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Ratings

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San Francisco Municipal Transportation Agency; Transit

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Table Of Contents

Rating Action

Negative Outlook

Credit Opinion

Enterprise Risk Profile: Very Strong

Financial Risk Profile: Strong

Significant Tax Support

Related Research

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San Francisco Municipal Transportation Agency; Transit

Credit Profile		
San Francisco Municipal Transportation Agency rev rfdg bnds		
Long Term Rating	AA-/Negative	Downgraded
San Francisco Municipal Transportation Agency ICR		
Long Term Rating	AA-/Negative	Downgraded

Rating Action

S&P Global Ratings lowered its long-term rating to 'AA-' from 'AA' on the San Francisco Municipal Transportation Agency's (SFMTA) revenue bonds outstanding. The outlook is negative.

The rating action reflects the application of our updated "Global Not-for-Profit Transportation Infrastructure Enterprises Criteria," published Nov. 2, 2020, on RatingsDirect, and changes in credit characteristics.

Certain gross pledged revenue before the payment of SFMTA expenses secures the bonds, although our analysis of financial performance is on a net basis after payment of operating expenses. This pledged revenue consists of passenger fares; traffic fines, fees, permits, and taxi medallion fees; parking meter revenue and parking citations; parking garage and surface parking lot revenue; Assembly Bill 1107 revenue; rent and advertising revenue; State Transit Assistance revenue; and Transportation Development Act sales tax revenue. Transfers to SFMTA from the city's general fund, including the baseline and the "in lieu of parking" tax, are not pledged to the bonds, but have historically been a significant revenue source to the agency (43% of gross revenue in fiscal 2020), and are projected to be materially lower than pre-pandemic levels. All pledged revenue is set aside, deposited into the SFMTA enterprise account, and then transferred to the trustee for the debt service fund. Bond provisions include an additional bonds test of 3x pledged revenue, but, in our view, an additional bonds test based on a gross pledge is permissive. Cash-funded stand-alone debt service reserve funds, except for the series 2017 bonds, provide additional liquidity to bondholders, if needed. Although the series 2017 bonds do not have a debt service reserve, we do not consider this a significant credit weakness given SFMTA's strong overall liquidity position.

Total SFMTA debt outstanding as of June 30, 2020, was $323 million.

Credit overview

The rating action reflects our view that SFMTA's transportation activity-based revenue such as passenger fares and parking revenue have been significantly affected since March 2020 and will continue to be severely or materially depressed or unpredictable for the remainder of fiscal 2021 (ending June 30) and beyond as a result of social risks and related measures to promote health and safety given the COVID-19 pandemic and associated effects that are outside of management's control. The negative outlook reflects our view of the significant financial and operational challenges posed by the ongoing pandemic and our view that, as or if the pandemic worsens and becomes more prolonged, further credit deterioration is possible to the extent the SFMTA is unable to align expenditures with a lower revenue base or if additional federal funding does not materialize.

The 'AA-' long-term rating reflects a very strong enterprise risk profile, a strong financial risk profile, and significant support by various tax revenue. While we believe SFMTA entered the pandemic financially and operationally very strong, the rating reflects our view of the pandemic's negative effects on SFMTA's market position assessment, which we assess as very strong instead of extremely strong, resulting in an enterprise risk profile assessment of very strong. Additionally, our expectation of significant stress to SFMTA's key financial metrics such as coverage (S&P Global Ratings-calculated) resulted in a financial risk profile assessment of strong, which reflects our expectation that SFMTA's overall liquidity position will remain no less than strong and that SFMTA's debt and liabilities capacity will be strong, despite our view of its very large $2.5 billion five-year capital plan. "Financial support provided by various tax revenue the SFMTA receives, which is not directly reliant on transportation activity, also was an important credit consideration along with SFMTA's diverse revenue mix. More specifically, tax revenue, typically accounting for around 10% to 12% of gross revenue , is incremental to the significant support provided by other nonfare or parking revenue, including support by the City and County of San Francisco as relates to general fund transfers that alone totaled $474 million, or 43% of gross revenue, in fiscal 2020. Operating grants, taxes, and general fund support typically account for almost two-thirds of gross revenue. General fund support, however, declined 10% in fiscal 2020 with a 29% decline projected for fiscal 2021.

SFMTA ridership declined 25% in fiscal 2020, and management projects it will be down approximately 66% in fiscal 2021 as compared with fiscal 2019. The severe drop in ridership, in our view, has diminished SFMTA's overall credit quality, putting pressure on financial metrics over the near term, with SFMTA's diverse revenue mix somewhat tempering this. For additional information, see "Ratings Outlooks On U.S. Transportation Infrastructure Issuers Revised To Negative Due To COVID-19 Pandemic," published March 26, 2020, and "Activity Estimates For U.S Transportation Infrastructure Show Public Transit And Airports Most Vulnerable To Near-Term Rating Pressure," published June 4, 2020.

