

RatingsDirect®

Summary:

Philadelphia; General Obligation; General Obligation Equivalent Security; Joint Criteria; Note

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Credit Profile

Philadelphia GO		
<i>Long Term Rating</i>	A+/Stable	Upgraded

Rationale

Standard & Poor's Ratings Services raised its long-term rating and underlying rating (SPUR) on Philadelphia's general obligation (GO) debt two notches to 'A+' from 'A-' based on its recently released local GO criteria. The outlook is stable.

Standard & Poor's also raised to 'A+' from 'A-' its long-term rating and SPUR on Philadelphia Redevelopment Authority's, Philadelphia Authority for Industrial Development's, and Philadelphia Municipal Authority's GO-equivalent appropriation debt, supported by the city.

A pledge of the city's full faith credit secures the GO bonds.

The rating reflects our assessment of the following strengthening factors for the city:

- Very strong management conditions with strong policies;
- Very strong liquidity providing very strong cash levels to cover both debt service and expenditures;
- Strong budgetary performance, which takes into account fiscal oversight provided by the Pennsylvania Intergovernmental Cooperation Authority (PICA); and
- Adequate budgetary flexibility with 2013 unaudited actual reserves at 7.2% of general fund expenditures.

Our view of tempering factors includes the city's:

- Weak economy, with high unemployment despite participating in the broad and diverse economy of the Philadelphia-Camden-Wilmington metropolitan statistical area (MSA); and
- Weak debt and contingent liabilities position.

Adequate budget flexibility

In our opinion, the city's budgetary flexibility is adequate. The city's financial statements are audited according to generally accepted accounting principles (GAAP), though management also reports results on a budgetary basis given the significant amount of business income and receipts tax (BIRT) payments received in advance of being earned on the modified accrual basis. As a result, we have adjusted the city's GAAP results to reflect the budgetary basis. In addition, we adjusted revenues and expenditures for various one-time items. The actual unaudited general fund balance for fiscal 2013 is \$256.9 million, up from \$146.8 million at the close of 2012, and represents 7.2% of adjusted

expenditures. We believe this factor score could weaken in fiscal 2014 due to the budgeted use of reserves to fund labor obligations. The adopted budget projects an ending general fund balance of \$86.5 million (2.3% of budgeted expenditures after removing the provision for labor obligations). We believe the city has demonstrated the ability and willingness to raise taxes in recent years, demonstrated by a 9.9% real estate tax increase in fiscal 2011 and a five-year sales tax that expires in fiscal 2014.

Very strong management

We view the city's management conditions as very strong, with strong financial practices. Management develops revenue and expenditure assumptions based on past trends, and adjusts them for internal and external forecasts. Budget officials use regional economic models for revenue forecasting, and management consults with regional Federal Reserve Bank officials when developing estimates, as well as review the surveys of professional forecasters. Management tracks revenue daily and expenditures monthly, and delivers formal revenue reports to elected officials monthly. The city submits quarterly reports to elected officials and PICA.

In addition to the current-year budget, Philadelphia annually produces formal rolling five-year financial plans that elected officials and PICA review. The five-year plan takes into account all known effects on revenue and expenditures, factors in expected tax rate reductions and labor cost increases, and identifies risks to the plan. In cases where material challenges arise after the five-year plan's introduction, PICA requires the city to submit a revised plan. Philadelphia's formal six-year capital improvement plan (CIP) includes the current budget year. Management updates the CIP annually; once the city council approves the CIP, Philadelphia submits it for PICA's oversight. In addition, management identifies funding sources for each project in the CIP. The city has a formal investment policy that is updated periodically most recently in 2011. The policy outlines permissible investments and forbids investment in certain derivatives, such as inverse floaters, leveraged variable-rate debt, and interest- or principal-only debt.

Very strong liquidity

Supporting the city's finances is what we consider to be very strong liquidity, with total government available cash at 8.3% of total governmental fund expenditures and 133.8% of debt service. We believe the city has exceptional access to external liquidity as it has issued multiple security types frequently in the past 15 years.

Philadelphia's series 2009B multimodal refunding GO bonds are variable rate and hedged with a swap. The bonds, with \$100 million currently outstanding, are also supported by a letter of credit with BNY Mellon that expires March 2016. The reimbursement agreement between the city and bank includes events of default we deem permissive and the remedies available to the bank include declaring principal on any outstanding liquidity advances immediately due and payable. The city also has a lease purchase agreement with acceleration risk following what we believe are permissive events of default. In our view, these are nonremote contingent liabilities but the risk is moderated by the city's strong cash balances relative to principal at risk of acceleration.

Strong budgetary performance

The city's budgetary performance, in our view, has been strong overall with a surplus of 1.5% for the general fund in fiscal 2013 (unaudited actual) and 2.1% for the total governmental funds. The principle general fund revenue categories are wage earnings and net profits tax (33% of 2013 unaudited on a budgetary basis), real estate tax (15%), and BIRT (12%). While we believe there is some volatility in this revenue stream, we view PICA's strong financial

controls and oversight, which have been in place since Philadelphia encountered financial stress in the early 1990s, as credit strengths.

The fiscal 2014 budget was adopted with a modest increase in revenue (\$25.6 million compared with 2013 unaudited actual results) and a sizable increase in expenditures (\$232.1 million). The expenditure increase reflects the budget impact of various labor settlements (actual as well as projected) in addition to rising pension, employee benefit, and debt service costs. While we recognize that the city has deferred pension payments in the recent past, we expect the financing tied to those deferrals to be fully repaid in fiscal 2014. Moreover, we believe the city's inclusion of expenditures related to unsettled labor contracts to be a proactive budgeting measure.

