

# RatingsDirect®

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**Summary:**

## Massachusetts School Building Authority Massachusetts; Sales Tax

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## Summary:

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### Credit Profile

US\$721.175 mil sub dedicated sales tax rfdg bnds fed taxable (Massachusetts) ser 2019 B due 10/15/2041

<i>Long Term Rating</i>	AA/Stable	New
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Massachusetts Sch Bldg Auth sales tax

<i>Long Term Rating</i>	AA+/Stable	Affirmed
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## Rationale

S&P Global Ratings assigned its 'AA' rating and stable outlook to the Massachusetts School Building Authority's (MSBA) \$721.175 million series 2019B subordinated dedicated sales tax refunding bonds.

S&P Global Ratings also affirmed its 'AA+' rating on the authority's \$5.0 billion senior sales tax revenue bonds outstanding, and its 'AA' rating on the authority's \$1.2 billion subordinated bonds outstanding. The outlook on both the senior and subordinate bonds is stable.

A subordinate lien on the authority's dedicated sales tax revenue, after payment of senior bonds, secures the series 2019B and parity bonds.

The ratings reflect our assessment of:

- A dedicated 1% sales tax that is levied statewide and is not subject to reduction or diversion pursuant to the statute and trust agreement;
- MSBA's pledge of sales tax revenue on a gross basis and not subject to annual legislative appropriation;
- The underlying strength and diversity of the Massachusetts (general obligation rating: AA/Stable) economy, with approximately 6.9 million residents that have well-above-average income levels;
- Relatively low sales tax revenue volatility and sustained long-term growth trends. Revenue growth has been healthy following a dip during the 2008-2010 recession years. We expect growth to continue at a healthy pace due to strong economic fundamentals; and
- Good debt service coverage (DSC), which we expect to continue due to statutory caps on the rate of growth of MSBA capital commitments and an adequate 1.4x additional bonds test (ABT) for the senior bonds, and 1.3x for the subordinate bonds.

We understand that MSBA will use the 2019B bond proceeds to refund its senior series 2011B bonds for debt service savings and to release associated debt service reserve funds.

A 1% statewide sales tax, excluding sales-tax revenue on meals, and on sales occurring in certain portions of Boston,

Cambridge, and the Springfield Convention Center area, secures the senior and subordinate bonds. The pledged 1% tax accounts for a portion of Massachusetts' overall 6.25% sales-tax rate. Pledged sales tax is not subject to annual budget appropriation.

Although the pledged revenue stream has shown some volatility during recessions, we believe MSBA has managed its debt program so as to maintain strong coverage, and we expect it will manage this new debt issuance in a way that preserves what we view as the authority's future strong coverage. MSBA plans to increase the use of pay-as-you-go capital funding to about 20%-30% of its capital spending, reducing somewhat the amount of future bonding needs.

MSBA was created in 2004 to manage and plan reimbursements of Massachusetts' school construction and renovation grant program. Under the enabling legislation, the maximum amount of principal outstanding at any given time backed by this revenue pledge cannot exceed \$10 billion, compared with current senior and subordinate debt outstanding of \$6.2 billion as of Oct. 1, 2019. The liability for the authority's remaining waiting list projects and previous grant projects that it inherited on its creation totaled \$220 million, while it had entered into new feasibility study agreements and project funding agreements for \$6.67 billion of new project grants. Of the new project grant commitments, approximately \$1.6 billion of funding commitments are still outstanding. There is a statutory cap on new grants per year, which limits growth to the lesser of the rate of dedicated sales tax growth, or 4.5%.

**Revenue volatility: Very low for senior bonds; Low for subordinate bonds**

We believe pledged sales tax revenue will have relatively low volatility, based on the broad nature of the economic activity covered by the pledged sales tax and a statewide economic base. The sales tax has shown good long-term growth trends, with some dips in recession years. Pledged sales-tax revenue fell by a cumulative 7.9% during fiscal years 2008-2010, but has since increased each year, including 5.0% growth in the fiscal year ended June 30, 2015, 4.5% in fiscal 2016, 2.3% in fiscal 2017, and 3.8% in fiscal 2018. The preliminary unaudited growth rate in 2019 was 5.3%, and the state is estimating 6.8% growth in fiscal 2020 based on its current forecast projection.

**Coverage and liquidity: Very strong**

We calculate fiscal 2018 pledged revenue of \$847.9 million covers estimated combined subordinate and senior-lien maximum annual debt service (MADS) in 2025 of \$443.5 million after this issuance by 1.91x, which we consider strong. This calculation of MADS assumes annual debt service is reduced by the release of various series of senior bonds' debt service reserves when those series mature, and does not include provision for federal interest subsidies or interest earnings. Without release of reserves, MADS would be \$608.0 million in fiscal 2031 and MADS coverage would decline to an adequate 1.39x. Using unaudited fiscal 2019 revenue of \$893.2 million, coverage of combined senior and subordinate MADS would be 2.01x using debt service reserve releases, and 1.47x without debt service reserve releases. Our base-case analysis assumes that reserves will be available and released on time because of strong annual DSC.

