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CREDIT OPINION
5 July 2022

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San Francisco Muni.Transp. Agcy., CA

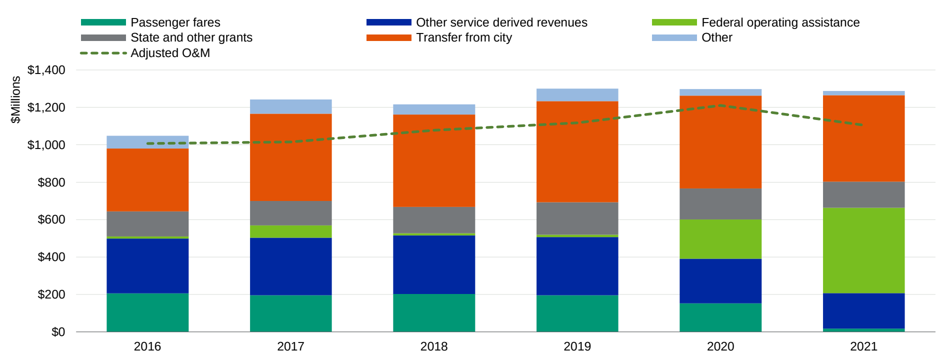
Update to credit analysis following outlook revision to stable

Summary

The credit quality of the San Francisco Municipal Transportation Agency, CA (SFMTA, Aa3 stable) is supported by its strategic importance as the main public transportation provider in the City and County of San Francisco (Aaa stable), its revenue diversity, and sound liquidity. The agency also benefits from proactive and conservative fiscal management as well as demonstrated financial support from the City and County of San Francisco, State of California (Aa2 stable) and the federal government. These strengths are offset by the agency's labor shortage challenges, significant deferred capital needs and high fixed costs for pensions and OPEB. Also, like other transit systems in the US, SFMTA's ridership remains significantly lower than pre-pandemic levels, and recovery is expected to be slow. While substantial federal pandemic aid will offset the agency's fare revenue losses in the near term, permanent ridership losses driven by shifting working patterns will likely require SFMTA to seek additional revenue streams and/or restructure operations in the outer years to balance operations.

On July 1, 2022, we downgraded the rating on SFMTA's revenue bonds to Aa3 from Aa2 and changed the outlook to stable from negative.

Exhibit 1
SFMTA benefits from diverse revenue stream, and significant federal aid is blunting the effects of fare revenue losses under the pandemic
Fiscal year



O&M is adjusted to net out depreciation, interest expense and use annual cash contributions for pensions contribution and OPEBs; transfer from city exclude general obligation bond proceeds dedicated to capital projects
Source: SFMTA; Moody's Investors Service

Credit strengths

» Large service area

» Availability, in the near term, of federal relief funds to offset fare revenue losses

» Diverse revenue stream that includes fares and parking fees as well as subsidies from federal, state and city government

» Low debt levels with strong coverage by both pledged revenues and net revenues

» Proactive and conservative fiscal management

Credit challenges

» Slow recovery of ridership because of the coronavirus pandemic and limited return to office work

» Relatively high fixed costs and long term liabilities largely attributable to pensions

» Significantly deferred capital needs

» Significant labor shortage challenges

Rating outlook

The stable outlook reflects our expectation that the agency's finances will be balanced with federal aid over the next 18-24 months as fare revenue remains depressed. Further, we expect ongoing fiscal support from the City of San Francisco. Over the longer term, we expect that SFMTA will proactively seek additional revenue sources or make expenditure adjustments, if needed, to maintain structural balance.

Factors that could lead to an upgrade

» The addition of significant new sources of revenues to the existing pledged revenue mix, combined with limited issuance of new debt

» Significant reduction in pension liabilities and deferred capital needs

Factors that could lead to a downgrade

» Significant and long term reduction in ridership and essentiality beyond current projections

