



RATING ACTION COMMENTARY

Fitch Rates Massachusetts' \$1 Billion GO Bonds 'AA+'; Outlook Stable

Thu 13 Apr, 2023 - 5:12 PM ET

Fitch Ratings - New York - 13 Apr 2023: Fitch Ratings has assigned a 'AA+' rating to approximately \$1 billion Commonwealth of Massachusetts general obligation (GO) bonds, consisting of:

--\$720 million General Obligation Bonds Consolidated Loan of 2023 Series A;

--\$275 million General Obligation Bonds Refunding Bonds 2023 Series A.

Par amounts are subject to change pending final sale. The bonds are expected to be offered by negotiation mid-May 2023. Bond proceeds will finance or reimburse the Commonwealth for various capital expenditures and refund outstanding bonds.

Fitch has also affirmed the commonwealth's Long-Term Issuer Default Rating (IDR) at 'AA+' and the ratings on GO and other bonds linked to the IDR of the commonwealth as detailed at the end of this release.

The Rating Outlook is Stable.

RATING ACTIONS

ENTITY / DEBT ↕	RATING ↕		PRIOR ↕
Massachusetts, Commonwealth of (MA) [General Government]	LT IDR	AA+ Rating Outlook Stable	AA+ Rating Outlook Stable
	Affirmed		
Massachusetts Turnpike Authority Metropolitan Highway System (MA) /Metro Highway System Revenues - Subordinated Obligations/1 LT	LT	AA+ Rating Outlook Stable	Affirmed AA+ Rating Outlook Stable
Massachusetts, Commonwealth of (MA) /Commonwealth Guaranteed Revenues/1 LT	LT	AA+ Rating Outlook Stable	Affirmed AA+ Rating Outlook Stable
Massachusetts, Commonwealth of (MA) /General Obligation - Unlimited Tax - MDFA/1 LT	LT	AA+ Rating Outlook Stable	Affirmed AA+ Rating Outlook Stable
Massachusetts, Commonwealth of (MA) /General Obligation - Unlimited Tax/1 LT	LT	AA+ Rating Outlook Stable	Affirmed AA+ Rating Outlook Stable

[VIEW ADDITIONAL RATING DETAILS](#)

SECURITY

The GO bonds are general obligations of the commonwealth, to which its full faith and credit are pledged. A statutory state tax revenue growth limit does not exclude principal and interest on debt obligations from the ramifications of the limit, but any impairment of debt service due to tax revenue growth is highly unlikely.

ANALYTICAL CONCLUSION

The commonwealth's 'AA+' IDR reflects its considerable economic resources, adroit management of economic and revenue cyclicalities and strong budget controls. A strong reserve funding mechanism that shields the general fund from capital gains-related volatility has accelerated rebuilding of Massachusetts' stabilization fund. The commonwealth carries a long-term liability burden for debt and Fitch-adjusted net pension liabilities that is well above the U.S. state median, but remains a moderate burden on resources.

Economic Resource Base

The commonwealth has a broad and wealthy economy. Education levels are high, and although population growth is below the U.S. average, it is strong within the northeast region. The strength of the health care, technology and education sectors has supported GDP growth comparable with the nation's over time, and leaves it well-positioned for solid future gains. Measured by per capita personal income, Massachusetts is the wealthiest state in the nation.

KEY RATING DRIVERS

Revenue Framework: 'aaa'

Tax revenues are diverse but dominated by individual income taxes, which are sensitive to economic conditions, particularly the components related to capital gains. Baseline growth prospects for taxes are strong, driven by the commonwealth's underlying economic fundamentals.

Expenditure Framework: 'aaa'

Consistent with most states, the natural pace of spending growth is likely to marginally exceed expected revenue growth over time, requiring ongoing cost control. The commonwealth has ample ability to reduce spending through the economic cycle.

Long-Term Liability Burden: 'aa'

Liability levels in Massachusetts, while comparatively high for a U.S. state, are a moderate burden on resources. The commonwealth's above-average liability position is partly the result of state funding of both capital needs and pensions that are more commonly funded at the local level, primarily for K-12 education.

Operating Performance: 'aaa'

The commonwealth has superior gap-closing capacity supported by conservative budgeting, ongoing fiscal monitoring and a requirement to cut spending in response to revenue gaps, and a mechanism to redirect a portion of economically sensitive capital gains tax receipts into the stabilization fund, the commonwealth's budget reserve.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--Continued efforts to maintain structural balance during periods of economic growth, particularly in light of increasing carrying costs, and/or preservation of reserves at or near current levels could lead to an improvement in Fitch's assessment of budget management;

--A sustained reduction in the long-term liability burden closer to, or below, 10% of personal income, accompanied by a reduction in carrying costs.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A slowing of economic growth that signals the commonwealth's revenue growth prospects will trail national economic growth;

--Rapid growth in spending demands, particularly for fixed costs such as pension liabilities, which weakens Massachusetts' expenditure flexibility and historically strong operating performance;

--An increase in long-term liabilities that results in an elevated burden consistently exceeding 20% of personal income.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating

horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

CURRENT DEVELOPMENTS

Massachusetts Economic Update

Massachusetts has recovered a lot of economic activity lost to the pandemic. Early in the pandemic, Massachusetts suffered a more severe job market shock than the nation as a whole, with non-farm payrolls falling 18% from February to April 2020, steeper than the national decline (15%). While Massachusetts has recovered 99% of jobs lost at the pandemic's trough, this is well below the states median of 111% national jobs recovery rate as of February 2023.

