

RatingsDirect®

Summary:

Massachusetts; General Obligation

Primary Credit Analyst:

David G Hitchcock, New York (1) 212-438-2022; david.hitchcock@standardandpoors.com

Secondary Contact:

Robin L Prunty, New York (1) 212-438-2081; robin.prunty@standardandpoors.com

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Credit Profile

US\$171.8 mil GO rfdg bnds (SIFMA Index Bnds) ser 2014E due 02/01/2017		
<i>Long Term Rating</i>	AA+/Stable	New
US\$33.435 mil GO rfdg bnds (SIFMA Index Bnds) ser 2014D due 02/01/2016		
<i>Long Term Rating</i>	AA+/Stable	New
Massachusetts GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services has assigned its 'AA+' rating and stable outlook to Massachusetts' \$205.235 million general obligation (GO) refunding bonds (SIFMA index bonds), which include \$33.435 million 2014 series D, maturing Feb. 1, 2016; and \$171.8 million 2014 series E, maturing Feb. 1, 2017.

Factors supporting the 'AA+' rating include what we view as Massachusetts':

- Strong budget performance, with timely monitoring of revenues and expenditures and swift action when needed to make adjustments, with a focus on structural solutions to budget balance;
- Ongoing progress in improving financial, debt, and budget management, including formalized policies relating to debt affordability, as well as multiyear capital investment and financial planning, which are key improvements from a credit standpoint;
- Healthy budget stabilization fund (BSF) balance, which has been key to managing budget volatility;
- High wealth and income levels; and
- Deep and diverse economy, which continues to experience steady economic recovery.

Standard & Poor's believes the commonwealth's high debt burden and significant unfunded pension and other postemployment benefit (OPEB) liabilities are offsetting considerations to the current rating. Although we view Massachusetts' total postretirement liabilities as relatively high, we believe the commonwealth has been actively managing these liabilities with a focus on cost control and reform in recent years.

The SIFMA index bonds are general obligations of the Commonwealth of Massachusetts and will bear interest at a weekly variable rate equal to the SIFMA index rate, plus or minus a fixed number of basis points determined at time of sale, payable monthly. The interest rate cannot be higher than 11% or less than 0%. The bonds are being issued to refund a portion of SIFMA index bonds outstanding: series 2011A, 2012A, 2013A, and 2014A. The amortization of the bonds, in conjunction with other variable-rate debt, has been structured by the commonwealth to match the notional amount of a 2005 interest rate swap agreement, which is being used to hedge interest rate risk.

Massachusetts' economy has experienced steady recovery, outpacing national and regional trends by most measures. The commonwealth's average annual unemployment rate in 2013 was 7.1% compared with 7.4% for the nation. The

preliminary state unemployment rate as of October 2014 has fallen to 5.8%, compared with 6.0% for the nation, the result of continued strong growth in private-sector employment. Employment growth has been strong relative to other states and the commonwealth regained its pre-recession employment peak in 2013 according to the Bureau of Labor Statistics. IHS Global Insight Inc. forecasts continued state employment growth in 2015 and 2016, although slightly slower than that of the nation at 1.5% and 1.2%, respectively, compared with its forecast of 1.9% in 2015 and 1.5% in 2016 for the U.S. In our view, Massachusetts' economic fundamentals and key anchors, which are centered on higher education, technology, and health care, should contribute to continued expansion. Income growth has also been strong relative to that of other states, with per capita personal income now ranked second in the U.S. behind Connecticut in 2013, 28% above the U.S. average.

We view Massachusetts' budget as generally structurally balanced with good reserves. The commonwealth ended fiscal 2014 on a budgetary basis with an estimated operating funds' balance of \$1.4 billion, including \$1.2 billion in the BSF, or what we see as a good 3.9% of operating funds expenditures (primarily the general fund and transportation fund), on a combined basis, or 6.0% of tax revenues. Fiscal 2014 tax revenues rose approximately 5.6% in fiscal 2013; the commonwealth is budgeted for about 4.5% tax revenue growth in fiscal 2015. On Nov. 19, 2014, Massachusetts released a mid-fiscal 2015 updated budget projection, identifying a potential fiscal 2015 budget gap of \$329 million compared with its enacted 2015 budget, or only about 0.8% of budget. (Actual year-to-date revenues through October were only \$32 million below budget.) The projected full year shortfall reflected a \$70 million decrease in projected income tax, a \$176 million projected shortfall in fees and reimbursements, and an \$82 million shortfall in economic development act revenues. In response, the governor has proposed \$225 million of spending reductions, \$47 million of which would require legislative approval. Massachusetts expects that federal revenues and quasi-public partnership contributions could cover the remaining budget gap. It has budgeted to end fiscal 2015 with what we would consider a still-good operating funds' balance of \$1.2 billion, including a \$30 million BSF drawdown, for what we view as a still-good combined 3.1% of operating funds expenditures, or 5.1% of projected tax revenue. Preliminary indications are that another reduction in the income tax rate to 5.15% from 5.20% could occur in January 2015, based on current revenue growth that is above Massachusetts' 2.5% trigger set in law for a reduction, assuming current growth trends continue for the next three months. This would lead to a loss of about \$70 million in tax revenue; however, it would be offset by the higher revenue growth that triggered the rate reduction.

A November ballot initiative repealed inflation indexing of motor vehicle excise taxes; however, the potential loss of excise taxes will come only from future inflation adjustments beginning Jan. 1, 2015. A separate initiative that would have repealed certain casino authorizing legislation and eliminate \$73 million of related budgeted revenues in fiscal 2015 was defeated.

On a generally accepted accounting principles basis, Massachusetts ended fiscal 2013 (the most recent audited year) with an available assigned and unassigned general fund balance of \$1.68 billion, plus a BSF balance of \$1.56 billion, for a combined balance that we view as a strong 11% of general fund expenditures.

