S&P Global Ratings

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Summary:

Massachusetts; Gas Tax; Miscellaneous Tax

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Credit Profile		
US$225.0 mil commonwealth transp fund rev rfdg bnds ser 2024A due 06/01/2044		
Long Term Rating	AAA/Stable	New
US$150.0 mil commonwealth transp fund rev bnds (Rail Enhancement Program) ser 2024A due 06/01/2053		
Long Term Rating	AAA/Stable	New
US$125.0 mil commonwealth transp fund rev bnds (sustainability bnds) (Rail Enhancement Prog) ser 2024B due 06/01/2050		
Long Term Rating	AAA/Stable	New
Massachusetts GASTAX		
Long Term Rating	AAA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'AAA' rating to the Commonwealth of Massachusetts' estimated $150 million 2024 series A (rail enhancement program) commonwealth transportation fund (CTF) revenue bonds, estimated $125 million 2024 series B (rail enhancement program) CTF sustainability revenue bonds, and estimated $225 million 2024 series C (rail enhancement sustainability) CTF revenue refunding bonds .
- At the same time, S&P Global Ratings affirmed its 'AAA' rating on the state's $3.4 billion parity bonds outstanding.
- The outlook is stable.

Security

The CTF bonds are secured by pledged revenues that include motor fuel and gasoline taxes and motor vehicle registration fees levied statewide.

Bond proceeds are being used to:

- 2024 series A: Fund #authorized transportation projects,
- 2024 series B: Fund a portion of the South Coast Rail project costs, and
- 2024 series C: Refund certain prior CTF bonds.

Credit overview

We rate the bonds based on our "Priority-Lien Tax Revenue Debt," criteria (published Oct. 22, 2018), which accounts for the strength and stability of the pledged revenues as well as the general credit quality of the obligor where taxes are distributed and/or collected--in this case, the commonwealth. We consider the linkage between the priority-lien pledge and the commonwealth to be close; therefore, the rating on the CTF bonds is constrained by the GO rating.

Debt service coverage has remained very strong for the pledged CTF revenues, albeit moderately lower than historical levels. In fiscal 2024, pledged CTF revenue increased 3.7% to $1.35 billion but remained below pre-pandemic levels.

Overall, we expect ongoing recovery in pledged CTF revenues.

Key credit considerations include our view of:

- Very strong and diverse economy of 7.03 million people generating pledged revenues;
- Low revenue volatility, with historically stable pledged revenues before the pandemic;
- Very strong debt service coverage (DSC) and liquidity, with over 5x coverage of pro forma maximum annual debt service (MADS) following the series 2024 bonds, based on fiscal 2024 pledged revenue that captures revenue loss due to the effects of the pandemic;
- Very strong bond covenants, including a very strong CTF additional bonds test (ABT) requiring 4x coverage of MADS by historical pledged revenues and a covenant not to allow changes in the rate of motor fuels tax or registry fees unless pledged revenues equal at least 4x MADS. In our view, strong DSC mitigates the lack of a debt service reserve; and
- Our establishment of a one-notch upward limitation on the ratings from that of the GO rating on Massachusetts.

Ratings above the sovereign

The CTF bonds are eligible to be rated above the sovereign because we believe pledged revenues can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions" (published Nov. 19, 2013), U.S. states are considered to have moderate sensitivity to country risk. State-derived revenues are the sole source of security on the bonds, and the institutional framework in the U.S. is predictable, with significant state autonomy and flexibility.

Environmental, social, and governance

We consider Massachusetts' chronic physical risks moderately negative in our analysis of the pledged revenues because of the commonwealth's coastal exposure to rising sea levels, with about two-thirds of its population in the Boston MSA and substantial property value in the combined Boston and Cape Cod areas exposing the state to significant economic disruption following a high-impact event. However, we also note that the commonwealth has been addressing environmental risks through its climate protection plan and has historically maintained a stable management and policy framework to respond to developing risks. We view social and governance as neutral to the credit rating analysis. For more information about our rating on the state, please see our analysis published Sept. 16, 2024, on RatingsDirect.

Outlook

The stable outlook reflects that of the commonwealth and our view that Massachusetts' underlying economy and currently very strong reserves could support the rating, despite its economically sensitive revenues and potential nationwide contraction. We also believe that Massachusetts' substantial and diverse economy will support stable pledged revenues over time.

Downside scenario

We could lower the rating if we lower our GO rating on Massachusetts. Although unlikely, should there be very significant deterioration in CTF bond DSC, we could also lower our rating on the CTF bonds. While the commonwealth's capital program for rail, bridges, and roads could require substantial new capital funding, we feel that the very strong current DSC and very strong ABT should provide strong protection against future debt dilution.

We could downgrade our rating on Massachusetts if we believe it will fail to make budget adjustments to maintain structural balance or maintain strong reserves if its revenue weakens. Other factors that could lead to a downgrade include significant increases in debt or other fixed costs, or a significant decline in pension-funded levels due to the commonwealth falling significantly behind required pension funding contribution levels.

Credit Opinion

Economic fundamentals: Very strong

We view Massachusetts' economic fundamentals as very strong. We believe its economy, anchored by a Boston metropolitan area that includes many higher education institutions and associated technology companies, represents an important credit strength.