Headline unemployment in February of 3.7% is just above the 3.6% national unemployment rate. The commonwealth's employment-to-population ratio (EPOP) in February 2023 of 62.6% remains below its pre-pandemic ratio of 64.0% but compares favorably to the national EPOP of 60.2%.

Massachusetts Budgetary Update

Massachusetts has navigated the economic and fiscal disruptions of the pandemic without materially affecting its strong operating performance, and remains well-positioned to continue doing so. The state's position has been bolstered by a solidly funded stabilization fund, the commonwealth's budget reserve, the substantial federal economic stimulus and pandemic aid, and strong revenue performance emerging from the pandemic.

Individual income tax receipts drove state revenues to continue to outperform prudent budget expectations in fiscal 2022. Fiscal 2022 tax revenues of \$41.1 billion (including tax-related settlements) were 11.6% higher than the January 2022 revised forecast of \$36.9 billion. Revenue performance has slowed in fiscal 2023, as the state anticipated, with the January 2023 consensus revenue forecast for tax revenues now more than 3% below the prior year, but still marginally higher than budgeted at \$39.8 billion.

The transfer of capital gains revenue above the statutory threshold brought the stabilization fund to a new high of \$6.9 billion (16.9% of total revenue) in fiscal 2022, marking significant increases from the \$4.6 billion balance (13.5% of total revenue) in fiscal 2021, and the \$2.3 billion balance the commonwealth had in fiscal 2007 heading into the Great Recession.

The current fiscal 2023 budget included several one-time items and no tax reductions. Notable items included a \$485 million increase in chapter 70 aid to cities and towns, \$266 million to the Massachusetts Bay Transportation Authority (MBTA) for safety upgrades, and an additional \$1.5 billion to the stabilization fund, although that will be dependent on the size of the capital gains taxes to be collected.

Newly-elected Governor Healey filed two supplemental appropriations totaling just over \$1 billion that would include additional funding for the emergency shelter system, an extension of universal school meals, an offramp from federal nutrition assistance programs, and fully paying down pension liabilities attributable to the 2015 early retirement incentive program, among other priorities. The legislature has so far approved \$388 million for priorities including emergency shelter, enhanced nutrition assistance, and school meals.

The governor's budget proposal for fiscal 2024 incorporates a 1.6% increase in consensus revenues to \$40.41 billion, excluding \$1 billion from the 4% surtax on personal income above \$1 million that was approved by voters in November 2022 and will be allocated to education and transportation initiatives. The governor's budget proposal increases spending 4.1% above the fiscal 2023 budget and incorporates tax reductions totaling \$859 million; \$742 million of the reduction will come from the operating budget.

Massachusetts received \$5.3 billion in direct ARPA federal aid for the state, as well as \$3.4 billion for local governments and over \$1 billion for transit. Approximately \$5 billion of ARPA funds have been allocated to a specific use with 2.3 billion spent as of Dec. 31, 2022. The commonwealth allocated the funds to health and human services (\$1.1 billion), homeownership and housing (\$600 million), the unemployment trust fund (\$500 million), essential workers (\$500 million), water, sewer and environmental infrastructure (\$400 million) and other one-time projects (\$900 million).

Chapter 62F Revenue Growth Limits Triggered in Fiscal 2022

Fiscal 2022 is the first year since 1987 that commonwealth revenue growth exceeded the limit, leading to approximately \$2.9 billion in income tax refunds scheduled for fiscal 2023 and drawn from the sizeable fiscal 2022 ending balance, most of which was paid out in

November and December of 2022. Chapter 62F limits state tax revenue growth of a given fiscal year to the average of the prior three years' wage and salary growth.

CREDIT PROFILE

Fitch has affirmed the ratings on the commonwealth's GO and GO-linked bonds of the commonwealth as follows:

--GO bonds at 'AA+';

--Massachusetts Development Finance Agency (MDFA) special obligation bonds (commonwealth contract assistance) at 'AA+';

--Commonwealth guaranteed bonds issued by the MBTA and the University of Massachusetts Building Authority, at 'AA+';

--MassDOT metropolitan highway system revenue bonds (subordinate), commonwealth contract assistance secured, at AA+.

For the commonwealth contract assistance bonds issued by MDFA and commonwealth-guaranteed bonds issued by the MBTA and the University of Massachusetts Building Authority, the commonwealth's obligation under the contract to make payments equal to debt service is a general obligation of the commonwealth, to which its full faith and credit are pledged.

For the MassDOT MHS subordinate revenue bonds, the commonwealth's annual fixed, dedicated payments are a full faith and credit obligation of the commonwealth and are expected to cover all subordinated debt service, linking the rating to the 'AA+' rating of the commonwealth, rather than to the MHS toll revenues, which are also pledged to the bonds on a subordinated basis.

Although a large share of outstanding debt is variable rate and thus exposed to potential, though unlikely, risks associated with variable rate debt, Fitch expects that MassDOT would work with the commonwealth if necessary to ensure that the annual payments are sufficient for debt service.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis and Committee for a Responsible Federal Budget.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit

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APPLICABLE CRITERIA

[U.S. Public Finance Tax-Supported Rating Criteria \(pub. 04 May 2021\) \(including rating assumption sensitivity\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

ADDITIONAL DISCLOSURES

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Massachusetts Bay Transportation Authority (MA)

EU Endorsed, UK Endorsed

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