March 21, 2018

San Diego Association of Governments
401 B Street, Suite 800
San Diego, CA 92101
Attention: Mr. Andre Douzdjian, Director of Finance

Re: US$537,480,000 San Diego County Regional Transportation Commission, California, Subordinate Sales Tax Revenue Short-Term Notes (Limited Tax Bonds), 2018 Series A, dated: Date of delivery, due 04/01/2021

Dear Mr. Douzdjian:

Pursuant to your request for an S&P Global Ratings rating on the above-referenced obligations, S&P Global Ratings has assigned a rating of "AA". S&P Global Ratings views the outlook for this rating as stable. A copy of the rationale supporting the rating is enclosed.

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S&P Global Ratings
Public Finance Department
55 Water Street
New York, NY 10041-0003

The rating is subject to the Terms and Conditions, if any, attached to the Engagement Letter applicable to the rating. In the absence of such Engagement Letter and Terms and Conditions, the rating is subject to the attached Terms and Conditions. The applicable Terms and
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mc
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c: Ms. Mudra Patel, Senior Analyst
Public Financial Management, Inc.
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Summary:
San Diego County Regional Transportation Commission, California; Sales Tax

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Secondary Contact:
Jennifer Hansen, San Francisco (1) 415-371-5035; jen.hansen@spglobal.com

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Credit Profile

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Rationale

S&P Global Ratings has assigned its 'AA' long-term rating to the San Diego County Regional Transportation Commission, Calif.'s $537.48 million series 2018 A subordinate sales tax revenue short-term notes (limited tax bonds).

At the same time, S&P Global Ratings affirmed its 'AAA', 'AAA/A-1', and 'AAA/A-1+' ratings on the commission's senior lien sales tax bonds outstanding and its 'A' rating on the commission's series 2017 junior subordinate lien sales tax Transportation Infrastructure Finance and Innovation Act (TIFIA) loan. The outlook is stable.

Senior lien security and key credit factors
The 'AAA' senior-lien long-term rating reflects our view of the commission's:

- Participation in the broad and diverse San Diego County economy;
- Diverse sales tax revenue base incorporating more than 3 million people;
- Strong maximum annual debt service (MADS) coverage of 2.7x based on fiscal 2017 revenue; and
- Strong additional bonds test (ABT) of 2.0x.

A gross senior lien on a 0.5% sales tax levied countywide (commonly known as TransNet), net of administrative costs paid to the California Department of Taxes and Fees Administration (CDTFA), secures the senior lien bonds. The sales tax is effective through March 31, 2048, in accordance with voters' reauthorization of the tax in 2004, which was first collected in 1988. Sales tax revenues are paid to the bond trustee directly from the CDTFA and are released to the commission for other purposes only after principal and interest have been set aside, according to the bond documents.

The commission's senior lien bonds are eligible to be rated above the sovereign, because we believe the commission can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above the Sovereign—Corporate and Government Ratings: Methodology and Assumptions" (published on Nov. 19, 2013, on
Summary: San Diego County Regional Transportation Commission, California; Sales Tax

RatingsDirect), U.S. local governments are considered to have moderate sensitivity to country risk. The commission's locally derived revenues are the source of security for the bonds, and the institutional framework in the U.S. is predictable, with significant U.S. local government autonomy. In a potential sovereign default scenario, U.S. local governments would maintain financial flexibility through the ability to continue collecting locally derived revenues and U.S. local governments have independent treasury management.

The short-term component of the ratings on series 2008A, 2008B, 2008C, and 2008D reflect that liquidity provider. For more information on the short-term ratings, see the articles: "San Diego County Regional Transportation Commission, California; Sales Tax" (published Nov. 1, 2017), "San Diego County Regional Transportation Commission, California; Sales Tax" (published June 4, 2015), and "San Diego County Regional Transportation Commission, California; Sales Tax" (published March 7, 2014).

- Series 2008A and 2008B: the 'A-1' short-term component of the rating is based on the rating on the standby bond purchase agreement (SBPA) with JPMorgan Chase Bank N.A., which expires March 2019.

Based on fiscal 2017 revenues, senior lien MADS coverage was a strong 2.7x. We understand the commission plans to issue about $200 million to $300 million of additional senior lien bonds through 2023, of which about $75 million is expected to fund a portion of the $1.81 billion Mid-Coast Corridor Transit Project. Key components of the project include an extension of the existing light rail system.

**Subordinate lien security and key credit factors**

The 'AA' subordinate lien long-term rating reflects our view of the commission's:

- Participation in the broad and diverse San Diego County economy;
- Diverse sales tax revenue base incorporating more than 3 million people;
- Strong ABT of 1.5x.

These strengths are partially mitigated by:

- The historical volatility in pledged revenues as the TransNet collections decreased by about 18% during the economic recession; and
- The commission's additional capital needs on the senior lien, which could dilute future coverage over the length of the loan term.

A second lien on a 0.5% sales tax levied countywide, net of administrative costs paid to CDTFA, secures the subordinate lien bonds. The second lien is subordinate to existing senior obligations that include the rated TransNet bonds, and parity to $100 million commercial paper authorization, of which the commission currently has $25.9 million outstanding, and credit and liquidity provider fees and expenses and termination payments on existing swaps. The
sales tax is effective through March 31, 2048, in accordance with voters’ reauthorization of the tax in 2004, which was first collected in 1988. Sales tax revenues are paid to the bond trustee directly from the CDTFA and are released to the commission for other purposes only after principal and interest have been set aside, according to the bond documents.

The bonds are structured with interest payments through note maturity, in 2021, and payment of note principal repaid from a future long-term debt obligation. The commission intends to pay the principal on the notes from the proceeds of a draw on a TIFIA loan agreement entered into on June 27, 2017, with the U.S. Department of Transportation in an amount not to exceed $537,484,439.