S&P Global Ratings believes that uncertainty remains high about the evolution of the COVID-19 pandemic. Reports that at least two experimental vaccines are highly effective and might gain initial approval by the end of the year are promising, but this is merely the first step toward a return to social and economic normality; equally critical is the widespread availability of effective immunization, which could come by the middle of next year. We use this assumption in assessing the economic and credit implications associated with the pandemic. As the situation evolves, we will update our assumptions and estimates accordingly.

S&P Global Ratings will monitor the impact of the ongoing COVID-19 pandemic on SFMTA's ridership, parking activity, and key credit metrics, but we believe SFMTA's liquidity, mitigation measures taken thus far, and the $378 million in Coronavirus Aid, Recovery, and Economic Security (CARES) Act funding allotted (which is all being used in fiscal years 2020 and 2021) will allow SFMTA to weather the near-term activity decline. We could weaken SFMTA's enterprise and/or financial risk profile if ridership and parking activity remains depressed for an extended period, pressuring financial metrics on a sustained basis.

The very strong enterprise risk profile assessment reflects our view of SFMTA's:

- Very strong market position, reflective of an essential public transit system with varied offerings (bus, light rail, streetcar, and cable car) that plays a vital role within a service area that has historically steady ridership trends, tempered by exposure to potentially prolonged weak or unpredictable ridership as a result of the ongoing pandemic and lingering ancillary effects (such as the pandemic-induced recession, shifting travel restrictions, stay-at-home and social-distancing restrictions, or behavioral changes with respect to use of public transit) that are outside of management's control;
- Extremely strong service area economic fundamentals, including favorable economic activity as measured by GDP per capita and historically low unemployment, although unemployment has worsened during the pandemic, but in line with national trends;
- Low industry risk relative to that of other industries; and
- Extremely strong management and governance, with a management team that has considerable expertise and a record of success in routinely meeting or exceeding fiscal targets, mitigating risk, and successfully managing all operating divisions.

The strong financial risk profile assessment reflects our view of SFMTA's:

- Strong financial performance, reflecting our expectation of debt service coverage (S&P Global Ratings-calculated) that will be significantly weaker for fiscal years 2020 to 2022 (lower than levels we consider extremely strong in fiscal 2019 and earlier) and a relatively diverse revenue mix;
- Strong debt and liabilities capacity, with a relatively low debt burden for a transit agency of its size and no immediate debt plans, offset by a large capital plan of about $2.5 billion; and
- Strong liquidity and financial flexibility, reflecting 224 days' cash on hand on average in the previous three fiscal years, which we expect will be preserved at no less than 180 days through fiscal 2021 partly as a result of $378 million of CARES receipts, which SFMTA will use in fiscal years 2020 and 2021 to limit draws on its cash reserves.

SFMTA is an enterprise department of the City and County of San Francisco (the city; AAA/Stable general obligation rating). 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 and 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.

Environmental, social, and governance factors

We analyzed SFMTA's environmental, social, and governance risks relative to its market position, management and governance, and financial performance, and determined that, with the exception of social risks, all are in line with our view of the sector standard. SFMTA is exposed to health and safety social risks related to social distancing that will continue to present financial and operational challenges in the short term, particularly if transit activity remains low and parking-related revenue significantly underperforms. We will evaluate these risks as the fluid situation evolves.

Negative Outlook

Downside scenario

Rating pressure could increase over the next one to two years if financial metrics suffer sustained weakness absent offsetting expenditure adjustments, revenue recovery, and, if received, federal grants or stimulus funding. While we believe that general fund contributions, operating grants, and tax support bolster and stabilize the credit from a revenue diversity standpoint, debt service coverage or liquidity that are consistently and materially lower than our expectations, or sustained and depressed transit and parking activity could result in a lower rating.

Return to stable scenario

If SFMTA is able to maintain liquidity and enact expenditures adjustments to bring its budget into alignment, or, if transit and parking activity and operating revenue rebound to levels we believe are sustainable and sufficient to cover all obligations, we could revise the outlook to stable.

Credit Opinion

Enterprise Risk Profile: Very Strong

Our assessment of SFMTA's enterprise risk profile considers its service area economic fundamentals, industry risk, market position, and management and governance.

