FITCH RATES MASSACHUSETTS SBA'S $721MM SUB SALES TAX BONDS 'AA+'; OUTLOOK STABLE

Fitch Ratings-New York-30 October 2019: Fitch Ratings has assigned a 'AA+' rating to the following Massachusetts School Building Authority (MSBA) subordinated sales tax bonds:

--$721,175,000 subordinated dedicated sales tax refunding bonds, 2019 series B (federally taxable).

The bonds are scheduled to be offered by negotiated sale on or about Nov. 6, 2019.

Proceeds of the current sale will partially refund outstanding senior dedicated sales tax bonds, 2011 series B.

The Rating Outlook is Stable.

SECURITY
The authority's bonds are secured by an irrevocable dedication of one cent of Massachusetts's 6.25-cent sales tax, with some exclusions.

ANALYTICAL CONCLUSION
The ratings on the MSBA's dedicated sales tax revenue bonds are based on structural protections that insulate the bonds from the Commonwealth's general operations and on the strong growth prospects and resilience of dedicated sales tax revenues relative to Fitch's expectations for cyclicality. As of Oct. 1, 2019, the MSBA has $5.0 billion in senior lien and just under $1.2 billion in subordinated lien bonds outstanding, rated 'AAA' and 'AA+' by Fitch, respectively. The insulation provided by the bonds' structural protections and the substantial cushion provided by the additional bonds test (ABTs) allow for ratings on the senior and subordinate liens that are linked to, but not capped by, the Commonwealth's 'AA+' Issuer Default Rating (IDR).

KEY RATING DRIVERS
STRONG GROWTH PROSPECTS: Performance of the dedicated sales tax securing the senior and subordinate lien bonds is strong and likely to remain so over time, reflecting the broad nature of the tax and the fundamental strength of the Commonwealth's economy.

SUBSTANTIAL CUSHION: Dedicated sales tax revenues have been subject to cyclicality, including a steep, three-year decline in the last recession, and Fitch expects future performance to be consistent with this history. The ABTs for both the senior and subordinate liens provide substantial cushion to ensure coverage of debt service, including under stress scenarios consistent with Fitch's tax supported criteria covering the impact of a moderate, national downturn and based on the highest consecutive historical revenue decline. This cushion is higher for the senior bonds, supporting the one notch rating distinction from the subordinate bonds.

STRONG STRUCTURAL PROTECTIONS: Revenues dedicated for school capital are segregated from the Commonwealth general fund, and the authority has no role in funding school operations. Strong legal covenants protect against diversion of revenues or lowering of the tax rate, although the base can be changed.

COMMONWEALTH CREDIT QUALITY: Massachusetts' 'AA+' IDR reflects its considerable economic resources, strong budget controls and a record of careful financial management. The

Commonwealth carries a long-term liability burden that is well above average for a U.S. state but remains a moderate burden on resources.

RATING SENSITIVITIES

DEDICATED SALES TAX PERFORMANCE: The ratings are sensitive to expectations for strong performance of the dedicated sales tax revenue and continued solid debt service coverage levels.

COMMONWEALTH CREDIT QUALITY: The ratings are sensitive to changes in the Commonwealth's 'AA+' IDR, to which they are linked.

ECONOMIC RESOURCE BASE

Massachusetts has a fundamentally strong economy with strong growth prospects. Its dynamic, service-oriented economic profile includes numerous institutions of higher education and health care that lend stability, in addition to supporting development and innovation in other sectors. At 131% of the U.S. average in 2018, per capita personal income is the second highest of the states. Educational attainment is very high, and population growth has been strong during this decade, a shift from historical experience of slow population gains. Despite this shift, the Commonwealth's population profile remains older than the U.S. average, consistent with other states in the region.

Economic performance has been highly sensitive to national trends. In the most recent recession, Massachusetts performed significantly better than the national experience, in contrast to 2002-2004 when it suffered among the steepest employment drops in the country. Employment losses in the Great Recession were slightly less severe than those of the U.S. (down 6% in Massachusetts versus 6.3% for the U.S.). Employment growth since then has been consistently solid.

DEDICATED TAX CREDIT PROFILE

The Commonwealth has imposed a sales tax since 1966. Average annual sales tax growth has been about 6.6% since the inception of the tax, inclusive of rate and base changes. Since the one-cent tax pledge for MSBA was fully phased in, in fiscal 2011, dedicated sales tax performance has been strong. Actual YoY growth in sales tax was 3.8% for fiscal 2018, preliminary growth was 5.3% in fiscal 2019 (which ended on June 30), and estimated growth is 6.8% for fiscal 2020. Base changes in the fiscal 2020 forecast reflect extending sales taxes to online vendors, following the U.S. Supreme Court's South Dakota v. Wayfair decision. For the fiscal year to date through September, total sales tax collections are 5.3% above and baseline collections are 4.7% above prior year figures.

Collections have also been economically sensitive, including a three-year, cumulative 7.9% dedicated sales tax decline in the last recession. Although performance of sales taxes in the last recession was weak, coverage of maximum annual debt service (MADS) remained solid. Additional bond issuance under the authority's $10 billion authorization requires 1.4x maximum annual senior debt service coverage for senior bonds and 1.3x coverage of total MADS for subordinated bonds, providing a substantial cushion to ensure coverage relative to historical revenue cyclicality.

