MOODY'S
INVESTORS SERVICE

New Issue: Moody's assigns A1 to Buffalo, NY's $25.6M GOLT bonds and MIG 1 to $7.3M BANs; outlook stable

Global Credit Research - 04 Mar 2014

Affirms A1 G.O. rating on outstanding debt

BUFFALO (CITY OF) NY
Cities (including Towns, Villages and Townships)
NY

Moody's Rating

ISSUE		RATING
Bond Anticipation Notes 2014		MIG 1
Sale Amount	$7,300,000	
Expected Sale Date	03/11/14	
Rating Description	Note: Bond Anticipation	
General Improvement Serial Bonds 2014		A1
Sale Amount	$25,600,000	
Expected Sale Date	03/11/14	
Rating Description	General Obligation Limited Tax	

Moody's Outlook STA

Opinion

NEW YORK, March 04, 2014 --Moody's Investors Service has assigned an A1 rating to the City of Buffalo's (NY) $25.6 million General Improvement Serial Bonds - 2014 and a MIG 1 rating on $7.3 million Bond Anticipation Notes - 2014; the outlook is stable. The bonds and BANs are general obligations of the city as limited by the Property Tax Cap Act (Chapter 97 (Part A) of the Laws of the State of New York, 2011. Concurrently, Moody's has affirmed the A1 rating with a stable outlook on all rated debt secured by the city's general obligation pledge. Proceeds of the bonds will permanently finance $13.9 million in BANs and provide $11.6 million in new money largely for infrastructure improvements. The BANs will refinance $2.2 million in outstanding notes and provide $5.1 million in new money for various capital improvements around the city.

SUMMARY RATINGS RATIONALE

The A1 rating reflects the city's overall solid reserves and liquidity despite current declines and a multi-year plan that includes structurally imbalanced budgets. The rating also factors: (1) challenges posed by the city's below average demographic profile; (2) a high debt burden that is expected to gradually moderate; (3) the challenges posed by open employee contracts (4) the oversight of city operations by the Buffalo Fiscal Stability Authority (BFSA, sales tax and state aid secured bonds rated Aa1), which has approved the city's four-year financial plan; (5) the city's improved revenue-raising flexibility given modest growth in assessed valuation and improved taxing margin; and (6) additional bondholder security provided by the city's legally-required bi-annual set-aside of debt service payments from first property taxes collected, held by the bond trustee.

The stable outlook reflects Moody's belief that the city's liquidity and reserve position will remain adequate, evidenced by elimination of the need for seasonal cash flow borrowing in the last six fiscal years. The currently healthy cash position is expected to provide satisfactory cushion against near-term fund balance and liquidity declines.

The MIG 1 rating reflects the city's long-term credit quality and demonstrated market access, largely for long-term bonds, over the past three years. The city issued short-term notes last year and received nine bids.

STRENGTHS:

-State oversight board provides third-party supervision of city's finances

-Conservative budgeting and strong management have led to a solid reserve position and liquidity

-Direct pay of first-in property tax money to the trustee for payment of debt service

CHALLENGES:

-Uncertainty around outstanding union contracts and pending litigation

-State aid cuts could put significant pressure on city's finances

DETAILED CREDIT DISCUSSION

DEMONSTRATED MARKET ACCESS

The city is a frequent debt issuer with a strong history of favorable market access, although it has only issued notes once without BFSA as the issuer in the past five years. The city received nine bids from a variety of local and regional banks on its 2013 note issuance. Offsetting the lack of a record of short-term note issuance is the city's overall credit profile, including oversight of city finances by BFSA and ample liquidity. Given the city's overall credit profile, Moody's expects that the city will be able to refinance the notes at maturity on April 30, 2015.

