



The Research Bureau

A Bright Spot Amidst Clouds of Doom and Gloom

It would be an understatement to say that the nation's economy has not been doing well over the last few months. But despite the problems, millions of individuals, businesses, governments, and nonprofit organizations continue to live within their means, invest wisely, and manage their resources well. For individuals, their financial acumen and discipline are reflected in their credit ratings; and for businesses and governments, the measurement is their bond rating.

In September 2008, the City of Worcester received good news. Standard and Poor's upgraded the City's bond rating from "A-/Negative" to "A-/stable," Moody's and Fitch affirmed their previous A3 and A ratings, respectively, but both of them noted improvements the City has made in its finances during the past year.

A municipality's bond rating is important for several reasons. First, the rating offers a rough measurement of the city's overall economic, operational, and financial strength. Second, it has a direct impact on the cost of borrowing money to finance capital improvement projects. The money saved from having a high bond rating can be substantial depending on how many bonds a community issues. For instance, if two communities were to request a bond sale of \$90 million to construct a new high school, and one community received an Aaa rating and another a Baa rating, the difference in debt paid could amount to \$200,000 annually, or \$4 million over the life of a 20-year bond. Therefore, a decline in a city's bond rating compels taxpayers to pay more to finance the projects undertaken by the municipality.

Rating agencies consider several factors when determining municipal bond ratings. The factors cited most often in bond rating reports include: the strength of the local economy, current and future-year municipal finances, local management policies and practices, and manageability of debt levels. Changes in any of these areas can affect Worcester's rating. The City's twenty-five year history of sound financial management, due, in no small measure, to effective leadership in the budgeting, auditing, treasury and assessing departments, has had a positive impact on the City's bond rating. City Manager O'Brien has been able to save millions of dollars to maintain services by redesigning municipal employee premium payments and co-payments for health insurance to more closely approximate those typically found in the private sector. He has also instituted a five-point plan to stabilize the City's financial situation. The rating agencies have been and will continue to be particularly interested in Worcester's adherence to its first-ever *Five-Point Financial Plan*, adopted by the City Council on November 24, 2006, and effective July 1, 2007. Fitch has recently reiterated its approval of the plan as follows: "A key rating driver is Worcester's adherence to its Five-Point Plan for improving reserve levels."

Moody's and Standard & Poor's also indicated that the City's commitment to The plan will stabilize its financial situation.

Worcester's Five-Point Financial Plan
(1) Five-year forecasting and long-term planning of City finances and projects
(2) Strengthening of reserves, including creation of Bond Rating Stabilization Fund
(3) Quarterly financial reporting
(4) \$16.85 million cap on borrowing (can be adjusted for inflation)
(5) Capital Improvement Plan to achieve debt service stability in budget

In anticipation of reductions in local aid from the Commonwealth in FY10 because of decreasing corporate income tax and capital gains tax revenues, the City Manager has proposed further changes in the City's payment to municipal employee health insurance premiums. He is recommending that employees pay 25%, while the City pays 75% of any plan, a split which is common in the private sector. (In fact, many private-sector employers pay 75% of the lowest-cost plan only.) The City Manager would use the savings, which would amount to some \$9 million in FY10 if the City also joins the state's General Insurance Commission [GIC], the plan for all state employees, to help maintain the City's core services of public safety, public education, and public infrastructure, at their current levels without substantial increases in property taxes. Such planning is an essential part of the City's five-point financial plan and integrally linked to maintaining or improving the City's bond rating. The City Council should adopt the Manager's recommendations.

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