MOODY'S
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CREDIT OPINION
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Update

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Pawtucket (City of), RI

Update: Moody's Upgrades Pawtucket, RI's GO to A3 from Baa2

Summary Rating Rationale

Moody's Investors Service has upgraded the rating on the City of Pawtucket, RI's general obligation debt to A3 from Baa2 and the stable outlook has been removed. Concurrently, Moody's has upgraded the rating to A1 from A3 on two Rhode Island Health and Educational Building Corporation (RIHEBC) pool financings that the city is a participant in: those relating to the Series 2006A and 2009D bonds. Approximately $50 million in debt is affected by the rating action.

The upgrade to A3 from Baa2 primarily reflects the improved and stabilized financial position of the city. The A3 takes into account the city's moderate-sized tax base, weak wealth and income indices, diverse tax base, and elevated fixed costs comprised of OPEB, debt service and required pension costs.

The upgrade to A1 from A3 for the RIHEBC pooled financing ratings reflects the upgrade of Pawtucket's GO rating. The rating takes into account the credit quality of the pool participants, the portion of debt service that is directly paid to RIHEBC by the state, and the legal structure of the program. RIHEBC's 2006A and 2009D bond issues are unenhanced pools and are rated using a 'weak link plus' approach under our Public Sector Pool Financings methodology. For the 2006A bonds, the participants and their respective GO ratings are as follows: the Bristol Warren Regional School District (Aa3), the Town of Burrillville (Aa2), the Town of Portsmouth (Aa2), the Town of Tiverton (A1) and the City of Pawtucket (A3). For the 2009D bonds, the participants and their respective GO ratings are as follows:Tiverton (A1) and Pawtucket (A3).

Credit Strengths

» Improved financial position

» Low taxpayer concentration

» High state level reimbursement for debt service

Credit Challenges

» High fixed costs (combined pension, OPEB costs and debt service)

» Low wealth and income indicators

» Increasing debt

» Weak tax base growth

Rating Outlook

Moody's does not typically assign outlooks to local government credits in the A rating category with this amount of debt outstanding.

Factors that Could Lead to an Upgrade

» Sustained increase in reserve levels

» Improvement in wealth and income indices

» Reduction in pension and OPEB liabilities leading to greater operating flexibility

Factors that Could Lead to a Downgrade

» Decline in reserve levels

» Significant increase in debt and pension costs

» Sustained contraction of the tax base

Key Indicators

Exhibit 1

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Pawtucket (City of) RI	2011	2012	2013	2014	2015
Economy/Tax Base					
Total Full Value ($000)	$ 4,591,034	$ 4,348,217	$ 3,597,170	$ 3,575,583	$ 3,448,729
Full Value Per Capita	$ 64,316	$ 61,031	$ 50,548	$ 50,139	$ 48,360
Median Family Income (% of US Median)	76.2%	77.5%	76.6%	75.1%	75.1%
Finances					
Operating Revenue ($000)	$ 174,832	$ 175,326	$ 185,445	$ 190,379	$ 195,820
Fund Balance as a % of Revenues	-0.2%	0.5%	4.4%	7.7%	8.3%
Cash Balance as a % of Revenues	3.8%	-0.8%	3.9%	7.5%	9.4%
Debt/Pensions					
Net Direct Debt ($000)	$ 50,630	$ 49,355	$ 51,009	$ 50,498	$ 67,576
Net Direct Debt / Operating Revenues (x)	0.3x	0.3x	0.3x	0.3x	0.3x
Net Direct Debt / Full Value (%)	1.1%	1.1%	1.4%	1.4%	2.0%
Moody's - adjusted Net Pension Liability (3-yr average) to Revenues (x)	N/A	N/A	2.22x	2.62x	2.78x
Moody's - adjusted Net Pension Liability (3-yr average) to Full Value (%)	N/A	N/A	11.4%	13.9%	15.8%

Source:

Detailed Rating Considerations

Economy and Tax Base: Diverse Moderate-SIzed Tax Base; Weak Wealth and Income Levels

The city, located outside of Providence (Baa1 negative) and 40 miles southwest of Boston (Aaa stable), is a mix of residential and commercial properties with a full valuation of $3.6 billion in 2015. Favorably the city has had two years of tax base growth through fiscal 2017 after three years of declines.

