

RatingsDirect®

Summary:

Albany, New York; General Obligation

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US\$18.849 mil GO (Serial) bnds ser 2020 dtd 03/26/2020 due 03/15/2030

Long Term Rating

A+/Stable

New

Rating Action

S&P Global Ratings assigned its 'A+' long-term rating and stable outlook to Albany, N.Y.'s series 2020 general obligation (GO) serial bonds and affirmed its 'A+' long-term rating and underlying rating (SPUR), with a stable outlook, on the city's existing GO debt.

The city's faith-and-credit-GO pledge secures the bonds, including the statutory authorization to levy ad valorem taxes on all real property in the city, subject to applicable statutory limitations.

We understand officials intend to use series 2020 bond proceeds to finance various capital projects in the city.

Credit overview

Albany, New York's state capital, continues on its path of economic and budgetary improvement. As much of its land is tax-exempt, the city has benefited from growth in other parts of its economy, such as health care, education, and technology, while downtown revitalization efforts are bearing fruit with continued residential and mixed-use development. That said, the rating remains constrained by several factors. Albany remains reliant on state support, some of it appropriated by the state on an annual basis. Outstanding labor contracts with police unions could, when settled, trigger substantial retroactive pay, resulting in pressure on the city's finances. Pension and other postemployment benefit (OPEB) costs remain substantial and the city continues to defer pension payments. That said, the city has also taken important steps to ensure the sustainability of its financial position in the medium term by taking measures to reduce reliance on landfill revenues and generating recurring savings through the acquisition of street lights. Overall, we therefore believe our rating on Albany will remain stable over our two-year outlook horizon.

The rating reflects our opinion of the city's:

- Adequate economy, with access to a broad and diverse metropolitan statistical area (MSA) and a local stabilizing institutional influence;
- Strong management, with good financial policies and practices under our Financial Management Assessment (FMA) methodology;
- Adequate budgetary performance, with operating results that we expect could deteriorate in the near term relative to fiscal 2018, which closed with operating surpluses in the general fund and at the total governmental fund level;
- Weak budgetary flexibility, with an available fund balance in fiscal 2018 of 4.4% of operating expenditures, as well as limited capacity to raise revenues due to consistent and ongoing political resistance;
- Adequate liquidity, with total government available cash at 3.8% of total governmental fund expenditures and 40.9%

of governmental debt service, but access to external liquidity we consider strong:

- Very weak debt and contingent liability profile, with debt service carrying charges at 9.3% of expenditures and net direct debt that is 60.0% of total governmental fund revenue, and significant medium-term debt plans and a large pension and OPEB obligation and the lack of a plan to sufficiently address the obligation, but rapid amortization, with 71.0% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Stable Two-Year Outlook

The stable outlook reflects S&P Global Ratings' opinion of the city's adequate economy, supported by the stabilizing presence of state government and other educational and health-care institutions. The outlook also reflects our opinion of the city's recent return to positive available fund balance. We believe management will likely maintain reserves during the next few fiscal years due to its recent efforts to reduce citywide departmental expenses. Therefore, we do not expect to change the rating during the two-year outlook period.

Downside scenario

If the city's efforts to generate additional revenue through service charges, continued state support, and plans to consolidate city services for expenditure savings do not successfully decrease budgetary gaps, we could lower the rating. In addition, if Albany were to settle its contracts outstanding with significant retroactive payments or fixed costs from pension and OPEB expenditures were to pressure the budget, causing liquidity to decline, we could lower the rating.

Upside scenario

If management were to maintain its efforts to improve operating performance, allowing it to rebuild fund balance while improving liquidity, without increasing its reliance on state aid, we could raise the rating.

Credit Opinion

Adequate economy

We consider Albany's economy adequate. The city, with an estimated population of 98,841, is in Albany County in the Albany-Schenectady-Troy MSA, which we consider broad and diverse. The city also benefits, in our view, from a stabilizing institutional influence. The city has a projected per capita effective buying income of 76.6% of the national level and per capita market value of \$50,572. Overall, market value has grown by 2.9% during the past year to \$5.0 billion in 2020. County unemployment was 3.7% in 2018.

Albany, the capital of New York State, serves as the central city of the Albany MSA. The presence of state government pervades local income and the city's property tax base. The state is the city's leading employer with over 49,000 employees. Approximately 63% of city property is tax exempt, 60% of which management attributes to state tax-exempt property. The level of tax-exempt property adversely affects market value per capita. At the same time, we believe employment in state government, higher education, and health care stabilizes the local economy.

Management expects continued development of residential property to support taxable property value growth in and around the city's downtown area. Besides residential developments, Albany's downtown area also benefits from a new theater and hotel development further aiding downtown revitalization efforts. In addition, the city expects development of new residential apartment buildings close to its largest employers, mostly hospitals and SUNY Albany.

