

**ADDITIONAL (VOLUNTARY) DISCLOSURE  
RATING AFFIRMED**

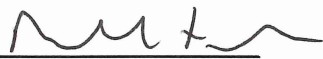
Dated: August 17, 2015

NOTICE IS HEREBY GIVEN that on August 10, 2015, Standard & Poor's Ratings Services ("S&P") affirmed the City of Sacramento's long-term issuer credit rating at "AA-", with a stable outlook. In addition, S&P also affirmed the rating and outlook of lease revenue bonds issued by the Sacramento City Financing Authority at "A+" and "Stable outlook", respectively. The Sacramento City Financing Authority is the issuer for the following issues:

- 1993 Lease Revenue Refunding Bonds, Series A
- 1993 Lease Revenue Refunding Bonds, Series B
- 2002 Capital Improvement Revenue Bonds
- 2003 Capital Improvement Revenue Bonds
- 2006 Capital Improvement Revenue Bonds, Series A
- 2006 Capital Improvement Revenue Bonds, Series B
- 2006 Capital Improvement Revenue Bonds, Series C
- 2006 Capital Improvement Revenue Bonds, Series D
- 2006 Capital Improvement Revenue Bonds, Series E

Attached to this notice is the report from S&P, including the full analysis for the ratings.

City of Sacramento



Russell T. Fehr  
City Treasurer

Attachment: Sacramento City Financing Authority; Appropriations; General Obligation rating report

# RatingsDirect®

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## Summary:

# Sacramento City Financing Authority Sacramento; Appropriations; General Obligation

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## Summary:

# Sacramento City Financing Authority Sacramento; Appropriations; General Obligation

## Credit Profile

US\$282.04 mil lse rev bnds (Sacramento) ser 2015 due 04/01/2050

<i>Long Term Rating</i>	A+/Stable	New
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US\$222.765 mil rfdg rev bnds (Sacramento) (Master Lease Program Facilities) ser 2015 dtd 09/03/2015 due 12/01/2036

<i>Long Term Rating</i>	A+/Stable	New
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Sacramento ICR

<i>Long Term Rating</i>	AA-/Stable	Affirmed
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## Rationale

Standard & Poor's Ratings Services assigned its 'A+' rating to the Sacramento Public Financing Authority, Calif.'s 2015 lease revenue bonds, issued for the Golden 1 Center. At the same time, Standard & Poor's assigned its 'A+' rating to the Sacramento City Financing Authority's 2015 refunding revenue bonds (master lease program facilities). In addition, Standard & Poor's affirmed its 'AA-' issuer credit rating (ICR) on Sacramento. Finally, Standard & Poor's affirmed its 'A+' long-term rating and underlying rating (SPUR) on Sacramento City Financing Authority's lease revenue bonds outstanding, issued on behalf of the city. The outlook is stable.

The 2015 bonds Golden 1 Center have an interest in lease payments to be made by the city to the Sacramento Public Financing Authority pursuant to a lease agreement for leased assets consisting of the Golden 1 Center, which is currently under construction in Sacramento. The agreement includes capitalized interest until Oct. 1, 2017, and the city expects substantial completion by Sept. 23, 2016. Outside consultants have concluded that the overall construction risk for the project is low.

The 2015 refunding revenue bonds (master lease program facilities) have an interest in lease payments to be made by the city to the Sacramento City Financing Authority pursuant to a lease agreement for leased assets consisting of almost \$749 million of city property. There is sufficient value in the leased assets which are consistent with our seismic risk assessment during the life of the bonds.

Under both lease purchase agreements, the leases are subject to annual appropriation. However, the city has covenanted to budget and appropriate annual lease payments. In addition, the leases are subject to abatement for damage or destruction, which we believe is mitigated by the city's covenant to maintain rental interruption insurance equal to 24 months of lease payments and casualty insurance for certain loss or damage equal to the replacement cost of the leased assets.

The 2015 Golden 1 Center bonds will be issued initially in a variable-rate mode at a fixed spread to LIBOR with a mandatory tender on Oct. 2, 2017. The variable-rate bonds may be remarketed to fixed-rate bonds by the city any time

before the mandatory tender date with 10 days' notice. Failure by the city to purchase the 2015 bonds on the mandatory tender date is not an event of default; however, bonds will then begin accruing interest at the maximum rate, until the bonds have been redeemed.

The 2015 Golden 1 Center bonds have been the subject of a lawsuit questioning the validity of the city's right to build the arena and issue the bonds. Following the trial, the city reached an agreement with the plaintiffs, and the lawsuit was dismissed with prejudice on Aug. 6. The dismissal is not subject to appeal.

