

RatingsDirect®

Summary:

Philadelphia; Note

Primary Credit Analyst:

Hilary A Sutton, New York (1) 212-438-7093; hilary.sutton@spglobal.com

Secondary Contact:

Linda Yip, New York (1) 212-438-2036; linda.yip@spglobal.com

Table Of Contents

Rationale

Summary:

Philadelphia; Note

Credit Profile

US\$175.0 mil tax and rev antic nts ser 2016A due 06/30/2017

Short Term Rating

SP-1+

New

Rationale

S&P Global Ratings assigned its 'SP-1+' rating to Philadelphia's series 2016-2017A tax and revenue anticipation notes (TRANs).

The rating reflects our opinion of the city's:

- Strong projected debt service coverage (DSC) of 3.38x at maturity; and
- Conservative budgeting practices that have resulted in a trend of actual coverage exceeding projections.

We believe financial oversight from Pennsylvania Intergovernmental Cooperation Authority and the recent modest improvement in general economic conditions provide additional support.

The TRANs are a general obligation of Philadelphia, but the city has not pledged its taxing power and therefore is not required to levy ad valorem taxes for TRAN payments. The TRANs are payable from, and secured by, a pledge of general fund taxes and revenues attributable to fiscal 2017. These amounts include general property taxes; wage taxes; business income and receipts (BIRT); sales taxes; and revenue from other governments.

TRAN proceeds will pay Philadelphia's general expenses prior to the receipt of income to be received in fiscal 2017 and pledged for note repayment. Principal and interest are due June 30, 2017, which coincides with the city's fiscal year-end. However, the repayment structure includes a fund held by the trustee into which officials are required to deposit the amount of principal borrowed on May 26, 2017, and the amount of accrued interest on June 27, 2017. It is our understanding these aggregate deposits will be sufficient to pay TRAN principal and interest due at maturity.

Philadelphia has a long history of cash-flow borrowing to finance seasonal cash flow needs. The principal amount for fiscal 2017 is flat relative to 2016 but up relative to the last three years (\$175 million in both fiscal 2016 and 2017 compared with \$130 million in 2015, \$100 million in 2014, and \$127 million in 2013). We do not view the increased par amounts in 2016 and 2017 as a credit negative given the strong coverage.

According to unaudited results, Philadelphia ended fiscal 2016 with a \$447.4 million general fund cash balance after repayment of the annual TRAN borrowing. Unaudited coverage of principal and interest was 3.5x at maturity, better than the 2.5x projected at the time of the sale. The city's quarterly report for the period ended June 30, 2016, shows tax revenues exceeding the adopted budget by \$39.1 million, with positive variances in sales tax receipts (\$18.3 million), real estate transfer taxes (\$15.7 million), wage and earnings tax receipts (\$8.9 million), and BIRT (\$1.3 million). Negative variances occurred in real property tax revenue (\$7.7 million) due to the resolution of outstanding

taxpayer appeals and other items (\$5.4 million). Expenditures are projected to be \$52.9 million above budget at \$4.05 billion due to overtime, vehicle shortages, and costs related to the Papal visit.

Projected fiscal 2017 DSC of principal by general fund cash balances is, in our view, a strong 3.48x on the May principal set-aside date. We also view projected DSC of principal and interest at maturity as strong at 3.38x. In our view, the city uses conservative assumptions when preparing its cash flow projections. Revenues overall are budgeted to rise 3.1% year-over-year, while expenditures are up 5.9%. Wage and earnings tax receipts account for 35% of revenue and budgeted to rise 3.9% year-over-year despite the continuation of the wage tax cuts. Property taxes are budgeted at 15% of total receipts, after a modest 2.4% increase. Philadelphia is showing a new revenue stream in its fiscal 2017 cash flow statement; city council passed a sweetened-beverage tax that is scheduled to take effect Jan. 1, 2017 and will be levied at a rate of 1.5 cents per ounce. Officials report the city conducted a comprehensive study of beverage consumption and assumed the tax will negatively affect demand; the cash flow assumes the tax will generate \$30.8 million (a small 1% of total revenue). We understand the \$30.8 million of new revenue will be offset by a like amount of expenditures for new initiatives in the areas of education and parks. We also understand the tax is being challenged in the courts and that the city will minimize related expenditures until certain of the revenue stream's future.

The city pools cash and investments in a consolidated cash account except those which, for legal or contractual reasons, cannot be commingled. The fund is segregated into two funds: an operating fund that contains the general fund and a capital fund that houses bond proceeds. As of June 30, 2017, the projected balance of the operating fund is \$357.9 million, which is slightly lower than the general fund (\$427.6 million) due to a deficit in the grants revenue fund. Nevertheless, coverage based on \$357.9 million is still strong at 2.99x.

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 for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

Copyright © 2016 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription) and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.