



Bond Rating Analysis:

Rating & Outlook Changes For Chicago GO Bonds

November 28, 2022

The City Council Office of Financial Analysis (COFA) has prepared the following summary and analysis in regard to recent rating and outlook adjustments made relating to the City of Chicago's General Obligation (GO) bonds. COFA analyzes the actions of the four major rating agencies—Moody's, Standard & Poors, Fitch Ratings, and Kroll—for the City's General Obligation Bonds.

Summary of Rating and Outlook Changes

	Fitch	Moody's	S&P	Kroll
Rating	BBB (upgrade)	Baa3 (upgrade)	BBB+*	A*
Outlook	Positive	Stable*	Positive	Positive

As of 11/28/2022

* No change from last update.

Fitch Ratings

On October 21, 2022, Fitch Ratings upgraded the City of Chicago's GO bonds rating from BBB- to BBB, a one-notch increase.¹ This is the first rating update assigned by Fitch since March 2016 when the agency downgraded the City's GO bonds rating to BBB- from BBB+. Additionally, Fitch revised the City's rating outlook from 'Stable' to 'Positive.'

Fitch notes that the rating and outlook adjustment “reflects Chicago's improving pension funding practices, its commitment to maintaining a sound reserve position, and ability to institute structural budget measures that improve its capacity to respond to future cyclical challenges.” The agency views the City's advanced payment towards pensions liabilities, an improved budgetary outlook, and a continued strong recovery from the pandemic as positive signals for Chicago. Looking ahead, Fitch believes that Chicago's ability to find recurring fiscal solutions to ensure a structurally balanced budget in outyears will be critical to the City's future rating outcomes. If the City is unable to find solutions and relies on non-structural fiscal measures, depletes its reserves, or fails to fund the full statutory pension contribution, Fitch underscores how this could lead to negative ratings or downgrades in the future.



City of Chicago
Council Office of Financial Analysis
Kenneth P. Williams, Sr., Chief Administrative Officer

2 N. LaSalle St, Ste M550
Chicago, IL 60602
cofa@cityofchicago.org

Moody's

On November 8, 2022, Moody's upgraded the City of Chicago's GO bonds rating from Ba1 to Baa3, an important one-notch increase.² This is the first rating update assigned by Moody's since May 2015 when Moody's downgraded the City's GO bonds rating from Baa2 to Ba1, a two-notch decrease at the time. Moody's affirmed the City's rating outlook as 'Stable.'

This is a significant upgrade from Moody's for the City because the newly assigned Baa3 rating removes the speculative grade—or 'junk status'—tag tied to the City's GO bonds. Similar to Fitch, Moody's notes that the rating upgrade and affirmed "Stable" outlook is the result of "the city's substantial increase in pension contributions" and "improved budgetary management through a willingness and ability to increase revenue that reduced a structural deficit and facilitated the elimination of debt-based budget maneuvers and pension cost deferrals." A concern from Moody's is City's leverage and fixed costs that will most likely remain fairly high for many years, a result of pension obligations and a large, unionized workforce.

Standard & Poors

On November 10, 2022, S&P affirmed the City of Chicago's GO bonds rating of BBB+, an assigned rating which has not changed since July 2015.³ Additionally, S&P revised the City's rating outlook from 'Stable' to 'Positive.'

S&P notes that "Chicago made significant strides to achieve financial stability and executed transformative changes that built on the successes of the previous decade." The agency views the City's commitment to honoring its recent revised debt and pension policy, which was unveiled in the 2023 budget, as a positive sign for Chicago going forward. S&P stated that the reason why Chicago's credit rating is currently below the single-A ratings—which the City has not been assigned by S&P since 2015—because of "the ongoing structural imbalance on pension contributions." If Chicago can address its pension liability ratios, S&P believes the City will achieve an upgrade. S&P places a cap on ratings when "the borrower lacks a plan to address" long-standing structural budget imbalances.

