MOODY'S
INVESTORS SERVICE

New Issue: Moody's assigns MIG 1 to $1.2B of Massachusetts GO revenue anticipation notes

Global Credit Research - 10 Sep 2015

MASSACHUSETTS (COMMONWEALTH OF)
State Governments (including Puerto Rico and US Territories)
MA

Moody's Rating

ISSUE		RATING
General Obligation Revenue Anticipation Notes, 2015 Series A		MIG 1
Sale Amount	$400,000,000	
Expected Sale Date	09/22/15	
Rating Description	Note: Tax and/or Revenue Anticipation	
General Obligation Revenue Anticipation Notes, 2015 Series B		MIG 1
Sale Amount	$400,000,000	
Expected Sale Date	09/22/15	
Rating Description	Note: Tax and/or Revenue Anticipation	
General Obligation Revenue Anticipation Notes, 2015 Series C		MIG 1
Sale Amount	$400,000,000	
Expected Sale Date	09/22/15	
Rating Description	Note: Tax and/or Revenue Anticipation	

Moody's Outlook STA

NEW YORK, September 10, 2015 --Moody's Investors Service has assigned MIG 1 ratings to $1.2 billion of Commonwealth of Massachusetts general obligation revenue anticipation notes, consisting of $400 million 2015 Series A, $400 million 2015 Series B, and $400 million 2015 Series C. The notes are scheduled to price on September 22. The Series A notes mature April 27, 2016, the Series B notes mature May 25, 2016, and the Series C notes mature June 22, 2016.

SUMMARY RATING RATIONALE

The MIG 1 ratings reflect the credit quality of the Commonwealth of Massachusetts (Aa1 stable) and its full faith and credit general obligation pledge to pay note principal and interest when due, the healthy cash margins projected to be available at each of the staggered note maturity dates, and substantial alternative liquidity that could be provided by the commonwealth's budget stabilization fund, subject to legislation appropriation, if necessary.

OUTLOOK

The outlook for Massachusetts' long-term debt is stable, reflecting the commonwealth's strong budgetary reserves and efforts to regain structural budget balance. The outlook also reflects our expectation that the commonwealth will take proactive measures to close budget gaps if they emerge and continue its trend of strong financial management. Going forward, reliance on one-time budget solutions, tighter cash margins, unexpectedly severe economic deterioration, or a large increase in tax-supported debt could pressure the rating at its current level.

WHAT COULD MAKE THE RATING GO DOWN

-- Material weakening in the state's cash-flow margins beyond current estimate

STRENGTHS

-- Healthy forecasted ending cash balances at each note maturity, well-developed cash management practices including quarterly cash flow forecasts, and ample alternative liquidity in the commonwealth's Budget Stabilization Fund, subject to appropriation

-- Strong financial management practices, particularly a willingness to promptly identify and close budget gaps through expenditure reductions, revenue increases and overall prudent use of reserves

-- Budget reserves that provide an adequate cushion to another downturn and the commonwealth's commitment to maintain them at healthy levels

-- An economic base characterized by high wealth and high levels of educational attainment that has provided a degree of stability to the commonwealth's employment situation

CHALLENGES

-- Funds for note repayment are not segregated in advance of maturity dates

-- State debt ratios that are among the nation's highest

-- Large health-care and other social services costs that drive the budget and ongoing spending pressure related to the statewide transportation system

-- Budgetary burden of growing pension contributions as the commonwealth seeks to address its large unfunded pension liabilities

RECENT DEVELOPMENTS

Recent developments are incorporated in the Detailed Rating Rationale.

DETAILED RATING RATIONALE

LONG-TERM CREDIT QUALITY

Massachusetts' general obligation rating (Aa1 stable) reflects its strong financial management practices and its demonstrated willingness to balance its budget when necessary through spending cuts, revenue increases and use of reserves; a large education and health-care sector that generates high wages and helps to bolster employment; state debt levels that are among the highest in the nation; and large unfunded pension liabilities.

CASH FLOW

Seasonal imbalances between receipt of Massachusetts' revenues and outflow of its expenditures drive its cash-flow borrowings. The commonwealth's largest revenue source, the personal income tax (58% of estimate fiscal 2016 tax revenue), is received most heavily in the second half of the fiscal year (especially March, April and June). Local aid payments are one of the largest single expenditure line items (almost 14% of the total). Starting in fiscal 2014 they are disbursed in equal monthly installments. In prior years, those payments were made quarterly in approximately equal amounts. Massachusetts has issued revenue anticipation notes (RANs) every year since fiscal 2009 and since fiscal 2010 they have been sized at $1.2 billion, though the amount dropped to $800 million in fiscal 2014 due to a large surplus in fiscal 2013 (fiscal 2013 total tax collections were 4.8% greater than the prior year and $627 million greater than forecast). Prior to 2009, Massachusetts relied on commercial paper for its interim cash flow needs but has more recently used RANs for a lower cost of funds.

