13 FY14 YTD \$ Change	10/13 FY14 YTD Actual % Change	10/13 FY14 YTD Baseline % Change	FY14 YTD \$ Above/(Below) Benchmark Based on FY14 Estimate of \$22.797 Billion
Income - Total	834	31	3.8%	5.4%	(12)	3,892	268	7.4%	7.3%	89
Income Withholding	813	37	4.7%	6.3%	(0)	3,238	157	5.1%	4.9%	5
Income Est. Payments (Cash)	34	12	57.1%	57.1%	11	566	59	11.7%	11.9%	41
Income Returns/Bills	101	2	2.5%	2.5%	(2)	267	87	48.1%	48.2%	77
Income Refunds (Cash)	114	21	22.8%	22.8%	21	178	30	20.6%	20.6%	30
Sales & Use - Total	468	27	6.0%	6.1%	(0)	1,864	109	6.2%	6.0%	24
Sales - Regular	323	17	5.7%	5.7%	(4)	1,260	65	5.5%	5.3%	8
Sales - Meals	83	3	3.4%	3.4%	(1)	347	15	4.5%	4.5%	(2)
Sales - Motor Vehicles	62	6	11.7%	12.1%	4	257	29	12.8%	11.8%	17
Corporate & Business - Total	81	73	859.3%	876.5%	84	637	131	26.0%	27.1%	110
All Other	172	23	15.6%	3.4%	3	705	107	18.0%	9.5%	50
Total Tax Collections	1,555	154	11.0%	10.7%	75	7,098	616	9.5%	8.7%	273

Fiscal 2014 Revenue Collections Update

- Fiscal 2014 tax collections through October totaled approximately \$7.098 bn, an increase of \$616 mm, or 9.5%, over the same period in fiscal 2013, \$273 mm above the year-to-date benchmark.
- It is still too early in the year for the YTD collections to be meaningful (only four months into FY14).
- 54% of the year-to-date surplus is due to one-time settlements (\$148.1 mm).
- Estate tax collections, which are difficult to forecast, have contributed \$44.0 mm to the year-to-date surplus.
- Income withholding payments came in slightly stronger than expected. Non-withholding income tax and sales tax collections have been relatively strong, with moderate surplus in both.



Fiscal 2014 Revenue Collections Update

- Year-to-date withholding: \$3.238 bn, +\$157 mm, +5.1% actual, +4.9% baseline, \$5 mm above benchmark
- Year-to-date income tax payments with bills and returns: \$267 mm, +\$87 mm, \$77 mm above benchmark
 - Significant portion of this surplus is due to one-time revenue settlement-related payments (\$50 mm)
- Year-to-date sales & use tax collections: \$1.864 bn, +\$109 mm, +6.2% actual, +6.0% baseline, \$24 mm above benchmark
- Among “All Other” tax categories, estate tax collections: \$111 mm, +\$45 mm, \$44 mm above benchmark
- Corporate and business collections: \$637 mm, up \$131 mm, 26.0% actual, and 27.1% baseline, \$110 mm above benchmark
 - Significant portion of this surplus is due to one-time revenue settlement-related payments (\$98.1 mm)



Fiscal 2014 Revenue Estimate

- Fiscal 2014 Consensus Tax Revenue Estimate of \$22.334 bn
 - Agreed to on January 14, 2013
- Assumptions included:
 - 3.9% growth from the revised fiscal 2013 estimate of \$21.496 bn
 - A total of \$1.06 bn in capital gains tax
- By statute, the new updated capital gains tax threshold was set at \$1.023 bn for fiscal 2014
- Final Fiscal 2014 Tax Revenue Estimate of \$22.797 bn. Was based on the Consensus estimate plus subsequently signed incremental tax law and administrative changes as a part of the GAA budget (July 12, 2013) (*), and the transportation finance bill(**), which was enacted on July 24, 2013.
- On September 27, 2013, the newly enacted computer/software services sales tax was repealed.
- On October 15, 2013, the Secretary of A&F kept the \$22.797 billion estimate unchanged.

