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Summary:

San Francisco Municipal Transportation Agency, California; Transit

Primary Credit Analyst:

Mary Ellen E Wriedt, San Francisco (1) 415-371-5027; maryellen.wriedt@standardandpoors.com

Secondary Contact:

Paul J Dyson, San Francisco (1) 415-371-5079; paul.dyson@standardandpoors.com

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Summary:

San Francisco Municipal Transportation Agency, California; Transit

Credit Profile

San Francisco Municipal Transportation Agency rev rfdg bnds

Long Term Rating

AA/Stable

Affirmed

San Francisco Municipal Transportation Agency ICR

Long Term Rating

AA/Stable

Affirmed

Rationale

Standard & Poor's Ratings Services affirmed its 'AA' long-term rating on the San Francisco Municipal Transportation Agency (SFMTA), Calif.'s revenue bonds outstanding. Also, Standard & Poor's affirmed its stand-alone credit profile (SACP) of 'aa' and its 'AA' issuer credit rating (ICR) on the agency. The outlook on all ratings, where applicable, is stable.

The 'AA' rating is currently the highest rating on revenue bonds or certificates of participation issued by a transit agency in the U.S. The strength of the local market and strong management practices and policies when combined with both the parking and transit revenues of the SFMTA's operations result in an extremely strong enterprise risk profile and a very strong financial risk profile.

The ratings reflect our view of the SFMTA's:

- Very low industry risk, with low cyclical volatility of earnings during economic cycles, and very low competition;
- Extremely strong economic fundamentals, with extremely strong per capita income and no significant employment concentration;
- Very strong management and governance policies and practices, with very strong financial policies;
- Strong debt service coverage (DSC) and liquidity; and
- Low debt burden.

Partly offsetting the above strengths, in our view, are the SFMTA's relatively large, \$3.3 billion capital improvement plan that calls for a planned \$150 million in additional parity debt, which will increase system leverage and reduce DSC, and relatively mild ridership growth from 2008 to 2014. Securing the bonds is a gross revenues pledge of certain revenues before the payment of SFMTA expenses. The pledged revenues include passenger fares; traffic fines, fees, permits, and taxi medallion fees; parking meter revenues and parking citations; parking garage and surface parking lot revenues; the half-cent sales tax on the Bay Bridge (Assembly Bill 1107); and the Transportation Development Act sales tax. The transfers from the general fund, including the baseline and the parking taxes, are not pledged to the bonds. All pledged revenues are set aside, deposited into the SFMTA enterprise account, and then transferred to the trustee for the debt service fund. The bonds are additionally secured by fully funded, stand-alone debt service reserves.

The SFMTA is an enterprise department of the City and County of San Francisco (the city). The agency was created in 1999, consolidating the San Francisco Municipal Railway (MUNI, the transit provider for the City of San Francisco) and the Department of Parking & Traffic. The SFMTA is a comprehensive transportation agency, responsible for transit, parking meters, parking garages and lots, traffic, taxi regulation, accessible services, bicycles, and pedestrian accessibility programs.

Throughout the city, the agency manages 19 public parking garages and 19 surface parking lots (totaling 15,000 off-street parking spaces), and approximately 25,000 single-space parking meters and 470 multispace pay stations covering approximately 3,200 spaces (28,000 total on-street metered and off-street surface lot spaces) throughout the city. Management has indicated that the garage facilities require significant rehabilitation and equipment upgrades. This extensive parking system has a solid competitive position, in our opinion. The facilities have high utilization rates during peak hours. The agency owns and manages 30% of all downtown and 15% of all citywide spaces in garages and lots. The agency also issues parking citations and enforces parking regulations.

We believe that the SFMTA provides an essential service to the city and operates as a virtual monopoly. It serves a 49-square-mile service area composed of San Francisco. The agency is the eighth-largest transit operator in the country and the largest in the region. MUNI carries almost 45% of all transit passengers in the Bay Area, approximately twice the number of passengers of the second-largest transit operator in the area (Bay Area Rapid Transit). MUNI's infrastructure includes cable cars, light-rail trains, and buses, covering approximately 80 routes throughout San Francisco, and there is a transit stop within a quarter mile of everyone who lives in, works in, and visits the city.

The SFMTA's transit system, and, more generally, the mass transit industry as a whole, is mature and has historically demonstrated only minor cyclicity (including ridership trends), and therefore we characterize the cyclicity and volatility of operating earnings as low risk. We also characterize competition and the threat of substitute products or services as very low risk. Barriers to entry are very high given the size of the system and its large infrastructure. Given the above, we characterize the SFMTA's industry risk as very low.

