STANDARD & POOR'S

PUBLIC FINANCE

Massachusetts

Credit Profile		
US$621.43 mil GO bnds cons loan of 2009 Series B ser 2009B due 07/01/2038		
Long Term Rating	AA/Stable	New
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' $300 million general obligation (GO) bonds, series B, $250 million GO bonds, series 2009 C, and $71.43 million GO bonds, series D. At the same time, we affirmed the 'AA' long-term rating on the commonwealth's $16 billion parity debt outstanding.

Bond proceeds will reimburse the commonwealth for various capital expenditures that are included within the current capital spending plan.

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 wealth and income 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.

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, were 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.

In line with most other states, the commonwealth has adjusted its revenue forecast for fiscal 2009 several times. General fund revenue loss is estimated at $3.17 billion with adjustments in October 2008 ($1.4 billion), January ($1.1 billion), April ($156 million) and May ($953 million). To restore balance, the commonwealth has identified $1.3 billion of spending reductions, $236 million of revenue enhancements, $984 million of federal recovery aid, and $1 billion of stabilization fund balance. The original budget had assumed a $401 million drawdown of the rainy day fund. With the additional utilization in fiscal 2009, the stabilization fund balance is projected by the commonwealth to be about $800 million at fiscal 2009 year-end, or 4.4% of projected fiscal 2010 revenues. Due to the steady deterioration in revenues for fiscal 2009, the consensus revenue forecast for fiscal 2010 has been revised downward to $17.99 billion from $19.5 billion, and the budget remains under deliberation. 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 to $456 million in early May ($1 billion total program).

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.

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 have been stable in our opinion, with 2008 population estimated at 6.5 million, 2.1% above 2000 levels. Unemployment increased to 7.8% through April 2009, which is well above 2008's 5.3% but below the national level of 8.5%. Income levels are well above average in our opinion, with personal income 128% above national levels in 2008.

Outlook

The outlook reflects our view of the commonwealth's solid financial reserve position and pro-active approach to managing the current budget imbalance. These are important credit factors for Massachusetts given its dependence on personal income (and related capital gains) tax revenues, which has 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.

Fiscal 2010 Budget Update

On Jan. 28, 2009, Governor Deval Patrick released his 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 at $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 and the contribution into the fund suspended. This leaves about $850 million to address any future budget shortfalls. The proposal also relies on the use of about $711 million of federal stimulus funds.

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, which, in our opinion, should ease the transition back to structural budget balance when a more normal revenue growth returns. Since the time of the budget release, the American Recovery and Reinvestment Act was approved and increased federal funding is now expected to be available. The House of Representatives approved a budget for fiscal 2010 that used the original consensus tax revenue estimate of $19.5 billion. An increase in the state sales tax to 6.25% from 5% was included in the budget. The new consensus revenue forecast is now $17.99 billion. On May 13, the Senate Committee on Ways and Means released its budget, which includes the updated revenue forecast but does not include an increase in the sales tax. Under the Senate's plan, the stabilization fund would be decreased by $314 million.

Debt And Liabilities

By most measures, Massachusetts' debt burden remains high relative to other states. The commonwealth has about $16 billion of GO debt. Of this amount, 78% is fixed rate while $3.6 billion (22%) is variable rate and $3.3 billion of this amount is hedged with interest-rate swaps. The commonwealth has a range of other debt obligations outstanding, including those supported by the state-wide sales tax, contract assistance debt, and debt subject to annual appropriation. Budgeted debt service on GO bonds was 6.4% of budgeted expenditures in fiscal 2008. The commonwealth's capital investment plan through 2013 totals $14.3 billion, with $8.9 billion of bond issuance projected. 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 extended to provide the commonwealth's guaranty to the Massachusetts Turnpike Authority's swap obligations to avoid significant termination costs. The authority is expected to make the required annual payments. We believe the commonwealth's unfunded pension liability is sizable at $12.1 billion (state employees and teachers). The funded ratio through Jan. 1, 2008, improved to 78.6%, which is slightly below the 83% average for major state public pension plans. The report for the State Retirement System, released on Jan. 1, 2009, shows a market value decline of 29.4%. The commonwealth's accrued other postemployment benefits (OPEB) liability as of December 2008 was $15.64 billion, assuming no prefunding of the liability. If prefunded, the liability is reduced to $11.6 billion. The State Retiree Benefits Trust Fund was created and received a one-time transfer of $400 million in fiscal 2008. A special commission was created and released a report in July 2008 that recommended that a strategy be developed to fund the liability. Three funding sources were identified: tobacco settlement funds, budgetary surpluses, and legislative appropriations. No funding is included in the fiscal 2009 budget but the governor has proposed a funding plan that begins in fiscal 2011.

Related Research

USPF Criteria: "GO Debt," Oct. 12, 2006

Ratings Detail (As Of 18-May-2009)		
Massachusetts GO bnds cons ser D dtd 11/01/2001 due 11/01/2003-2012 2014-2021		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Massachusetts GO bnds (ARS) ser 2007D1 & D2 dtd 08/16/2007 due 08/01/2018		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Massachusetts GO cons ln bnds ser 1989B dtd 04/01/89 due 04/01/2009		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Massachusetts GO cons loan (wrap of insured) (FGIC & BHAC) (SEC MKT)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Massachusetts GO rfdg & cons ln bnds ser 1991A-C dtd 09/01/1991 due 08/01/2012		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Massachusetts GO		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.