Notes:

(*) *Delay of FAS 109 deductions (\$45.9 mm), Amazon agreement (\$36.7 mm), Tax enhancements-administrative and technical provisions (\$35 mm)*

(**) *1) Three cents increase in gas & special fuels tax (motor fuels tax); 2) Tying gas and special fuels tax to inflation (motor fuels tax); 3) Taxation of computer & software services (sales and use tax), which was later repealed retroactively to the date (July 31, 2013) the tax took effect; 4) Tobacco/cigarette tax increase (tobacco tax); 5) Sales factor sourcing of services (corporate & business tax); 6) Elimination of public utility tax category and taxing them as corporations (corporate tax).*



Fiscal 2014 Revenue Collections Update

Personal income tax rate reduction:

- Two years ago, through a statutory certification process, it was determined that the growth in the state's inflation-adjusted baseline revenues exceeded the statutory growth thresholds
 - So, the state income tax rate was reduced from 5.30% to 5.25% (effective January 1, 2012)
- Last year, it was determined that there was not enough growth in inflation-adjusted baseline revenues
 - Therefore, the income tax reduction of 5.25% to 5.20% was not triggered
- The Department of Revenue is going through the same certification process this year
 - The result of that process will determine if the income tax rate reduction of 5.25% to 5.20% will be triggered effective January 1, 2014.
- On September 4, 2013, the Commissioner of Revenue certified that fiscal 2013 inflation-adjusted baseline revenues grew by 3.99% from fiscal 2012, which exceeded the initial trigger (2.5%) for the income tax rate reduction. The first two three-month certifications issued in September and October also indicated that the statutory threshold was met.
- Two more certifications for three-month periods through December 2013 are necessary.
- It will not be known if the rate reduction will be triggered until the Commissioner of Revenue issues a final certification on December 16, 2013 as to whether or not all of the statutory triggers were met.
- If the rate reduction is triggered, the revenue impact for FY2014 would be between \$60 mm and \$70 mm (with a mid-point of \$65 mm) and the impact for FY2015 would be between \$125 mm and \$140 mm (mid-point of \$132.5 mm).

3. FY2013 Budget Update



Fiscal 2013 Budget Update

- Fiscal 2013 officially ended with the publication of the Statutory Basis Financial Report (document can be located at www.mass.gov/osc under the “Publications and Reports” section).
- Fiscal 2013 was a challenging year for fiscal management, given uncertainties around tax revenue performance due to slow economic recovery and the “fiscal cliff” and federal tax law changes.
- Yet as a result of prudent and proactive budget management, Fiscal 2013 ended on a positive note:
 - The end-of-Fiscal 2013 balance for the Rainy Day Fund is \$1.557 bn, a very healthy balance, third in the nation in absolute size (based on estimates released by NASBO in June) and less than \$100 mm lower than the end-of-Fiscal 2012 balance.
 - There were sufficient available resources to ensure funding for the entirety of previously enacted fiscal 2014 spending contingent on fiscal 2013 consolidated net surplus (including \$25 mm for the Community Preservation Trust Fund, \$19.5 mm for Life Sciences and \$10 mm for an Affordable Housing Trust) plus an additional \$21 mm to properly fund IT operations in state government.
 - In addition, the year-end supplemental bill also utilized available fiscal 2013 resources to fund fiscal 2014 exposures that developed subsequent to the signing of the fiscal 2014 budget in July.



4. FY2014 & FY15 Budget Update



Fiscal 2014 & 2015 Budget Update

- On July 12, 2013 Governor Patrick signed into the law the fiscal 2014 budget, totaling \$34.102 bn after accounting for approximately \$435 mm in veto overrides and fiscal 2014 legislation proposed by the Governor that included \$40 mm in supplemental appropriations
- The current projected fiscal 2014 ending balance for the Stabilization Fund is \$1.379 bn
- While ANF is currently tracking a number of non-tax revenue and spending exposures, after taking into account year-to-date revenue collections, we are optimistic regarding the state's current fiscal condition but will continue to monitor things closely.
- November is a relatively small month for tax collections, several more months will provide greater clarity on where tax revenues are trending.
- Administration is in the early stages of developing the Governor's fiscal 2015 budget recommendations, which will be filed in late January 2014.
- The Secretary of Administration and Finance and House and Senate Ways and Means Committees will be holding their annual Consensus Revenue Hearing in early December. At this hearing they consult with economists, actuaries, state officials and other groups on matters ranging from tax revenue estimates for the current and next fiscal year, pension funding , Lottery revenue projections, and other state finance related topics.