In our view, the underlying strength of SFMTA's catchment area -- with steady population and employment growth and high wealth levels -- help provide stable demand for transit services. Gross population growth for San Francisco from 2009 to 2014 was 7%, and employment growth over the same period was 17%. Projections from Global Insight indicate population and employment growth will continue. San Francisco's per capita income level is 193% of the national average. We consider SFMTA's economic fundamentals as extremely strong.

SFMTA's ridership has been relatively stable, despite fare increases, service reductions, and the economic recession. According to management, passengers totaled 233 million in fiscal 2015, up from 216 million in fiscal 2010. (Data from automatic counters indicated lower ridership, but management believes these data are not accurate.) During the five-year period of fiscal 2010 to fiscal 2015, gross ridership growth was 7.7%. We consider SFMTA's market position as extremely strong, with growth in ridership and SFMTA's status as a virtual monopoly for public transit in San Francisco. We consider the SFMTA's market position as very strong, as some historical ridership fluctuations are mitigated by the SFMTA's status as a virtual monopoly for public transit in San Francisco.

Voters in San Francisco approved two ballot measures in November 2014: Proposition A authorizing the city to issue up to \$500 million in general obligation bonds to finance various transportation projects and Proposition B amending the city's charter to adjust the required annual appropriation from the general fund to the transportation fund to reflect population growth. We consider this support to be a credit strength.

In terms of management and governance, the SFMTA has detailed strategic initiatives and examples of market leadership and innovation, including technology improvements providing real-time information to users. The SFMTA uses several key performance indicators typical to the industry, and management has demonstrated a strong track record of meeting benchmarks while addressing operating risks. We view senior management as experienced and broad, and the SFMTA's board of directors' experience in the fields of government, finance, labor relations, and public transportation provides strategic direction. Given these key factors, we view the SFMTA's management and governance as very strong.

In summary, our analysis of the four factors that constitute the SFMTA's enterprise risk profile results in an enterprise risk profile score of extremely strong.

The SFMTA maintains prudent financial policies when it comes to transparency and disclosure, liquidity, long-term financial planning, and debt management. The SFMTA produces and publishes monthly operational and financial reports, and financial audits are clean. The SFMTA has formal reserve and liquidity policies to maintain financial stability and ensure adequate funds to cover various risks of losses. Debt is managed consistent with the SFMTA's debt policy, and the agency maintains a five-year detailed capital plan that identifies sources and uses of funding. The SFMTA has covenanted to adopt a two-year balanced budget in accordance with the city charter. In addition, the SFMTA has covenanted that it will maintain pledged revenues in each fiscal year equal to or greater than the total of annual debt service, operating costs of the transit system, and any subordinate obligations. Management has also covenanted to the continued operation and maintenance of the transit system. Given these key factors, we view the SFMTA's financial policies as strong.

The SFMTA receives funds from a diverse set of sources. The bulk of total revenues comes from operations, including parking/traffic (25% in fiscal 2015) and passenger fares (21%); in our opinion, this combined percentage represents a significant portion of revenue, or almost 50%, over which the agency has direct control. City general fund contributions account for 34% of total revenues, and 15% of revenues are from operating grants. The remainder is derived from rent, advertising, and interest. Total fiscal 2015 revenues were \$1.0 billion. The pledged revenues totaled \$626 million in fiscal 2015. In our opinion, the agency has proactively managed its expenses. While facing significant labor costs, management has worked to reduce burdens. Total expenses, including transfers, were \$977 million in fiscal 2015.

Although a gross pledge of certain revenues legally secures the bonds, we consider the finances and operations of the agency as a whole when evaluating the credit and DSC according to our criteria. The agency benefits from the strength of the revenue supplied by the parking operations, while the transit operations ultimately generally lead to break-even results. DSC on a net revenue basis was 3.1x in fiscal 2015 and was 5.8x in fiscal 2014; we expect DSC may decline as debt is added. These figures include transfers to capital as well as appropriated fund balances. We view SFMTA's DSC as strong.