Based on our analysis of the commonwealth's September 2015 cash-flow forecast, ending cash balances at each note maturity provide noteholders with a healthy cushion. At the April maturity of Series A, the projected cash balance is 6.7% of forecasted tax revenue and 4.3% of total revenue. For Series B, the projected cash balance is 5.3% of forecasted tax revenue and 3.5% of total revenue. For Series C, the projected cash balance is 9.4% of forecasted tax revenue and 6.1% of total revenue.

The commonwealth's rainy day fund, the Budget Stabilization Fund, is not included in the cash flow, although because the RANs are general obligations, we consider the fund a possible source of alternate liquidity, subject to legislative appropriation. The commonwealth had a healthy Stabilization Fund balance of $2.1 billion prior to 2009 that it was able to rely on during the last recession. The commonwealth was able to partially rebuild the Stabilization Fund in 2011 and 2012 -- to $1.65 billion -- but made several withdrawals in the fiscal years since then. Preliminary estimates show the Stabilization Fund with a fiscal 2015 ending balance of $1.25 billion balance, or 5% of tax revenue. An ending balance of $1.18 billion is projected for fiscal 2016, equal to 4.6% of estimated tax revenue.

LEGAL COVENANTS

The commonwealth's short-term borrowings are statutorily required to be repaid by the end of the fiscal year. The three staggered maturities of the notes (April 27, 2016; May 25, 2016; and June 22, 2016) is a key structural feature that provides strong cash margins for each separate series of notes. There are no advance set-asides prior to maturity, but the risk is mitigated by accuracy of past projections and quarterly cash flow updates.

MANAGEMENT

The commonwealth's financial best practices are generally very strong. Per statute, the Secretary of Administration and Finance is required to develop a consensus tax revenue forecast for the ensuing fiscal year with the house and senate committees of ways and means by January 15 of each year, before budget recommendations are developed. Subsequently, the secretary certifies the accuracy of the consensus revenue forecast two times per year and prepares new estimates if the estimate starts to diverge materially from actual collections.

The state devises multi-year financial plans and publishes a five-year forecast in its Long-Term Fiscal Policy Framework. The governor has executive authority to cut expenses without legislative approval resulting from a revenue shortfall. The commonwealth also conducts a debt affordability analysis and reports its audited financial results on a timely basis. Budget enactments have also been timely, and the commonwealth's financial flexibility is strong. There are no constitutional caps on revenue raising or spending increases. The commonwealth is subject to ballot initiatives, though per the state constitution, initiative petitions are subject to repeal or amendment by the legislature and initiative petitions that become statute can be amended like any other state law.

The commonwealth is required to deposit the entire year-end surplus and any tax revenue from excess capital gains into the Stabilization Fund, with 5% of the amount deposited then transferred to the State Retiree Benefits Trust Fund and 5% transferred to the commonwealth's Pension Liability Fund. However, the deposit of excess capital gains revenues into the Stabilization Fund has been suspended for fiscal 2015 and fiscal 2016. The commonwealth is also required to deposit certain one-time settlements and judgments into the Stabilization Fund.

KEY STATISTICS

-- Note maturities: April 27, 2016; May 25, 2016; June 22, 2016

-- Note borrowing % of projected receipts, FY2016: 2.9%

-- Projected cash balances: 6.1% of receipts in FY2016; 5.3% of receipts in FY2015

-- Audited cash balance, FY2014: 3.6% of revenues

OBLIGOR PROFILE

The Commonwealth of Massachusetts has a population of 6.7 million people and a gross state product of approximately of more than $420 billion. The state is economically well diversified and has very high wealth levels.

LEGAL SECURITY

The notes are general obligations of the commonwealth to which its full faith and credit will be pledged for the payment of principal and interest when due.

USE OF PROCEEDS

Proceeds of the notes will be used to bridge seasonal imbalances between revenue inflows and expenditure outflows.

RATING METHODOLOGIES

The principal methodology used in this rating was Short-Term Cash Flow Notes published in April 2013. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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