FitchRatings

Fitch Affirms San Diego County RTC, CA's Senior Sales Tax Revs at 'AAA'; Outlook Stable

Fitch Ratings-San Francisco-24 June 2019: Fitch Ratings has affirmed the following San Diego County Regional Transportation Commission (the commission), CA ratings:

--$644 million senior sales tax revenue bonds, 2014 series A and 2016 series A at 'AAA'.
--$537.5 million subordinate sales tax revenue short-term notes 2018 series A at 'AA'/'F1+';
--$537.5 million TIFIA loan junior subordinate sales tax revenue bond 2017 TIFIA series at 'A'.

The Rating Outlook is Stable.

SECURITY
The senior sales tax revenue bonds are payable from a first lien on the half-cent retail transactions and use tax (sales tax) authorized by the voter-approved TransNet extension ordinance and levied throughout San Diego county (the county), net of California Department of Tax and Fee Administration (CDTFA) collection charges. The subordinate notes are secured by a second lien on the half-cent sales tax, and the junior subordinate TIFIA bonds are secured by a third lien. The TransNet sales tax expires on March 31, 2048 (after maturity of all notes and bonds).

ANALYTICAL CONCLUSION
The sales tax revenue bond ratings reflects solid growth prospects for pledged revenues and Fitch's expectation that the commission will limit leverage to maintain stronger coverage cushions than required under its legal covenants. The 'F1+' short-term rating on the 2018 notes reflects Fitch's assessment of the market access implied by the strong long-term credit quality of the commission's borrowing program. The commission has secured a loan agreement from the U.S. Department of Transportation to refund the notes as junior subordinate lien debt, limiting refinancing risk.

KEY RATING DRIVERS
Solid Growth Prospects: Fitch views growth prospects for pledged revenues as solid due to San Diego County's consistent population growth and long-term trends in employment, personal income and taxable sales.

Solid Resilience at Expected Leverage: Resilience to economic downturns is very strong at the senior and subordinate lien levels at expected leverage levels and solid at the junior subordinate lien levels.

No Issuer Default Rating (IDR): The commission does not have material exposure to operating risk. As such, Fitch has not assigned an IDR.

RATING SENSITIVITIES

Pledged Revenue Performance and Leverage: The ratings are sensitive to performance of the pledged revenues and to leverage levels. While not anticipated, a sustained and material reduction in revenue growth prospects or a significant expansion of borrowing plans could put downward pressure on the ratings. The junior subordinate lien TIFIA loan rating could rise if the commission's borrowing plans remain below prior expectations.

DEDICATED TAX CREDIT PROFILE

The commission allocates funding for public transit systems and oversees the construction and improvement of roads, highways, and other transit projects. The commission does not own or operate a public transit system. Due to the limited nature of the system's operations, Fitch does not assign an IDR to the commission.

The CDTFA administers collection of the sales tax and remits revenue, net of the administrative fees, directly to the bond trustee. The CDTFA distributes the sales tax revenues on a monthly basis according to a predetermined formula with quarterly true-ups. Residual sales tax revenues following debt service payments are released to the commission for other purposes, including distributions to local transit agencies, investments in capital project, and administrative costs.

The bonds and notes are supported by a sales tax collected on all taxable sales in San Diego County, which has a population estimated at about 3.3 million. The payer base is diverse, and growth prospects are solid. The 10-year CAGR of revenues was just above inflation at 1.9% in 2018. Sales tax collections were heavily influenced by the housing boom that ended in 2008 as well as the subsequent bust. Fitch expects the CAGR to recover to a level that more convincingly exceeds inflation over the next couple of years. Viewed over a longer period where the impact of the housing boom and bust is less pronounced, revenues have grown at a 3% CAGR since 2000. Future growth should remain above inflation and may approach GDP due to consistent population growth and the ongoing diversification of the local economy.

Pledged revenue coverage is currently very strong (2.8x at the senior lien level in 2018) and expected to remain strong throughout a typical, moderate U.S. recession. To evaluate the sensitivity of the dedicated tax revenue stream to cyclical decline, Fitch considers both a revenue sensitivity scenario (using a 1% decline in national GDP scenario) and the largest consecutive decline in revenues over the period covered by the revenue sensitivity analysis. Based on the commission's sales tax revenue history, Fitch's FAST model generates a 4.2% decline in pledged revenues during the first year of a moderate recession. The largest cumulative revenue decline historically was 17.6% during the collapse of the housing sector from 2008 to 2010.

Assuming issuance up to the 2x ABT, the senior structure could tolerate a 50% drop in revenues. Based on the commission's capital and debt plans, which incorporate the referendum's limitation on capital spending (and by extension debt) to about 42.4% of revenues over the life of the program, Fitch does not expect the commission to leverage to the ABT on any of the liens. The commission currently plans to issue about $200 million to $300 million over the next five years, a level of borrowing that is significantly lower than previously expected. At expected leverage, maximum annual debt service (MADS) coverage for the senior lien would remain at 2.4x or higher. At this leverage level, the senior lien bonds could withstand a 58% drop in revenues before reaching 1x coverage. That is 13.8x the revenue loss expected in a moderate recession and 3.3x the worst consecutive decline. Based on these results, Fitch assesses financial resilience of the senior lien at the 'aaa' level.

The subordinate structure could tolerate a 33% drop in revenues, assuming issuance up to the 1.5x ABT. Fitch does not expect the authority to leverage to the ABT. At expected leverage levels, MADS coverage would remain 2x or higher, and the subordinate lien bonds could withstand a 50% drop in revenues. That is 11.9x the revenue loss expected in a moderate recession and 2.8x the worst consecutive decline. Fitch assesses financial resilience of the subordinate lien at the 'aa' level. This analysis assumes that the 2018 notes only remain in the subordinate lien temporarily before being taken out with the approved TIFIA loan in 2021. The subordinate coverage calculations include three years of interest on the notes but exclude the bullet principal payment at note maturity, which is expected to be taken out with the TIFIA loan rather than 2021 sales tax revenues.

The junior subordinate structure could only tolerate a 13% drop in revenues with issuance up to the 1.15 ABT. Fitch does not expect the authority to leverage to the ABT. At expected leverage levels, MADS coverage would remain at 1.6x or higher, and the junior subordinate lien bonds could withstand a 38% drop in revenues. That is 9x the revenue loss expected in a moderate recession and 2.2x the worst consecutive decline. Fitch assesses financial resilience of the junior subordinate lien at the 'a' level. The assessment incorporates the fact that MADS is far in the future and Fitch's belief that the nature of the revenue stream makes it likely to grow over time.

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Additional information is available on www.fitchratings.com
Applicable Criteria
Short-Term Ratings Criteria (pub. 02 May 2019)
U.S. Public Finance Short-Term Debt Rating Criteria (pub. 01 Nov 2017)
U.S. Public Finance Tax-Supported Rating Criteria (pub. 03 Apr 2018)

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