The ratings reflect our opinion of the city's:

- Strong economy, with access to a broad and diverse metropolitan statistical area (MSA);
- Strong management, with "good" financial policies and practices under our financial management assessment (FMA) methodology;
- Strong budgetary performance, with an operating surplus in the general fund and a slight operating surplus at the total governmental fund level;
- Strong budgetary flexibility, with an available fund balance in fiscal 2014 of 13.5% of operating expenditures;
- Very strong liquidity, with total government available cash of 100.2% of total governmental fund expenditures and 12.4x governmental debt service, as well as access to external liquidity we consider strong;
- Very weak debt and contingent liability position, with debt service carrying charges of 8.1% of expenditures and net direct debt that is 158.4% of total governmental fund revenue, as well as a large pension and other postemployment benefit (OPEB) liability and the lack of a plan to sufficiently address the obligations; and
- Strong institutional framework score.

### **Strong economy**

We consider Sacramento's economy strong. The city, with an estimated population of 482,381, is located in Sacramento County in the Sacramento--Roseville--Arden-Arcade,MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 86% of the national level and per capita market value of \$81,933. Overall, the city's market value grew by 7% over the past year to \$39.5 billion in 2015. The county unemployment rate was 7.3% in 2014.

Sacramento is in Sacramento County and is located in the northern section of California's Central Valley at the confluence of the Sacramento and American rivers. Because Sacramento is the state's capital, its employment base centers on government, with roughly a quarter of jobs in the area in the government sector. The city's tax base is very diverse with the top 10 taxpayers accounting for only 4% of assessed value.

### **Strong management**

We view the city's management as strong, with "good" financial policies and practices under our FMA methodology, indicating financial practices exist in most areas, but that governance officials might not formalize or monitor all of them on a regular basis. To plan for revenue growth, management works closely with the county assessor to determine property tax revenue and with an outside consultant to project sales tax revenue. On a formal basis, the budget is adjusted during a mid-year review, although it can be adjusted more often if necessary. The budget is monitored on an informal basis continuously throughout the fiscal year. The mid-year review focuses on structural balance and meeting financial targets such as funding reserve levels. In addition, the city maintains a five-year general fund forecast with a focus on balancing operations and is updated annually. The city maintains a five-year capital improvement plan, which

it updates annually and identifies funding sources. The city's investment management policy and practices include at-least quarterly reporting to the city council, which reviews the portfolio for performance and compliance with state law. The city has a debt management policy. Finally, the city has a 10% general fund contingency reserve policy and has been building the reserve's balance over the past four years to meet that policy.

### **Strong budgetary performance**

Sacramento's budgetary performance is strong in our opinion. The city had surplus operating results in the general fund of 3.4% of expenditures and slight surplus results across all governmental funds of 0.9% in fiscal 2014. The city's general fund operating results have been stable over the past three years, with surpluses of 2.1% in 2013 and 2.3% in 2012.

The 2014 audit is the third year in a row that the city has posted a general fund surplus. The city expects to post another surplus in fiscal 2015, and we expect that this trend will continue over the near term. The 2016 budget shows a \$3.7 million deficit, but excluding \$8.1 million of one-time expenditures, ongoing operations show a small surplus.

### **Strong budgetary flexibility**

Sacramento's budgetary flexibility is strong, in our view, with an available fund balance in fiscal 2014 of 13.5% of operating expenditures, or \$51.3 million. We do not expect that budgetary flexibility will decrease in the next few years given the city's continued budgeted surpluses. However, we do not expect that reserves will increase to very strong levels as surpluses are relatively small compared with the budget as a whole, and the city plans to use some of the fund balance for one-time expenditures in fiscal 2016.

### **Very strong liquidity**

In our opinion, Sacramento's liquidity is very strong, with total government available cash at 100.2% of total governmental fund expenditures and 12.4x governmental debt service in 2014. In our view, the city has strong access to external liquidity if necessary. The city has issued certificates of participation and water and sewer debt during the past eight years, showing its strong access to the market. The city has a diversified portfolio, which we do not consider to be aggressive. The majority of investments have maturities less than five years, with about one-third maturing in less than five years. The county does have some investments in equities, but it is less than 10% of total investments.

In May 2007, the city entered into a swap agreement for its \$73.725 million series 1997 lease revenue bonds financing for Arco Arena (home of the National Basketball Assn. Sacramento Kings). The city uses lease payments it receives from the Kings to cover debt payments, but ultimately the city is obligated to budget and appropriate debt service payments from its general fund, regardless of payments made by the Kings. The swap terminates July 19, 2017, when the bonds are subject to a mandatory tender. At the time of the mandatory tender, the city intends to refund the bonds through a fixed- or variable-rate bond issue and has pledged in bond documents to do so at least 90 days prior to the tender date. As of July 15, 2014, the current notional amount of the swap is \$57.315 million, or less than 10% of Sacramento's general fund-related debt portfolio. The 1997 bonds are the only bonds that were issued in a variable-rate mode, and these have been synthetically fixed.

