Moody's
INVESTORS SERVICE

New Issue: MOODY'S ASSIGNS A2 UNDERLYING AND Aa2 ENHANCED RATING TO SPRINGFIELD'S (MA) $17.8 MILLION GO QSC BONDS; OUTLOOK IS STABLE

Global Credit Research - 03 Jun 2010

A2 UNDERLYING RATING AND STABLE OUTLOOK APPLY TO $333 MILLION OF GENERAL OBLIGATION DEBT, ENHANCED Aa2 RATING WITH STABLE OUTLOOK ALSO APPLIES

Municipality
MA

Moody's Rating

ISSUE	UNDERLYING RATING	RATING
State Qualified General Obligation Qualified School Construction Bonds (Federally Taxable)	A2	Aa1

Sale Amount	$17,864,000
Expected Sale Date	06/01/10
Rating Description	General Obligation State Qualified

Opinion

NEW YORK, Jun 3, 2010 -- Moody's Investors Service has assigned an A2 underlying rating and an enhanced Aa2 rating to the City of Springfield's $17.8 million State Qualified General Obligation Qualified School Construction Bonds. Concurrently, Moody's has affirmed the city's long term A2 rating, affecting approximately $333 million in outstanding general obligation debt; the outlook remains stable. The bonds are issued as Federally Taxable Qualified School Construction Bonds and are secured by the city's general obligation limited tax pledge as debt service has not been voted exempt from the levy limitations of Proposition 2 ½. The bonds are issued to finance school construction projects and are structured as term bonds due on June 1, 2027. The city plans to deposit annual debt service payments to a sinking fund, which are intended to be used to offset the anticipated loss in state aid in fiscal 2027 when the State Treasurer intercepts Springfield's state aid payments to retire the bonds. Approximately $333 million of Springfield's outstanding bonds are authorized under the Commonwealth of Massachusetts (G.O. rated Aa1/stable outlook) Qualified Bond Program (QBP) and carry an enhanced rating of Aa2 with a stable outlook.

The A2 rating reflects the city's sizeable tax base, an improved financial position, with significant transfers to reserves, and Springfield's progress toward establishing sound financial and administrative management practices as it completes its first year of autonomous operations after 5 years under a control board. The rating also incorporates the city's weak economy, with high unemployment, declining population, and very low wealth measures, although it does benefit from institutional presence and it remains a regional employment and services center. Additionally, the rating reflects an above-average debt profile heavily supported by state reimbursements. The stable outlook reflects Moody's expectation that in the long term the city will continue to manage in compliance with recently adopted financial management ordinances.

STATE QUALIFIED BOND PROGRAM PROVIDES ENHANCED SECURITY

The Aa2 rating with a stable outlook assigned to the Commonwealth of Massachusetts' Qualified Bond Program reflects the inherent strength of the direct-pay arrangement authorized by state statute in which the State Treasurer makes debt service payments on qualified bonds and notes directly to a state-approved paying agent. The State Treasurer then withholds an amount equivalent to the debt service payment from the local unit's quarterly state aid payments. Moody's believes that the program's sound mechanics and Springfield's adequate 6.75 times coverage levels projected in fiscal 2011 provide sufficient funds for timely debt service payments. The qualified bond program rating is linked to the Commonwealth of Massachusetts' strong general obligation credit rating of Aa1 with a stable outlook.

SPRINGFIELD FINANCE CONTROL BOARD DISBANDED, LOCAL CONTROL RE-ESTABLISHED

The Springfield Financial Control Board (FCB) was established in July 2004 to secure the financial stability of the city after several years of significant operating deficits, depleted reserves and other accumulated financial liabilities in the city's internal service funds including health insurance. The authorization expired and the FCB was disbanded on June 30, 2009. Under the FCB Springfield was granted the city access to a $52 million trust fund, with aggregate borrowing to be fully repaid, albeit without an interest charge, originally required by fiscal 2012. The city has borrowed the entire $52 million from the trust fund but expended only $32 million. The $20 million remainder was originally reserved for economic development. Subsequently these funds, along with $26.8 million from general fund reserves, were transferred to a trust fund to support a city-wide financial aid counseling and scholarship program for graduation high school seniors, using the interest earnings from the trust fund. Legislation was enacted to extend repayment of the state loan for 15 years (through fiscal 2022), which has reduced the city's medium-term debt service obligations and is expected to improve operating flexibility.