» Inability to maintain balanced operations

» Material weakening of debt service coverage

» Sustained erosion of liquidity position

Key indicators

Exhibit 2

Fiscal Year	2017	2018	2019	2020	2021
Annual Ridership (000)	225,786	224,611	222,938	170,284	61,641
Annual Ridership Change (%)	-2.8%	-0.5%	-0.7%	-23.6%	-63.8%
Utilization (Trips/ Population)	256	253	250	190	69
Farebox Recovery Ratio (%)	19.3%	18.8%	17.5%	12.6%	1.6%
3-Year Average Fixed Costs as % of Operating Expenditures	12.8%	12.8%	13.3%	13.7%	14.3%
Net Deb/ Revenues	0.3	0.3	0.3	0.3	0.4
3-Year Average Annual Debt Service Coverage by Net Revenues (GAAP)	7.9	6.6	8.3	5.0	6.1
Days Cash on Hand	335	221	230	222	236
Additional Measures					
Pledged Revenues ($000)	616,089	652,919	689,996	764,755	789,614
Annual Change in Pledged Revenues	-0.8%	6.0%	5.7%	10.8%	3.3%
Annual Debt Service Coverage by Pledged Revenues (Indenture) (x)	37.0	24.8	27.2	30.1	33.6

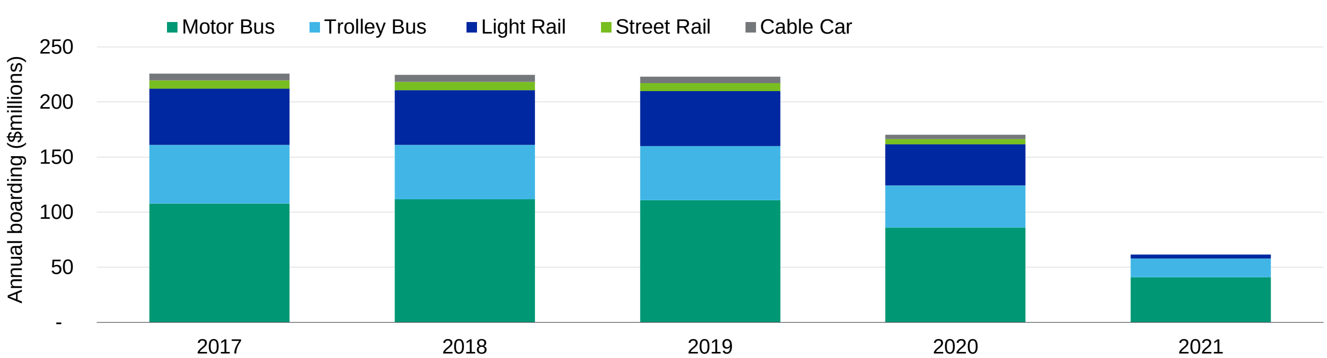
Source: SFMTA; Moody's Investors Service

Profile

SFMTA is an enterprise department of the City and County of San Francisco, responsible for the management of all ground transportation in the city. SFMTA oversees public transit as well as bicycling, para

transit, parking, traffic, pedestrian safety and infrastructure, and taxis. SFMTA has autonomy to set its passenger fares, parking fees, and fines.

Exhibit 3
SFMTA offers a diverse fleet of vehicles for its transit services
Fiscal year ridership breakdown



Note: ridership count not completed for street rail in fiscal 2021 due to staff availability; cable car service did not operate in FY2021
Source: SFMTA; Moody's Investors Service

Detailed credit considerations

Size and market position

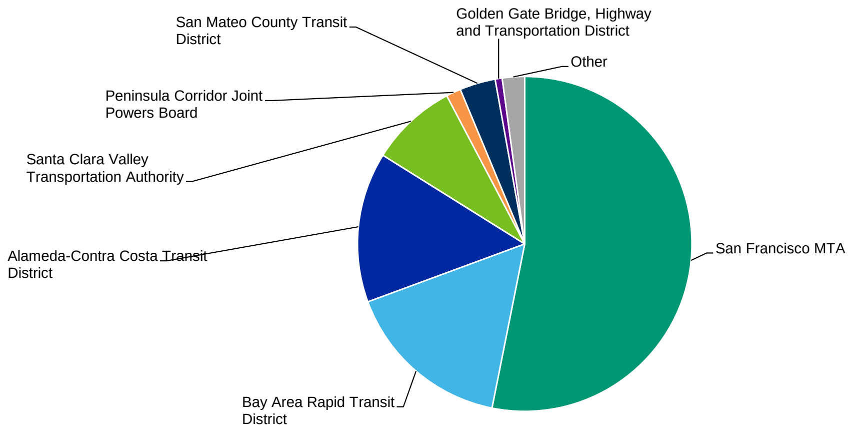
We expect SFMTA's ridership levels will slowly recover to 85% of pre-pandemic levels in a few years, as the pandemic is permanently shifting working patterns. The agency's system utilization, measured by ridership over population, will remain among the highest in the nation as SFMTA will continue to play an important role in reducing congestion in the city as more commuters return to office and tourism resumes.