The indenture also provides that the commission agrees to use its best efforts to draw on the TIFIA loan agreement or to issue senior or parity debt to provide funds sufficient to pay the notes. For purposes of computing MADS under the ABT, principal payments on debt the commission intends to pay with future debt obligations are treated as if they are amortized over 30 years or until the TransNet sunsets, whichever occurs first. Under this methodology, projected MADS coverage would be about 1.9x on subordinate lien bonds to take out the notes, assuming 5% interest rate and level amortization.

The notes will finance the commission’s Mid-Coast Corridor Transit Project. Altogether, the project is expected to require $1.81 billion, of which the notes will finance about 30%. Additional funding is expected to come from TransNet pay-as-you-go and federal grants.

**Junior subordinate lien security and key credit factors**

The ‘A’ junior subordinate lien long-term rating reflects our view of the commission’s:

- Participation in the broad and diverse San Diego County economy;
- Diverse sales tax revenue base incorporating more than 3 million people;
- Strong MADS coverage of 1.7x based on fiscal 2017 revenue; and
- Adequate ABT of 1.15x.

These strengths are partially mitigated by:

- The historical volatility in pledged revenues as the TransNet collections decreased by about 18% during the economic recession;
- The lack of a debt service reserve fund (DSRF) unless annual coverage fell below 1.35x; and
- The commission’s additional capital needs on the senior lien, which could dilute future coverage over the length of the loan term.

A third lien on a 0.5% sales tax levied countywide, net of administrative costs paid to CDTFA, secures the junior subordinate lien bonds. The third lien is subordinate to existing senior and subordinate (second lien) obligations that include the rated TransNet bonds, and to credit and liquidity provider fees and expenses and termination payments on existing swaps. The sales tax is effective through March 31, 2048, in accordance with voters’ reauthorization of the tax in 2004, which was first collected in 1988. Sales tax revenues are paid to the bond trustee directly from the CDTFA and are released to the commission for other purposes only after principal and interest have been set aside, according
to the senior bond documents.

Based on the estimated 21-year amortization of the loan, MADS coverage on the loan would be about 1.7x.

**The county economy**
San Diego County is the second-most populous county in California and the eighth-most populous county in the U.S. Altogether, its economy is broad and diverse as it encompasses more than 3 million residents. As a result, the county's income and wealth indicators reflect those of its regional peers, as the per capita effective buying income (EBI) is 107% of the national level and the projected median household EBI is 102% of the national level, both of which we consider good. San Diego County has a diversified economy based on tourism, international trade, military, and high-technology manufacturing. County unemployment continues to decline and has historically tracked below the state level, a trend that is poised to continue. The number of notices for defaults and foreclosures has declined steadily since its peak in 2009, and notices of default are close to 2005 levels.

**Pledged revenues and the commission**
The commission is a component unit of the San Diego Association of Governments (SANDAG). The commission was formed to administer transportation improvement projects funded through the 0.5 cent sales tax, but other agencies in the region are responsible for operations of the various transportation programs. The SANDAG board serves as the commission's board, and is composed of representatives from the county and 18 cities within the county. Following voter approval of the sales tax in 1987, the commission began financing transportation improvements in 1988.

Overall, the TransNet revenue stream is demonstrating a trend of positive revenue growth as the 0.5 cent sales tax revenue grew 39% in the past seven years to $284.5 million for fiscal 2017. Pledged revenues faced a cumulative decline of about 21% between fiscal years 2007 and 2010, partially due to the economic recession. In particular, peer agencies in the state posted similar, but slightly higher, multiyear revenue declines (at about 25% to 30%) during the same period. Looking ahead, we expect TransNet revenues to continue to increase at a stable rate. Supporting this assumption is our view of the historical trend, the broader economic improvement in the county and greater metropolitan statistical area, as well as the county's population growth. However, the historical volatility in fiscal years 2007 through 2010 could return and affect our forward assumption, should the county's economic recovery falter.

Overall, we are forecasting stability or growth for the urban centers in California as continued home price appreciation and statewide growth in technology and other professional sectors. Therefore, we expect the broader macroeconomic forces to support our view and expectation of the county's TransNet tax receipt growth. However, constrained housing supply and a cooling of employment growth in higher-paying professional industries may slow the pace of growth in the near term. For additional information, please refer to our "U.S. State And Local Government Credit Conditions Forecast" (published Nov. 1, 2017).

**Bond and loan provisions**
Senior bond provisions include a 2.00x MADS ABT based on historical revenue for the senior lien. The indenture requires 1.5x MADS coverage by historical revenues for additional subordinate lien bonds. For purposes of computing MADS under the subordinate lien ABT, principal payments on debt the commission intends to pay with future debt obligations are treated as if they are amortized over 30 years or until the TransNet sunsets, whichever occurs first. Junior subordinate loan provisions include a 1.15x MADS based upon historical revenues from 12 of the last 18
months.

**Outlook**

The stable outlook reflects our expectation that the broad and diverse region will maintain stable to positive economic growth and that coverage will remain above ABT coverage ratios, despite future debt financing needs. We do not expect to change the rating during the two-year outlook period.

**Upside scenario**

We could raise the rating on the subordinate and junior subordinate lien ratings if the commission’s MADS coverage improves to a level in line with those of higher-rated peers due to TransNet revenue growth above our expectations.

**Downside scenario**

We could lower the rating should additional debt issuances or declines in pledged revenues dilute coverage.

**Ratings Detail (As Of March 21, 2018)**

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<tr>
<th>Rating Details</th>
<th>Rating</th>
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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.capitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings’ public website at www.standardandpoors.com. Use the Ratings search box located in the left column.