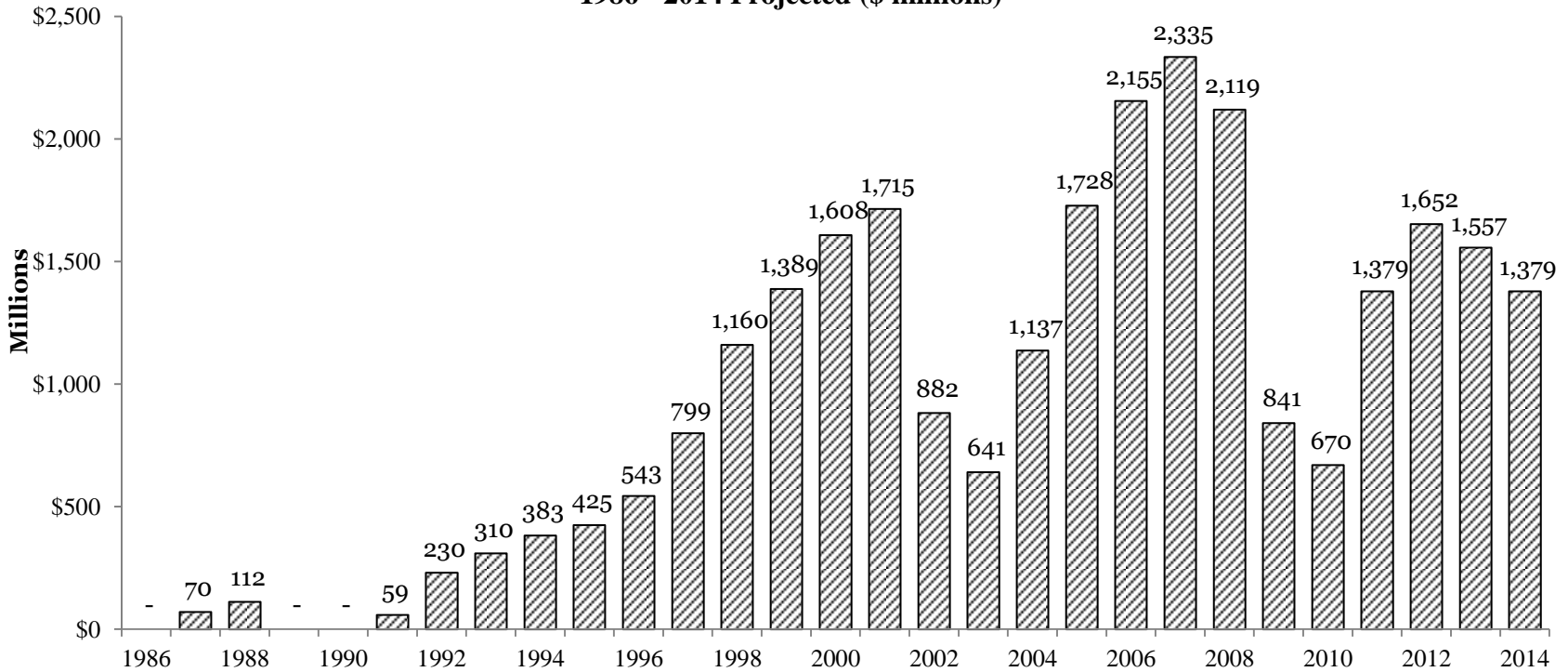
Fiscal 2014 & 2015 Budget Update - Key Dates

- On October 15, January 15 and April 15, the Secretary is required to submit revised estimates for the current fiscal year (FY14) unless, in his opinion, no significant changes have occurred since the last estimate of total available revenues.
- On or before January 15 of each year, the Secretary is required to develop jointly with the House and Senate Committees on Ways and Means a consensus tax revenue forecast for the following fiscal year, in this case fiscal 2015.
- January 15, 2014 - The next triennial pension funding schedule is due to be filed by the Secretary of Administration and Finance.
- Late January – Governor Patrick files his fiscal budget recommendations (House 2)
- Early to mid-April – The House Committee on Ways & Means files its version of the budget. It is then debated and amended by the House later that month.
- Early to mid-May – The Senate Committee on Ways and Means files its version of the budget. It is then debated and amended by the Senate later that month.
- June – A House and Senate conference committee reports a final compromise bill to the House and Senate for a final vote of acceptance in each branch.
- June/July - The Governor has 10 days to review and take action on the enacted budget.



