New Issue: Moody's assigns A1 to Buffalo, NY's $30.1M GOLT bonds; outlook stable

Global Credit Research - 02 Apr 2015

Affirms A1 rating on outstanding GO Debt

BUFFALO (CITY OF) NY
Cities (including Towns, Villages and Townships)
NY

Moody's Rating

ISSUE		RATING
General Improvement Serial Bonds - 2015		A1
Sale Amount	$30,078,985	
Expected Sale Date	04/07/15	
Rating Description	General Obligation Limited Tax	

Moody's Outlook STA

NEW YORK, April 02, 2015 --Moody's Investors Service has assigned a A1 rating to the City of Buffalo, NY's $30.1 million General Improvement Serial Bonds - 2015. Concurrently, Moody's affirms the A1 rating on outstanding rated debt.

SUMMARY RATING RATIONALE

The A1 rating reflects the city's overall solid reserves and liquidity despite current declines and structurally imbalanced budgets in the multi-year plan. The rating also factors: (1) challenges posed by the city's below average demographic profile; (2) a high debt burden that is expected to gradually moderate; (3) the challenges posed by open employee contracts (4) the oversight of city operations by the Buffalo Fiscal Stability Authority (BFSA, sales tax and state aid secured bonds rated Aa1), which has approved the city's four-year financial plan; (5) the city's improved revenue raising flexibility given modest growth in assessed valuation and improved taxing margin; and (6) additional bondholder security provided by the city's legally required and trustee-held bi-annual set-aside of debt service payments from first property taxes collected.

OUTLOOK

Moody's stable outlook reflects our belief that the city's liquidity and reserve position have improved substantially, as evidenced by elimination of the need for seasonal cash flow borrowing. The currently healthy cash position is expected to provide satisfactory cushion against risks related to the weak economy, potential state budget cuts and disbursement delays as well as liabilities related to open labor contracts and ongoing litigation. The outlook factors our expectation that management will maintain its currently strong financial position in the face of these challenges, despite continued use of reserves to balance the budget.

WHAT COULD MAKE THE RATING GO UP

- Demonstrated ability to maintain satisfactory financial flexibility and liquidity relative to peers

- Structurally balanced budgets which reduce the annual fund balance appropriation and declining reserve position

- Continued strengthening of city financial policies

- Significant increases in socio-economic profile

WHAT COULD MAKE THE RATING GO DOWN

- Continued use of reserves to support operations

- Structurally imbalanced operating results

- Reversal of trend of increasing taxing capacity

STRENGTHS

-State oversight board provides third-party supervision of city's finances

-Conservative budget and strong management have led to solid reserve position and liquidity

-Direct pay of first-in property tax money to the trustee for payment of debt service

CHALLENGES

-Uncertainty around outstanding union contracts and pending litigation

-State aid cuts could put significant pressure on city's finances

-Use of Fund balance to balance budgets

RECENT DEVELOPMENTS

Recent developments are incorporated in the Detailed Rating Rationale.

DETAILED RATING RATIONALE

ECONOMY AND TAX BASE: TAX BASE CONTINUES TO EXPAND DRIVEN BY NEW DEVELOPMENT DESPITE CONTINUED POPULATION LOSSES

Despite large population declines, income levels well below state averages and high poverty rates major real estate developments continue throughout the city. According to U.S. Census figures, the city's 2010 population was 261,310, down 10.7% from 2000, a continuation of the trend that began in 1950 when the city's population peaked at 580,132. Positively, the rate of decline appears to have slowed as the city's population has lost 0.9% since 2010. Despite this slower rate of decline, Moody's Analytics reports in its January 2015 report that the demographic picture for the Buffalo MSA is bleak; among the nation's 100 largest metro areas only Cleveland, Detroit, and Rochester are expected to lose more residents over the next decade.

New York State Governor Andrew Cuomo has made economic development of the Buffalo region one of his top priorities. The goal of his "Buffalo Billion" plan was to infuse $1 billion into the Buffalo economy over 10 years. As a result of this initiative, there has been considerable development in the Buffalo MSA.

Recently, SolarCity announced that it planned to invest up to $5 billion in the Riverbend Project, up from the $750 million under previous ownership, to construct the largest solar production facility in the western hemisphere. When complete the Riverbend Project is expected to support up to 3,000 new high paying technology jobs. As part of the Buffalo Billion, International Business Machines Corporation (IBM, Aa3 stable), announced in 2014 its commitment to bring 500 new information technology jobs to the city. In addition, the city has significant economic development activity within in the city and along the waterfront and inner harbor. These include the Buffalo Sabres' HARBORcenter Development, LLC a new hockey-themed complex along the inner harbor, the ongoing developments at the Buffalo Niagara

Medical Campus and the University of Buffalo. In total these projects represent nearly a $1 billion in investments within the city and will result in thousands of new jobs.

Despite recent building activity the employment picture continues to be a concern. While the city's unemployment rate has been in decline over the past three years this has largely been due to a declining workforce and not an improvement in the labor participation rate. As of December 2015, the number of employed in the city had reached its lowest level yet. We do expect the employment numbers to improve over the long-term though driven by continued development within the city and a more family friendly downtown.

FINANCIAL OPERATIONS AND RESERVES: RESERVES STILL STRONG DESPITE RECENT DRAW DOWN

Over the past decade reserves have improved significantly driven by conservative budget management and oversight of operations by BFSA. Over the past five years total Operating Fund (City General Fund, BOE General Fund, City Debt Service Fund and BOE Debt Service Fund) has averaged approximately 30% of revenues. Fiscal 2014 finished at the lowest level since 2009 following an operating deficit of $34 million. The City General Fund finished with a $24 million decline, the result of a planned $12 million draw, a settlement with both the police and fire collective bargaining units, judgments and claims against the city and additional pay-go capital. Positively, the city did not incur additional debt as a result of either the new collective bargaining contracts or the judgments and claims, a common occurrence for local governments in New York. Additionally, the city made its full pension payment on-time and did not partake in the amortization program. The BOE's General Fund declined by $10 million, after the BOE was able to replenish $20 million in originally budgeted appropriations. The better than budgeted result is attributable to conservative budgeting for expenses.

