MOODY'S
INVESTORS SERVICE

New Issue: Moody's revises Pittsburgh PA's outlook to positive; affirms A1

Global Credit Research - 07 Aug 2014

Assigns A1 to $50M Ser. 2014 GO bonds; city has $580M GO debt outstanding

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

Moody's Rating

ISSUE	RATING
General Obligation Bonds, Series of 2014	A1
Sale Amount $50,000,000	
Expected Sale Date 08/15/14	
Rating Description General Obligation	

Moody's Outlook POS

Opinion

NEW YORK, August 07, 2014 --Moody's Investors Service has assigned an A1 rating to the City of Pittsburgh, PA's $50 million General Obligation Bonds, Series 2014. We have affirmed the A1 rating on approximately $530 million of outstanding general obligation debt. At this time, we have also revised the city's outlook to positive from stable.

Proceeds of the 2014 bonds will be used to fund part of the city's capital improvement program, including work on bridges, roads, urban redevelopment, and parks. The bonds are secured by the city's General Obligation unlimited tax pledge.

SUMMARY RATING RATIONALE

The A1 rating reflects the city's large and diverse tax base, with substantial contributions from universities, hospitals, and government institutions. The rating also incorporates the city's below-average socioeconomic profile, including a high poverty rate and weak resident income levels. Finally, the rating recognizes significant fixed costs from a heavy debt burden, large pension liabilities, and post-retirement health care, as well as sizeable capital needs relating to aging infrastructure.

The positive outlook reflects the steps the city has taken to reduce its long-term liabilities. The city's long-term plan seeks to control costs, reduce debt, and increase pension funding, all while maintaining operating stability and a healthy fund balance. As the city makes progress in this plan, its finances are likely to strengthen and its debt burden will decrease.

STRENGTHS:

Large, diverse tax base with significant institutional presence

Sensible long-term plan to reduce pension liabilities and debt

CHALLENGES:

Large legacy costs including debt service and pension and post-retirement healthcare benefits

Below-average socioeconomic profile

DETAILED CREDIT DISCUSSION

ACT 47 PLAN ADDRESSES LEGACY COSTS WHILE MAINTAINING HEALTHY RESERVES

The city's recovery plan is likely to result in a gradual reduction in unfunded long-term liabilities while maintaining healthy reserves.

The city entered the Act 47 program for distressed cities in 2003, and will remain in the program until at least 2018.

The latest 5-year plan, filed this year, utilizes a sharp drop in debt service beginning in 2018 as capacity to increase funding for pension and other post-employment benefits (OPEB) liabilities, as well as invest in the city's aging infrastructure.

The long-term projections assume that revenue trends will continue at the current pace, which we consider reasonable. A reversal of the recent economic expansion would depress tax revenues relative to current forecasts and disrupt the city's long-term plan, leading either to lower fund balance or weaker pension, OPEB, and capital funding than initially planned.

TAX BASE STRENGTHENING; INSTITUTIONAL PRESENCE PROVIDES STABILITY

After many decades of decline, the city's tax base has begun to stabilize. The presence of large healthcare and higher ed institutions, including the University of Pittsburgh Medical Center (rated Aa3 stable), the University of Pittsburgh (rated Aa1 stable), and Carnegie Mellon University, has bolstered employment opportunities and attracted businesses to the city. Other stable employers such as the US government, the Commonwealth of Pennsylvania (rated Aa3 stable), and members of the finance and technology industries help to round out the base.

Businesses are attracted to Pittsburgh because of its young, well-educated work force and low labor costs. The median family income of the city's residents as of the 2012 American Community Survey was 82% of the US median, which is below-average, but consistent with other medium-sized, formerly manufacturing cities.

Some pockets of the city remain weak. The poverty rate is high at 22.5%, and the median home value of $88,500 is far below the US median of $181,400. After a county-wide revaluation and a large wave of tax appeals, the latest estimate of the city's full value is $17 billion, which equates to a below-average $55,584 per capita. The $17 billion full value does not include the substantial presence of tax-exempt properties, which represent 39% of the base.