Extremely strong economic fundamentals

We consider SFMTA's service area economic fundamentals as extremely strong, reflecting a high GDP per capita of near $115,000 and a historically below-average unemployment rate compared with the national level. The unemployment rate for San Francisco was 7.8% in September 2020 compared with the national rate of 7.9%. SFMTA serves a city population of approximately 880,000 in addition to those commuting into the city by auto or other public transit. In our view, the underlying strength of the SFMTA's catchment area--with generally steady population and employment growth and high income levels--helps provide stable demand for transit services. With national virus transmission rates rising to new peaks, economic uncertainty is elevated again. Several states have implemented partial shutdowns of their economies and instituted quarantine restrictions that could erode the bounceback in third-quarter 2020 real GDP growth of 29.5% (annualized). The recovery remains fragile. Real-time indicators indicate that the economic picture is improving, but at a decelerating pace as higher uncertainty about the pandemic and federal stimulus introduces downside risks for the economic outlook in the fourth quarter and beyond. (See "The U.S. Economy Reboots, With Obstacles Ahead," published Sept 24, 2020 and "U.S. Real-Time Data: A Cloudy Economic Outlook As COVID-19 Resurges," published Oct. 23, 2020.)

Very strong market position

We believe that SFMTA provides a highly essential service to the 49-square-mile city and operates as a virtual monopoly within most of its service area, although in many areas other providers provide overlapping service, such as Bay Area Rapid Transit (BART). Muni carries an estimated 45% of all transit passengers in the overall Bay Area, about twice the number of passengers of the second-largest transit operator in the area (BART). Muni's infrastructure includes more than 800 motor and trolley buses, approximately 150 light rail vehicles, more than 40 historic streetcars, and approximately 40 cable cars, covering approximately 90 routes throughout San Francisco and providing a transit stop within a quarter-mile of everyone who lives in, works in, and visits the city.

Throughout the city, the agency also manages 38 off-street public parking garages and lots (totaling about 15,000 off-street parking spaces) as well as approximately 28,500 on-street parking meters. The extensive parking system has a solid competitive position, in our opinion. The facilities generally have high utilization rates during peak hours. The agency owns and manages 30% of all downtown spaces and 15% of all citywide spaces in garages and lots. The agency also issues parking citations and enforces parking regulations.

Prior to the pandemic's onset in March 2020, SFMTA's ridership had been relatively stable over the prior decade, with slight ridership growth (but also with mild declines in some recent years) despite fare increases and the economic recession. Boardings totaled 224.2 million in fiscal 2019, down 3.5% from the recent peak of 232.3 million in 2016 but relatively unchanged since 2009. These statistics suggest ridership was already weakening slightly for SFMTA before the pandemic, a trend also seen at other large mass transit agencies across the country, but SFMTA's declines were much more modest.

The local effects from the ongoing COVID-19 pandemic began to unfold in March 2020, with a shelter-in-place order put in place for the seven Bay Area counties on March 17 followed by the governor's issuance of a statewide stay-at-home order on March 19. California and the Bay Area in particular were particularly conservative in terms of social distancing restrictions, and many restrictions that were eased over the past few months have been re-triggered as a result of surging COVID-19 cases. Muni reported a 95% decline in ridership in April 2020 year over year, with ridership improving gradually since then but remaining at a fraction of pre-pandemic levels. Only buses are operating, but almost two-thirds of bus routes have been suspended; light rail, streetcars, and cable cars are not operating.

Ridership declined 25% in fiscal 2020 (ended June 30), and management projects a ridership decline of 66% for fiscal 2021 when averaging larger declines in the first half with assumed continued higher partial recovery through June 2021. As of Nov. 18, 94% of the state was in the governor's most restrictive, purple tier, but San Francisco remains in the less restrictive red tier, in which relatively more nonessential indoor businesses and services are open or allowed to operate at a higher capacity (although subject to change given the fluid surging virus situation). As technology has advanced to allow for a greater percentage of office workers to seamlessly telecommute during the pandemic, we believe that after the pandemic or once a vaccine is widely available, SFMTA will suffer a permanent loss of a meaningful portion of 'ridership that could take several years to recover from. We believe that this phenomenon will likewise affect SFMTA's parking revenue. We will factor these considerations into our view of the SFMTA's overall essentiality and importance as we assess its market position in the future.

Extremely strong management and governance

Our managerial and governance assessment reflects SFMTA's strategic positioning, risk management and financial management, and organizational effectiveness.

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 generally demonstrated a strong track record of meeting benchmarks while addressing operating risks. We view senior management as experienced and broad, and as seemingly capable and experienced to lead the agency through challenges such as the pandemic.

The SFMTA maintains prudent financial policies on 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 in a manner consistent with SFMTA's debt policy, and the agency maintains a five-year detailed capital plan that identifies sources and uses of funding.

Financial Risk Profile: Strong

Our assessment of SFMTA's financial risk profile considers SFMTA's financial performance, debt and liabilities capacity, and liquidity and financial flexibility. Our financial profile assessment also considers SFMTA's financial policies, which we consider credit neutral.