SFMTA's available cash and investments totaled \$596 million, or 185 days' cash, in fiscal 2015, including the \$100 million available commercial paper capacity. Cash balances have been growing over the past five years, and management does not project significant changes in cash balances for fiscal years 2016 and 2017. Cash (including cash in reserve funds) to debt service was 38x in fiscal 2015 and is projected to decline to 30x by fiscal 2017 with the issuance of some additional debt. In our view, SFMTA has exceptional access to external liquidity, with a track record of access to capital markets and banks. Based on these factors, we view SFMTA's liquidity as very strong.

The farebox recovery ratio for the system -- farebox revenue (plus parking revenue in the case of SFMTA) divided by operating costs -- in fiscal 2015 was, in our view, strong, at 35%. In our view, this indicates strong financial flexibility, in that SFMTA is more in control of its revenue than are other agencies that receive a lower share of total revenue from fares. Farebox and parking/traffic revenues provided approximately 50% of total revenues in fiscal 2015. Effective fiscal 2011, the SFMTA has adopted an "Automatic Indexing Implementation Plan." Under this plan, transit fares, parking citations, garage parking rates, and other charges not governed by law are increased periodically according to a set formula as part of the agency's budget. The formula adjusts charges by a rate equal to one-half of any change in the Consumer Price Index for the Bay Area, plus one-half of the annual percentage increase or decrease in the agency's labor costs included in the budget. The increase is then rounded up to the nearest 25 cents, 50 cents, or \$1.00 depending upon the base charges as long as the rounding does not result in more than a 10% increase in the charge. The board may increase or decrease charges by more or less than those derived from the formula. Revenues not automatically indexed are calculated at cost recovery. We consider the plan to be favorable for the agency. Currently, the basic adult cash fare for transit is \$2.25. The last fare increase was effective Sept. 1, 2014; prior to that time, the fare was \$2.00. We view SFMTA's financial flexibility as strong.

The SFMTA has a substantial \$3.3 billion five-year capital program. The agency, like most transit and transportation agencies, faces challenges in maintaining infrastructure in a state of good repair. Projects include transit infrastructure needs, fleet replacement, the Central Subway Project (an extension of the Third Street light rail line into Chinatown), and transit expansion and enhancement. The revenue sources for the capital program include federal grants (primarily for the Central Subway), state & local funds, debt (including revenue and GO debt), and SFMTA resources in place. SFMTA expects to issue parity bonds, in addition to the outstanding and current bonds, totaling \$150 million (the first \$75 million will be issued in fiscal 2017). Debt to total revenues in fiscal 2015 was very low, in our opinion, at 0.19, with debt to net revenues at 3.86, but these ratios are set to rise to 0.25 and 12.18 by fiscal 2017, respectively. We view SFMTA's debt burden as low.

In summary, our analysis of the five factors that comprise the SFMTA's financial risk profile results in a financial risk profile score of very strong.

Given our view of the extremely strong enterprise risk profile and the very strong financial risk profile scores, the final SACP is 'aa+', per our criteria (see criteria, table 1). Based on peer comparisons, we did apply one notch of flexibility in the process of arriving at the final SACP of 'aa', and no rating caps applied. We are assigning the 'aa' SACP rather than the 'aa+' SACP due to the increasing debt burden and its uncertain effect on DSC and liquidity. No rating cap applied. Given our view that the SFMTA is not a government-related entity (GRE) under Standard & Poor's GRE criteria, SFMTA's ICR is also 'AA'.

Given our analysis of the SFMTA's bond provisions, the issue rating for the revenue bonds is also 'AA'. Bond provisions include an additional bonds test (ABT) of 3x pledged revenues. While an industry standard, an ABT based on a gross pledge is, in our opinion, weak. The fully funded debt service reserves are, in our opinion, a credit strength.

Outlook

The stable outlook reflects our expectation that the SFMTA's market position will remain at least very strong, especially given projected ridership growth, and that the SFMTA will continue to produce very strong financial metrics, including strong DSC. The outlook also reflects our expectations that the SFMTA's capital needs will receive adequate funding to ensure continued system preservation and that the agency will continue receiving support from federal, state, and local governments so that its debt burden does not materially escalate beyond projected levels.

Upside scenario

We don't expect to raise the ratings within the next two years, due to our expectation of potentially lower future DSC and liquidity levels as a result of additional planned debt.

Downside scenario

We don't expect to lower the rating, given the SFMTA's very strong financial metrics and extremely strong economic fundamentals.

Related Criteria And Research

Related Criteria

- General Criteria: Mass Transit Enterprise Ratings: Methodology And Assumptions, Dec. 18, 2013
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.

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