The 1997 bonds were issued in a variable-rate mode with interest rates that reset every three months at the rate of LIBOR plus 25 basis points. The city synthetically fixed the interest rate at 5.607% by entering into an interest rate swap with counterparty Golden Sachs Capital Markets L.P., now Goldman Sachs Bank USA, a direct subsidiary of the

Goldman Sachs Group Inc. (A-#?#Negative). The city does not have a swap management policy and does not have specific plans to enter into additional swaps at this time. In our opinion, the likelihood of the city being required to make a termination payment is relatively remote, considering that the city's underlying 'A+' credit rating would need to fall to 'BB+' before a termination payment would be triggered.

### **Very weak debt and contingent liability profile**

In our view, Sacramento's debt and contingent liability profile is very weak. Total governmental fund debt service is 8.1% of total governmental fund expenditures, and net direct debt is 158.4% of total governmental fund revenue. The city participates in the California Public Employees' Retirement System and contributes 100% of its annual required pension contribution. We recognize that the city has adjusted its pension and OPEB cost structure, including eliminating OPEB benefits for new hires in most employee groups, and most city employees are now required to contribute to the California Public Employees' Retirement System. However, this will continue to be a large and growing cost for the city over the near term.

In our opinion, a credit weakness is Sacramento's large pension and OPEB liability, without a plan in place that we think will sufficiently address the obligation. Sacramento's combined pension and OPEB contributions totaled 12.1% of total governmental fund expenditures in 2014. Of that amount, 9.8% represented contributions to pension obligations and 2.2% represented OPEB payments. The city made its full annual required pension payment in 2014. The pension funded ratio is 72%.

### **Strong institutional framework**

The institutional framework score for California municipalities required to submit a federal single audit is strong.

## **Outlook**

The stable outlook reflects our view of the city's strong budgetary flexibility, with small surpluses projected over the next few years. Further strengthening the ratings is our view of the city's strong management practices and good financial policies. We do not expect to change the ratings within our two-year outlook horizon due to our anticipation that the city will maintain adequate reserves and a very weak debt profile with high pension and OPEB costs. Should the city management be unable to maintain balanced operations and significantly draw on reserves, we could consider lowering the rating. Conversely, should the city be able to improve its debt and liabilities position, including reducing pension and OPEB costs, we could consider raising the rating.

## **Related Criteria And Research**

### **Related Criteria**

- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- USPF Criteria: Local Government GO Ratings Methodology And Assumptions, Sept. 12, 2013
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009
- USPF Criteria: Appropriation-Backed Obligations, June 13, 2007
- USPF Criteria: Debt Statement Analysis, Aug. 22, 2006
- USPF Criteria: Financial Management Assessment, June 27, 2006

## Related Research

Institutional Framework Overview: California Local Governments

### Ratings Detail (As Of August 10, 2015)

#### Sacramento City Fincg Auth, California

Sacramento, California

Sacramento City Fincg Auth (Sacramento) cap Improv rev bnds (Comnty Reinvestment Cap Improv Prgm) ser 2006 B

<i>Long Term Rating</i>	A+/Stable	Affirmed
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#### Sacramento City Fincg Auth cap Imp (300 Richards Blvd Bldg Acquisition) ser 2006C

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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#### Sacramento City Fincg Auth (Comnty Reinvestment Cap Improv Prgm) ser 2006A

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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#### Sacramento City Fincg Auth (Master Lse Prog Facs) ser 2006E

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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#### Sacramento City Fincg Auth (Sacramento) 2003 cap imp rev bnds (911 Call Ctr & other mun proj) dtdt 09/30/2003 due 12/01/2008-2024 2027 2033

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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#### Sacramento City Fincg Auth (300 Richards Blvd Bldg Acquisition) ser 2006D

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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#### Sacramento City Fing Auth (City Hall & Redev Proj) ser 2002A dtd 07/02/2002 due 12/01/2003-2022 2028 2032

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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#### Sacramento Fincg Auth, California

Sacramento, California

Sacramento Fin Auth lse rev rfdg bnds ser 1993B (MBIA) (National) (SEC MKT)

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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Sacramento Fin Auth (Sacramento)

<i>Long Term Rating</i>	A+/Stable	Affirmed
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Sacramento Fin Auth (Sacramento) lse rfdg ser 1993A (AMBAC)

<i>Unenhanced Rating</i>	A+(SPUR)/Stable	Affirmed
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Many issues are enhanced by bond insurance.

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