New Issue: Moody's assigns MIG 1 to Philadelphia, PA's $130M TRANs, Ser. 2014-2015A

PHILADELPHIA (CITY OF) PA
Cities (including Towns, Villages and Townships)
PA

Moody's Rating

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<td>Tax and Revenue Anticipation Notes, Series A of 2014 2015</td>
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| Sale Amount | $130,000,000 |
| Expected Sale Date | 11/13/14 |
| Rating Description | Note: Tax and/or Revenue Anticipation |

Moody's Outlook STA

Opinion


The notes are secured by the city's general fund receipts, which include all city taxes except the property tax levy collected on behalf of the Philadelphia School District (Ba3 negative) and the income taxes pledged for the Pennsylvania Intergovernmental Cooperation Authority special tax bonds (Aa2 stable).

The city has agreed to a set-aside schedule under which the entire principal payment is required to be deposited with the trustee on May 22, 2015, and the entire interest payment to be deposited on June 26, 2015.

Moody's maintains a rating of A2 with a stable outlook on the city's long-term general obligation debt and parity obligations.

SUMMARY RATING RATIONALE

The MIG1 short-term rating on the city's Tax and Revenue Anticipation Notes reflects: ample coverage of principal and interest by projected cash balances; a solid trend in tax revenues; adequate long-term credit quality reflected in the city's general obligation rating of A2 and stable outlook ; and a history of reasonable and accurate cash-flow projections. The rating also recognizes that the city's revenue composition is economically sensitive and therefore subject to volatility, and that the recent improvements in the city's cash balances and tax revenues have begun to flatten.

STRENGTHS

Ample coverage of principal and interest by projected cash balances

Solid trend in tax revenues

CHALLENGES

Volatile and economically sensitive revenue composition

Flattening out of recent improvements in tax revenues and cash balances
DETAILED CREDIT DISCUSSION

AMPLE CASH BALANCES PROJECTED TO COVER NOTE PRINCIPAL

Cash balances will provide ample cushion for repayment of TRAN principal and interest. The city projects a cash balance of $358 million at the end of April, and net cash inflows of $104.3 million in May. The total cash available in May of $462 million will be sufficient to cover the May 22 principal set-aside of $130 million by 3.6 times, a solid level of coverage. Cash balances in June will be sufficient to cover June 26 set-aside by a much higher multiple, as the June payment consists solely of the interest on the notes.

The pledged revenues, consisting of all General Fund receipts, totaled an estimated $3.8 billion in 2014. The $130 million note represents a modest 3.5% of total pledged receipts.

CASH-FLOW BORROWING NEEDS HAVE DECREASED ON STRONGER CASH BALANCES

The city has issued TRANs every year except one since 1972. The city's property tax levy (14% of revenues) is due at the end of March and business income and gross receipts taxes (12%) are typically paid at the tax filing deadline in April. Combined with state aid (7%) that ordinarily comes late in the fiscal year (ending June 30), much of the city's revenue collections are weighted toward the last few months of the year.

As the city's revenue base has improved in the aftermath of the recession, its cash balances have increased and its need to fill cash flow gaps has decreased. The city began fiscal 2011 with a General Fund cash balance of $23 million, leading it to issue $285 million of notes that year. The opening cash balance increased each year from 2012 to 2014, leading to progressively smaller TRAN borrowings. The borrowing in 2014 was $100 million.

Because of an estimated decline in the cash balance during 2014, the city has modestly increased its TRAN borrowing to $130 million in 2015.

HIGHER REVENUES, SMALLER NOTES LEAD TO HIGHER COVERAGE

As the city's receipts have increased and the size of TRAN borrowings has decreased, coverage of TRAN principal and interest by cash flows has been rising. In fiscal 2011, the beginning cash balance plus net inflows in May totaling $325 million were sufficient to cover the $285 million note principal by a narrow 1.14x. In 2014, the estimated cash available in May of $490 million covered the $100 million note principal by 4.9 times.

This trend is likely to reverse modestly beginning this year, as revenues decline due to the resumption of tax cuts, a program that was suspended in the aftermath of the recession. The city's long-term plan calls for reductions in the rate of some of its most important tax sources, including wage and business taxes, which is projected to decrease revenues and cash balances. Coverage is likely to remain solid.

REASONABLE CASH FLOW PROJECTIONS

The city has made reasonable projections of cash flow in the past few years, outperforming on both inflows and outflows by a few percentage points annually.

The city has significantly underestimated its actual available cash in May for each of the last three years. For example, the city estimated it would have $436 million in available cash in May 2014 to repay the $100 million in note principal; actual cash available was $64 million higher than that.

The city projects a 2% decline in revenues for 2015, reflecting cuts in the rates to its business income tax and sales tax. The projections are reasonable, although given the city's economically sensitive revenue base, an economic downturn would apply downward pressure on General Fund cash flows more so than other cities.

STABLE UNDERLYING CREDIT PROFILE

The city's underlying long-term credit profile is stable. The General Fund balance of 8% at the end of fiscal 2013 was the highest in seven years, and marked a substantial improvement from the low fund balance of negative 4% in 2010. Most of the city's important tax revenue sources are performing well, but fund balance is likely to flatten given the city's planned tax cuts. The city estimates an ending fund balance of 6% in 2014.

The economic profile of the city has begun to see modest improvement, as several decades of population loss have begun to reverse. The socioeconomic profile of the city remains below average, and will continue to be a drag on its long-term credit quality.
Earlier this month, the City Council indicated it would not approve a proposed $1.9 billion sale of the Philadelphia Gas Works (Baa2 positive). The city would have deposited net proceeds from the sale in its pension fund, reducing its adjusted net pension liability. Had the sale proceeded, the reduction in net pension liabilities would have been a modest positive, but the failure of the sale does not materially change our view of the city’s fundamentals.

The city’s debt and pension burdens remain high. Direct debt burden is 4.4% of full value. The city’s pension burden, as measured by Moody’s Adjusted Net Pension Liability (ANPL), is 2.5 times annual revenues.

WHAT COULD MAKE THE NOTE RATING GO DOWN:

Return to negative fund balance position

Economic downturn depressing currently solid tax revenue trend

KEY STATISTICS

Security: Pledge of General Fund receipts

Underlying GO rating: A2 stable

Maturity: June 30, 2015

Required principal set-aside: May 22, 2015

Required interest set-aside: June 26, 2015

TRANs issued as % of estimated receipts: 3.5%

Projected coverage of TRAN principal by available cash: 3.6x

Estimated 2014 General Fund balance: 6% of revenues

Estimated 2014 General Fund revenues: $3.8 billion

Estimated 2014 General Fund cash balance: $449 million

The principal methodology used in this rating was Short-Term Cash Flow Notes published in April 2013. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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