Weak economy

We consider Philadelphia's economy to be weak, with participation in the broad and diverse Philadelphia-Camden-Wilmington MSA. Philadelphia County, which is coterminous with the city, had an unemployment rate averaging 10.8% in calendar 2012. The city's projected per capita effective buying income is 76.3% of the nation and its per capita market value is \$64,578 for fiscal 2014. The city reassessed its tax base in fiscal 2014 at full market value, resulting in a 167% year-over-year assessed value increase. We understand the property tax base will be reassessed annually and expect growth given the number of major projects under construction.

Weak debt and contingent liability profile

In our opinion, the city's debt and contingent liability profile is weak, with total governmental funds debt service at 6.2% of total governmental funds expenditures and net direct debt at 64.4% of total governmental funds revenue. Additional debt is planned for the near term, but is not expected to change the factor score.

The city maintains two single-employer defined-benefit plans -- the Municipal Pension Plan (City Plan) and the Gas Works Plan (PGW Plan). The city plan covers all officers and employees as well as officers and employees of five other governmental and quasigovernmental organizations. Its funded status was 48.1% as of July 1, 2012. For fiscal 2012, the city's pension contribution was \$555.7 million, or 77% of the annual required contribution (ARC). The combined ARC pension and other postemployment benefits (OPEB) pay-as you-go costs for fiscal 2012 were 13% of expenditures. As of July 1, 2011, the city's unfunded actuarial accrued OPEB liability was \$1.2 billion. The city has actively sought material pension reforms through collective bargaining and continues to do so.

Strong institutional framework

The Institutional Framework score for Pennsylvania first-class cities is strong.

Outlook

The stable outlook reflects Standard & Poor's view of the city's strong budget performance due, in part, to oversight from PICA. We believe that if the economic recovery stagnates or retrenches, Philadelphia's strong management practices will allow it to continue to take the necessary actions to address imbalances and balance its five-year financial plan. We do not expect to change the rating in the next two years but note that rating direction will likely hinge on continued economic expansion – potentially resulting in a drop in unemployment to below 10% - as well as improved reserves.

Related Criteria And Research

Related Criteria

- USPF Criteria: Local Government GO Ratings Methodology And Assumptions, Sept. 12, 2013
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007

Related Research

S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013

Ratings Detail (As Of December 23, 2013)		
Philadelphia go rfgd bnds ser 2013B due 06/30/2039		
<i>Long Term Rating</i>	A+/Stable	Upgraded
Philadelphia GO multi modal ser 2009B		
<i>Long Term Rating</i>	AAA/A-1+	Affirmed
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded
Philadelphia GO rfdg bnds		
<i>Long Term Rating</i>	A+/Stable	Upgraded
Philadelphia Redev Auth (Neighborhood Transformation Rev) (wrap of insured) (FGIC & AMBAC) (SEC MKT)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded
Philadelphia TRANS ser 2013-2014A due 06/30/2014		
<i>Short Term Rating</i>	SP-1+	Affirmed
Philadelphia GO		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded
Philadelphia Redev Auth		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded
Philadelphia Auth for Indl Dev, Pennsylvania		
Philadelphia, Pennsylvania		
Philadelphia Auth for Indl Dev rev bnds RMKTD 5/31/2012 ser 2007B-2		
<i>Long Term Rating</i>	AAA/A-1+	Affirmed
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded
Philadelphia Auth for Indl Dev (Philadelphia) city svc agreement		
<i>Short Term Rating</i>	SP-1+	Affirmed
Philadelphia Auth for Indl Dev (Philadelphia) city svc agreement rfdg rev bnds (Retirement Sys)		
<i>Long Term Rating</i>	A+/Stable	Upgraded
Philadelphia Auth for Indl Dev (Philadelphia) multi modal lse rev rfdg bnds ser 2007B-1		
<i>Long Term Rating</i>	AAA/A-1	Affirmed
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded
Philadelphia Auth for Indl Dev (Philadelphia) multi modal lse - 2007B-3		
<i>Long Term Rating</i>	AAA/A-1	Upgraded
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded
Philadelphia Auth for Indl Dev pension fdg		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Upgraded

Ratings Detail (As Of December 23, 2013) (cont.)

Philadelphia Auth for Indl Dev (Cultural & Commercial Corridors Prog)

Unenhanced Rating A+(SPUR)/Stable Upgraded

Philadelphia Auth for Indl Dev (Philadelphia) multi modal lse - 2007B-4

Unenhanced Rating NR(SPUR)

Philadelphia Auth for Indl Dev (Philadelphia) GO

Unenhanced Rating A+(SPUR)/Stable Upgraded

Philadelphia Mun Auth, Pennsylvania

Philadelphia, Pennsylvania

Philadelphia Mun Auth (Philadelphia) city agreement rev rfdg bnds (Philadelphia) ser 2013A due 11/15/2018

Long Term Rating A+/Stable Upgraded

Philadelphia Mun Auth (Philadelphia) lse rev

Long Term Rating A+/Stable Upgraded

Philadelphia Mun Auth (Philadelphia) lse

Unenhanced Rating A+(SPUR)/Stable Upgraded

Philadelphia Redev Auth, Pennsylvania

Philadelphia, Pennsylvania

Philadelphia Redev Auth (Philadelphia) rev rfdg bnds (City of Philadelphia Neighborhood Transformation Initiative) ser 2012

Long Term Rating A+/Stable Upgraded

Philadelphia Redev Auth (Philadelphia) (City of Philadelphia Neighborhood Transformation Initiative) (BAM)

Unenhanced Rating A+(SPUR)/Stable Upgraded

Many issues are enhanced by bond insurance.

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