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Fitch Rates Philadelphia Redevelopment Authority, (Pennsylvania) 2005 Bonds 'BBB+'

Ratings

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Fitch Ratings-New York-February 14, 2005: Fitch Ratings assigns a 'BBB+' rating to the Redevelopment Authority of the City of Philadelphia's $148 million revenue bonds, series 2005A, 2005B, and 2005C. The Rating Outlook is Negative. The bonds were originally scheduled to price in 2004, and Fitch's rating action today reflects the new sale date, series date, and quantity. The bonds are scheduled for negotiated sale on Feb. 15 through Samual A. Ramirez & Co., Inc. Fitch also affirms the rating on Philadelphia's $1 billion of outstanding general obligation bonds at 'BBB+'. The Rating Outlook is Negative.

The rating on the Redevelopment Authority of the City of Philadelphia (RDA) bonds relies on the general creditworthiness of the City of Philadelphia. The bonds are payable from current revenue under a noncancelable service contract with the city, which is not subject to future appropriation decisions by the city council; as such, the bonds are rated the same as Philadelphia's GO bonds.

Fitch downgraded Philadelphia's GO and related service contract bonds on Oct. 19, 2004 to 'BBB+' from 'A-' and maintained a Negative Rating Outlook. The downgrade was the result of poor revenue growth and significant increases in fixed and discretionary spending over the past several years, leading to the depletion of the city's reserve position.

The Negative Rating Outlook reflects Fitch's ongoing concerns that the fiscal 2005 and the next succeeding fiscal years are overly reliant on economic improvement and speculative operating efficiencies to offset already enacted tax cuts and rising benefit costs. While the cost of new labor contracts was approved in the city's amended five-year plan, it is significant and not fully offset by an aggressive work force reduction plan. The Pennsylvania Intergovernmental Cooperation Authority (PICA), a state authority that oversees Philadelphia's finances, approved the amended plan in December 2004. A new five-year plan covering fiscal years 2006-2010 was presented at the end of last month and awaits city council and PICA approval.

This offering completes planned borrowing for the administration's $275 million neighborhood transformation initiative, a multiyear plan to demolish or stabilize vacant property, remove graffiti, clear streets and empty lots of abandoned cars and debris, and assemble property for taxable redevelopment. The city reports success with this program, citing thousands of cars towed and tons of trash removed, as well as rising property values in neighborhoods served to date.

Under the 2002 service agreement between the city and the RDA, the city is required to make service fee payments directly to the trustee, as assignee of the RDA, equal to debt service on the bonds, plus any credit facility or swap obligation payments and administrative expenses. The city's obligation under the service agreement is absolute and unconditional and it covenants to make full annual appropriations without further action by the city council. The service agreement limits annual debt service for the program to $20 million per year, unless a higher amount is approved by city council. With this issuance, aggregate debt service does not exceed $19 million. The full $20 million limit is included in each year of the five-year financial plan.

The city's financial condition has markedly deteriorated over the past four fiscal years. A delay in the receipt of state aid reimbursements of more than $90 million contributed in fiscal 2004 to a $148 million audited unreserved general fund deficit under generally accepted accounting principles. Fitch notes that had the reimbursements been received in fiscal 2004, the resulting budgetary general fund balance of about $45 million would still represent only 1.4% of expenditures, down significantly from reserves as high as 10% of spending in 2000.

The weaker fiscal performance reflects not only a sluggish local economy and a stubbornly high unemployment rate but also the city's long-running program of incremental annual wage and business tax reductions. Fitch notes that while the tax reductions may be of long-term benefit to the city's competitiveness, they have had a dampening effect on revenues that has not been offset by spending reductions.

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