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Summary:

San Francisco Municipal Transportation Agency, California; Transit

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Summary:

San Francisco Municipal Transportation Agency, California; Transit

Credit Profile		
US$75.0 mil rev bnds ser 2014 due 03/01/2044		
Long Term Rating	AA/Stable	New
San Francisco Municipal Transportation Agency rev rfdg bnds		
Long Term Rating	AA/Stable	Upgraded
San Francisco Municipal Transportation Agency ICR		
Long Term Rating	AA/Stable	Upgraded

Rationale

Standard & Poor's Ratings Services raised its long-term rating to 'AA' from 'AA-' on the San Francisco Municipal Transportation Agency (SFMTA), Calif.'s revenue bonds outstanding. The raised rating reflects our view of the agency's strengthened market position. Also, we raised the SFMTA's stand-alone credit profile (SACP) to 'aa' from 'aa-' and our issuer credit rating (ICR) on the SFMTA to 'AA' from 'AA-'. Finally, Standard & Poor's assigned its 'AA' rating to the SFMTA's $75 million series 2014 revenue bonds. The outlook on all ratings where applicable is stable.

The 'AA' rating is currently the highest rating on revenue bonds or certificates of participation (COPs) 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 cyclicality and 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, $3.4 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, allowing the agency to charge the third-highest monthly parking pricing in the U.S. 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 81 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 cyclicality (including ridership trends), and therefore we characterize the cyclicality 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 the SFMTA's catchment area -- with steady population and employment growth and high wealth levels -- helps provide stable demand for transit services. Gross population growth for San Francisco from 2008 to 2013 was 6%, and employment growth over the same period was 15%. Projections from Global Insight indicate population and employment growth will continue. San Francisco's per capita income level is 180% of the national average. We consider the SFMTA's economic fundamentals as extremely strong.

The SFMTA's ridership has been resilient, despite fare increases, service reductions, and the economic recession. Passengers totaled 225 million in fiscal 2014, down from the historical high of 226 million in fiscal 2009, but up from 206 million in fiscal 2007 and, more recently, 223 million in fiscal 2013. During the five-year period of fiscal 2009 to fiscal 2014, gross ridership growth was negative 0.49%, down slightly from the historical high. We consider the

SFMTA's market position as very strong, as some ridership fluctuations are mitigated by the SFMTA's status as a virtual monopoly for public transit in San Francisco. Management project average annual ridership growth of 3.3% through fiscal 2020, which we consider aggressive.

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 (27% in fiscal 2014) and passenger fares (22%); in our opinion, this combined percentage representing a significant portion of revenue, or almost 50%, over which the agency has direct control. City general fund contributions account for 33% of total revenues, and 15% of revenues are from operating grants. The remainder is derived from rent, advertising, and interest. Total fiscal 2014 revenues were $955 million. The pledged revenues totaled $623 million in fiscal 2014. 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 $900 million in fiscal 2014.

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 5.8x in fiscal 2014 and was 8.4x in fiscal 2013; we do expect DSC will decline as debt is added. These figures include transfers to capital as well as appropriated fund balances. We view the SFMTA's DSC as strong.

The SFMTA's available cash and investments totaled $594 million, or 244 days' cash, in fiscal 2014, including the $100 million available commercial paper capacity. Cash balances have been growing during the past five years, and management does not project significant changes in cash balances for fiscal years 2015 and 2016. Cash (including cash in reserve funds) to debt service was 54x in fiscal 2014 and is projected to decline to 37x by fiscal 2016 with the issuance of some additional debt. In our view, the SFMTA has exceptional access to external liquidity, with a track record of access to capital markets and banks. Based on these factors, we view the SFMTA's liquidity as very strong.

The farebox recovery ratio for the system -- farebox revenue (plus parking revenue in the case of the SFMTA) divided by operating costs -- in fiscal 2014 was, in our view, strong, at 38%. In our view, this indicates strong financial flexibility, in that the 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 2014. Effective fiscal 2011, the SFMTA 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 the SFMTA's financial flexibility as strong.

The SFMTA has a substantial $3.4 billion, five-year capital program. The agency, like most transit and transportation agencies, faces challenges in maintaining infrastructure in a state of good repair. Of the $3.4 billion, 49% is for transit infrastructure needs and fleet replacement, 23% is for the Central Subway Project (an extension of the Third Street light rail line into Chinatown), and 28% is for transit expansion and enhancement projects. The revenue sources for the capital program are 36% federal grants (primarily for the Central Subway), 5% state, 30% local, 15% debt (including revenue and general obligation debt), and 15% SFMTA resources in place. The SFMTA expects to issue parity bonds, in addition to the outstanding and current bonds, totaling $150 million in fiscal 2017. Debt to total revenues in fiscal 2014 was very low, in our opinion, at 0.15, with debt to net revenues at 2.16, but these ratios are set to rise to 0.23 and 13.11 by fiscal 2016, respectively. We view the 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. We don't expect to raise the ratings within the next two years due to our expectation of lower future DSC levels as a result of additional planned debt. 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
- General Criteria: Methodology: Industry Risk, Nov. 20, 2013
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011

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