HEALTHY RESERVES AND CONSERVATIVE MANAGEMENT PROVIDE BUFFER AGAINST NEAR-TERM RISKS

Moody's believes the city's financial flexibility and liquidity will remain strong given capable financial management, solid financial policies, oversight of budgets and the multi-year plan despite a current and projected draw down in reserves. The city's overall fund balance (General Fund and City School District) increased to a strong $374.1 million (29.7% of combined revenues) as of fiscal 2013, from $40.6 million (6.0% of revenues) in 2002. The city's combined net cash position improved to a ample 51.4% of combined revenue, from a narrow 5.4% in 2003. In fiscal 2008, the city first began funding its Rainy Day Fund, set by city charter to equal 30 days' operating expenditures. While the reserve position has improved over the past decade, the city and City School District (CSD) plan to draw down on reserves over the next four years. These declines were planned as part of the city's multi-year budget and were approved by the state control board, the Buffalo Fiscal Stability Authority (BFSA). The use of reserves is expected to gradually decline and the city anticipates to return to structurally balanced budgets at the end of the forecast period. Management expects total fund balance at the city level to be between 17%-20% of revenues with the CSD maintaining reserves in the 12%-15% of operations level.

Management originally appropriated $11.2 million in General Fund balance in the fiscal 2013 budget, but ended the year with a $52 million increase. The addition to reserves was largely due to one-time items, including the settlement of a labor contract, a settlement with the Seneca Nation of Indians (see Moody's Credit Outlook dated June 17,2013 for additional information regarding the settlement) and $10 million in state aid advancement. The city did experience savings in personnel services and fringe benefits. The CSD was unable to replenish an appropriation of $20 million in reserves and finished fiscal 2013 with a $12 million decline in fund balance, despite savings in personnel benefits. Overall, combined fund balance increase was $40 million.

The city's fiscal 2014 budget was balanced with approximately $15.8 million in appropriated fund balance, and included a 2% increase in sales tax and no increase in property tax revenues. To date, management anticipates finishing the year with a slight budgetary surplus but will not replenish the majority of the fund balance appropriation. The city has once again seen expenditure savings and better-than-budgeted sales tax collections. This is offset with weaknesses in some revenues, particularly charges for services. The CSD appropriated $31.1 million in fund balance for the fiscal 2014 budget. The current projection is for the CSD to draw $25 million in reserves. The surplus relative to budget is the result of conservative budgeting of expenses.

While the city remains exposed to risks associated with potential state aid cuts, open labor contracts, and ongoing litigation, we believe that the city's current financial position and conservative fiscal management provide satisfactory cushion against these risks. For example, management has implemented a number of policies, including the Rainy Day Fund and four-year financial forecasting. Additionally, financial flexibility to pay debt service is available for the city with approximately $6 million in cash available in the city's Debt Service Fund and $77.7 million in the BOE Debt Service Fund.

FOUR-YEAR PLAN APPROVED BY BUFFALO FISCAL STABILITY AUTHORITY; ADVISORY PERIOD ESTABLISHED

The Buffalo Fiscal Stability Authority (BFSA) was created by act of the State Legislature on July 3, 2003 to control and supervise the financial affairs of the City of Buffalo. The BFSA has been charged with the creation and implementation of a four-year recovery plan, annual budget review and revenue forecasting. On May 29, 2012, BFSA voted 6 to 1 to move to an advisory board from a control board effective July 1, 2012, the beginning of the city's fiscal 2013 year. Under an advisory role, the board's powers are largely limited to financial oversight and responsibilities. BFSA can re-impose a control period if the city were to fail to adopt a balanced budget, default on its debt, or incur an operating deficit greater than 1% of any major fund of the city, among other provisions. City management notes that it will continue to implement policies and procedures that BFSA required while in the control period, and we expect the city and BFSA will maintain a solid working relationship over the life of the control board.

The city's four-year plan (fiscal years 2014 through 2017) was approved by the BFSA on June 19, 2013. Moody's considers the development of a multi-year plan and the oversight provided by BFSA to be key credit strengths for the city. The current plan assumes annual budget growth of 2.8% in fiscal 2015, primarily driven by increased sales tax revenues. Budget growth in fiscal 2016 and 2017 is expected to be flat. Pension benefits are expected to level out and begin declining over the next two years, which will help the city meet its budget targets. The plan budgets for sales tax growth of 6.8% in 2015, given that BFSA will reduce its withholding due to lower debt service costs. Sales tax in the out years is budgeted at a more conservative 2.5% increase. This growth assumption reflects healthy sales tax increases for the city and county due to the weak US dollar and increased cross-border traffic from Canada. The plan assumes the use of reserves throughout the forecast period ranging from $2.5 million to $5.8 million. To help close the budget gaps management will look to a mix of one-time items and consolidation of services and buildings.

