Tax Supported
New Issue

San Diego, California

Ratings

New Issue	
2010–11 Tax and Revenue Anticipation Notes, Series A, B, and C	F1+
Outstanding Debt	
San Diego	
General Obligation Bonds	AA–
Certificates of Participation (1993 Balboa Park/Mission Bay Park), Series 2003	A+
San Diego Public Facilities Financing Authority	
Lease Revenue Bonds, Series 2002B	A+
Lease Revenue Bonds, Series 2007A	A+
Lease Revenue Refunding Bonds, Series 2010A (Master Refunding Project)	A+
San Diego Metropolitan Transit Development Board	
Lease Revenue Refunding Bonds, Series 2003	A+
Convention Center Expansion Financing Authority	
Lease Revenue Bonds, Series 1998A	A+

Rating Outlook

Stable

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New Issue Details

Sale Information: $166,885,000 2010–11 Tax and Revenue Anticipation Notes, Series A, B, and C via negotiation the week of June 21.
Security: Payable from unrestricted revenues, including taxes, income, revenue, cash receipts, and other monies attributable to fiscal 2011.
Purpose: Finance the city's cash flow and working capital needs.
Final Maturity: Series A: Jan. 31, 2011; series B: April 29, 2011; and series C: May 31, 2011. Not subject redemption prior to maturity.

Rating Rationale

- Fitch's highest short-term rating reflects San Diego's sound repayment structure, strong coverage of note repayment set asides, and substantial available and borrowable funds, which largely offset any risk of significant taxation revenue adjustments.
- The city benefits from above-average socio-economic characteristics, a diverse economy, diverse revenue streams, and its desirable location as a place to live and work, or visit.
- While the city's largest employers are in the traditionally stable military, education, government, and healthcare sectors, the city's unemployment rate has risen significantly during the economic downturn.
- Simultaneously, the city's key general fund revenue sources have declined and are projected to stabilize at their current much lower levels through fiscal 2011. Nevertheless, the city continues to demonstrate its commitment to conservative financial management policies, multiyear budget planning, midyear budget modifications, and general fund balance and reserves preservation.
- Absent revenue increases to offset rising pension payment costs, the city is delaying progress toward achieving its reserve level policy goals. However, the city is balancing its fiscal 2011 budget without eroding its reserves below fiscal 2010 levels.
- The debt burden is low to moderate, with moderately below-average amortization.

Key Rating Drivers

- Maintenance of general fund structural balance within the context of pressured general fund revenues.
- Continued progress toward achieving policy target reserve levels and reduction of existing unfunded pension and OPEB liabilities.

Credit Summary

San Diego is the second largest city in California, with a population of approximately 1.3 million. While the city has diverse employment and tax revenue bases and above-average socio-economic characteristics, some of its largest operating revenues are declining due to decreased taxable property values (negative 0.6% in fiscal 2010, with no growth projected in fiscal 2011), softened tourist business and retail sales activity, and contraction in most employment sectors, resulting in a high unemployment rate of 10.4% in April 2010.

The city ended fiscal 2009 with an $80.5 million unreserved general fund balance, which represents 7.1% of spending. This was in line with the city's fiscal 2008 results and provides good flexibility. Despite significant expenditure reductions throughout fiscal 2010 to respond to marked declines in nearly all of the city's general fund revenues, the city still has a $7.8 million budget deficit to close due to further unexpected declines in general fund revenues. However, the city will not need

Related Research

Applicable Criteria

- *Tax-Supported Rating Criteria, Dec. 21, 2009*
- *U.S. Local Government Tax-Supported Rating Criteria, Dec. 21, 2009*

Other Research

- *San Diego Public Facilities Financing Authority, California, California, May 4, 2010*
- *San Diego, California, June 10, 2009*

Rating History — GO Bonds

Rating	Action	Outlook/ Watch	Date
AA–	Affirmed	Stable	6/7/10
AA–	Affirmed	Stable	4/30/10
AA-	Revised	Stable	4/30/10
A+	Affirmed	Stable	6/8/09
A+	Upgraded	Stable	12/11/08
BBB+	Affirmed	Positive[a]	3/27/08
BBB+	Downgraded	Negative	5/27/05
A	Downgraded	Negative	2/16/05
AA	Affirmed	Negative[a]	9/23/04
AA	Downgraded	Negative	2/27/04
AAA	Upgraded	—	5/28/02
AA+	Assigned	—	4/3/98

[a]Rating Watch.

