THE COMMONWEALTH OF MASSACHUSETTS
EXECUTIVE OFFICE FOR
ADMINISTRATION AND FINANCE

STATE HOUSE ▪ ROOM 373 BOSTON, MA 02133

Wednesday, December 4, 2024
11:00 a.m.

In accordance with Section 20 of Chapter 20 of the Acts of 2021, as extended by Chapter 107 of the Acts of 2022, this meeting will be conducted, and open to the public, via Zoom and Teleconference.
Zoom URL: https://us02web.zoom.us/j/88341180123?pwd=3hWx0EmPojQ4ZUBAo840r4zck8Auk4.1
Meeting ID: 883 4118 0123; **Passcode**: 472047
Teleconference line: 1-646-558-8656; **Passcode**: 472047#

Minutes:
The meeting was called to order at 11:04 am

Board members comprising a quorum:

Kaitlyn Connors, Chair, Executive Office for Administration & Finance
Martin Benison, Appointee of the Treasurer
Pauline Lieu, Office of the Comptroller
Susan Perez, Office of the Treasurer and Receiver-General
Michelle Scott, Massachusetts Department of Transportation
Catherine Walsh, Appointee of the Governor

Others in attendance:
Christopher Czepiel, Senate Committee on Ways & Means
Sydney Steinberg, Office of Senator Ed Kennedy
Aidan Bettencourt, Office of State Representative Michael Finn
Michael LaFlamme, Office of State Representative Michael Finn
Josh Tavares, Office of Senator Ryan Fattman
Cory Bannon, Office of the Treasurer and Receiver-General
Christina Marin, Office of the Treasurer and Receiver-General
Timur Kaya Yontar, Executive Office for Administration and Finance
Colin Young, State House News Service

Minutes:

Ms. Connors called the meeting to order and conducted the roll to establish quorum. She then moved to the first item of business which was approval of the minutes from the November 22, 2024 committee meeting. Upon a motion made by Mr. Benison, and duly seconded, the minutes were approved unanimously.

Ms. Connors then moved on to the next item on the agenda: DAC Modeling. She first reviewed the upcoming DAC schedule and reiterated that the work of the Committee would largely be focused on modeling going forward. She noted that the next meeting is scheduled for the coming Friday, Dec 6th at 1pm.

She then went over the topics for today's meeting, noting that today's discussion would largely be a continuation of discussions from the prior committee meeting, mostly related to features of the model. She noted in the prior meeting not all Committee members were present and this meeting provides an opportunity for the full Committee to discuss questions, concerns, and considerations that have come up over the course of the Committee's work.

Ms. Connors then reviewed the modeling inputs. She referenced the fact that the Committee had been working with financial advisors to revamp the DAC model – used to model debt projections under various economic scenarios. She provided a recap of the new features, noting that one of the most significant changes to the model related to the refinement of how future debt was projected and the increased flexibility to align debt structuring within the model to current trends, including the addition of a premium feature. Premium, she reported, was one of the topics that was discussed at the prior meeting where a number of questions came up. She then turned the presentation over to Ms. Perez.

Ms. Perez walked the Committee through historical trends related to premium. She explained that the amount of bond premium received is determined by the difference between the coupon rate on the bonds offered and the AAA Municipal Market Data (MMD) curve; as AAA MMD rises and bond premium will be reduced. She noted that in Oct 2023 MMD spiked, which explains why the premium in Oct of 2023 was low relative to transactions done over the past two years. She also reenforced the notion that premium can shift depending on market conditions.

Ms. Connors pointed out that the committee would model out various debt scenarios, including scenarios that assumed premiums. She asked Ms. Perez whether it made sense to discuss potential premium scenarios now. Ms. Perez noted that for budgeting purposes she is currently assuming a 10% premium but is working with Commonwealth financial advisors on the best approach for forecasting MMD, noting there is a relationship between treasuries and MMD that might be able to provide insight that could help inform near-term premium assumptions.

Mr. Benison asked if there was any reason to expect a discount (vs. a premium) in the future, stating he recalled that many years ago Commonwealth bond transactions would sometimes have a discount (i.e. actual bond proceeds received are less than the face value of the bonds).

Ms. Perez acknowledged that her predecessor would sell par bonds that would have a discount. She noted that the decision to do so is a choice. She pointed out that there is a trade-off between premium and debt service, in addition to receiving bond optionality, which enables the Commonwealth to refund bonds for savings. Ms. Perez noted that the Treasurer's Office watches the coupons to make sure optionality and premium is preserved. She also said it pays attention to market liquidity in terms of how bonds sell and trade on the secondary market. She also referenced the fact that as rates go up, the premium decreases, but you could increase the premium if you chose to increase the coupon, although that would result in higher interest rates.

