FitchRatings

Fitch Rates NYC Transitional Finance Auth $1.1B FTS Bonds 'AAA'; Outlook Stable

Ratings Endorsement Policy
18 Oct 2013 4:53 PM (EDT)

Fitch Ratings-New York-18 October 2013: Fitch Ratings assigns an 'AAA' rating to the following New York City Transitional Finance Authority (TFA) subordinate fixed rate future tax secured (FTS) bonds:

Approximately $1,092,470,000 fiscal 2014 series A bonds, including the following subseries:

--650,000,000 subseries A-1 tax-exempt subordinate bonds;
--$350,000,000 subseries A-2 taxable subordinate bonds;
--$92,470,000 subseries A-3 taxable subordinate bonds (qualified school construction bonds).

In addition, Fitch affirms its 'AAA' rating on the following outstanding TFA FTS bonds:

--$2.1 billion senior bonds;
--$19.6 billion subordinate bonds;
--$1.1 billion recovery subordinate bonds.

The Rating Outlook is Stable.

The bonds are scheduled to sell on October 23 through negotiation.

SECURITY
The bonds are payable from revenues derived from a personal income tax (PIT) and a sales and use tax imposed by New York City (the city), as authorized by New York State (the state). Payment of the PIT and sales tax revenue to the TFA is not subject to city or state appropriation.

Sales tax revenues will be available for the payment of bonds if PIT revenues are projected to be insufficient to provide at least 150% of the maximum annual debt service (MADS) on the TFA's outstanding bonds.

Senior bonds are subject to a $330 million limit on quarterly debt service. Additional bonds may be issued as senior bonds if tax revenue for the 12 consecutive calendar months preceding authorization is at least 3x the amount of annual senior debt service or $1.32 billion.

The subordinate additional bonds test (ABT) requires that tax revenues for the most recent fiscal year are at least 3x the sum of $1.32 billion plus projected subordinate debt service.

KEY RATING DRIVERS
STRONG LEGAL FRAMEWORK: The bankruptcy-remote, statutorily defined nature of the issuer and a bond structure involving a first perfected security interest in the PIT and sales tax revenues are key credit strengths. Payment of the PIT and sales tax revenue to the TFA is not subject to city or state appropriation. Statutory covenants prohibit action that would impair bondholders.

TAX RATE RISK LOW: The state can unilaterally modify or repeal tax law as it relates to the PIT or sales tax and could risk default by exercising this right in an extreme city fiscal crisis scenario. Fitch believes that the risk of this is negligible.

STATUTORY CASH FLOW PROVISIONS: The PIT and sales tax are imposed by the city pursuant to state statute and collected by the state. Revenues from the PIT (and the sales tax, if required) flow directly from the state comptroller to the TFA trustee and are not subject to state or city appropriation. The city receives residual revenues only after advance quarterly funding of debt service.

ROBUST COVERAGE: Although senior bonds have a first claim on statutory revenues, Fitch does not make a rating distinction between the liens due to the high coverage levels. Even with sizable debt issuance plans over the next four years, pro forma MADS coverage is expected to remain strong.

SOLID ECONOMIC UNDERPINNINGS: Statutory revenues are derived from a broad economic base, benefiting from the city's unique role as a national and international center for commerce and culture.

DEPENDENCE ON WALL STREET: Financial activities account for about 12% of jobs and 30% of earnings. Recession-related job declines were well under comparable national averages. Overall employment has since shown solid growth although weakness in financial services employment is evident. The city's unemployment rate has declined to near the U.S. average.

CREDIT SUMMARY

STRONG LEGAL FRAMEWORK PROTECTS BOND REPAYMENT

The 'AAA' rating is based on the very strong legal structure which insulates bondholders from any operating risk of New York City (GO bonds rated 'AA' by Fitch). The rating reflects the bankruptcy-remote, statutorily defined nature of the issuer, the bond structure involving a first perfected security interest in revenues that are not subject to appropriation, statutory covenants prohibiting action that would impair bondholders, New York State as collection agent, and the existence of two separately levied cash flow streams (the statutory revenues).

PIT and sales tax revenues are imposed by the city and collected by the state. Revenues from the PIT as well as the sales tax, if required, flow directly from the state comptroller to the TFA trustee, and are not subject to state or city appropriation. The city receives residual revenues only after advance quarterly funding of debt service.

The state is able to unilaterally modify or repeal tax law as it relates to the PIT or sales tax and could risk default by exercising this right in an extreme city fiscal crisis scenario; however, Fitch believes that the risk of this is negligible.

PLEDGED REVENUES EXHIBIT STABILITY DESPITE SOME VARIATION

The PIT consists of a base rate and a 14% surcharge. The PIT rate has changed over time, most recently with a base rate increase in 2010. Both the base rate increase and the 14% surcharge, originally imposed in 2002, are set to expire on Jan. 1, 2015 unless extended with state approval. Failure to approve continuation of both the current base rate and the 14% surcharge could result in significant declines of pledged revenue.