SIGNIFICANT IMPROVEMENT IN ADMINISTRATIVE EFFICIENCY

The city has completed a comprehensive review and restructuring of non-school departmental operations, which is expected to yield significant departmental expenditure savings in the medium term. Notable accomplishments include: the January 2007 transfer of administrative responsibility for employee health benefits to the commonwealth's Group Insurance Commission (GIC), which is expected to minimize premium increases in the long term; the August 2005 transfer of the Springfield Contributory Retirement System's roughly $280 million in assets to the commonwealth's Pension Reserves Investment Trust (PRIT) in an effort to streamline administrative costs and enhance investment return; and most notably, Springfield's successful settlement of 28 of its outstanding labor contracts, covering over 5,000 represented employees eliminating a potential $40 million liability for retroactive salary increases related to a wage freeze implemented on July 1, 2003. Expirations range from fiscal 2010 to 2013, providing stability in labor costs in the near term with annual payroll increases projected at a reasonable 3.1%, assuming the maintenance of current employment levels. The city also appointed a new chief administrative and financial officer, police commissioner and superintendent of schools. Although the city may experience pressure to increase public safety expenditures near term due to Springfield's serious city-wide public safety issues, officials report that each department is undergoing thorough reorganization to modernize operations and improve services. The city's school department, which represented 56% of fiscal 2009 expenditures and the majority of city employees, is currently under review for possible consolidation of similar city and school administrative functions as well as improved operating efficiency and purchasing procedures, all of which could result in savings.

STATE AID CUTS CONTINUE TO PRESSURE OPERATING BUDGET

Springfield's financial position improved dramatically through fiscal 2008, however reductions in state aid and generally sluggish local revenue performance in fiscal 2009 and 2010 have pressured the city's ability to boost reserves. Anticipating a mid-year $4.6 million state aid decrease, the city reduced expenditures to offset the cut and operations in fiscal 2009 generated a modest operating surplus. Undesignated general fund balance rose to $41.7 million, a satisfactory 7.4% of general fund revenues. However, the Financial Reserves Stabilization Fund was tapped for one-time capital needs and dropped by roughly $6 million to $36.5 million, bringing available reserves to $87 million, a reasonable 15.5% of revenues but a decline from the fiscal 2008 peak of $109 million, a more healthy 19.7% of revenues. The city's expenditure reductions were maintained in fiscal 2010 and operations are expected to be positive, replenishing the $10 million in appropriated free cash and generating a small $1.4 million surplus. Springfield's Stabilization Fund is expected to total $43.6 million at year-end (June 30) after a $21 million transfer in from fiscal 2009 free cash and an appropriation out of $12.5 million toward the fiscal 2011 budget. City officials plan to increase free cash, the commonwealth's certification of legally-available fund balance, incrementally to maintain between 5 and 10% of operating revenues in reserve.

The fiscal 2011 budget is under development and the current proposal includes an overall 1% expenditure increase. Management successfully closed a $45.5 million budget gap by imposing additional departmental expenditure reductions, including school department cuts, extending the city's pension funding schedule to 2040 (from 2028) and an appropriation of $12.5 million in reserves. Springfield's ongoing reliance on free cash appropriations to fund operating budgets could limit improvement in long-term financial and credit strength. Despite the medium-term certainty provided by the city's collective bargaining contracts, recently settled through fiscal 2012 (although the teachers' contract expires in fiscal 2010, representing nearly half of the city's 5000 municipal employees), the city faces ongoing expenditure pressure from salary-related expenditures as pension contributions increase to improve the current 42.6% funding status and meet the commonwealth's recently-extended required full-funding deadline of 2040.