The Commonwealth of Massachusetts - Trend of Reserve Levels

**Stabilization Fund Balance Fiscal Year End
1986 - 2014 Projected (\$ millions)**



5. Big Topic: Review of 2013 Pension Actuarial Report



Commonwealth Actuarial Valuation

- State, Teachers, Boston teachers and Local COLA reimbursements
- Annual Actuarial Valuations since 2000
- January 1, 2013 (report released September 25, 2013)
 - Available on the website www.mass.gov/perac



Funding

- Prior to 1990, pay as you go
- Original schedule 40 year (to 2028)
- Schedule updated at least every 3 years
- In good times, schedule reduced (2018)
- Later extended to 2023 then 2025
- In wake of 2008 loss, schedule extended to 2040 / Provides responsible relief
- New schedule to be developed in 2014



Valuation Results (in millions)

- Complete results page 9 of report

	1/1/2012	1/1/2013
• Total normal cost	\$1,358	\$1,372
• Employee contributions	<u>\$1,023</u>	<u>\$1,058</u>
• Net normal cost	\$ 335	\$ 314
• Actuarial Liability	\$67,547	\$71,866
• Assets (Actuarial Value)	<u>\$43,942</u>	<u>\$43,517</u>
• Unfunded Actuarial Liability (UAL)	\$23,605	\$28,348



Reasons for Increase in UAL (in millions)

• Increase in UAL	\$4,743
• Change in assumptions	\$1,640
• Asset loss (primarily final recognition of 2008 investment loss)	\$2,778
• Other (primarily increasing amortization schedule)	\$ 325



Unfunded Actuarial Liability

- Unfunded actuarial liability (UAL) \$28.3 billion
- History of UAL- page 6 of report
- Dollar basis- doesn't show progress



Funded Ratio

- Funded ratio 60.6%
- Funded ratio history- page 7 of report
- Better measure of progress made
- Overall, better than anticipated
 - Regress to the mean



Actuarial Assumptions

- Prior valuations - Investment return 8.25%
- PERAC “standard” assumption 8.0% since 1997
- Adopted 8.0% for 1/1/13 (See page 4)
- Other assumptions determined by experience studies
 - State and Teachers’ studies completed (reports not yet released)
 - Mortality changes included in 1/12 results for SRS and estimated for TRS
 - Final mortality changes for TRS in 1/1/13 results
 - Salary change partially mitigates impact of lower investment return assumption
 - Over longer term, investment return and salary should move together
 - Both have inflation components



6. Debt & Capital Update



Debt / Capital

- The State Treasurer's Office (STO) continues to issue debt periodically to fund the state's capital budget, following the guidelines of the Executive Office for Administration & Finance's (A&F) Debt Affordability Analysis
- For Fiscal 2014, the STO is preparing to borrow \$2.85 bn (preliminary and subject to change), which includes both general obligation bonds and special obligation bonds
- The STO has completed its FY14 Plan of Finance, which outlines the expected schedule, structure and sizing of each new-money borrowing in the fiscal year
- The STO's initial FY2014 funding of the capital budget was a \$600 mm competitive bond sale in July
- The STO had completed its annual cash flow borrowing in September
- The STO has also completed its FY14 borrowings for the Accelerated Bridge Program
- In terms of future issuance, the STO expects to issue general obligation bonds in late November or early December, representing the Q2 borrowing for FY2014
- The STO is still determining the interest rate mode on the Q2 bonds (fixed-rate or variable-rate) and whether the bonds will be sold via competitive auction or negotiated



Disclosure Enhancements: Investor Communication

- The Commonwealth will continue to hold live investor calls approximately one week after each disclosure update
 - Regular updates on the economy, revenues, budgets, forward calendar/ capital plans, as well as one “big topic” per call
 - Access to senior leadership of the state
- Twitter feed for investors: @BuyMassBonds
- Hold the Date: 2013 Massachusetts Investor Conference Thursday, December 12th
- Today’s call represents the 6th and final live investor call for 2013
- We are planning to hold our first investor call for 2014 in mid-January
 - Big Topic will be a review of the FY13 financial statements

Commonwealth of Massachusetts 2013 Investor Disclosure & Conference Call Schedule

Disclosure Update	Targeted Investor Conference Call	"Big Topic"	Participants
8-Jan-14	15-Jan-14	Review of FY 2012 Financial Statements	State Comptroller
7-Mar-14	14-Mar-14	Review of New Investor Website	Treasury
7-May-14	14-May-14	Review of the Five-Year Capital Plan / Debt Portfolio	A&F / Treasury
22-Jul-14	29-Jul-14	Review of FY13 Revenue Collections	Dept. of Revenue
8-Sep-14	15-Sep-14	Review of Major Spending Categories	State Budget Director
7-Nov-14	17-Nov-14	Review of Pension Actuarial Report	State Actuary / PERAC

7. Questions & Follow-Up



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