Tagging Info

Fitch Rates Buffalo, NY's LTGOs 'A+'; Outlook Stable

Ratings Endorsement Policy

04 Mar 2014 3:05 PM (EST)

Fitch Ratings-New York-04 March 2014: Fitch Ratings assigns an 'A+' rating to the following city of Buffalo, New York (the city) obligations:

--$24,504,147 general improvement serial bonds - 2014.

Proceeds will be used to refund outstanding bond anticipation notes and finance various capital projects. The bonds are scheduled for competitive sale the week of April 7.

In addition, Fitch affirms approximately $95 million of the city's outstanding limited tax general obligation (LTGO) bonds and $110 million of the city's outstanding unlimited general obligation (ULTGO) bonds at 'A+'.

The Rating Outlook is Stable.

SECURITY

The current issue and the series 2011E, F, G, the 2012A, B, C and D and 2013 bonds are general obligations of the city for which it has pledged its full faith and credit, subject to the 2011 state statute limiting property tax increases to the lesser of 2% or an inflation factor (the tax cap law). This limit can be overridden by a 60% majority vote of the city common council. The city has pledged its full faith and credit and unlimited taxing power for debt service on outstanding GO bonds issued prior to these bonds. No exemption is made under the tax cap law for debt service on outstanding GO debt; however, the constitutionality of this provision has not been tested.

KEY RATING DRIVERS

SOUND FISCAL FOUNDATION: The city has restored a sound fiscal foundation, resulting in much improved reserve levels. The Buffalo Fiscal Stability Authority (BFSA) a state-imposed oversight entity in place since 2003, was a key factor in this improvement. Though the BFSA is now in an advisory period, the city has maintained the fiscal discipline established by the authority.

ECONOMIC GROWTH DESPITE DOWNTURN: The economic base is benefitting from extensive investment by the University at Buffalo, the Buffalo Niagara Medical Campus, the state of New York, and various private businesses.

BELOW AVERAGE SOCIOECONOMIC INDICATORS: Socioeconomic indicators are weak with below average income levels, high individual poverty rates, and high unemployment rates.

ELEVATED UNFUNDED OPEB LIABILITY: An elevated burden of unfunded other post-employment benefit (OPEB) liabilities is notable. Overall carrying costs are high despite the city not fully funding its OPEB liability.

NO RATING DISTINCTION FOR LT DEBT: The bonds are rated on parity with outstanding debt as the city may exceed the property tax cap in any one year with 60% approval of the common council.

RATING SENSITIVITIES

MAINTENANCE OF SOUND RESERVES: The rating is sensitive to the city's ability to work towards consistently balanced operations and maintain reserves consistent with those projected in the current four-year plan.

IMPROVED ECONOMIC INDICATORS: Increases in assessed value and wealth levels and stabilization of the population from the city's extensive economic development activity could move the rating upward.

CREDIT PROFILE

Buffalo is located in upstate New York near the Canadian border and is the second largest city in the state. The city benefits from cross-border tourism, and retains a fairly large manufacturing presence. Population has experienced chronic declines over the past few decades, including an 11% loss in the past decade, and now stands at about 260,000 residents.

ECONOMIC GROWTH DESPITE DOWNTURN

The city has a diverse economic base that benefits from its proximity to Canada with consistent tax base growth for the past five years, though market value per capita remains low at $26,000. Notable economic anchors include Buffalo-Niagara Medical Campus (BNMC), Erie County Medical Center Corporation, Kaleida Health, and the University at Buffalo.

In particular, BNMC, which employs roughly 12,000 people, has over $500 million in new projects planned and is expected to add 4,000 new employees in the near future. Additionally, the RiverBend project, a $1.5 billion private investment by two clean energy companies, combined with a $225 million investment from the state, was recently begun and is projected to result in as many as 5,000 jobs, and IBM recently announced it will be adding 500 jobs in Buffalo.

BELOW AVERAGE SOCIOECONOMIC PROFILE

Socioeconomic indicators are below average with per capita income levels at 63% and 72% of the state and national levels, respectively. Poverty rates are more than double the statewide average, and the city's unemployment rate has been persistently above the state and national averages over the past decade, though it is down from past highs.

The most recent monthly unemployment figure for December 2013 was 8.0%, well below the 10.2% recorded a year prior due to a combination of an increase in jobs and a reduction in the labor force. The 8.0% for December 2013 remains well above the state rate of 6.6% and the U.S. rate of 6.5% for the same period.