We calculate coverage of senior-lien MADS alone of \$385.1 million, assuming use of bond reserves to make individual series' final maturities, is also strong, in our view, at 2.20x based on historical fiscal 2018 pledged revenue, and 2.32x based on unaudited fiscal 2019 revenue. Without availability of senior bond debt service reserve (DSR) releases to reduce net debt service, senior MADS would be \$573.3 million in 2031 and MADS coverage would be a good 1.48x based on fiscal 2018 revenue and 1.56x based on unaudited fiscal 2019 revenue. Although MSBA plans to issue future

debt under its subordinated lien, the senior lien remains open to potential additional debt issuance.

MSBA next plans to sell about \$300 million of additional subordinated new money debt toward fiscal year-end 2020.

The senior-lien ABT requires at least 1.4x MADS coverage on the senior-lien bonds by historical revenues, and 1.3x MADS coverage on the subordinate bonds. The subordinate bonds do not have a DSR, and MSBA has established senior bond series' DSRs on a case-by-case basis. There is a pledge of federal interest subsidies received under the Build America Bond program and the Qualified School Construction Bond program for certain of the subordinate bonds outstanding. These subsidies have been reduced slightly in the past and could be reduced again; however, we have calculated DSC without regard to the receipt of federal subsidies.

Senior bonds have DSRs securing each of their respective series of debt. These reserves will total \$443.6 million after this refunding, and will be released as each series of senior bonds mature and are expected to be used to pay debt service when released. Senior debt service reserves are also expected to be released as individual senior-lien bond issues are refunded. None of the subordinate bonds has a DSR.

The pledged sales tax is credited by the commonwealth without appropriation, allotment, or other action to the School Modernization and Reconstruction Trust Fund. MSBA's obligations to make payment of principal, and premium, if any, and interest on debt service on the senior and subordinate bonds are senior to all other claims on the sales tax.

### **Economic fundamentals: Very strong**

We view Massachusetts' economic fundamentals as very strong. We believe the commonwealth's economy remains deep and diverse, anchored by a Boston metropolitan statistical area that includes many higher education institutions and associated technology companies, although employment growth appears to have slowed down somewhat in 2019, after earlier growth that strongly outpaced national and regional trends by most measures.

The U.S. Census Bureau population estimate for Massachusetts in 2018 is 6.9 million, a 0.6% increase from 2017. Over the past 10 years, the commonwealth's population increased 6.7%, compared with 7.6% for the nation. Although below that of the nation, state population growth has outpaced the region since 2007 and we expect this trend to continue. The commonwealth's age dependency ratio of nonworking-age population to working-age population, at 56.3% in 2017, was better than that of the nation (61.8%).

IHS Markit reports private sector employment growth for the three months through August 2019 grew a good 1.4%, with the well-paying professional, scientific, and technical services sector showing nearly half of the growth. The commonwealth's average annual unemployment rate of 3.3% in 2018 was below that the national 3.9% rate. Commonwealth unemployment edged even lower at 2.9% in August, primarily due to a slight decline in the labor force. Overall, IHS Markit forecasts 1.0% employment growth in calendar 2019 and 0.9% in calendar 2020, compared with 1.4% and 1.1%, respectively, for the nation. Massachusetts has an above-average high-technology employment sector, which IHS Markit estimates at about 10% of state employment, compared with 6.5% for the country as a whole. The increasing role of services in the economy reflects growth in research laboratories, computer software, management consulting, other business services, and health care. Higher education anchors, a high level of federal research funding, and venture capital give the commonwealth a leading edge in emerging industries, such as biotechnology, software, communications equipment, and surgical instruments.

Total commonwealth personal income rose a strong 4.3% in 2018, and state per capita income was 130% (second only to Connecticut), although down from 131% the year before. In our view, Massachusetts' economic fundamentals and key anchors, which center on higher education, technology, finance, and health care, should contribute to continued expansion.

IHS forecasts real GDP to increase 2.3% in calendar 2019, 2.3% in calendar 2020, and 2.0% in calendar 2021, near its respective U.S. real GDP forecast of 2.5%, 1.8%, and 1.8% for the same years.

### Linkage to state general creditworthiness

We view MSBA sales tax obligations as linked to the commonwealth of Massachusetts' creditworthiness. Pledged sales tax revenues are not subject to annual appropriation by the Massachusetts legislature. However, in our view, the collection and distribution of pledged revenues by the commonwealth itself exposes the revenues to Massachusetts operations. For this reason, under our "Priority-Lien Tax Revenue Debt" criteria (published Oct. 22, 2018), we consider the linkage between the priority-lien pledge and Massachusetts to be close. Given Massachusetts' current creditworthiness (AA/Stable), we don't view linkage as a limiting rating factor for the authority's debt.

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or more information on the commonwealth and its economy, see our most recent Massachusetts GO report, published Sept. 23, 2019, on RatingsDirect.

## Outlook

The stable outlook reflects our view of the magnitude and diversity of the statewide tax base supporting the bonds. We believe DSC will remain strong and near current coverage levels. Should coverage decline significantly due to deteriorating revenue or an acceleration of debt issuance, this could negatively pressure the rating. We will not likely raise the rating in the two-year outlook horizon based on the possibility of additional debt issuance.

Ratings Detail (As Of October 30, 2019)		
Massachusetts Sch Bldg Auth subord sales tax		
<i>Long Term Rating</i>	AA/Stable	Affirmed
<b>Massachusetts Sch Bldg Auth, Massachusetts</b>		
Massachusetts		
Massachusetts Sch Bldg Auth sub dedicated sales tax bnds (Massachusetts)		
<i>Long Term Rating</i>	AA/Stable	Affirmed

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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