While continued growth in the tax base will likely continue to be slow, the city has cited various residential, retail and commercial projects in various stages of developments, including multiple projects in the downtown area. Projects include redevelopment of historic mills into a brewery and loft-style apartments on various properties. Furthermore, the state and city has secured about $40 million in funding to build a commuter rail station with construction slated to begin in 2017.

The tax base is diverse with the top ten taxpayers representing just 3.3% of assessed value for fiscal 2017. Top taxpayers are primarily in the following sectors: real estate (apartments), shopping centers, and manufacturing.

Income levels are weak, with median family income at 75% of the national median. Similarly, wealth levels as measured by full value per capita at $48,360 is well bellow the state median of $124,621. The city's unemployment rate as of June 2016 was 5.8%, above the state (5.1%) and national (4.9%) median.

Financial Operations and Reserves: Multiyear Trend of Favorable Operating Performance

The city's combined operating funds (General Fund and School Unrestricted Fund) have had four consecutive years of improvement (through fiscal 2015). While the General Fund has historically maintained adequate reserves, the School Unrestricted Fund up until fiscal 2014 had many years of deficit operations due to overspending and state aid cuts resulting in negative ending fund balances. In fiscal 2010, the city and school implemented a multi-year deficit funding plan and eliminated the negative fund balance two years ahead of schedule in fiscal 2014. The School Unrestricted Fund as of fiscal year end 2015 was $2.7 million, materially better than the -$4.7 million accumulated deficit six years earlier.

The city continued to increase reserves and stabilize its fiscal position in fiscal 2015. The combined Operating Fund balance grew $4.3 million to $18.9 million or 9.7% of revenues, the fourth consecutive year of improvement in the Operating Fund. The General Fund achieved a positive variance in state aid, licensing and permitting fees, and interest revenue. The School Unrestricted Fund experienced a meaningful increase of $2.7 million in fund balance in fiscal 2015 over the fiscal 2014's narrow $25,000 reserve levels. Of the increase, $1.8 million was due to lower than anticipated medical claims.

For fiscal 2016, management indicated they are expecting an approximately $0.2 million operating surplus (before transfers) in the General Fund with revenues slightly under budget by nearly $200,000 and approximately $400,000 of favorable expenditure variances. School Unrestricted Fund operations were also favorable with management estimating a $900,000 surplus due mostly to savings in salaries in benefits. While the city had operating surpluses in the General and School Unrestricted Funds, reserves will likely decline as the city is transferring approximately $4.2 million ($1.8 million from the General Fund, $2.4 million from the School Unrestricted Fund) to their internal service fund (ISF) per the state's accounting guidance on ISF reserves. The estimated Operating Fund reserve levels would be a satisfactory $15.4 million, well above the $8.2 million just three years earlier in fiscal 2012.

The fiscal 2017 General Fund budget has increased 2.49% and does not include a tax rate increase or appropriation of fund balance. Much of the $2.9 million in new spending relates to growth in salaries. Favorably the city is allocating $200,000 to its OPEB Trust. The School Unrestricted Fund budget grew 5.16% in fiscal 2017. The schools are budgeting for a healthy $4.4 million increase in education funding from the state due to increased enrollment and the continuation of the multi-year phase-in of the public school funding formula in Rhode Island. Expenditure growth largely results from increases in teacher salary and benefit costs.

The city's primary revenue source is property taxes typically accounting for half of all Operating Fund revenues. Intergovernmental revenues are the second largest consistently comprising approximately 40% of revenues. Education expenditures are the largest cost to the city averaging 55% of spending in the past five years.

