STANDARD & POOR'S RATINGS SERVICES
McGRAW HILL FINANCIAL

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Summary:

Boston, Massachusetts; General Obligation

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Summary:

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Credit Profile		
US$140.0 mil GO bnds ser 2015 A due 04/01/2035		
Long Term Rating	AAA/Stable	New
US$139.9 mil GO rfdg bnds ser 2015 B due 04/01/2029		
Long Term Rating	AAA/Stable	New
Boston GO		
Long Term Rating	AAA/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'AAA' long-term rating to Boston, Mass.' series 2015 general obligation (GO) bonds. In addition, Standard & Poor's affirmed its 'AAA' long-term rating on Boston's previously issued GO bonds. The outlook is stable.

The city's full faith and credit secures the bonds. The rating reflects our assessment of the following factors for the city:

- Deep and diverse economy, which is the anchor for the state and broader New England region;
- Strong budgetary flexibility with 2015 audited available reserves in excess of 20% of general fund expenditures and no plans to materially draw them down;
- Strong budgetary performance and stable revenue profile with no appreciable funding interdependence with the state or federal government;
- Very strong liquidity providing very strong cash levels to cover both debt service and operating expenditures;
- Very strong management environment and strong financial policies;
- Strong debt and contingent liability position, albeit bolstered by the city's low debt-to-market value and aggressive amortization; and
- Still sizable pension and other postemployment benefit (OPEB) liabilities, although we acknowledge that management is proactively managing them.

Proceeds from the series A bonds will be used to finance various capital projects. Proceeds from the series B bonds will be used to refund portions of the series 2005A, 2006A, 2007A, 2008A, and 2009A bonds outstanding for interest rate savings.

Very strong economy

We consider Boston's economy very strong. Boston is the 21th-largest city in the nation and the economic hub of New England. The city is the state capital and center for government-related activities. In addition, its economic strengths include world-renowned biomedical research capabilities, a large and broad-based high-tech and life science sector, and a substantial financial services sector. Supporting these strengths are a well-educated workforce and world-class higher education and academic medical centers, both within the city and surrounding area.

The city's projected per capita effective buying income is 126% of the U.S. level. Local unemployment is favorable, in our view, with the preliminary estimate for December 2014 at 4.5%. More broadly, unemployment in Suffolk County was 4.6% in December 2014. Unemployment has historically been below the national average. Based on our forecasts, we anticipate continued modest employment growth and steady unemployment rates through 2016. Gains will be varied and across multiple industries, but professional, financial, scientific, and technical services will be the largest sources of growth.

The city's tax base began recovering in 2012 following several years of decline as a result of the recession. The tax base is 65% residential, and the 10 leading taxpayers account for just 12% of assessed value (AV). Residential properties continue to show strength. Our latest forecasts show the region's median home price continuing to improve into 2016, boding well for the city's AV. We also anticipate that AV will continue to benefit from numerous economic development projects planned or under construction. Through 2015, the Boston Redevelopment Agency pipeline will have about 272 such projects, totaling $23 billion in development costs. The current market value per capita is $174,000.

Very strong management conditions

Through strong and proactive management actions and a versatile economy that has produced better-than-budgeted local revenue for the city's general fund, Boston has been able to maintain a strong financial position since the mid-1990s.

The city has been successful in managing discretionary spending and maintains tight control over employee headcount. We note that the city has effectively used an employee position review committee to maximize city resources, and that it has implemented a number of health insurance reforms that have provided significant cost savings, stabilizing a major budget driver.

On the whole, we consider Boston's management practices "strong" under our financial management assessment (FMA) methodology, indicating our view that the city's financial practices are strong, well embedded, and likely sustainable. Boston maintains "best practices" deemed critical to supporting credit quality, and these are well embedded in the government's daily operations and practices. Formal policies support many of these activities, adding to the likelihood that they will continue and transcend changes in the operating environment or personnel.

The city analyzes its revenue and expenditure forecasts over a two-year period, including the current operating budget. Officials update the three-year financial model annually and fully integrates it into the five-year capital improvement plan. Line-item and departmental budget assumptions, as well as revenue assumptions, are developed using adopted techniques such as multivariate regression modeling and historical trend analysis. The city monitors intrayear spending on an ongoing basis.

The city's Office of Budget Management prepares monthly variance reports that forecast a department's year-end position using actual year-to-date information. The mayor, with the approval of the city council, can make supplemental appropriations and budget adjustments on a regular basis. The mayor can also make certain adjustments up to a certain threshold within the total budget, without city council approval. City investments are made under local and commonwealth guidelines, with a dedicated treasury staff regularly reporting on holdings and investment performance. The city has formal debt management policies beyond debt limits prescribed by commonwealth statute. It also has informal targets for debt-service-to-budget limits and net present value savings thresholds for refundings.