SFMTA serves the City and County of San Francisco with a population of around 875,000. It is the eighth largest transit system in the country and the largest in the San Francisco Bay Area, based on total ridership before the pandemic. As of calendar year 2021, the agency carried a little over 50% of total Bay Area riders (see exhibit below), up from around 45% before the pandemic; several other transit systems in the area, including Bay Area Rapid Transit District, CA (GO bond rating Aaa stable) and Peninsula Corridor Joint Power Board, CA (revenue bond rating A2 positive) are experiencing slower recovery in ridership than SFMTA.

Exhibit 4

SFMTA remains the largest transit operator in the San Francisco Bay Area

Distribution of calendar year 2021 ridership

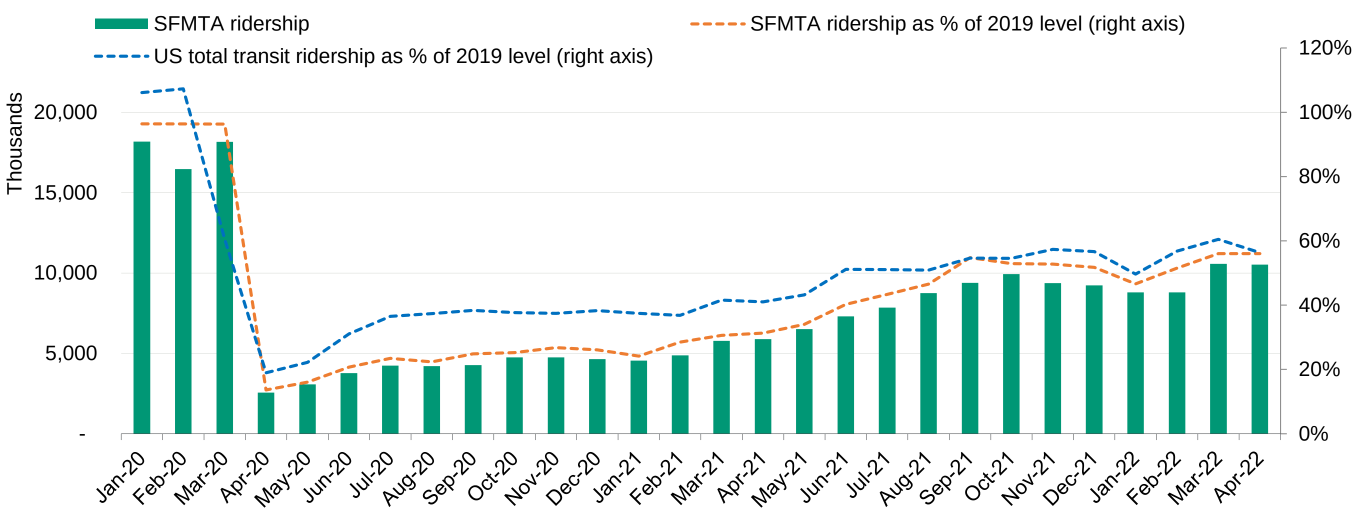


Source: Federal Transit Administration National Transit Database

Like all transit systems nationwide, SFMTA has experienced a severe drop off in ridership as a result of the coronavirus pandemic. At the lowest point in April 2020, SFMTA's monthly ridership was just 13.6% of the April 2019 level. While the agency's ridership recovery initially lagged the nation (see Exhibit 5), it has picked up in recent months. As of April 2022, SFMTA's ridership was 56% of its April 2019 level, roughly in-line with the national transit ridership recovery rate. While San Francisco has a higher share of workers who can likely work remotely, we expect that attraction of major cities will endure.