Although funding of OPEB liabilities is not required in Massachusetts, the city is in compliance with GASB 45 reporting requirements and has identified a preliminary unfunded accrued actuarial liability of up to $450 million; future funding for this liability above the current pay-as-you-go level of $57 million has not been budgeted and could exert additional expenditure pressure in the future. The city's success in resolving its projected operating deficits will be an important factor in maintaining a healthy long-term credit profile. Aid from the commonwealth remains Springfield's primary revenue source at 56.4% of general fund revenues in fiscal 2009. Under the state-wide Proposition 2 ½ property tax limit, Springfield remains constrained in its ability to raise additional property tax revenues which represented 28.1% of revenues in fiscal 2009. Collections had averaged roughly 97% since 2000 but have improved to over 99% in fiscal 2008 and 2009, although some of the improvement reflects aggressive collection of prior years' overdue accounts. While the city's financial position has improved, Springfield is likely to face continuing challenges in the intermediate term as operating and capital expenditures continue to rise and state and local revenue growth remains flat.

TAX BASE DECLINES LIMIT PROPERTY TAX GROWTH

Springfield's $8.4 billion tax base is expected to continue to experience mild contraction in assessed values in the near term, in line with regional and national real estate market trends. Valuations dropped by 7.2% and 3.4%, respectively, in fiscal 2009 and 2010 and an additional drop of 5% is expected in fiscal 2011, reflecting market values as of January 1, 2010. However, assessed valuation declines are uniquely problematic in Springfield, as the city's available levy capacity under Proposition 2 ½ has been depleted in fiscal 2010, and subsequent assessed valuation declines could reduce growth in the city's property tax levy in future years, exerting additional pressure on the operating budget. Proposition 2 ½ was enacted in 1980 and has dual limits: the annual property tax levy may increase up to 2 ½% of the prior year's levy but ultimately the property tax levy is limited to 2 ½% of assessed value. The city's available levy capacity was a narrow $18 million in fiscal 2009 and dropped to $4 million in fiscal 2010, an extremely slim 2.3% of the fiscal 2010 tax levy. This capacity peaked recently in fiscal 2008 at $40 million, a more comfortable 27% of the fiscal 2008 levy. Following a 30% decline in the early 1990's the city experienced a sustained period of assessed valuation growth averaging 7.4% annually since 2000. However, declines in fiscal 2009 and 2010 reflected regional weakening in the residential sector, which in Springfield comprises a substantial 81% of the tax base. The city is the center of economic activity in western Massachusetts, with health care, financial services, government, manufacturing and higher education sectors represented as major employers. While the city has enjoyed modest new growth revenue, averaging $4.2 million annually since 2004, it provides only limited additional financial flexibility relative to its $560 million operating budget. Building permit activity is expected to continue as city-wide redevelopment projects progress. City officials report that new growth is driven by single-family home construction and renovations as well as commercial development and newly-captured personal property levies. Not captured in the city's equalized value are the tax-exempt facilities of Western New England College and Law School (rated Baa2), Springfield College (rated Baa1), Springfield Technical Community College (not rated) and American International College (not rated). Total enrollment is estimated at 24,300 while employment totals an estimated 2,000 full-time-equivalent positions. Recent expansion of these institutions has yielded approximately $37 million in new educational facilities, underscoring the importance of the higher education sector as an important source of stability and growth to the local economy.

City officials plan to maximize tax base growth through implementation of a neighborhood development plan designed to target commercial redevelopment and blight reduction as well as roadway, parks and infrastructure upgrades. Funding sources have not yet been identified for every project, however the city is seeking significant private, federal and state participation in this initiative. Construction of a new federal courthouse was recently completed and other notable projects include roadway improvements, funded by ongoing commonwealth Chapter 90 funding, and a $12 million private redevelopment of the former basketball hall of fame that became an entertainment and fitness facility. The city may offer tax incentives to private developers to encourage additional development but officials are evaluating the tax incentive policy before finalizing future agreements. Springfield is also coordinating public and private agencies to manage residential bank foreclosures, which have increased over 28% since 2007. Reflecting its struggle with economic decline in recent decades, the city's Income and wealth levels remain significantly lower than state medians: the 1999 poverty level is elevated at 23.1% and the February 2010 unemployment level of 14.5% is significantly higher than commonwealth and national medians of 10% and 10.4%, respectively. The city's equalized value per capita of $56,292 is well below commonwealth and national medians of $142,509 and $87,927, respectively.

