New Issue: Moody's assigns MIG 1 to Oakland City's (CA) TRAN

Global Credit Research - 02 Jun 2015

$159.0M short-term debt affected

OAKLAND (CITY OF) CA
Cities (including Towns, Villages and Townships)
CA

Moody's Rating

ISSUE	RATING
2015-2016 Tax and Revenue Anticipation Notes	MIG 1
Sale Amount $159,000,000	
Expected Sale Date 06/10/15	
Rating Description Note: Tax and/or Revenue Anticipation	

Moody's Outlook STA

NEW YORK, June 02, 2015 --Moody's Investors Service has assigned a MIG 1 rating to Oakland City's (CA) 2015-2016 Tax and Revenue Anticipation Notes (TRAN) totaling approximately $159.0 million. The Series A notes, par amount $49.4 million, are being issued to fund the city's fiscal year cash flow needs and are secured by a pledge of unrestricted fiscal 2016 general fund receipts. The Series B (Federally Taxable) notes, par amount $109.6 million, are being issued to pre-fund the city's annual CalPERS obligation for pension rate savings and are also secured by a pledge of unrestricted fiscal 2016 general fund receipts. Both series of notes will be issued simultaneously in July 2015 and will mature on June 30, 2016.

SUMMARY RATING RATIONALE

The MIG 1 rating reflects the city's strong short-term credit metrics and also the city's long-term credit quality. The rating also reflects the stable and ample cash margins projected for fiscal 2016 and ample alternate funds available for note repayment. The credit strength of the notes benefits from the sound predictability of revenues and timing of receipts for TRAN repayment, with noteholder protections that include the segregation of repayment funds into a dedicated fund held by the fiscal agent. We have incorporated the city's quality management, as measured by the accuracy of past projections and reasonable future cash flow assumptions, into the rating.

OUTLOOK

Outlooks are not assigned to short-term ratings.

WHAT COULD MAKE THE RATING GO UP

-N/A

WHAT COULD MAKE THE RATING GO DOWN

-Reduction of cash position

-Erosion of alternate sources of liquidity prior to set aside dates

-Large borrowing amount relative to pledged receipts

-Low projected yearend ending cash balance

STRENGTHS

-Annual note issuer

-Actual cash flows are consistently better than projections

-Conservative projections with reasonable assumptions

-Healthy amount of borrowable alternate liquidity

CHALLENGES

-Larger than typical TRAN borrowing

-Late set aside timing, though within 30 days of maturity

RECENT DEVELOPMENTS

Recent developments are incorporated in the Detailed Rating Rationale.

DETAILED RATING RATIONALE

LONG TERM CREDIT QUALITY: STRONG LONG-TERM CITY RATING

Oakland City has an Aa2 stable general obligation rating that was last reviewed in April 2015. The city's long-term rating reflects the recovery of the local economy and healthy financial position of the city that should remain stable, though will be challenged by increased demand for city services and rising pension and medical costs. The city also has manageable outstanding debt that includes general obligation bonds, pension obligation bonds, and lease-backed securities.

CASH FLOW: HEALTHY CASH POSITION BASED ON CONSERVATIVE ASSUMPTIONS

The city has strong projected cash balances at the time of note repayment that will likely be stronger than the current projections. The city projects to have approximately $914.1 million in total general fund cash receipts by the end of fiscal 2016 and an ending general fund cash balance of $163.7 million, which is 17.9% of total fiscal 2016 general fund receipts. Historic cash flow projections have traditionally been conservative compared to the actual cash flows, and these conservative assumptions add credit strength to the city's already solid cash flow estimates. We traditionally expect to see ending cash from pledged funds at least 5% of total receipts for the MIG 1 rating level. The receipt of revenues from property taxes is highly reliable with scheduled and timely collection dates and does not depend on voter approval. We note, however, the city's dependence on several economically sensitive revenues, but this weakness is offset by the positive growth these revenues are currently undergoing.

Adequate Alternate Sources of Liquidity

General fund cash receipts for June 2016 should be $109.4 million, which is smaller than the approximately $161.1 million due for note repayment on June 30, 2016. This weakness is offset by the additional credit strength of the city's alternate funds available, but not legally pledged, for TRAN repayment. Management expects to have approximately $77.9 million of available funds held outside the general fund for note repayment should the city need to access additional cash at maturity. We do not anticipate these funds will be needed for note repayment; however, the availability of these funds adds strength to the TRAN rating. The combined June 2016 and alternate liquidity provide a strong 116.3% of available cash for note repayment should the city be unable to set aside cash for TRAN repayment as described below.

Larger Borrowing Relative to Past Borrowings; Borrowing Still Small Relative to Pledged Receipts

Because of the additional cash borrowing to pre-fund the city's fiscal 2016 CalPERS pension contributions for pension rate savings, the current borrowing is larger than the city's typical borrowing amount. That current borrowing, however, is still small relative to pledged receipts. The $159.0 million note is 17.3% of the pledged fiscal 2016 general fund receipts available for note repayment. A typical borrowing size for a Moody's-rated MIG 1 note is generally less than 35% of pledged revenues.