TFA estimates indicate that annual FTS revenue at the minimum base rate with no surcharge would decline by $5.9 billion by fiscal 2017. This level would still provide over 4x coverage assuming additional debt is issued on the current schedule and no change to the sales tax rate. Fitch believes this is an extreme scenario given the importance of this source to the city's budget and the consistent reauthorization of both a base rate above the minimum authorized and the 14% surcharge.

The PIT comprised 58% of fiscal 2012 FTS revenue. Since fiscal 2003, both PIT and sales tax revenue have declined in only one fiscal year. The significant 16.5% FTS decline in fiscal 2009 was due in part to an adjustment for prior-year PIT overpayments, and in part to the recession.

The city anticipates a large 10.6% increase in PIT revenue in fiscal 2013, largely due to recognition of capital gains prompted by federal tax law changes. Following this increase, fiscal 2014 PIT revenue is forecast to decline 9.5%, which would bring revenues to 5.2% above the fiscal 2012 level.

STRONG COVERAGE EXPECTED EVEN WITH FUTURE DEBT ISSUANCE

Debt service coverage on all FTS bonds from fiscal 2012 revenue was 9.2x. Combined with sizable debt issuance plans, projected coverage is expected to remain high at a minimum of 6.4x through fiscal 2017 using TFA's projected annual pledged revenue growth assumptions, or 5.2x assuming no growth from audited fiscal 2012 pledged revenue. The TFA assumes a conservative 5% interest rate on variable rate debt, which makes up about 16% of total debt.

Not included in coverage figures are BAB and QSCB subsidies, which are not pledged as security for the bonds. The reduction in subsidies resulting from federal sequestration has a minimal impact on revenue available for debt service.

The city in its fiscal 2014 budget assumes modest growth in wage rates, offsetting weakness in securities sector bonus payouts. Following volatility related to the aforementioned 2013 federal tax rate changes, annual PIT growth is forecast in the 3%-4% range, assuming moderate economic recovery. Similarly, the budget assumes continued strong visitor-related spending and moderate economic growth will yield annual sales tax growth in the 4% range. Fitch believes these tax revenue growth forecasts are reasonable but vulnerable to down-side risk.

Coverage projections assume the issuance of approximately $10.7 billion in additional FTS bonds in fiscal 2014-2017, in accordance with the city's capital improvement plan. Coverage is projected to well exceed the subordinate ABT that requires that historical statutory revenues cover at least 3x the full $1.32 billion maximum allowable senior debt service plus projected subordinate debt service.

ECONOMY HAS INHERENT STRENGTHS BUT NOT WITHOUT CHALLENGES

Fitch considers the city's unique economic profile, which centers on its singular identity as an international center for numerous industries and major tourist destination, to be a credit strength. The character of the New York City economy has contributed to its relative employment stability during the recession and ability to regain by March 2012 the number of private sector jobs that existed prior to the recession. The city's tourism sector is performing exceptionally well, attracting a record 52 million visitors in 2012, the third record year in a row.

The city's economic profile also benefits from good wealth levels; although census data indicate that per capita and median household income are similar to the U.S. average, market value per capita is over $100,000. However, the above-average individual poverty rate of 19.4% in 2011, compared to 14.3% for the U.S., indicates significant income disparity.

The city's economy (and operating budget) is strongly linked to the financial sector, which accounts for approximately 12% of total employment but 30% of earnings. Financial activities employment declined 0.2% in 2012. The high-earning securities and commodities component of the sector showed similar trends in 2012, shedding roughly 2,500 jobs or 1.5%.

Tightening financial reforms and regulation, reduced bank revenue, evidence of a shift in bonus and compensation practices away from cash, uncertain economic recovery, and concerns in Europe are among several factors that figure to weigh on financial sector prospects over the near- to intermediate-term.

The city's resident employment base grew by 1% in 2012, above the state's slight 0.4% growth but behind the U.S. at 1.9%. The unemployment rate increased to an average of 9.3% in 2012 from 9% in 2011. Recent data are more encouraging - the August 2013 rate of 8.7% compares favorably to the August 2012 rate of 9.4%, and the improvement was due to strong employment growth of 2.5%. However, the most recent rate is still a full percentage point above the U.S. average.

Contact:
Primary Analyst
Amy Laskey
Managing Director
+1-212-908-0568
Fitch Ratings, Inc.
One State Street
New York, NY 10004

Secondary Analyst
Karen Wagner
Director
+1-212-908-0230

Committee Chairperson
Marcy Block
Senior Director
+ 1 212 908-0239

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at 'www.fitchratings.com'.

Applicable Criteria and Related Research:
--'Tax-Supported Rating Criteria' (Aug. 14, 2012);
--'U.S. Local Government Tax-Supported Rating Criteria' (Aug. 14, 2012).

Applicable Criteria and Related Research:
Tax-Supported Rating Criteria

U.S. Local Government Tax-Supported Rating Criteria

Additional Disclosure
Solicitation Status