Mr. Benison commented that it sounds like the approach is more of a strategic decision.

Ms. Perez agreed that some of it is strategy. She noted that the Treasurer's Office is always trying to get the best overall price and outcome given market conditions. She noted that in some cases it makes sense to lower the coupon. She also mentioned that refunding opportunities are something her office pays very close attention to, but she cautioned that the savings from refundings are realized over the remaining life of the bonds.

Ms. Connors reported that the concept of refundings had been discussed in conversations related to modeling in general and the model refresh but ultimately the model does not factor in potential refunding opportunities, as they are hard to predict. Excluding them is the more conservative approach. Ms. Perez agreed.

Mr. Yontar asked for clarification around his understanding of premium which he summarized as the cash above the bond par amount. Ms. Perez confirmed that was accurate.

Ms. Connors noted that the direct debt limit is based on the par value of the bonds, so the premium does not count towards the limit. Ms. Connors recognized that premium, being a newly added model feature, is a concept that the Committee had not discussed until this year.

Mr. Benison asked whether the Committee's formal recommendation included premium. Ms. Perez responded that the formal recommendation relates to the bond cap – which is the budget for capital spending (which is supported by bond proceeds), so the recommendation is tied to the spending, not the par.

Mr. Benison stated he is supportive of this new way of looking at and forecasting the direct debt limit and would like the Committee to apply a consistent approach to how it analyzes direct debt, presumably similar to the approach the committee takes to the debt service policy limits. He asked if there was a formal policy that had been used with respect to long term direct debt projections. Ms. Connors replied that while the debt limit was always factored into the Committee's analysis, targets around the direct debt limit have not been formalized.

Ms. Connors then provided a recap of the input assumptions for revenue growth and interest rates that had been discussed last week, noting that the proposed recommendation is to use the prior years' approach. For revenue growth that means maintaining the CAGR approach and excluding Fair Share surtax revenue from calculation, which is the conservative approach. For interest rates, Moody's analytics would be used. She noted that Moody's projections have not been updated since the presidential election.
Ms. Perez noted that the Committee's recommendation letter should be clear on the assumptions used, including premium and Fair Share assumptions. She also noted that the letter should clearly note that the Committee's analytics do not factor in any future federal policy shifts that could have market and economic impacts. Ms. Perez stated she believed DOR and other economists are not factoring in potential policy shifts into their analytics.

Ms. Scott asked whether Moody's would have updated projections, Ms. Connors stated that Moody's projections had not been updated since the election and that DOR did not expect to have updated projections before mid-December.

Ms. Scott agreed that it makes sense to exclude the surtax revenue, and asked how special obligation bonds would factor into revenue growth. Ms. Connors replied that special obligation bonds do not impact revenue assumptions, but that the debt service on the special obligation bonds is included when evaluating debt services as a percentage of tax revenue. Ms. Connors noted that special obligation bonds are not part of the direct debt limit calculation.

Ms. Perez asked how the model applies interest rates (on par or proceeds). Given the relationship between premium and rates, Ms. Perez said it was important to understand how the model worked to ensure that it was not overstating the premium benefit. Ms. Connors said she would confirm.

Ms. Lieu asked for clarification on the direct debt calculation with respect to Special Obligation bonds to make sure she heard correctly. Ms. Connors confirmed that Special Obligation debt was not part of the direct debt limit.

Ms. Connors then provided a recap of preliminary results from various illustrative scenarios at max bond cap growth (+$125M annual growth). She noted the early modeling suggested debt service as a percentage of revenues was within affordability limits, and that the direct debt limit is the more constraining factor to consider for this year's recommendation, as modeling showed the debt limit could be reached somewhere around 2029 or 2030 under the max growth scenario. However, she mentioned the model was in the process of being further refined to better align with actual bond issuances timing and that will likely decrease some pressure on the debt limit.

Ms. Perez emphasized that the model updates were necessary to better align model projections with actual bond issuance timing and were not being made to produce more favorable results. She explained that the nature of capital spending coupled with the fact that the Commonwealth issues bonds in arrears results in bond issuances for capital spending spanning 2 fiscal years – for example the last bond issuance to support fiscal 2024 capital spending occurred in early fiscal 2025.

Ms. Connors noted that the meeting was at time and wrapped up the meeting by discussing next steps, which included running additional modelling scenarios with the new model, and starting to draft the final recommendation letter. She reminded the Committee that the next meeting was this Friday.

Ms. Scott moved a motion to adjourn the meeting, which was seconded by Ms. Walsh. The meeting was adjourned at 12:02 pm.