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FITCH RATES MASSACHUSETTS' $250MM GO BONDS 'AA+'; OUTLOOK STABLE

Fitch Ratings-New York-16 June 2010: Fitch Ratings assigns an 'AA+' rating to the following Commonwealth of Massachusetts general obligation (GO) bonds:

--$250 million consolidated loan of 2010, series B.

In addition, Fitch affirms the following ratings:
--Approximately $17.5 billion of outstanding Commonwealth GO and Commonwealth guaranteed bonds at 'AA+'.

The Rating Outlook is Stable.

The series 2010B bonds are expected to sell through negotiation the week of June 21, 2010.

RATING RATIONALE:

--Massachusetts has a fundamentally strong and wealthy economy, although population growth is slow.
--The Commonwealth has benefited from conservative budgeting and sound financial practices over time. Although significantly reduced in the downturn, reserves remain to provide a hedge against the Commonwealth's somewhat volatile revenue stream.
--Debt levels are high.

KEY RATING DRIVER:

--Continued timely action to ensure budget balance and maintenance of an adequate budgeted reserve position.

SECURITY:

Massachusetts' 'AA+' rating reflects considerable economic resources and a record of prudent financial management. Credit strengths are tempered by a very heavy debt burden; net tax-supported debt equals about 9% of personal income and Fitch expects that debt levels will remain high. The Rating Outlook is Stable based on the expectation that the Commonwealth will continue to act to ensure budget balance and maintain an adequate budgeted reserve position in a weak economic and revenue environment and as federal stimulus funds that have supported the budget expire.

The Commonwealth, with a somewhat volatile revenue system that quickly reflects changing economic conditions, has taken timely action to ensure budget balance in recent downturns while maintaining some level of reserves. With economic deterioration, tax revenue forecasts were reduced significantly over the course of fiscal 2009, from $21.4 billion in the enacted budget to actual results of $18.3 billion. The year ended down 13% (baseline) compared to fiscal 2008. Sales taxes dropped 6%, and personal income taxes fell 15.5%. The Commonwealth responded with spending cuts and controls, the application of extraordinary federal stimulus assistance funds, and a large reserve draw, and the year closed with a small surplus. The stabilization fund balance dropped from $2.1 billion at the close of fiscal 2008 to $841 million at fiscal 2009 year-end.

The budget for fiscal 2010, which ends on June 30, included a 25% increase in the Commonwealth's sales tax rate (to 6.25%) and other revenue measures totaling about $1 billion, as well as additional spending control, another reserve fund draw, and federal stimulus to address a gap of about $5 billion. Gaps that have developed over the course of the year, due to reduced revenue expectations and increased spending needs (largely for social services), have been addressed promptly. Through May 2010, actual revenue performance was $70 million below the downwardly revised estimate of $18.5 billion (as compared to the original budget forecast of $18.9 billion). Total taxes were down 4.6% (baseline) versus fiscal 2009, reflecting a 4.1% sales tax drop, a 5.9% personal income tax decline, and a 0.4% corporate and business tax increase. Underperformance in income tax revenues, largely attributable to weaker than expected capital gains-related revenue, is largely offset by above-forecast returns of the other tax revenues. Fiscal 2010 is expected to end with a stabilization fund balance of about $650 million.

The consensus tax revenue forecast for fiscal 2011 assumes baseline growth of 2.5% from fiscal 2010. The executive budget proposal for the year was released in late January 2010. The governor's proposal closed an estimated gap of $2.75 billion, including through federal stimulus funds of $1.4 billion (with more than $600 million of that from an assumed six-month extension of federal stimulus funds related to the Medicaid program), up to $300 million from debt restructuring for budget relief, and a $175 million reserve fund draw. Following the 25% increase in the sales tax rate that became effective on Aug. 1, 2009, the executive budget did not include any broad-based tax increases. The House and Senate budgets do not incorporate a reserve fund draw or any revenue actions, replacing those monies with local aid and higher education cuts. As the extension of federal stimulus funds related to the Medicaid program has not yet been approved, the governor recently proposed additional cuts in the amount of the funds; the legislature is expected to finalize a budget that is balanced in the absence of these monies before the end of the fiscal year.

The variability and unpredictability of capital gains-related tax revenue has been a key factor in the volatility of the Commonwealth's overall budget. The governor has proposed a new mechanism for budgeting capital gains-related tax revenue that would limit the amount of such revenue that could be included in the Commonwealth's budget going forward, with excesses dedicated to reserve and other post-employment benefit (OPEB) funding. Fitch believes that this change, which has been passed by both the House and the Senate, would be a budgeting policy improvement.

Massachusetts has a fundamentally strong and wealthy economy, with the third highest personal income per capita in the nation (127% of the U.S.). The Commonwealth experienced among the steepest employment drops in the country during the last recession and, despite registering year-over-year employment gains in every month from July 2004 to September 2008, did not regain its prior peak. Employment began to decline in November 2008 but losses have been below those of the U.S. The year-over-year rate of loss in the Commonwealth was 0.9% for April 2010, compared to 1.0% for the nation, following losses of 3.6% and 4.3%, respectively, in 2009. The Commonwealth's unemployment rate of 9.2% in April 2010 was high for Massachusetts but 93% of the U.S. level. Job losses have been significant across all sectors except for the important education and health services sector.

Applicable criteria available on Fitch's website at 'www.fitchratings.com' include:

--'Tax-Supported Rating Criteria' (Dec. 21, 2009);
--'U.S. State Government Tax-Supported Rating Criteria', (Dec. 28, 2009).

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