Exhibit 5

After suffering a larger decline at the beginning of the pandemic, SFTMA's ridership recovery now trails the nation



Source: Federal Transit Administration

San Francisco has a diversified economy and is a global leader of technology and innovation with strong resident incomes measures, including median family income representing 172.6% of US and per capita income representing 203.6% of US. The city's unemployment rate was 2.2% as of April 2022, outperforming the state (3.8%) and the nation (3.3%) for the same period.

Financial flexibility and metrics

SFMTA's budget will be balanced over the next two years given the influx of federal pandemic aid and better than projected outlook of the city's financial health, as transfers from the city's general fund represents a large revenue source for SFMTA. While the agency's ridership is not projected to fully recover to pre-pandemic levels even in the outer years, we expect that management will redesign fares and identify new revenue sources to maintain structural balance once federal pandemic aid is exhausted. We also believe that the proactive management team will continue to monitor economic, financial and service conditions to update the agency's multi-year financial forecasts and tighten operations, if conditions worsen versus the current forecast.

The agency's finances benefit from a diverse mix of operating revenues (see Exhibit 1). Transfers from the city's general fund represented the largest source for operating revenue, at around 40%, prior to the pandemic. The general fund transfers are formula-driven, voter approved and embedded in the City Charter. They do not require appropriation by the city and cannot be diverted to other city purposes. This revenue source suffered a moderate decline at the start of the pandemic, but outperformed earlier projections and is expected to remain a major source of the agency's revenue as the city's financial outlook has improved.

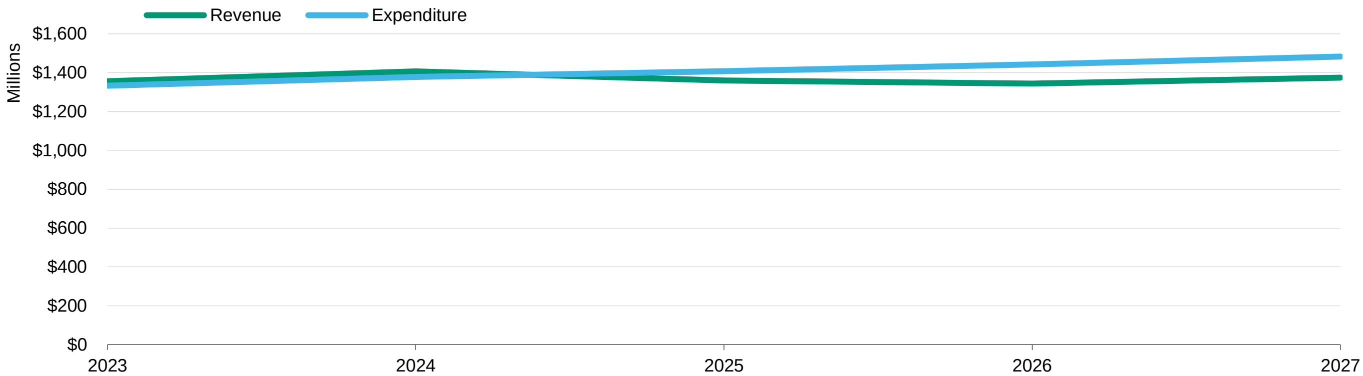
Service derived revenue, mainly passenger fares, parking fees and fines, advertising and license and permits, made up around 39% of total operating revenue prior to the pandemic. While farebox revenue remains depressed, especially as SFMTA has paused indexing its fares and extended its free-muni-for-youth program, parking fees and fines have positively recovered to close to pre-pandemic levels. Overall, declines in service derived revenues as a result of the pandemic will be covered by federal pandemic aid through fiscal 2024, based on the planned use of available federal relief dollars received.

The agency's revenue also includes: dedicated tax subsidies, including AB 1107, the ½-cent BART sales tax, a portion of which is allocated by formula to SFMTA; State Transit Assistance (STA) made up of a state sales taxes on diesel fuels allocated to counties for transit; and state Transportation Development Act (TDA) funding, made up of a state ¼-cent sales tax returned to counties for transit. We expect these sources will remain a stable revenue source for the agency. Most of SFMTA's operating revenues, with the primary exception of the general fund transfers, are pledged to the revenue bonds.