We believe that Massachusetts' economy, with a substantial high-technology sector presence in the Boston MSA, has been a bright spot, with a substantial proportion of highly skilled workers with strong income levels. Per capita income at, 128% of the nation, has increased slightly faster than that of the nation and is the second highest in the nation spurred by growth in the high-paying professional, scientific, and technical services sector that suffered less in the recent recession than lower-paying, service sector jobs. S&P Global Market Intelligence forecasts continued employment growth slightly stronger than the nation in 2025 at 0.8% compared to its forecast of 0.7% for the U.S.

The U.S. Census Bureau population estimate for Massachusetts in 2024 is slightly over 7 million. S&P Global Ratings' baseline forecast continues to project a growth slowdown nationwide. Employment and national output will continue to cool for the balance of the year and into 2025. With the expectation of the monetary policy gradually easing into next year, a soft landing remains on target, though a mix of geopolitical risks, a potentially disruptive U.S. election in the fall, and disorderly reaction to financial markets could weigh on the overall macroeconomic outlook. (For additional information see, "A Cooling U.S. Labor Market Sets Up A September Start For Rate Cuts," published Aug. 6, 2024, on RatingsDirect.) Overall, we expect inflation will remain above the Federal Reserve's 2% growth target through much of 2024, primarily due to persistently high service price inflation.

Revenue volatility: Low

Our macro volatility assessment begins with an assessment of the historical volatility of the economic activity being taxed, and includes an analysis of societal, demographic, political, and other factors that could affect these activities. Based on the variance of national economic activity that we believe most closely represents the taxing base over multiple economic cycles, it is used to inform our opinion on expectations of future volatility.

We view the pledged revenues as having low volatility based on historical trends despite recent declines. The major revenues supporting the bonds include a portion of motor fuels tax revenue, which accounted for 53% of total pledged funds (chapter 64A, chapter 64E, and chapter 64F receipts) in fiscal 2024, not including federal Build America bond (BAB) interest subsidies. The fuel tax rate was increased to 24 cents from 21 cents in 2013, with 6.86 cents of that amount pledged to the prior-lien special obligation gas tax bonds, which have now matured, on a first-lien basis. The gas tax rate remains below the average gas tax rates charged in the Northeast region. Massachusetts collects gas taxes monthly from gasoline distributors.

The other key revenue supporting the program is motor vehicle registry fees (47% of total revenue in fiscal 2024, excluding BAB subsidies), which are collected daily by the Registry of Motor Vehicles and swept daily by the state treasury and credited to various fee accounts. Passenger vehicle registration fees rose to $60 from $50 in fiscal 2015. Registry fees were also adjusted in fiscal 2009, which offset flat-to-declining revenue performance in previous years.

Pledged revenues have grown an average of 1.7% annually in the last three years. We believe the commonwealth has a history of increasing both pledged gas tax and registration fees when necessary to meet its transportation capital program.

Coverage and liquidity: Very strong

Fiscal 2024 pledged revenue of $1.35 billion covers pro forma MADS of $266.1 million in 2024 after this issue, by what we consider a very strong 5.1x.

The commonwealth anticipates issuing an additional $640 million of parity CTF debt by the end of fiscal 2030 for both the rail and accelerated bridge programs. We believe there could be significant additional debt, beyond the proposed additional debt described above, following the January 2021 transportation bond bill, Chapter 383 of the Acts of 2020, which authorizes $16.3 billion of capital authorization for the commonwealth's transportation infrastructure, expected to be issued as either GO bonds or special obligation bonds. However, the commonwealth indicates the capital authorization covers all the projected project costs before anticipated federal reimbursements, which could reduce the amount of actual bonds needed.

Despite the potential additional issuance, we view the very strong 4x ABT and the need to use surplus CTF funds for transportation operations as providing significant protection against DSC dilution from future debt issuances. However, we believe the potential remains for the CTF to become a regular contributor to the MBTA's very significant capital plans as the authority continues to work on extending and improving its green, orange, and red mass transit lines as well as extending the South Coast Rail line. Nevertheless, the commonwealth projects DSC will remain very strong through 2056, based on current anticipated future debt issuances and no increase in the projected fiscal 2024 revenue.

The fuel tax and registration fees pledged to the bonds are deposited in a revenue account of the CTF, where it is subject to annual appropriation by the state before transfer to the bond debt service account. We believe appropriation risk is mitigated by trust agreement covenants that prevent the large amount of surplus pledged revenue available from being used for other purposes until debt service is paid first. Since the first issuance of special obligation bonds in 1992, the legislature has never failed to make the required appropriations.

Linkage to commonwealth general creditworthiness

Because the commonwealth collects the pledged revenues, we view the rating on the CTF revenue bonds as linked to Massachusetts' creditworthiness. Although the commonwealth constitution restricts transportation-related revenues to transportation-related purposes, these can be purposes other than specifically the repayment of debt. In our establishment of a one-notch upward limitation on the transportation revenue bond rating compared with the state GO rating, we included our view that the state provides critical public services into our analysis. While we consider that statutory and bond covenant restrictions on the use of CTF revenues as providing some uplift, in our view, the collection and distribution of pledged revenues by the commonwealth exposes the revenues to operating risk if there should be a distress situation. For this reason, under our priority-lien criteria, we consider the linkage between the priority-lien pledge and the commonwealth close.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of September 17, 2024)		
Massachusetts GASTAX		
Long Term Rating	AAA/Stable	Affirmed
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.