Rating History — Lease Revenue Bonds and COPs

Rating	Action	Outlook/ Watch	Date
A+	Affirmed	Stable	6/7/10
A+	Affirmed	Stable	4/30/10
A+	Revised	Stable	4/30/10
A	Affirmed	Stable	6/8/09
A	Upgraded	Stable	12/11/08
BBB-	Affirmed	Positive[a]	3/27/08
BBB-	Downgraded	Negative[a]	5/27/05
A-	Downgraded	Negative[a]	2/16/05
AA-	Affirmed	Negative[a]	9/23/04
AA-	Downgraded	Negative	2/27/04
AA+	Assigned	—	5/28/02
AA+	Assigned	—	4/3/98

[a]Rating Watch.

Rating History — TRANs

Rating	Action	Outlook/ Watch	Date
F1+	Assigned	—	6/7/10

to draw down on its reserves to do so because of planned expenditure and transfer reductions.

The city has already closed a $179.1 million budget gap for fiscal 2011 with a combination of ongoing and one-time budget adjustments, including $24.6 million in fiscal 2010 savings set aside for fiscal 2011. However, a January 2010 annual actuarial valuation of the pension system indicated that the general fund would need to contribute $9.8 million more than budgeted to the annually required pension contribution in fiscal 2011. The pension system's unfunded liability has increased significantly ($2.1 billion, up from $1.3 billion the prior year) due to market losses. That increased pension contribution, combined with lower than expected tax revenues In the first half of fiscal 2010, lowering the revenue baseline for fiscal 2011 resulted in a further $28.2 million budget gap in fiscal 2011, which will be closed by a mix of expenditure reductions.

The city's five-year outlook forecasts operating deficits for fiscal years 2012–2015, even after assuming no personnel cost increases, which Fitch believes is unlikely. While the city has a record of solving such deficits without adversely affecting its general fund balances and reserves, the options available to it will diminish over time, absent significant revenue increases.

The city states that maintenance of required reserves at fiscal 2010 levels is a priority but, due to general fund revenue declines, has postponed by one year increasing reserves levels in fiscal 2011 as had been previously planned.

The direct debt burden is low at $411 per capita, or 0.3% of market value. Taking debt issued by overlapping entities into account, overall net debt is a more moderate $3,496 per capita, or 2.6% of market value. Debt amortization is below average at 42% in 10 years. Debt levels are expected to remain affordable despite anticipated future debt issuances.

2010–11 Tax and Revenue Anticipation Notes, Series A, B, and C

The 2010–11 tax and revenue anticipation notes, series A, B, and C, (the notes) are designed to finance the city's cash flow and working capital needs, including the fiscal 2011 pension obligation payment that is made up front.

The city expects to set aside the $51.5 million needed to repay principal and interest on the 2010–11 notes, series A, beginning Jan. 1, 2011 in advance of those notes' Jan. 31, 2011 final maturity. Similarly, the $47 million principal and interest set aside for the series B notes will begin April 1, 2011 in advance of the April 29, 2011 final maturity, and the $71.7 million principal and interest set aside for the series C notes will begin May 1, 2011 in advance of the May 31, 2011 final maturity. Based on May 28, 2010 fund balances, the city expects to have approximately $621 million available for short-term interfund borrowing. Even without such borrowable resources, note coverage is high under Fitch's stress scenarios, including significant declines across all revenue sources, without the city taking any expenditure actions in response.

The city covenants not to issue any parity debt but reserves the right to issue subordinated 2010–11 notes secured by a junior lien against the same pledge. However, the city does not expect issuing such subordinated notes will be necessary.