FINANCIAL OPERATIONS IMPROVED DURING BFSA CONTROL PERIOD

The city experienced financial pressures early in the past decade, resulting in chronic fiscal imbalance and ultimately a strain on liquidity. Consequently, in 2003, state lawmakers created the BFSA to facilitate financial reforms within the city. From inception, the authority operated as a hard control board, and as such its powers included the ability to invalidate union contracts, impose wage and hiring freezes, and approve budgets and debt issuances.

The authority moved to an advisory role in 2012 as the city had achieved predetermined benchmarks. The hard control period can be reimposed if certain fiscal conditions are not maintained. Fitch looks favorably on management's efforts to codify many of the policies required by the BFSA so that best practices remain in place regardless of the nature of the oversight board.

The city achieved operating surpluses every year from fiscal 2003 through fiscal 2010. During this period, the general fund unreserved fund balance improved from $9.7 million or 2.6% of expenditures and transfers out to over $110 million or 24.5%.

DEFICIT OPERATIONS IN FY 2011 and 2012

The city recorded a $12.8 million net operating deficit after transfers (2.8% of spending) in fiscal 2011, and a larger $16.3 million net operating deficit after transfers (3.5% of spending) in fiscal 2012. Fitch notes that both deficits partially resulted from the city prudently reserving funds for the resolution of several unsettled labor contracts. The fiscal 2012 unrestricted general fund balance declined to $77.7 million or a still adequate 16.6% of spending.

2013 RESULTS OUTPERFORM BUDGET

The city's fiscal 2013 budget included an $11.5 million fund balance draw, reducing the unrestricted fund balance to approximately 13% of expenditures. The budget included a one-time $18.7 million spin-up payment from the state. The spin-up was the acceleration of a March 2014 payment from the state to June 2013, so the city benefits from the payment in fiscal 2013 while the state is unaffected, as the payment remains within its 2014 fiscal year. State aid is expected to revert to approximately its prior level in fiscal 2014.

The city greatly outperformed its budget in fiscal 2013, finishing with a $52.2 million surplus that increased unrestricted fund balance to $130 million or 28% of expenditures. The positive variance was driven by two key factors. First, the state resolved a dispute with the Seneca Nation regarding a gaming contact, so the city received $16 million of revenue that had been withheld. Second, the city had $32.6 million of booked revenue from the resolution of past labor contracts for which the city had conservatively accrued for salary increases that were greater than the ones actually awarded. Additionally, personnel and pension costs came in under budget.

FUTURE DEFICITS PROJECTED

The city's four-year financial plan features annual fund balance appropriations. The original fiscal 2014 budget included a $12 million deficit, and current projections increase the deficit to up to $18 million. The budget included a flat property tax levy and the use of the final $12 million of state funds allocated to the city by BFSA. The forecasts for fiscal years 2015-2017 include smaller draws. Assumptions in the four-year plan appear reasonable, including 2% annual growth in the sales tax, the return of $3 million a year of sales tax revenues now being used by BFSA for debt service, the first property tax increase in several years in fiscal 2016, and conservative increases for unsettled contracts. Assuming the projected deficits, unrestricted fund balance would remain over 20%, which Fitch believes is still a sound level. Fitch would be concerned if operating imbalances persisted, leading to continued fund balance declines.

MODERATE DEBT & PENSION BURDENS WITH HIGH OPEB LIABILITY

The city's overall debt burden is low on a per capita basis at $1,434 but elevated at 5.5% of the city's weak market value. Total debt outstanding has declined consistently since fiscal 2002. Future debt needs are modest with annual issuance below the amount of debt amortized, and principal amortization is very rapid with 93% retired in 10 years.

Employees participate in well-funded state-sponsored defined benefit pension plans, and the city has made all required pension payments to the state. Payments have been increasing but state-provided projections show payments leveling off.

As of July 2013, the city's other post-employment benefits (OPEB) liability totaled $1.5 billion or a very high 22% of market value. The city currently funds its liability on a pay-go basis. A recently signed labor contract for firefighters included an increased employee healthcare contribution that lowered the OPEB liability. Total carrying costs for debt, pension and OPEB claimed an elevated 25% of governmental fund spending.

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In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was additionally informed by information from Creditscope, University Financial Associates, S&P/Case-Shiller Home Price Index, IHS Global Insight, Zillow.com, National Association of Realtors.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria' (Aug. 14, 2012);
--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

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Tax-Supported Rating Criteria
U.S. Local Government Tax-Supported Rating Criteria

Additional Disclosure
Solicitation Status