Despite dramatic declines in service derived revenues, the agency ended fiscal 2020 and 2021 with balanced operations primarily with federal pandemic support funds. The agency also enacted expenditure cuts, including hiring freezes and overtime controls, and redirected to operating accounts revenues previously earmarked for capital, including the “City Population-Based Baseline”, a third general fund transfer provided for in the City Charter, and certain transit development fees. Management expects to end fiscal 2022 with operating savings exceeding $40 million primarily driven by unfilled positions.

Going forward, remaining federal pandemic aid will support balanced operations through fiscal 2024 by funding around 13% of budget. Notably, the fiscal 2023 and 2024 budget includes adding human resource and workforce development staff and resources to help fill significant vacancies. However, the agency has set specific targets across several performance measures and will pause staffing augmentation if ridership and revenue recovery do not meet expectations. Over the long term, management expects to seek additional voter approved taxes at a future election date to achieve financial stability, as a deficit of $48 million (3.4% of expenditure) is projected starting in fiscal 2025 and will grow (see Exhibit 6). Potential revenue measures include transportation special tax, parking tax, and property development revenue. Absent additional revenues, SFMTA will likely need to enact additional spending cuts and possibly defer capital projects.

Exhibit 6
SFMTA is projecting a small but growing structural revenue gap starting in fiscal 2025
Fiscal year



Source: SFMTA; Moody's Investors Service

Liquidity
SFMTA's liquidity is strong. As of fiscal end 2021, its unrestricted cash and investments totaled $714.5 million, representing 236 days cash on hand, well exceeding its contingency reserve policy that targets reserve at 10% of operating expenditures. As of March 31, 2022, SFMTA had $825.3 million unrestricted cash and investment balance. SFMTA also has the ability to borrow from the city's investment pool. if needed.

Leverage and fixed costs

SFMTA has a large capital plan, given its significant statement of good repair needs. However, the agency's direct debt burden is relatively low due to the availability of external funding for its sizable capital needs, including federal grants, state and regional grants, Proposition K sales tax funds from the San Francisco County Transportation Authority, and voter approved San Francisco general obligation bonds in the past. As of fiscal 2021, SFMTA's direct debt burden represented 0.4 times operating revenue.

Notably, in June 2022, San Francisco voters did not approve a $400 million GO bond measure that would fund SFMTA projects, signaling diminished local voter support for transit funding likely as the pandemic will permanently reduce transit ridership. The agency and city are still contemplating whether SFMTA would issue revenue bonds or seek voter-approved bonds at a future date to fund desired capital projects. Diminished local support for transit funding, if continued, will hamper SFMTA’s capacity to address significant capital backlogs.

Legal security
SFMTA's revenue bonds are secured by a gross pledge on diverse mix of operating and non-operating revenues including transit fares, parking revenues, parking and traffic fines, and dedicated taxes, but excluding transfers from the city's General Fund and certain other restricted revenues.

Legal protections as defined in the agency's bond resolution provide satisfactory security for bondholders. SFMTA covenants to adopt balanced budgets and manage its operations and set charges so that pledged revenues in each fiscal year, and available fund balances, will be at least equal to annual debt service and payment of all costs reasonably necessary to operate the transportation system. The additional bonds test is set at a strong 3.0 times maximum annual debt service for all outstanding revenue bonds and additional bonds.

Debt structure and debt service coverage
SFMTA's revenue bonds are long-term fixed obligations with a final maturity in 2051. The maximum annual debt service represents around 2.2% of fiscal 2021 operating revenue. SFMTA has a policy to maintain debt service at below 5% of its operating budget.

Pledged revenues for fiscal 2021, including federal relief funds, provided 28.3 times coverage of maximum annual debt service on the agency's outstanding revenue bonds. Excluding federal relief funds, fiscal 2021 pledged revenue provided 12.2 times coverage of MADS.