Fiscal 2015 (June 30 year end) is currently tracking on budget for the city and slightly positive for the BOE. However, the City budgeted the use of $27 million in reserves to the year and expects to use nearly all the appropriations. Despite savings in fuel and pension costs, the city was hard hit by seven feet of snow in November 2014 which eliminated any savings in the budget to date. Management is in discussions with the Federal Emergency Management Agency (FEMA) to be reimbursed for costs. It is unclear as to how much FEMA will reimburse the city and management is not currently projecting a reimbursement. The BOE budgeted the use of approximately $10 million and currently expects to conservatively use half of its appropriations.

The fiscal 2016 budget process is in its early stages, and the city has no estimates for the next fiscal year. However, management is required to do four year financial plans. As of May 2014, the city had anticipated using another $25 million to balance the budget in fiscal 2016. Another $25 million decline, on top of what is currently projected for 2015, would bring the city's General Fund down to approximately $100 million, approximating the city's informal policy. It would also be a significant decline in financial flexibility that had been built up over the past decade. The BOE also plans to continue to use reserves to balance the budget, however at a much lower level. Failure to adhere to the city's informal policies, and structurally balance operations going forward, could result in negative rating pressure in the future.

Liquidity

Liquidity for the combined Operating Fund is strong, at over 30% of revenues. The city has not required the issuance of short-term cash flow notes since 2007.

Debt and Pensions

Debt will remain manageable despite its elevated position given additional tax base growth and a policy to not issue more debt than what is being retired. Direct debt is a high 5.1% of full value, well above the state wide median of 1.8%. This figure includes debt that is issued for schools, however. Most cities in New York do not combine school debt with city debt. Management anticipates issuing approximately $20-25 million in new money on an annual basis.

Debt Structure

All of the debt is fixed rate.

Debt-Related Derivatives

The city is not exposed to derivatives.

Pensions and OPEB

Like all local governments in New York, the city continues to be challenged with pension and OPEB costs. However, management continues to make pension payments in full and on time and has no plans to amortize payments in the future. The City contributes to the New York State Police and Fire Retirement System (PFRS), Teachers Retirement System (TRS) and Employees' Retirement System (ERS), all of which are multi-employer cost-sharing defined benefit plans. The Annual Required Contribution (ARC) for 2013 for PFRS, TRS and ERS was $76.8 million or 6.3% of total operating expenditures. The districts combined adjusted net pension liability for 2013, under Moody's methodology for adjusting reported pension data, was $1.9 billion, or an average 0.94 times total operating revenues. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities. We determined the city's share of liability for the state-run plans in proportion to its contributions to the plans and do not factor in the town's recent amortizations.

Similar to all other local governments in New York, the city and BOE pays OPEB on a pay-as-you-go basis. In 2014 the pay-go portion of OPEB was $111 million (9.3% of expenses). Because the city does not fully fund the ARC ($276.5 million), the unfunded OPEB liability increases ever year. At the end of fiscal 2014, the OPEB liability amounted to $3.5 billion.

Management and Governance

Management for the city is strong, with informal reserve policies, formal "Rainy Day Funds", and a debt policy to not issue more debt than what is being issued. Management is also required to submit its budgets and four year financial plans to BFSA for review and do quarterly financial reporting. In addition, pursuant to the state enabling legislation, the city is required to set up a debt service reserve fund, to be funded with first-in property tax revenues, for the payment of debt service.

New York cities, towns and villages have an institutional framework score of 'A' or moderate. Revenues are largely comprised of property, sales, and mortgage taxes, as well as building permits. Property tax revenues are subject to the tax cap but can be overridden with a 60% vote of the local legislative body. Economically sensitive revenues remain below peak levels prior to recession. Expenditures are largely predictable but the presence of strong collective bargaining groups make it difficult to reduce expenditures.

KEY STATISTICS

2015 Full Value: $6.9 billion

2015 Full Value Per Capita: $26,425

Median Family Income as % of US: 57.6%

Fiscal 2014 Fund balance as a % of Revenues: 31.6%

5-Year Dollar Change in Fund Balance as % of Revenues: 11.1%

Fiscal 2014 Cash Balance as % of Revenues: 32.8%

5-Year Dollar Change in Cash Balance as % of Revenues: 7.4%

Institutional Framework: A

5-Year Average Operating Revenues / Operating Expenditures: 0.96x

Net Direct Debt as % of Full Value: 5.1%

Net Direct Debt / Operating Revenues: 0.3x

3-Year Average of Moody's ANPL as % of Full Value: 16.5%

3-Year Average of Moody's ANPL / Operating Revenues: 1.0x

OBLIGOR PROFILE

Buffalo is the second largest city by population in the State, after New York City. Located in western New York, on the border to Canada, the city is the economic hub of the region.

LEGAL SECURITY

The bonds are secured by a general obligation pledge as limited by the Property Tax Cap - Legislation (Chapter 97 (Part A) of the Laws of the State of New York, 2011).

USE OF PROCEEDS

Bond proceeds will permanently finance $7 million in outstanding BANs and fund various capital projects throughout the city, the largest of which is for infrastructure improvements.

RATING METHODOLOGY

The principal methodology used in this rating was US Local Government General Obligation Debt published in

January 2014. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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