SUBSTANTIAL DEBT BURDEN REFLECTS STATE LOAN

Moody's anticipates that the city's elevated direct debt burden (4.6% of equalized value) will increase over the medium term as the city begins to address accumulated deferred maintenance and other capital needs while also assuming the burden of repayment of the commonwealth's $52 million loan. Amortization of principal is above average at 80.1% within 10 years, inclusive of the proposed repayment of the state loan. The city receives annual reimbursement from the commonwealth for 90% of debt service related to bonds originally issued to finance school construction projects, which represent roughly 62% of the city's outstanding general obligation debt. The city's debt burden falls to a still-elevated 4.3% after deducting the expected school construction reimbursement. Gross debt service accounted for a reasonable 7.5% of the city's operating expenditures in fiscal 2009. Springfield is re-evaluating its capital improvement program (CIP) and financing plans for are incomplete at this time. However city management expects to leverage state and federal funding for up to 60% of the CIP. Furthermore, included in management's comprehensive financial policies are prudent debt limits including maximum future general fund debt service of 5% of annual revenues and a minimum principal amortization schedule of 65% within 10 years. Springfield has no exposure to variable or auction rate debt or swap agreements.

Outlook

The stable outlook reflects Springfield's stabilizing financial position with satisfactory reserve levels, as well as the city's improving capacity for local financial management following the disbanding of the FCB . Nonetheless, serious financial and administrative challenges remain and are compounded by recessionary economic conditions and persistent appropriations of free cash. Also incorporated in the stable outlook, and balancing the solid positive financial and administrative progress achieved under the FCB, are significant unfunded pension and OPEB liabilities, a weak regional economy, declining state aid, negligible flexibility under Proposition 2 ½ and limited ability to raise local revenues. Adherence to sound financial and management policies, effective long-term capital planning and sound economic development programs will be critical to enhancing the city's credit strength.

WHAT COULD MOVE THE RATING UP?

*Trend of operating surpluses and augmentation of unrestricted reserves outpacing revenue growth

*Effective multi-year planning resulting in balanced budgets without use of one-time revenues

*Compliance with Springfield's financial ordinances

*Tax base expansion resulting in new growth revenue exceeding current levels

*Progress toward required funding of pension and management of OPEB liabilities

WHAT COULD MOVE THE RATING DOWN?

* Return to deficit operations

*Increasing reliance on one-time revenue sources in the medium term

*Reduced liquidity requiring a return to cash flow borrowing for operating needs

*Failure to maintain adequate control over operating expenditures

*Less conservative budgeting assumptions

*Reductions in state and federal aid below current levels

*Significant declines in tax base growth

KEY STATISTICS

2008 Population (estimate, US Census): 150,640 (-0.9% since 2000)

2009 Equalized Valuation: $8.48 billion

2009 Equalized Valuation per Capita: $56,292

Average Annual Growth, Equalized Valuation (2003-2009): 9.7%

Direct Debt Burden: 5.2% of equalized valuation

Overall Net Debt Burden, adjusted for commonwealth school construction aid: 4.3% of equalized valuation

Amortization of Principal (ten years): 80%

1999 Per Capita Income: $15,232 (58.7% of commonwealth, 70.6% of nation)

1999 Median Family Income: $36,285 (58.8% of commonwealth, 72.5% of nation)

FY09 General Fund Balance: $58 million (10.4% of General Fund revenues)

FY09 Available Reserves: $87 million (15.5% of General Fund revenues)

Post-sale long-term G.O.L.T. debt outstanding: $337 million ($333 million state-qualified)

PRINCIPAL METHODOLOGY

The principal methodology used in assigning the rating was "General Obligation Bonds Issued by U.S. Local Governments," published in October, 2009, and available on www.moodys.com in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

LAST RATING ACTION

The last rating action with respect to the City of Springfield, Massachusetts was on April 21, 2009 when a municipal finance scale underlying rating of Baa2 with a stable outlook was assigned to the City of Springfield's General Obligation State Qualified Municipal Purpose Loan of 2009 Bonds. That rating was subsequently recalibrated to A2 on April 23, 2010.

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