DEBT AND LEGAL COVENANTS: ADEQUATE SET ASIDE PLAN FOR REPAYMENT

The credit rating of the notes benefits from a short maturity and the timely set aside of the pledged receipts. We anticipate that the city will set aside funds for TRAN repayment 30 days in advance of note maturity. For the tax-exempt Series A, the city is planning to set aside $79.5 million in March 2016 and $81.6 million in May 2016 from receipts in each of these respective months. For the taxable Series B, the City is planning to set aside monthly principal payments from July 2015 through May 2016 and interest in May 2016 from receipts in each of these respective months. These set asides are adequately in advance of note repayment by meeting our 30 day threshold for a MIG 1 rating. The set asides will be deposited in trust in the city's "2015-2016 Tax and Revenue Anticipation Notes Special Account" held by the fiscal agent. Any money deposited by the fiscal agent into the account will be for the benefit of the note holders.

Debt Structure

The notes will be issued in July 2015 and will mature on June 30, 2016.

Debt-Related Derivatives

The city has one stand-alone swap that is not associated with any outstanding bonds. The rating termination triggers for the swap are a function of the city's and the swap provider's (Goldman Sachs Mitsui Marine Derivative Products) ratings, with the city's option to terminate if the counterparty's rating falls below A3 and the counterparty's option to terminate if the city's rating falls below Baa3. The most recent mark to market valuation was -$7.7 million as of May 29, 2015, which is not burdensome given the city's available unrestricted cash and reserves. Under the swap, the city pays the counterparty a fixed payment of 5.6775% and receives a variable payment computed at 65% of LIBOR rate (total rate not to exceed 12%). The city's payments to the counterparty are insured.

Pensions and OPEB

Pension-driven budgetary pressures for Oakland City could prove to be a budgetary burden.

Moody's adjusted net pension liability (ANPL) for the city, under our methodology for adjusting reported pension data, is $3.2 billion, or an above-average 4.4 times operating revenues. Rate increases will increase the funded ratio to 75% for each the city's California Public Employees' Retirement System (PERS) plans, which are currently at 67.9% for the Safety Plan and 69.5% for the Miscellaneous Plan. The city makes 100% of its annual pension costs for each of the PERS plans. These annual costs in fiscal 2014 were $98.6 million (16.4% of operating revenues), which is slightly above-average relative to other California cities. The city also maintains its Police and Fire Retirement System (PFRS) plan, which should be fully funded by 2026. The city issued its Pension Obligation Bonds to prepay PFRS contributions in July 2012 and reduced the unfunded liability by $210.0 million. PFRS obligations are supported by dedicated tax override revenues ("TOR).

Oakland has a large unfunded OPEB liability of $463.8 million, and is currently making approximately half of its annual required contribution (ARC) of $40.5 million (6.7% of 2014 revenues). The city's goal is to fully-fund its ARC. The city has budgeted $8.0 million one-time and $5.0 million ongoing in its fiscal 2016 budget and $3.0 million ongoing in its fiscal 2017 toward its OPEB liability. Additionally, the city paid $2.9 million to date toward the unfunded liability and has budgeted to pay $665,000 annually until June 30, 2022.

MANAGEMENT: SATISFACTORY CASH PROJECTIONS AND REASONABLE ASSUMPTIONS

Management's past projections have been conservative and reflect reasonable assumptions. The beginning cash balance in the projected cash flows for fiscal 2015 is less than the ending cash balance in the fiscal 2014 year audit. The city projects to have generally lower cash receipts in fiscal 2015 than the actual cash receipts in fiscal 2014 audit as a conservative measure. The ratios calculated using these conservative cash flow estimates are still strong, and can only improve, which we anticipate given the historically conservative nature of the city's estimates. Actual cash receipts have consistently been higher than the original projections for the past several fiscal years.

KEY STATISTICS

-Long-Term Rating or Equivalent: MIG 1

-Cash Balance/Receipts at Time of Repayment: MIG 1

-Predictability of Revenues: MIG 2

-Timing of Receipts: MIG 1

-Amount Borrowed/Receipts: MIG 1

-Reliability of Beginning Cash Balance: MIG 1

-Accuracy of Past Projections: MIG 1

-Reasonableness of Future Projections: MIG 1

-Segregation of Funds: MIG 1

OBLIGOR PROFILE

The City of Oakland is located in the County of Alameda on the eastern shore of the San Francisco Bay, approximately seven miles from downtown San Francisco via the San Francisco-Oakland Bay Bridge. Occupying approximately 53.8 square miles, the city is the largest and most established of the "East Bay" cities.

LEGAL SECURITY

The notes are secured by a pledge of unrestricted fiscal 2016 general fund receipts.

USE OF PROCEEDS

The Series A notes are being issued to fund the city's fiscal year cash flow needs and are secured by a pledge of unrestricted fiscal 2016 general fund receipts. The Series B (Federally Taxable) notes are being issued to pre-fund the city's annual CalPERS obligation for pension rate savings and are also secured by a pledge of unrestricted fiscal 2016 general fund receipts.

PRINCIPAL METHODOLOGY

The principal methodology used in this rating was Short-Term Cash Flow Notes published in April 2013. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the rating action on the support provider and in relation to each particular rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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