The city has experienced slight population and employment growth during the past few years, the latter of which management attributes to improvements outside of state government in the manufacturing, health care, and education sectors. Moreover, thanks to Albany's favorable location, Amazon is currently building a distribution center outside the city, which will bring approximately 800 new jobs to the region. We believe the establishment of, and investment in, the Albany NanoTech complex helps diversify the city's economy.

Strong management

We view the city's management as strong, with good financial policies and practices under our FMA methodology, indicating that financial practices exist in most areas but that governance officials might not formalize or regularly monitor all of them.

Albany suffered a ransomware attack in March 2019. While it did not pay the ransom, the city paid about \$300,000 (0.2% of 2019 general fund expenditures) in recovery costs. Notwithstanding the successful attack, the city's defense system alerted officials of the breach in a timely manner and according to the city, no personal information of residents or city staff was compromised, which we view favorably. In addition, backups of critical servers allowed the city to restore services quickly. Following the attack, Albany has taken additional measures, including increasing staff levels, to protect itself from future attacks.

Management uses at least three to four years of trend analysis for revenue and expenditure assumptions and makes adjustments based on recent revenue trends realized or contract considerations. The city's board of estimate monitors revenue and expenditures biweekly. Officials prepare financials for the treasurer's and budget director's offices for budgetary purposes, and they present financial updates to the common council quarterly.

The city maintains a five-year formal capital improvement plan (CIP) and an investment policy, with holdings and performance disclosed in annual reports to the council. As part of the CIP, the city is also taking resiliency measures: for instance, measures to prevent flood water from entering the sewer system. While the city currently lacks a formal reserve policy, it maintains a debt-management policy that details how it could issue debt, as well as carrying-charge targets, excluding revenue-supported debt.

The city does not maintain a five-year, long-term financial plan. It, however, has worked with the state's financial restructuring board and public financial management firm to draft a three-year plan to improve finances.

Adequate budgetary performance

Albany's budgetary performance is adequate in our opinion. The city had operating surpluses of 1.7% of expenditures in the general fund and of 12.6% across all governmental funds in fiscal 2018. Our assessment accounts for the fact that we expect budgetary results could deteriorate somewhat from 2018 results in the near term.

Our analysis includes adjustments for recurring transfers out of the general fund and current expenses associated with pensions deferred under the state's contribution-stabilization program.

Fiscal 2018 closed with an operating surplus of about \$2.3 million in the general fund and a surplus of \$4.4 million in the debt reserve, supported by significant savings on health care costs and steady growth of sales tax revenues. The city receives 32.17% of the sales tax revenue share that the county shares with municipalities. In fiscal 2018, sales tax revenues rose by 6.2% to \$35.4 million or 20% of general fund revenue.

Although management recognizes the limitations of the tax burden, applied to less than half of all property in the city, officials have looked to set charges for services, such as increased garbage-collection fees, commensurate with the cost of providing the services. Albany continued to receive \$12 million in Capital City Funding from the state, which it had budgeted for but was not assured until state budget adoption. In past years, the state provides the funds, also known as spin-up funds, as an accelerated payment for the 19-A program, approved by the New York State Legislature, under which the state provides payments in lieu of taxes to the city for the use of the Empire State Plaza government complex. Over 2017-2019, the funds were provided as new revenue to the city and did not decrease future payments under 19-A. While we believe the risk exists of the city losing the additional Capital City Funding considering the state's own budget gap, we think this risk is limited and understand Albany is actively trying to make the funding permanent under 19A. We also understand city management has contingency plans should the additional funding fail to be approved by the state.

For fiscal 2019, we understand the city expects another surplus and addition to its fund balance. Positive sales tax trends continued, while the city remained able to generate health care cost savings. Moreover, the acquisition of street lights in 2018 generated the anticipated savings. Over the next couple of years, the city expects to save between \$1 million-\$1.5 million annually.

The fiscal 2020 adopted budget includes a 2.4% increase in operating expenditures from fiscal 2019 and a \$1.8 million appropriation from debt fund reserves. In addition, the city budgeted for \$12 million in Capital City Funding, \$16.6 million in other state aid, and \$15 million in 19A payments. Overall, state support accounts for approximately a quarter of the city's budget. Albany has reduced its reliance on landfill revenue by cutting budgeted landfill revenue in half compared with in fiscal 2015; we view this positively. This step will allow the landfill's life to be extended and keep costs down for the city. The fiscal 2020 budget also includes a 0.5% increase in the property tax levy, after the levy was kept flat in fiscal 2019. This is well below the 4.5% permissible increase considering the city's levy bank capacity. We believe this provides Albany with additional flexibility should future budgetary pressures emerge.

There's a risk of a one-off draw from fund balance for retroactive payments should the city settle its outstanding labor contracts with certain parts of the police force. Although the contracts have been outstanding since year-end 2013, we understand retroactive pay would only have to be made from 2017 onward. Therefore, we believe budgetary performance will likely remain adequate.

Weak budgetary flexibility

Albany's budgetary flexibility is weak, in our view, with an available fund balance in fiscal 2018 of 4.4% of operating expenditures, or \$7.6 million. Negatively affecting budgetary flexibility, in our view, is limited capacity to raise revenues due to consistent and ongoing political resistance.

