FitchRatings

RATING ACTION COMMENTARY

Fitch Rates New York City TFA's $629 Million Building Aid Revs 'AA'; Outlook Stable

Fri 15 Jul, 2022 - 2:50 PM ET

Fitch Ratings - New York - 15 Jul 2022: Fitch Ratings has assigned 'AA' ratings to approximately $629 million in New York City Transitional Finance Authority (TFA) building aid revenue bonds, fiscal 2023 series S-1, consisting of:

--$557,285,000 subseries S-1A tax-exempt bonds;

--$71,230,000 subseries S-1B taxable bonds.

The bonds are scheduled to price the week of July 18, 2022, with series S-1A selling by negotiated sale and series S-1B selling by competitive sale.

The Rating Outlook is Stable.

The issuance of the fiscal 2023 series S-1 bonds does not affect the 'AAA' rating on the TFA's future tax secured bonds.

SECURITY

The bonds are payable from annual New York State appropriations of building aid to New York City (the city), assigned and paid to TFA.

ANALYTICAL CONCLUSION

The 'AA' rating, one notch below the state's 'AA+' Issuer Default Rating (IDR), reflects the inherent optionality of state-appropriated school building aid used for debt service and structural protections for bondholders that limit leverage and fund debt service several months in advance.

KEY RATING DRIVERS

LINK TO NEW YORK STATE CREDIT: School building aid that secures the bonds requires annual state legislative appropriation. Therefore, the rating is linked to the State of New York's credit quality, reflected by its 'AA+' Issuer Default Rating (IDR). Appropriation risk is minimal given the constitutional mandate for, and strong history of, state support for education.

STRUCTURAL PROTECTIONS STRENGTHEN CREDIT: The additional bonds test (ABT) only considers aid associated with projects that have already been approved even though aid related to additional projects that will be approved by the state in the future is also pledged to the bonds. Monies for debt service are retained in the city fiscal year prior to the year in which the debt service is due.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--An upgrade of the state's IDR.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A downgrade of the state's IDR.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

CREDIT PROFILE

Building aid revenue bonds, which are rated one notch below New York State's 'AA+' IDR, are payable from annual state appropriations of building aid. State building aid assists local school districts across the state with the cost of constructing and improving elementary and secondary education facilities. Appropriation risk is minimal given the constitutional mandate for, and strong history of, state support for education. Moreover, the ABT only considers aid associated with projects already approved by the state, even though aid related to additional projects that will be approved in the future is also pledged.

BONDS SUPPORTED BY APPROVED AND FUTURE BUILDING AID

In the 2006 state legislative session, the New York City TFA was authorized to have outstanding an amount up to $9.4 billion for education, supported by state building aid appropriations; almost $8.2 billion is currently outstanding prior to the 2023 series S-1 sale. As permitted by the legislation, the city assigned all of its state building aid to the TFA to secure the bonds.

State building aid, which is earned on an individual project basis, consists of confirmed building aid and incremental building aid. Confirmed building aid refers to aid payable for projects already approved by the state. Such aid is subject to annual state appropriation but is not subject to any additional statutory or administrative conditions or approvals. The state has covenanted that the calculation of reimbursable costs for a project will not change once the project is approved.

For subsequent projects, the base reimbursement rate can change over time pursuant to a statewide formula calculated every year. This ratio has shifted gradually downward, and is projected at 38.2% in fiscal 2023; it stood closer to 50% a decade ago.

Incremental building aid refers to state building aid to be received for projects approved by the state in the future. Fitch expects that the incremental building aid generated by the city's ongoing education capital program will result in higher actual coverage in the out years.

By statute, both confirmed and incremental building aid are the property of the TFA and are pledged to the bonds. However, the ABT considers only confirmed building aid. In order for additional bonds to be issued, confirmed building aid payable in the fiscal year preceding each year in which bonds are scheduled to be outstanding must be at least 1x debt service in that year. Since state building aid for a given project is provided over 30 years, debt service coverage by confirmed building aid drops from about 2.21x in fiscal 2023 to 1.4x in fiscal 2035, before increasing to nearly 18x in fiscal 2050.

