

Massachusetts

Primary Credit Analysts:

Robin Prunty
New York
(1) 212-438-2081
robin_prunty@
standardandpoors.com

Secondary Credit Analysts:

Howard Mischel
New York
(1) 212-438-1521
howard_mischel@
standardandpoors.com

Credit Profile

US\$430.315 mil GO bnds cons loan 2009 ser A due 03/01/2039

Long Term Rating	AA/Stable	New
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US\$96.465 mil GO rfdg bnds 2009 ser A due 03/01/2010-2022

Long Term Rating	AA/Stable	New
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Massachusetts GO

Long Term Rating	AA/Stable	Affirmed
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Rationale

Standard & Poor's Ratings Services assigned its 'AA' long-term rating, and stable outlook, to Massachusetts' \$430.315 million general obligation (GO) bonds and \$96.465 million GO refunding bonds. At the same time, we affirmed the 'AA' long-term rating, and stable outlook, on the \$16 billion parity debt outstanding.

The ratings reflect our view of the commonwealth's:

- Strong and conservative budget management practices, with swift action to restore balance after identifying shortfalls in tax revenues for the current fiscal year;
- Continued healthy reserve levels despite some planned reductions in the current fiscal year, which in our opinion provide flexibility to manage through the current economic climate;
- High income and wealth levels;
- Deep and diverse economy, with weak trends emerging in line with national trends.

Standard & Poor's believes the commonwealth's high debt burden and significant unfunded pension liability restrain the rating.

Bond proceeds will retire \$350 million of bond anticipation notes outstanding due in March and provide new money for capital projects. The refunding bonds will retire

contract assistance bonds outstanding for debt service savings. Both issues will be fixed-rate bonds.

Massachusetts' financial position through fiscal 2008 was strong in our opinion, with good reserves. The stabilization balance (on a statutory basis) was \$2.25 billion in fiscal 2008 (7.1% of budgeted revenues and other sources). This compares favorably with \$1.14 billion in fiscal 2004. Contributing to the growth in balances through 2008 in our view was a strong economy and conservative revenue assumptions, with actual revenues exceeding forecasts annually since fiscal 2004. A strong reserve position is important, given Massachusetts' dependence on personal income (and related capital gains) taxes, which have been cyclical over time.

After addressing a budget deficiency of \$1.4 billion (about 5%) in October 2008, the secretary of administration and finance announced another \$1.1 billion revenue deficiency in January. Following the October revision, \$1 billion of spending reductions were implemented. In addition to the spending measures, the commonwealth will draw an additional \$200 million from the stabilization fund, leaving a balance of \$1.7 billion that will provide additional flexibility to manage the budget in the future. The pension funding schedule was extended from 2023 to 2025, which will save \$100 million. In January, Governor Deval Patrick announced plan to address the shortfall with additional spending reductions of \$191 million (including \$128 million in local aid distributions), minor revenue revisions, \$533 million in anticipated federal stimulus funds, and an additional draw of \$327 million from the stabilization fund. In our opinion, the commonwealth has moved swiftly to restore balance and the early action on the spending cuts should maximize their effectiveness. Cash flow has been stable in recent months following revenue anticipation note issuance in 2008. The amount of commercial paper outstanding was reduced in February by \$200 million (\$1 billion total program).

Standard & Poor's views Massachusetts' economy as deep and diverse. Expansion in the higher education, health care, financial, and service sectors has offset declines over time in manufacturing. Demographic trends in Massachusetts have been stable in our opinion, with 2008 population estimated at 6.5 million, 2.1% above 2000 levels. Unemployment rates increased sharply in the second half of 2008 but remain below national levels at 5.9% through November 2008. This contrasts with a rate of 4.1% in April 2008. Income levels are well above average in our opinion, with personal income 127% above national levels in 2007.

By most measures, Massachusetts' debt burden remains high relative to other states. The commonwealth has about \$16 billion of GO debt. Including appropriation, contingent liability, special obligation, and moral obligation debt, total tax-supported debt rises to about \$27.1 billion. Debt per capita stands at \$4,196 and debt to personal income at 8.5%. The commonwealth's capital investment plan through 2013 totals \$8.9 billion. This plan adheres to a debt affordability model and an annual bond cap but represents a significant increase of authorized unissued debt in our view. Legislation was introduced by the governor to extend the option of using the commonwealth's guaranty to help the Massachusetts Turnpike refinance \$800 million of debt related to swaps outstanding that, if used, will drive the debt burden higher. We believe the commonwealth's unfunded pension liability is sizable at \$12.1 billion. The funded ratio, at 75.2%, is below the 81% average for major state public pension plans. Beginning with the fiscal 2008 audit, the commonwealth must report its other postretirement benefit (OPEB) liability. Its accrued OPEB liability as of Jan. 1, 2006, was \$13.287 billion, assuming no prefunding of the liability. If prefunded, the liability is significantly reduced to \$7.56 billion.

Standard & Poor's maintains a "strong" Financial Management Assessment (FMA) score for Massachusetts. A strong FMA indicates that practices are strong, well embedded, and likely

sustainable. Many of the commonwealth’s management practices related to debt and financial management are embedded in statute. (For further information, see Massachusetts’ state review published Oct. 3, 2008, on RatingsDirect.)

Fiscal 2010 Budget Update

On Jan. 28, 2009, Governor Patrick released his recommended budget. The budget is based on the consensus tax revenue estimate for fiscal 2010 of \$19.5 billion or 0.4% above fiscal 2009. This forecast assumes that the recession will continue through the middle of 2009 followed by a slow recovery. The budget gap to start fiscal 2010 was estimated to be \$3.6 billion. The budget proposal includes various revenue enhancements including the elimination of certain exemptions for sales tax for a total of \$325 million. Spending was also restrained, with growth of just 0.5% above expected spending levels in 2009. The budget relies on a modest use of the budget reserve in our view, with \$489 million included in the budget proposal with the contribution into the fund suspended. This leaves about \$850 million to address any future budget shortfalls. The proposal also relies on use of stimulus funds in the amount of \$711 million. The commonwealth has only included the enhanced federal Medicaid matching funds in the budget proposal due to the uncertainty surrounding other federal aid amounts, which is relatively conservative in our view. While including nonrecurring resources in the proposal to address the forecasted revenue weakness, there is also a focus on recurring revenue and expenditure measures in our opinion, which should ease the transition back to structural budget balance when a more normal revenue growth returns.

Outlook

The outlook reflects our view of the commonwealth’s solid financial reserve position, an important credit factor for the state given its dependence on personal income (and related capital gains) taxes, which have been volatile during economic cycles. Massachusetts’ economy is substantial in Standard & Poor’s view, with above-average income levels. However, the economy and revenue base have been cyclical over time, which, along with demonstrated prudent budget management, underscores the importance of maintaining financial reserves.

<i>Ratings Detail (As Of 13-Feb-2009)</i>		
<i>Massachusetts GO cons In bn ds ser 1989B dtd 04/01/89 due 04/01/2009</i>		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
<i>Massachusetts GO cons loan (wrap of insured) (FGIC & BHAC) (SEC MKT)</i>		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
<i>Massachusetts GO (wrap of insured) (ASSURED GTY & AMBAC) (SEC MKT)</i>		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
<i>Massachusetts GO (wrap of insured) (ASSURED GTY & MBIA) (SEC MKT)</i>		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Massachusetts GO		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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