Management expects another surplus and addition to fund balance in fiscal 2019. This marks a positive reversal from years of operating deficits, compounded by uncertainty related to state support from the 19-A program, requiring the

use of fund balance drawdowns, that led to an available fund balance of about negative 1% of operating expenditures in fiscal 2015. That said, we believe the city has a limited ability to raise revenue from property taxes, evidenced by the share of state-owned land within its jurisdiction and reliance on state support to balance the budget. We, therefore, believe Albany's budgetary flexibility will likely remain weak over our forecast horizon.

Adequate liquidity

In our opinion, Albany's liquidity is adequate, with total government available cash at 3.8% of total governmental fund expenditures and 40.9% of governmental debt service in 2018. In our view, the city has strong access to external liquidity if necessary.

In our opinion, the regular issuance of GO debt and bond anticipation notes evidences the city's strong market access. Although the state allows for what we view as permissive investments, the city holds its funds in deposit accounts, money-market funds and treasury bills, which we do not consider aggressive. Albany issued \$6 million in revenue anticipation notes in fiscal 2015, its first such issuance since 2009; it, however, has not issued revenue anticipation notes since 2015.

In fiscal 2018, cash levels weakened somewhat. However, we believe this change was caused by a lag in capital grants from the state. As mentioned before, if the police union were to receive significant retroactive pay, we believe it could put further pressure on Albany's liquidity levels.

Very weak debt and contingent liability profile

In our view, Albany's debt and contingent liability profile is very weak. Total governmental fund debt service is 9.3% of total governmental fund expenditures, and net direct debt is 60.0% of total governmental fund revenue. Negatively affecting our view of the city's debt profile is its significant medium-term debt plans. Approximately 71.0% of the direct debt is scheduled to be repaid within 10 years, which is in our view a positive credit factor.

Albany's total direct debt is approximately \$131 million. The city expects to issue up to \$80 million of additional debt, commensurate with its rolling five-year capital improvement plan, with nearly \$60 million in principal amortizing during the same period.

Pension and OPEB highlights

- We view pension and OPEB liabilities as a source of credit pressure for Albany, given that costs represent a large portion of the budget, combined with our expectation that they are likely to grow.
- Since 2011, Albany has chosen to defer pension expenses under the New York State Contribution Stabilization Program, a state-supported pension-smoothing program, which allows local governments to defer a portion of their expenses. The deferral amount outstanding as of 2019 is \$12.2 million and Albany must pay this amount in full to the plan by 2029.
- Although the city has some legal flexibility to alter OPEB, it may not be politically feasible. Furthermore, it is unable to prefund these costs, increasing the risk they could create budgetary pressure.
- Offsetting this risk somewhat is the minimal pressure expected from the city's pension liabilities, given strong plan funding status and limited escalating cost trajectory risk.

Albany participates in the following plans as of June 30, 2019:

- Police and Fire Retirement System: 96.93% funded, with a proportional share of the net pension liability equal to \$13.8 million.
- Employee Retirement System: 98.24% funded, with a proportional share of the net pension liability equal to \$3.6 million.
- A defined-benefit health care plan that provides retiree health care until death: 0% funded with an OPEB liability of about \$609.0 million as of Dec. 31, 2019.

Albany's combined required pension and actual OPEB contributions totaled 15.2% of total governmental fund expenditures in 2019. Of that amount, 7.5% represented required contributions to pension obligations, and 7.7% represented OPEB payments. The funded ratio of the largest pension plan is 96.9%. However, the plan's aggregate cost method essentially creates an open amortization policy using a level-percentage pay basis assuming a 3.8% payroll growth rate, which we generally view negatively because the plan will never reach full funding and costs will increase each year. Furthermore, the plan's discount rate of 7% could lead to some contribution volatility. However, its high funded status largely mitigates the risks of Albany's costs increasing significantly. The size of deferrals has also declined from a peak of \$6.0 million in 2013, to around \$460,000 in fiscal 2019.

Albany provides OPEB to its employees, which it funds on a pay-as-you-go basis. Its total OPEB liability was \$609.0 million as of December 31, 2019. The state does not permit OPEB liability prefunding. Given long-term medical cost trends, these obligations could become a source of budgetary pressure beyond our outlook horizon.

Strong institutional framework

The institutional framework score for New York cities, other than New York City, is strong.

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Ratings Detail (As Of March 9, 2020)		
Albany GO		
<i>Long Term Rating</i>	A+/Stable	Affirmed
Albany GO (serial) bnds		
<i>Long Term Rating</i>	A+/Stable	Affirmed
Albany GO (serial) bnds		
<i>Long Term Rating</i>	A+/Stable	Affirmed
Albany GO (AGM)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Albany GO (AGM)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Albany GO (BAM)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Albany GO (BAM)		
<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
Albany GO		
<i>Long Term Rating</i>	A+/Stable	Affirmed

Many issues are enhanced by bond insurance.

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