The TFA receives all building aid regardless of whether the project is financed with TFA building aid revenue bonds or through a different financing mechanism.

FLOW OF FUNDS

State building aid received by TFA is retained for debt service each year when the amount of building aid outstanding before the end of the city's fiscal year is not more than 110% of the debt service payable on the building aid revenue bonds in the following city fiscal year. Although the state's fiscal year runs from April-March, the state budgets education aid, which includes building aid, based on the city's fiscal/school year (July-June). The retention mechanism is likely to trap building aid in the April through June period for debt service payments in the following July and January. Building aid that is not required to be retained flows to the city.

The level and timing of state education aid, of which building aid is a part, has periodically been affected by the state's fiscal condition. In the Great Recession, education aid paid to the city declined and education aid payments were deferred, although the portion attributable to building aid continued to increase.

Early in the coronavirus pandemic, capital projects were suspended and the enacted budget for state fiscal 2021 allowed up to 20% recurring local aid reductions, including education aid, subject to approval of additional federal aid. The state ultimately delayed approximately $129 million in education aid, which was later paid. More recently, strong state fiscal performance is allowing for additional support for education; fiscal 2023 school aid in the enacted budget rises 7.2%, to $31.4 billion.

SUBORDINATION TO PRE-2007 TFA FUTURE TAX SECURED BONDS

Pursuant to the TFA indenture, since building aid is TFA revenue it must be available first to TFA future tax secured bonds (rated AAA/Stable) issued prior to the first issuance of building aid revenue bonds in fiscal 2007. Given the very strong coverage that the pledged personal income and sales tax revenues provide for future tax secured bonds, it is very unlikely that building aid would ever be needed for this purpose.

Only $75.4 million in TFA future tax secured debt remains outstanding from before the first issuance of building aid revenue bonds. TFA future tax secured bonds sold after the date of the initial issuance of the building aid bonds, of which $43.6 billion are currently outstanding, have no claim on building aid.

In addition to previously outstanding TFA future tax secured bonds, the payment of building aid is also subject and subordinate to certain other limited prior statutory and state constitutional claims on education aid, of which building aid is a part. Fitch does not believe that these will impair the ability to pay debt service.

Holders of the TFA building aid revenue bonds benefit from statutory covenants in the original TFA Act prohibiting action that would impair bondholders and the bankruptcy-remote nature of the issuer. However, since the pledged revenue stream requires annual state appropriation, the bondholders do not enjoy the same insulation from government operations that is a key factor in the 'AAA' rating of the TFA future tax secured bonds.

DATE OF RELEVANT COMMITTEE

07 July 2022

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS

CREDIT QUALITY OF NEW YORK STATE

The 'AA+' IDR reflects New York State's very strong gap-closing ability and responsive budget management that leave it well-positioned to address near-term fiscal challenges, including from inherent revenue cyclicality and expanding commitments for schools and Medicaid. New York's low long-term liability burden suggests significant capacity to address capital spending pressures, including for the Metropolitan Transportation Authority (MTA).

For more information on the state's 'AA+' IDR, see 'Fitch Assigns 'AA+' Rating to $2.2B NYSTA PIT Rev Bonds, Affirms New York 'AA+' IDR; Outlook Stable' (July 8, 2022). For more information on the TFA future tax secured bonds, see 'Fitch Rates NYC Transitional Finance Authority's $1.04 Billion Bonds 'AAA'; Outlook Stable' (March 4, 2022).

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
New York, State of (NY) [General Government]				
New York, State of (NY) /State Building Aid Appropriation Revenues/1 LT	LT	AA Rating Outlook Stable	Affirmed	AA Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

U.S. Public Finance Tax-Supported Rating Criteria (pub. 04 May 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

ADDITIONAL DISCLOSURES

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

New York City Transitional Finance Authority (NY)	EU Endorsed, UK Endorsed

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