In terms of reserves, the city affirms its commitment to maintaining an unassigned fund balance in excess of 15% of expenditures. Its required floors for its general fund reserves, except for the school department, include a segregated reserve fund equal to 2.5% of the preceding year's appropriation for city departments. The school department's policy is to maintain a contingency reserve at 1% of the current fiscal year's school department appropriation.

Very strong budget flexibility

We calculate available reserves at $784 million, or 29% of expenditures, at the close of 2014. Boston closed that year with an unassigned general fund balance of $532 million, equal to 19% of expenditures, and an assigned fund balance of $251 million, equal to 9% of expenditures. Despite the city's continued budget pressures stemming from reduced net state funding as well as higher expenditure demands, we anticipate that the city will adhere to its reserve policy limiting the unassigned fund balance in the general fund to 15% of the current fiscal year's operating expenditures.

Strong budgetary performance

In 2014, Boston realized a general fund surplus of $32.9 million, equal to 1.2% of operating expenditures. This marks the city's third consecutive annual general fund surplus. Across all governmental funds, after adjustment for capital outlay spent from bond proceeds, operations were also positive at 0.2% of expenditures.

The favorable budgetary performance stems from conservative budgeting and tight expenditure controls. We believe Boston maintains a stable and predictable revenue profile largely independent of state and federal revenue. Property taxes account for 63% of revenue, and collections are strong and stable. State aid accounts for 18%, and we note that state funding has also been stable recently, but we do recognize that net state assessments have continued to trend down as a percentage of budgetary expenditures.

We anticipate that Boston's operating performance will remain in line with that of years past. However, a winter with particularly heavy snow and ice totals could complicate matters and test management.

The 2015 budget totals $2.7 billion, a 3% increase over 2014 actual results, and includes a $40 million appropriation of reserves toward the OPEB trust fund. We note that the city recently entered into a successor agreement with its unions on health insurance that it anticipates will save roughly $45 million from the current baseline over the next five years. Moreover, the city settled collective bargaining contracts with 30 of its 31 unions, providing budgetary certainty through 2016. As a result, we anticipate a strong economy, and we believe that proactive and conservative budget management will likely continue and translate into strong budgetary performance during the next few fiscal years.

Very strong liquidity

Supporting the city's finances is what we consider very strong liquidity, with total government available cash at 38% of total governmental fund expenditures and at 785% of debt service. Further enhancing our view of the city's liquidity position is its strong access to external liquidity. The city is a regular market participant, having issued GO bonds frequently during the past several years.

Strong debt and liabilities

Following this bond issuance, Boston has roughly $1.2 billion of total direct debt. Overall, the city's total governmental funds debt service is 5% of total governmental funds expenditures and net direct debt is 40% of total governmental funds revenue. Bolstering our view of the city's debt burden is that the overall net debt is a low 1.4% of market value, and that amortization of principal debt is aggressive, with roughly 69% retired over 10 years.

In our view, the city's pension and OPEB liabilities will remain a budget pressure, but we acknowledge that management has proactively managed them. Pension and OPEB costs account for 10.9% of total governmental fund expenditures. The pension system is 70% funded with a current unfunded liability of $1.4 billion. The city anticipates fully funding the liability by 2025. Regarding OPEB, the unfunded actuarial accrued liability was lowered to an estimated $2.142 billion, as compared with $3.062 billion as of the prior valuation. The city has established OPEB trust funds and has begun funding them yearly. The amount on deposit in the OPEB trust funds to date is $255 million.

Outlook

The stable outlook reflects our view that Boston's strong underlying economy, very strong management, and predictable operating profile should translate into strong budgetary performance and operating flexibility during our two-year outlook horizon. The outlook also reflects our anticipation that Boston will maintain a strong debt and liability profile. Debt service costs, as well as pension and OPEB costs, should remain manageable within the current operating environment. For these reasons, we do not anticipate changing the rating during the next two years.

Related Criteria And Research

Related Criteria

- USPF Criteria: Local Government GO Ratings Methodology And Assumptions, Sept. 12, 2013
- Ratings Above The Sovereign: Corporate And Government Ratings—Methodology And Assumptions, Nov. 19, 2013

Related Research

- U.S. State And Local Government Credit Conditions Forecast, Dec. 10, 2014
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013

Ratings Detail (As Of March 6, 2015)		
Boston GO bnds		
Long Term Rating	AAA/Stable	Affirmed
Boston GO bnds		
Long Term Rating	AAA/Stable	Affirmed
Boston GO bnds		
Long Term Rating	AAA/Stable	Affirmed
Boston GO (wrap of insured) (FGIC & AGM) (SEC MKT)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
Boston GO		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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