Total GO debt outstanding was about \$20.7 billion at Oct. 31, 2014, while we calculate total tax-supported debt at about \$32 billion, including debt issued by state authorities and supported by the statewide sales tax, as well as contract assistance debt. By most measures, we believe Massachusetts' debt burden remains high compared with that

of other states. Debt per capita is high, in our view, at \$4,847 at fiscal year-end 2013 and 8.5% of personal income. Planned debt issuance remains within the parameters of the commonwealth's debt affordability policy and bond cap. A capital and debt affordability committee includes seven voting members and eight nonvoting members from the legislature and is charged with formally reviewing the capital investment plan and providing an estimate of debt authorization for the year. Massachusetts' capital plan, released June 30, 2014, calls for \$2.125 billion of GO borrowing in fiscal 2015 (not including \$237.6 million of GO self-financed project bonds), out of a total borrowing of \$3.39 billion. The five-year plan covering fiscal years 2015-2019 anticipates issuance of \$11.125 billion of GO bonds that are subject to the state bond cap. We view current debt service of about 8% of general governmental revenues as moderately high. Other long-term liabilities are also large, in our opinion. We believe unfunded pension liabilities of \$28.3 billion as of fiscal 2013 are high compared with that of other states at \$4,265 per capita, while unfunded OPEB was also moderately high at \$15.9 billion; however, the commonwealth has started to put aside extra money in an OPEB trust fund that could reach about \$197 million at fiscal year-end 2015, and the 2015 budget dedicates an extra \$163 million to accelerate the funding of its pension liability. Massachusetts has recently disclosed fiscal 2014 unfunded pension liabilities of \$29.0 billion. The mid-2015 budget gap-closing measures the governor proposed do not include any reduction in budgeted OPEB pre-funding.

Based on the analytic factors we evaluate for states, on a scale of '1.0' (strongest) to '4.0' (weakest), we have assigned a composite score of '1.8' to Massachusetts.

(For more information on the state of Massachusetts, see our most recent full analysis published on July 28, 2014, on RatingsDirect.)

Outlook

The stable outlook reflects our expectation that Massachusetts will continue to manage its budget proactively. Management initiatives to formalize long-term financial planning and to manage long-term debt and liabilities should allow for favorable budget structural alignment in the future. We believe the BSF provides significant flexibility to manage future fiscal challenges over our two-year outlook horizon. Despite steady economic expansion, the BSF was reduced \$309 million in fiscal 2014 and may diminish slightly by about \$30 million in fiscal 2015, which could offset future flexibility to manage budget volatility. If there were a sharp decline in reserves, or debt and liabilities were to increase sharply, this could pressure the rating. The level of long-term liabilities is currently constraining upside rating potential.

Related Criteria And Research

Related Criteria

- USPF Criteria: State Ratings Methodology, Jan. 3, 2011
- USPF Criteria: Financial Management Assessment, June 27, 2006

Related Research

- U.S. State And Local Government Credit Conditions Forecast, Dec. 10, 2014

Ratings Detail (As Of December 16, 2014)

Massachusetts GO bnds cons loan ser 2014 F due 11/01/2031		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Massachusetts GO bnds cons loan (Green Bnds) ser 2014 E due 09/01/2032		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Massachusetts GO rfdg bnds var rate dem bnds ser B dtd 02/20/2001 rmktd dtd 02/03/2012 due 01/01/2021		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Massachusetts GO rfdg bnds (SIFMA index bnds) ser 2014A due 02/01/2015		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Massachusetts GO VRDBs - C		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
Massachusetts GO VRDBs 1997B		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
Massachusetts GO VRDBs 2000A		
<i>Long Term Rating</i>	AA+/A-1/Stable	Affirmed
Massachusetts GO VRDBs 2000B		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
Massachusetts GO VRDBs 2006A		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
Massachusetts GO bonds, cons loan (Massdirect Notes) ser 2014 1-10 due 08/01/2024		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Massachusetts GO (wrap of insured) (ASSURED GTY & AMBAC) (SEC MKT)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Massachusetts GO (wrap of insured) (FGIC & BHAC) (SEC MKT)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Massachusetts GO (FGIC)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Massachusetts GO (MBIA) (Assured Gty)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Massachusetts GO		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Massachusetts Dept of Transp, Massachusetts		
Massachusetts		
Massachusetts Dept of Transp (Massachusetts) metro hwy sys rev bnds (subord) VRDO ser 2010A-6		
<i>Long Term Rating</i>	AA+/A-1/Stable	Affirmed
<i>Unenhanced Rating</i>	NR(SPUR)	
Massachusetts Dept of Transp (Massachusetts) GO VRDO 2010A-1		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
Massachusetts Dept of Transp (Massachusetts) GO VRDO 2010A-2 A-7		
<i>Long Term Rating</i>	AA+/A-1/Stable	Affirmed
Massachusetts Dept of Transp (Massachusetts) GO VRDO 2010B		

Ratings Detail (As Of December 16, 2014) (cont.)		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
Massachusetts Dept of Transp (Massachusetts) VRDBs 2010A-7		
<i>Long Term Rating</i>	AA+/A-1+/Stable	Affirmed
Massachusetts Development Finance Agency, Massachusetts		
Massachusetts		
Massachusetts Dev Fin Agy (Massachusetts) GO		
<i>Long Term Rating</i>	AA+/Stable	Affirmed
University of Massachusetts Building Authority, Massachusetts		
Massachusetts		
University of Massachusetts Bldg Auth (Massachusetts) GO (MBIA) (National)		
<i>Unenhanced Rating</i>	AA+(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		

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