Strong financial performance

Although certain gross revenue legally secures the bonds, we consider the finances and operations of the agency as a whole when evaluating the credit and coverage according to our criteria. S&P Global Ratings-calculated coverage on a net revenue basis was 7.3x in fiscal 2019, declining to negative 5.3x in fiscal 2020 given the ridership effects. Our coverage calculation excludes the $197 million in CARES funds that apply to fiscal 2020 (and another $177 million applied to fiscal 2021) as a result of its nonrecurring nature, but we do recognize that the total CARES funding of $378 million will allow SFMTA maintain its liquidity over fiscal 2021. (Coverage on a net revenue basis, inclusive of the CARES money was 4.2x for fiscal 2020.) Based on SFMTA's budget for fiscal years 2021 and 2022, and without inclusion of the use of fund balance as a revenue source, we calculate that coverage will be significantly less than 1x both years either with or without inclusion of CARES money. While this is a significant departure from historically extremely strong coverage during fiscal years 2015 to 2019, we understand the situation remains fluid pending the trajectory of the pandemic, availability of a vaccine, the permanence of increased telecommuting, system utilization, potentially additional budget adjustments to come, and the performance of other revenue sources such as taxes and general fund support.

SFMTA's strong revenue diversity partly offsets the steep declines in ridership and parking revenue. In a more typical year, fiscal 2019, the composition of SFMTA's $1.3 billion in gross revenue was as follows:

- General fund support (41%),
- Passenger fares (16%),
- Federal and state operating assistance (14%),
- Taxes (12%),
- Parking revenue (11%), and
- Other (6%).

We note that 73% of SFMTA revenue in fiscal 2019 was not directly tied to transportation activity (transit fares and parking) and provided the agency with a degree of financial stability during challenging times for system utilization such as the present. City and County of San Francisco general fund contributions accounted for a sizable 41% of total revenue. The base amount, first established in fiscal 2000, has been incrementally adjusted to account for SFMTA's taking on responsibilities of now consolidated divisions. The city controller adjusts the base amount each year by the percentage increase or decrease in aggregate city discretionary revenue that the mayor and board of supervisors can appropriate for any lawful purpose, and the base amount is subject to midyear adjustments, up or down. Since fiscal 2016, the base amount of this transfer has varied each year by population growth, with no decrease if population declines. Also transferred from the general fund is the SFMTA's 80% share of a tax that the city imposes on commercial off-street parking spaces throughout the city.

Strong debt and liabilities capacity

SFMTA has a substantial $2.5 billion five-year capital program for fiscal years 2021 to 2025. 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), a transportation management center, and transit expansion and enhancement (including the Van Ness bus rapid transit project). The revenue sources for the capital program include federal grants (primarily for the Central Subway), state and local funds, debt (including GO debt), and SFMTA resources in place. Debt to total revenue in fiscal 2019 was very low, in our opinion, at 1.9x, and average of 1.5x during fiscal years 2016 to 2019, but was negative 3.1x in fiscal 2020 given the steep decline in net revenue as a result of measures to promote health and safety amid the pandemic.

Strong liquidity and financial flexibility

SFMTA's available cash and investments totaled $735 million, or an adequate 222 days' cash, in fiscal 2020; liquidity has been relatively consistent on a 'cash basis versus fiscal years 2016 to 2019. Available liquidity to debt was 219%, which we view as extremely strong, in fiscal 2020. Overall, we assess SFMTA's liquidity and financial flexibility as strong, as we placed a greater emphasis on liquidity given SFMTA's significant operating expenses. Cash balances on a nominal basis have been growing since measuring $576 million in fiscal 2016. Management projects liquidity to decline to $587 million by the end of fiscal 2021 given the effect of lower activity and possibly decline further in fiscal 2022, but is uncertain about the estimated decline. We understand that the projected decline in liquidity for fiscal 2021 is likely to be smaller than anticipated given expenditure savings already realized or planned.

Significant Tax Support

In our view, the SFMTA receives significant tax support from a variety of sources, largely in the form of sales tax. SFMTA receives state Transportation Development Act revenue consisting of 0.25% of the total sales tax imposed within the city. SFMTA also receives State Transit Assistance funds from the state from a statewide tax on diesel fuel. In addition, SFMTA receives a portion of a half-cent sales tax imposed in Alameda County, Contra Costa County, and the city that the Metropolitan Transportation Commission allocates to SFMTA, BART, and AC Transit. In fiscal 2019, this tax revenue totaled $161 million, or 12% of gross revenue. This does not include SFMTA's general fund contribution, a large portion of which was likely initially generated from taxes, including property and sales taxes.

Related Research

- How We Apply Our Global Not-For-Profit Transportation Infrastructure Enterprise Criteria, Nov. 2, 2020
- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020