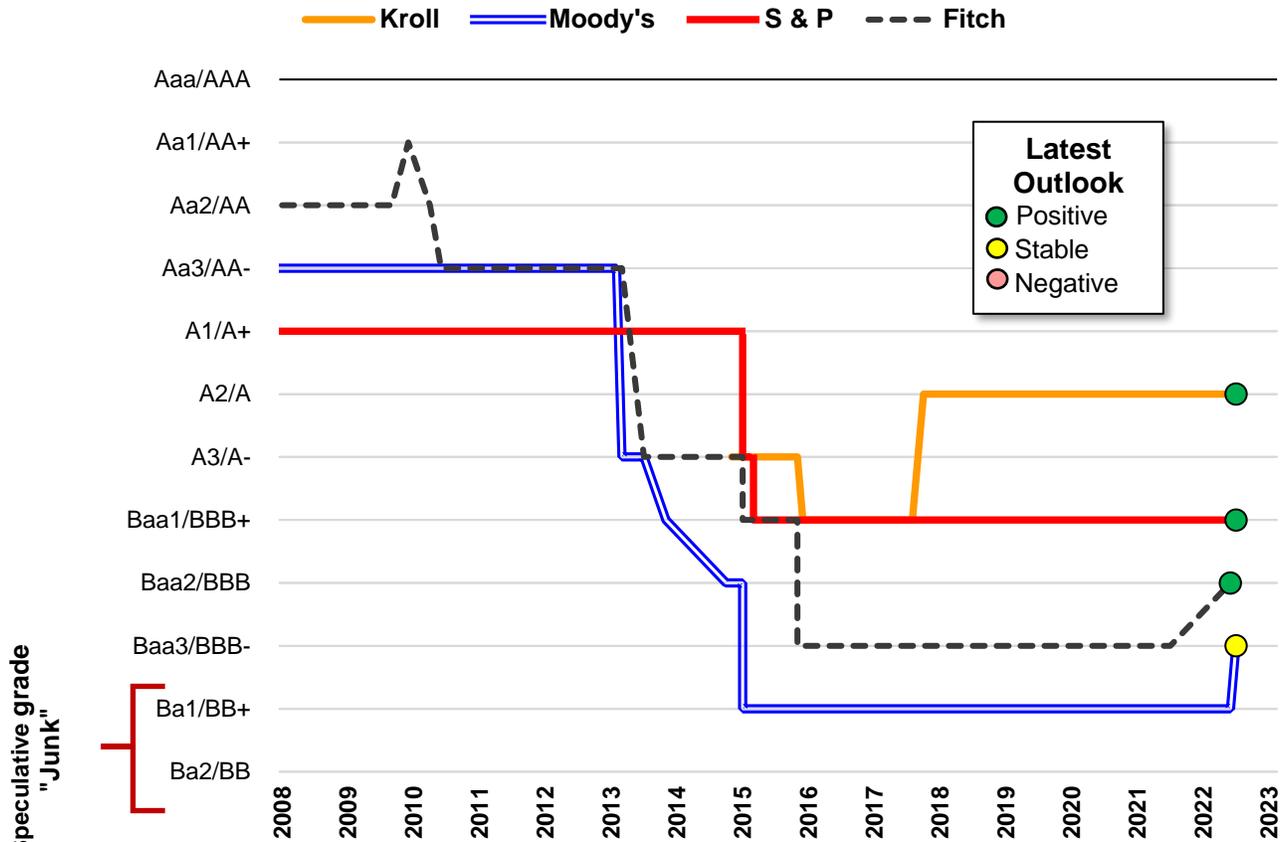
Kroll Bond Rating Agency

On November 10, 2022, Kroll affirmed their A rating for the City of Chicago's GO bonds, an assigned rating which has not changed since February 2018.⁴ Additionally, Kroll revised the City's rating outlook from 'Stable' to 'Positive.'

Kroll notes that the rating and outlook adjustment reflects the City's ability to reduce its "reliance on non-recurring revenues, and strengthened budgeting, forecasting and operational policies." Kroll views the City's need to "identify significant long-term funding sources" to fund pension obligations, as well as a "reliance on economically sensitive revenue sources to fund operations" as credit challenges for Chicago.

Below is a COFA chart displaying how the ratings have changed over time, dating back to 2008. The chart also shows the latest "outlook" assigned by each of the major agencies for the City's GO Bonds.

City of Chicago - General Obligation Bond Rating History



SOURCE: Fitch Ratings; Kroll Bond Rating Agency; Moody's Corporation; S&P Global Ratings
 NOTES: S&P and Kroll gave Chicago's GO Bonds an outlook of **Positive** in their latest issued reports. Fitch also gave Chicago's GO Bonds an outlook of *Positive* in their latest report, while Moody's gave an outlook of *Stable*.
 Ratings and outlooks as of November 14, 2022.

Implications

The recent rating actions by the four agencies is objectively good for the City of Chicago. A throughline in the recent rating and outlook adjustments COFA would like to highlight was the City's decision to make an advanced payment towards future pension obligations. The agencies view the City's decision to address future pension obligations as crucial to the City's long-term financial health and rating upgrades. Continuing to pay down pension obligations and lower the liability funded ratio may lead to positive outlooks and rating upgrades in the future.

The ratings assigned to the City's GO bonds impact significantly impact the interest rates, the pricing of bonds, and desire from potential investors. Ultimately, the ratings impact taxpayers

because, for example, lower interest rates will equate to freeing-up dollars to fund other City operations, programs, and initiatives, as the City will need less funds to pay for large projects. As a result, COFA believes that the City should continue to explore recurring revenue sources to stabilize the long-term structural budget imbalances and pension obligations.

Endnotes:

¹ Fitch Ratings. *Fitch Upgrades Chicago, IL's GO Bonds to "BBB" and Rates \$757MM GO Bonds "BBB"; Outlook Positive.* (2022, October 21). www.fitchratings.com

² Moody's. (2022, November 8). *Moody's upgrades Chicago, IL issuer rating & GO rating to Baa3; outlook is stable.* www.moodys.com

³ Shields, Y. (2022, November 11). *Pair of positive outlooks brings Chicago more uplifting rating news.* www.bondbuyer.com

⁴ Kroll Bond Rating Agency. (2022, November 10). *KBRA Assigns Long-Term Rating of A to the City of Chicago General Obligation Bonds Series 2023A; Outlook Positive* [Press release]. www.kbra.com