Including the expected refunding bonds, fiscal 2019 preliminary revenues provide more than 2.6x coverage of MADS for the senior bonds and just over 2.0x for senior and subordinate bonds together, without consideration of the federal interest subsidies associated with Build America Bonds and Qualified School Construction Bonds.

Many, but not all, of the authority's bonds issued to date on the senior lien have a standard debt service reserve fund. The debt service reserve level is not a rating factor for Fitch given the strong coverage and structural features of the bonds. As part of the current transaction, which partially refunds 2011 series B senior lien bonds, the debt service reserve associated with the refunded bonds will be released and applied to the refunding.

STRONG GROWTH PROSPECTS AND AMPLE COVERAGE UNDER FITCH SCENARIOS

Pledged sales tax receipts reflect the Commonwealth's fundamentally strong economic profile. Revenue growth has been solid since the last downturn. Consistent with Fitch's view of the Commonwealth's overall economic growth prospects, sales tax revenue growth prospects are likely to remain strong over time.

To evaluate the sensitivity of the dedicated revenue stream to cyclical decline, Fitch considers both revenue sensitivity results (using a 1% decline in national GDP scenario) and the largest actual decline in revenues over the period covered by the analysis. Based on a 20-year pledged revenue history, Fitch's analytical stress test (FAST) generated a 1.8% scenario decline in pledged revenues. The largest consecutive decline in this timeframe was 7.9%, based on recessionary losses during the fiscal 2008-2010 period.

Under both scenarios, dedicated revenue provides ample cushion relative to MADS. For senior bonds, the coverage cushion assuming issuance to the ABT equates to 16.1x the scenario decline and 3.7x the largest historical decline. On an aggregate basis, the coverage cushion equates to slightly lower 12.8x the scenario decline and 2.9x the largest historical decline.

LIMITED EXPOSURE TO ISSUER OPERATIONS
Fitch views MSBA's dedicated sales tax bonds as having limited exposure to the operations of the Commonwealth. The one cent sales tax pledged to the bonds is segregated from the Commonwealth's general fund. Dedicated sales tax receipts are credited to the School Modernization and Reconstruction Trust (SMART) fund, which is held by the Commonwealth treasurer exclusively for the purposes of the authority, and disbursed to the bond trustee on a monthly basis. SMART fund revenues are not commingled with Commonwealth funds and are not subject to appropriation, and bondholders have first claim on the dedicated sales tax. The authorizing legislation specifies that the treasurer shall act as trustee as it relates to the SMART fund and not on account of the Commonwealth.

Dedicated taxes after payment of bonds remain with the MSBA. The authority can choose to transfer excess dedicated sales tax revenues to the Commonwealth, but the Commonwealth has relinquished all claims to the revenue. Strong statutory covenants protect against diversion of revenues or lowering of the dedicated tax rate, although the base can be changed. Dedicated tax revenues support school capital, with MSBA otherwise playing no role in funding school operations.

Given the insulation of dedicated revenues from general operations of the Commonwealth, bond security and the ratings on the senior and subordinate lien bonds are driven by sales tax performance and closely linked to overall economic performance. These structural protections and the substantial coverage cushion for the bonds allow for ratings that are linked to, but not capped by, the Commonwealth's 'AA+' IDR. However, based on Fitch's criteria for rating state dedicated tax bonds above the IDR, the amount of credit Fitch will give to such a structure is tempered by the risk that a state could exercise its sovereign powers to the detriment of bondholders.

The authority was created in 2004 to address a substantial backlog of programs funded under the Commonwealth's prior school building assistance program and create a sustainable system for school capital funding going forward. Pre-existing contract assistance commitments to localities, a declining obligation through 2024, are paid annually from dedicated revenues after payment of debt service. The authority was authorized to fund up to $500 million in new projects annually starting in fiscal 2008 (with the limit adjusted up or down each year by the lesser of the dedicated sales tax revenue increase or decrease, or 4.5%); approval of new projects is contingent upon the availability of funds for this purpose. The authority does not have a waiting list. The authority consists of seven members: the Commonwealth Treasurer (chair), four treasurer appointments, and two ex-officio members.

CREDIT QUALITY OF MASSACHUSETTS

Massachusetts' 'AA+' IDR reflects its considerable economic resources, strong budget controls and a record of careful financial management. The Commonwealth carries a long-term liability burden that is well above average for a U.S. state but remains a moderate burden on resources. The Stable Outlook reflects the expectation that the Commonwealth will continue to act as needed to ensure budget balance and maintain an adequate budgeted reserve position.

For more information on the Commonwealth, see Fitch Research 'Fitch Rates Massachusetts' GO Revenue Anticipation Notes 'F1+" dated Oct. 11, 2019, available at www.fitchratings.com.

Contact:

Primary Analyst
Douglas Offerman
Senior Director
+1-212-908-0889
Fitch Ratings, Inc.
33 Whitehall Street
New York, NY 10004

Secondary Analyst
Kevin Dolan
Director
+1-212-908-0538

Committee Chairperson
Karen Krop
Senior Director
+1-212-908-0661

Date of Relevant Rating Committee: July 8, 2019

ESG CONSIDERATIONS
Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - 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 our ESG Relevance Scores, visit www.fitchratings.com/esg.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

Media Relations: Sandro Scenga, New York, Tel: +1 212 908 0278, Email: sandro.scenga@thefitchgroup.com.

Additional information is available on www.fitchratings.com

Applicable Criteria

U.S. Public Finance Tax-Supported Rating Criteria (pub. 03 Apr 2018)

https://www.fitchratings.com/site/re/10024656