The city is likely to continue to grow. A number of redevelopment projects are under way, and developers have invested $5 billion in the city since 2006. After peaking at almost 700,000 people in 1950, the city's population has finally stabilized at about 300,000.

FINANCIAL POSITION HEALTHY; TAX REVENUES INCREASING

The city's expansion has bolstered tax revenues and helped lead to a stronger financial position. The city's $480 million budget is funded by a property tax levy (27% of revenues), a 1.25% resident earned income tax (17%), a 0.55% gross payroll tax (12%), and a 37.5% parking tax (11%).

With the exception of the property tax levy, most of the city's tax revenues have been climbing during the expansion. The income tax has grown every year for the past decade even during the recession, although the strengthening of collection procedures under Act 32 has likely driven part of this growth. The payroll tax has also grown in the past three years, the result of business expansion. Property tax receipts decreased 7% in 2013 as the city dropped its millage rate for a revaluation by Allegheny County (rated A1 stable).

The result of the positive tax trend has been an increasing fund balance. The city finished 2013 with a fund balance of $96 million, or 20% of revenues, up from as low as 10% of revenues in 2010. This improvement is net of higher funding for pensions and OPEB.

The city's financial trend will remain strong as long as the economy continues to expand. However, the growth in fund balance is unlikely to continue, as the city will probably devote future surpluses to pensions, OPEB, and capital.

HEAVY DEBT AND PENSION BURDENS

Pittsburgh's debt and pension burdens are heavy. The city's plan will reduce or fund them, but only gradually and over many years.

The city's debt portfolio consists of about $607 million of gross debt including $580 million of direct General Obligation bonds and $24 million property tax-backed tax increment financings. The debt is high at 3.6% of city-estimated full value and 1.26 times revenues. The main driver of the high debt burden is the city's issuance of pension obligation bonds (1/3 of debt burden) in the 1990s, as well as refundings to back-load debt service in the 2000s. The high debt relative to full value also reflects the fact that full value does not include the significant tax exempt portion. The city's debt amortizes quickly with 70% of principal scheduled to be repaid within 10 years.

The city administers three pension plans, with an aggregate unfunded liability of more than $1 billion. Under Moody's methodology for adjusting reported pension data, the city's adjusted net pension liability has averaged about 2.6% of full value and 0.9 times revenues over the past three years. The adjustments are not intended to replace the city's reported liability information, but to improve comparability with other rated entities.

The city has taken significant steps to improve its pension funding, including devoting $13 million a year of parking revenues to over-fund its required contribution. The city recently reduced its assumed rate of return and extended its mortality assumptions, leading to increased required contributions.

The city also has nearly $500 million of OPEB liabilities. Two years ago, the city began to contribute $2.5 million a year to an OPEB trust. Although the funding ratio is still very low, the step is proactive and reflects well on management.

WHAT COULD CHANGE THE RATING - UP:

Demonstrable progress in the long-term plan to reduce pension liabilities and debt

Sustained strengthening of the tax base

WHAT COULD CHANGE THE RATING - DOWN

Failure to make progress in the plan to reduce pension liabilities and debt

Failure to maintain adequate fund balance while executing the long-term plan

KEY STATISTICS:

Full value: $17 billion

Full value per capita: $55,584

Median family income: 82%

Fund balance as % of revenues: 19.8%

5-year dollar change in fund balance as % of revenues: +8.87%

Cash balance as % of revenues: 16.1%

5-year dollar change in cash balance as % of revenues: 6.8%

Institutional framework (PA cities): Aa

5-year average of operating revenues to operating expenditures: 1.00x

Debt to full value: 3.57%

Debt to revenues: 1.26x

Moody's adjusted three-year net pension liability to full value: 2.64%

Moody's adjusted three-year net pension liability to operating revenues: 0.93x

The principal methodology used in this rating was US Local Government General Obligation Debt published in January 2014. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

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