The BFSA-approved four-year plan for the CSD projects the annual use reserves of approximately $39 million through 2017. While the CSD plans to reduce the use of reserves through a number of gap closing measures it does plan to utilize $69.7 million in rainy day funds (a total reduction in reserves of 38%) over the four year period. Management expects to close the gaps through a combination of school closures, staff reductions, and other cost-saving initiatives. The projections do not include a settlement of a decade-long labor contract dispute. The teacher and administrator unions have been without a contract since 2004 and there have been limited negotiations to date. Moody's will continue to closely monitor the CSD's use of reserves.

ECONOMY HAS BEGUN TO IMPROVE; POPULATION DECLINES CONTINUE

Despite a number of large investments in the city we expect the $6.4 billion tax base to remain challenged given continued population declines, high unemployment and poverty levels, and income levels that are well below state medians. According to U.S. Census figures, the city's 2010 population was 261,310, down 10.7% from 2000, a continuation of the trend that began in 1950 when the city's population peaked at 580,132. Despite the population loss, unemployment has consistently remained above the state and national averages, and was 8.0% in December 2013, above 6.6% and 6.5% for the state and nation, respectively. The city's employment numbers are at the highest levels since 2010, however. Moody's Analytics recently reported that the Buffalo MSA would have recouped all its jobs lost during the great recession, except for a late-year weakening in job growth.

New York State Governor Andrew Cuomo has made economic development of the Buffalo region one of his top priorities. The goal of his "Buffalo Billion" plan is to infuse $1 billion into the Buffalo economy over 10 years. Over the past six months, two major projects have been announced: the River Bend Project (see Moody's Weekly Credit outlook dated December 13, 2013 for additional information) and the development of a genomic research center. Both of these projects will result in immediate construction employment, but in the long-term, the projects are expected to bring in high paying technology jobs. These recent announcements are two in a string of economic development announcements over the past four years. In addition, the city has significant economic development activity along the waterfront and inner harbor. Recently, the Buffalo Sabres' HARBORcenter Development, LLC won a bid to build a new hockey-themed complex along the inner harbor. The project is estimated at $172 million and is expected to include a new hotel, retail, restaurants and two ice rinks. The project will generate 1,500 new construction jobs and 350 new full-time jobs upon opening. Additionally, management expects that, upon completion, the new complex will generate $4.1 million in new revenue for the city. As Moody's Analytics notes in its January 2014 report, the Buffalo MSA is also witnessing a revival in auto manufacturing with both Ford and General Motors making investments in the region.

DEBT BURDEN EXPECTED TO REMAIN WELL ABOVE AVERAGE

Moody's expects the city's overall debt burden (6.2% of full value) will remain high, but will gradually moderate, given modest tax base growth, rapid amortization of debt and management's policy of retiring more debt than is annually issues. While state school building aid reduces the city's debt burden, it remains well above average at 6.1% of full valuation. Pursuant to New York State Statute, the city has established a Debt Service Reserve Fund held by a trustee. The trustee intercepts all first-in property tax revenue for payment of debt service during each collection period (July 1 and December 1). After the trustee has sufficient cash to cover debt service for the period following the collections, the remainder of the property tax money is then remitted back to the city. This provides additional security for the payment of the city's debt service. The CSD maintains sizable capital needs, although these are expected to be financed by the Erie County IDA and should not alter the city's debt profile. Approximately $1.4 billion has been issued under this program since 2003 ($1 billion currently outstanding). These separately secured, parity issuances are each rated Aa3 positive, reflecting the CSD's obligation to make lease payments to the Erie County Industrial Development Agency (ECIDA) to pay debt service; a pre-default state aid intercept in the event of non-appropriation; a flow of funds that provides full segregation of debt service 30 days before annual principal and interest payment; and a Debt Service Reserve Fund that is funded at 50% of MADS. This debt is excluded from the city's debt statement based upon security mechanics and sources of payment from non-city funds, primarily state school building aid. All of the city's outstanding debt is fixed rate, and the city is not party to any derivative agreements.