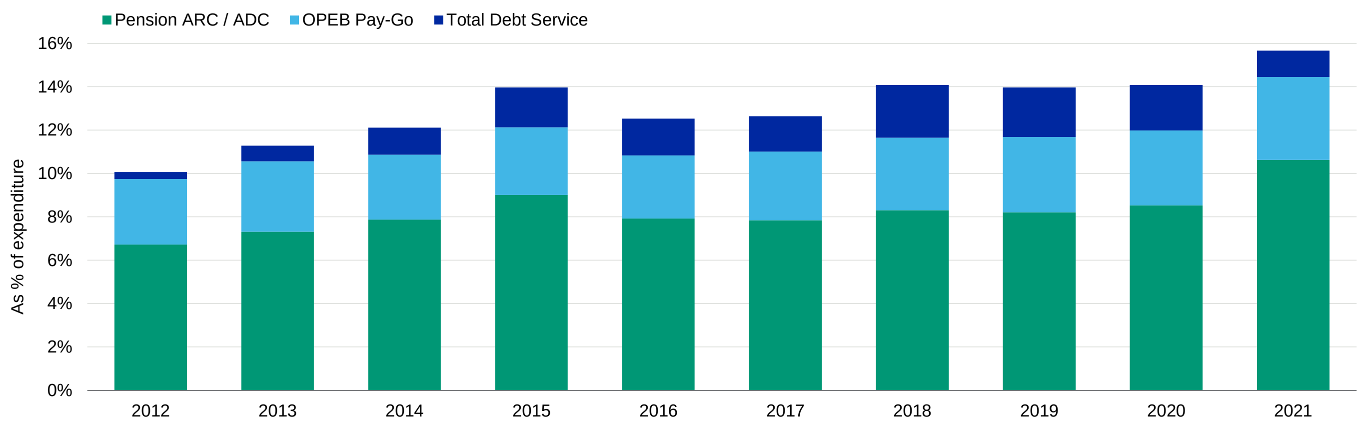
Using net revenue, the agency's debt service coverage was 3.2 times as of fiscal 2021.

Debt-related derivatives
SFMTA has no debt-related derivatives.

Pensions and OPEB
The trajectory of SFMTA's long term pension and other post-employment benefit (OPEB) solution is contingent upon City of San Francisco as SFMTA is a participant in the city's retirement and healthcare plans.

SFMTA's share of the city's pension liability is relatively elevated, with Moody's adjusted pension liability representing 363% of revenue as of fiscal 2021 reporting. For fiscal 2021, total fixed costs represented a relatively high 15.2% of adjusted operating expenses, mainly comprised of retiree benefits (see below exhibit). Positively, the agency's recent years pension contributions exceeded our treadwater calculation, meaning that reported liability will decline if investment targets are met.

Exhibit 7
SFMTA's fixed costs primarily consist of pension and OPEB contributions

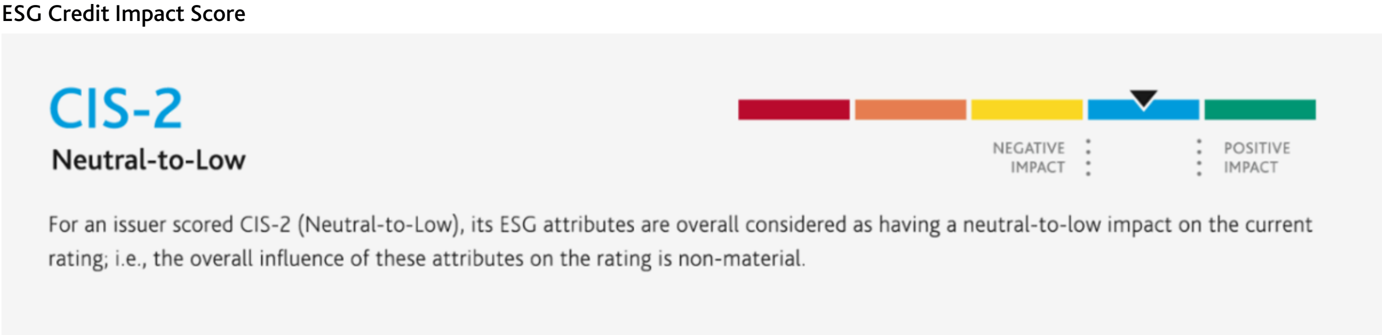


Source: SFMTA audit; Moody's Investers service

ESG considerations

SFMTA's ESG Credit Impact Score is neutral-to-low (CIS-2), reflecting moderately negative exposure to environmental and social risks and a positive governance profile.

