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Boston's Bond Position in Subprime Crisis

City's high bond rating should result in no direct impact with March issue

The benefits of the Menino Administration exercising prudent fiscal management through all economic cycles and maintaining healthy reserves will become more evident in March when the City will issue \$127M in General Obligation bonds. Because of the City's AA bond rating, the March issue should not be directly affected by the meltdown in the subprime mortgage market.

Boston is ranked at the highest AA rating for both Moody's Investors Service (Aa1) and Standard and Poor's (AA+) and has an AA rating from Fitch Ratings. Boston's manageable debt burden and its diverse economy have also contributed to the ratings.

The City should be successful in selling its bonds at a favorable rate in March due to:

- The City's high bond rating
- The current market in which investors are looking either for quality or for significantly higher yields for bonds with lower credit ratings than held by the City
- The Federal Reserve Bank's reduction of its benchmark rate to 3.0%

The City will also sell a refunding bond issue this March which should have the same results. For a \$100M GO bond issue and an \$85.4M refunding issue in 2007, the City's True Interest Cost (TIC) was 3.97% and 4.04%, respectively.

Municipalities with lower bond ratings than Boston could be affected by the deterioration

of the credit markets if they need to rely on bond insurance to increase the ratings of an issue. A number of the municipal bond insurers have acknowledged their own domestic exposure to subprime mortgage-backed securities which will affect their own bond ratings. Indeed, in December, Standard & Poor's assigned a negative outlook to several financial guarantors. A few guarantors were less affected but may now charge a higher premium.

Boston has purchased insurance from some of these guarantors (Ambac and MBIA) for certain special obligation bond issues. In other cases, the bond underwriters have purchased insurance for the whole or selected years of a bond issue. In both instances, any impact on prior insured bond issues due to the guarantor's subprime exposure would not affect the City but would be borne by holders in the secondary market. The City likely will not purchase insurance for the March bond issue due to its strong credit rating and the uncertainty surrounding the insurers' ratings.

The reach of the subprime mortgage crisis is wide. Restricted access to credit markets, declining sale prices and housing foreclosures will have some adverse affect on property values of individual parcels. However, this situation will not prevent the City from raising the tax levy by the full 2.5% over the prior year levy limit. Boston's levy ceiling, based on 2.5% of its taxable value, exceeds this year's tax levy by \$917.4M.