LIQUIDITY

Liquidity in the Operating Fund has improved materially over the last few years with net cash improving to $18.4 million or an adequate 9.4% of revenues in fiscal 2015 from -$1.4 million (0.8% of revenues) in fiscal 2012.

Debt and Pensions: Elevated Fixed Costs

The city's estimated direct debt burden at the end of fiscal 2016 was 2.3% and, while elevated, it will remain manageable due to the rapid payout of existing debt and high reimbursement rate on school projects. Over the next 10 years, 85.7% of principal is paid off. The city's capital plan (fiscal 2016 through fiscal 2022) includes $91.6 million of bonds however approximately two-thirds is for school projects which have high state reimbursement levels if current reimbursement rates apply.

The city issued $25 million of BANs in July of 2016 and plans to roll them into $41 million in BANs in June of 2017 with long-term takeout financing through RIHEBC planned for December 2017 related to the $33.5 million school portion. Favorably, debt service on the bonds are subject to high levels of state reimbursement at over 80%.

Fixed costs (required pension contributions, gross debt service and OPEB contributions) are elevated at 20.8%. The city's ability to keep these costs at a manageable level and retain financial flexibility will be a key component of our future reviews.

DEBT STRUCTURE

All outstanding debt is fixed rate.

DEBT-RELATED DERIVATIVES

The city is not party to any derivative agreements.

PENSIONS AND OPEB

The city participates in three defined benefit plans- two state administered plans and one locally administered plan. The city's pension burden is high and represents a growing budgetary pressure with the actuarially determined contribution for all of the plans accounting for 12.5% of expenditures.The locally administered plan is comprised of a new and old police and fire plan. The new plan represents 96% of the ADC for the combined police and fire plan. The reported funding ratio on the new plan is low at 42% however the city has been fully funding the contribution since fiscal 2013 (including a 100% budgeted contribution for fiscal 2017). To address this liability, the city has implemented changes to the plan including increased employee contributions. Failure to continue to adequately fund this liability would put downward pressure on the rating. As required by the state, the city has funded 100% of its required contributions for the state-administered plans.

The Moody's adjusted net pension liability (ANPL), under our methodology for adjusting reported pension data, was $476.9 million in 2015. The three-year average of ANPL to full value is very high at 15.8% of full value, and the three-year average of ANPL to operating revenues is also elevated at 2.8 times. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities.

The city's OPEB liability is sizeable at $345.2 million as of July 1, 2015. The city has historically funded the benefits on a pay-as-you-go basis. OPEB contributions were $10 million in fiscal 2015 representing 5.1% of revenues. Favorably, the city has established a trust and has budgeted a $200,000 contribution to begin addressing the liability. Benefit changes implemented during contract negotiations also will help to reduce the liability.

Management and Governance

Management has demonstrated sound and conservative budgeting practices in recent years leading to the improved fiscal health of the city.

Rhode Island towns and cities have an institutional framework score of “A”, or moderate. Revenues, consisting of property taxes and state aid, are moderately predictable with economically sensitive revenues accounting for a fairly small portion. Revenue raising flexibility is moderate; although there is a limit on an annual property tax levy increases, the cap is a fairly generous 4%. Expenditures mostly consist of personnel costs which are moderately predictable. Expenditure reduction ability is also moderate given the presence of public sector unions in the state. Pension costs will continue to rise despite reform on the state level.

Legal Security

The city's GO bonds are general obligations of the city and are secured by an unlimited tax pledge.

The RIHEBC bonds are ultimately secured by the general obligation pledge of the pool participants under the respective financing agreements with RIHEBC.

Use of Proceeds

Not applicable.

Obligor Profile

The city is located outside of Providence and 40 miles southwest of Boston. The estimated population is 71,313 in 2014.

Methodology

The principal methodology used in the general obligation rating was US Local Government General Obligation Debt published in January 2014. The principal methodology used in the pool rating was Public Sector Pool Financings published in July 2012. Please see the Ratings Methodologies page on www.moodys.com for a copy of these methodologies.

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