Exhibit 8
ESG Credit Impact Score



Source: Moody's Investors Service

Exhibit 9
ESG Issuer Profile Scores

Source: Moody's Investors Service

Environmental

Exhibit 10
Environmental subscores

E-3	Physical climate risk	Carbon transition	Water management	Natural capital	Waste and pollution
	3	1	2	2	2

Source: Moody's Investors Service

SFMTA's environmental issuer profile score is moderately negative (E-3), reflecting the area's elevated exposure to sea level rise, which poses risk to some of SFMTA's capital assets, particularly its subway in downtown San Francisco. Positively, San Francisco is actively planning and implementing seawall improvements to mitigate this costly, long-range challenge.

SFMTA will benefit from carbon transition opportunities because its various energy-efficient transportation modes, including light rail, biodiesel-electric hybrid buses, electric trolley buses and cable cars will likely see increased usage as governmental policies and public preference shift from carbon inefficient travel. The agency is also committed to transitioning all buses to electric vehicles by 2035 as the transit system plays a critical role in the City and County of San Francisco's air quality and climate action plan that targets net-zero emissions by 2040. SFMTA is also likely to benefit from state and local initiatives to reduce vehicle emissions.

Social

Exhibit 11
Social subscores

S-3	Customer relations	Human capital	Health and safety	Responsible production	Demographic and societal trends
	3	3	3	2	2

Source: Moody's Investors Service

SFMTA's social issuer profile score is moderately negative (E-3), given the agency's labor intensive and customer-oriented operations that is not atypical for a transit enterprise. The mass transit sector serves a wide range of customers with diverse service needs, and relies on customer satisfaction to maintain ridership levels (i.e. utilization) and support fare increases. Changes in customer satisfaction can be monitored through on-time performance metrics, and is susceptible to public perception regarding the effectiveness and adequacy of operating performance. Deterioration in public opinion can lead directly to operating revenue declines that increase the need for politically sensitive fare increases. In addition, SFMTA directly employs the majority of its labor force that are represented by strong collective bargaining units and thus has less flexibility to control cost growth. The transit sector will benefit from social opportunities as a responsible producer of energy efficient services and low-cost transportation; however this does not offset the potential risks mentioned above.

SFMTA's issuer profile score also incorporates the demographic and societal trends of its service area. While San Francisco benefits from a diverse economy with very strong resident income levels, it has among the highest income inequality and homeless rate in the nation. The high cost of living in San Francisco contributes to SFMTA's worker shortage that has been exacerbated under the pandemic, while homelessness causes operational challenges and incurs extra costs. Lastly, SFMTA will likely see permanent ridership loss driven by changing residential and commuting patterns following the pandemic. Nonetheless, permanent ridership decline and the potential for social resistance to fare increases are somewhat balanced by the area's strong wealth that make tax subsidies more affordable.

Governance

Exhibit 12

Governance subscores

G-1	Financial strategy & risk management	Management credibility & track record	Organizational structure	Compliance & reporting	Board structure, policies & procedures
	2	1	1	2	3

Source: Moody's Investors Service

Governance is a material consideration for all mass transit credits. Prudent planning, proper asset management and assistance from local, state and federal governments provide strong foundations for mass transit credits to weather economic downturns and the challenges of running capital intensive operations. Overall, the transit sector benefits from governance opportunities through supportive organizational structures that promote strong operating environments and generous funding for operations and capital projects. Pandemic related federal government aid to mass transit systems particularly demonstrates the strong support for mass transit by government entities.

SFMTA's positive G-1 issuer profile score reflects its prudent fiscal management with conservative budgetary practices, long term financial and capital planning, and institutionalized policies for reserve, debt, and investments. Most recently, SFMTA has proactively addressed operational and financial challenges as a result of COVID-19.

SFMTA was established in 2002 through consolidation, by a city charter amendment, of the San Francisco Municipal Railway (Muni), and the Department of Parking and Traffic.

The agency is an enterprise department of San Francisco governed by a seven member board of directors, appointed by the San Francisco mayor and confirmed by the city's Board of Supervisors. Transits overseen by a government municipality face some risk associated with board structure. This results from the concentrated control of a city or county's government and the risk of political opposition to required fare increases or capital investment.

REPORT NUMBER 1327003

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