FIXED COSTS CONTINUE TO PRESSURE THE CITY'S BUDGET; EXPECTED TO STABILIZE

Buffalo has a average defined-benefit pension burden, based on unfunded liabilities for a single-employer plan and for its Moody's-estimated share of a cost-sharing plan administered by the state. Reported unfunded liabilities consist primarily of $60 million for the multi-employer cost sharing New York State Teachers' Retirement System; $34 million for the multi-employer cost sharing New York State and Local Employees' Retirement System; $62 million for the multi-employer cost sharing New York State and Local Police and Fire Retirement System; $25 million for the multi-employer cost sharing New York State and Local Employees' Retirement System - Board of Education; and the $2 million for the multi-employer cost sharing New York State and Local Employees' Retirement System - Component Unit as of December 31, 2012.

Pension-driven budgetary pressures have stressed the city's budget over the past five years, but are expected to stabilize and decline in the next three years. The fiscal 2012 actuarially-determined, contractually-required contribution (CRC) for all the multi-employer plans rose to $72.6 million, or 6% of operating revenues, from $47.2 million, or 4% of operating revenues, in fiscal 2010. The city has made its full CRC annually and has not chosen to amortize a portion of the payments. Neither the city nor the CSD have plans to amortize pension payments in the future. Fixed costs continue to consume a greater proportion of the town's budget. In fiscal 2012, pension contributions, debt service and PAYGO costs for OPEB benefits represented 26% of operating expenses.

Moody's fiscal 2012 adjusted net pension liability (ANPL) for the city and CSD, under our methodology for adjusting reported pension data, is $1.1 billion, or an average 0.94 times operating revenues. The three-year average of Buffalo's ANPL to Operating Revenues is an average 0.77 times, while the three-year average of ANPL to full value is a high 13.7%. Moody's ANPL reflects certain adjustments we make to improve comparability of reported pension liabilities. The adjustments are not intended to replace Buffalo's reported liability information, but to improve comparability with other rated entities.

OUTLOOK

Moody's stable outlook reflects our belief that despite expected draws on reserves the city's liquidity and reserve position are at levels sufficient to maintain an A1 rating. The currently healthy cash position is expected to provide satisfactory cushion against risks related to the weak economy, potential state budget cuts and disbursement delays, as well as liabilities related to open labor contracts and ongoing litigation. The outlook factors our expectation that management will maintain its strong financial position in the face of these challenges, given its demonstrated conservative fiscal management and policies.

WHAT COULD MAKE THE RATING GO UP:

- Demonstrated ability to maintain satisfactory financial flexibility and liquidity relative to peers

- Structurally balanced budgets which reduce the annual fund balance appropriation and declining reserve position

- Continued strengthening of city financial policies

- Significant increases in socio-economic profile

WHAT COULD MAKE THE RATING GO DOWN

- Continued use of reserves beyond what is currently expected

- Structurally imbalanced operating results

- Reversal of trend of increasing taxing capacity

KEY FACTS

FY 2014 Full valuation: $6.4 billion

Full value per capita: $24,801

Median Family Income as a % of US (2010 American Community Survey): $35,575 (57.3% of the US)

Available Fund Balance as a % of Revenues: 24.5%

5-Year Dollar Change in Fund Balance as % of Revenues: 5.3%

Net Cash as a % of Revenues: 51.4%

5-Year Dollar Change in Cash Balance as % of Revenues: 27.5%

Institutional Framework : A

Operating History: 5-Year Average of Operating Revenues / Operating Expenditures: 1.01x

Net Direct Debt / Full Value: 6.2%

Net Direct Debt / Operating Revenues: 0.31x

3-Year Average of Moody's Adjusted Net Pension Liability / Full Value: 13.71%

3-Year Average of Moody's Adjusted Net Pension Liability / Operating Revenues: 0.77x

The principal methodology used in the long term rating was US Local Government General Obligation Debt published in January 2014. The principal methodology used in the short term rating was Bond Anticipation Notes and Other Short-Term Capital Financings published in May 2007. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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