San Diego, California

Leave Revenue Bonds

New Issue Report

Ratings

New Issues

San Diego Public Facilities Financing Authority Lease Revenue Bonds, Series 2012A (Capital Improvement Projects)	A+
San Diego Public Facilities Financing Authority Lease Revenue Refunding Bonds, Series 2012B (Fire and Life Safety Facilities Refunding)	A+
Convention Center Expansion Financing Authority Lease Revenue Refunding Bonds, Series 2012A	A+

Outstanding Debt

San Diego Implied General Obligations	AA–
San Diego Certificates of Participation (1993 Balboa Park/Mission Bay Park Refunding), Series 2003	A+
San Diego Public Facilities Financing Authority Lease Revenue Bonds, Series 2002B (Fire and Life Safety Facilities Projects)[a]	A+
San Diego Public Facilities Financing Authority Lease Revenue Refunding Bonds, Series 2007A	A+
San Diego Public Facilities Financing Authority 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[b]	A+

[a]To be refunded by the San Diego Public Facilities Financing Authority's Lease Revenue Refunding Bonds, Series 2012B.
[b]To be refunded by the Convention Center Expansion Financing Lease Revenue Refunding Bonds, Series 2012A.

Rating Outlook

Stable

Related Research

Fitch Rates San Diego, California Implied GO at 'AA–', Outlook Stable, April 13, 2012

San Diego, California, June 9, 2010

Analysts

Alan Gibson
+1415 732-7577
alan.gibson@fitchratings.com

Stephen Walsh
+1 415 732-7573
stephen.walsh@fitchratings.com

Amendment

The report was amended to correct the rating on the San Diego Implied General Obligations under Outstanding Debt in the Ratings on page 1.

New Issue Details

Sale Information: Approximately $89,000,000 San Diego Public Facilities Financing Authority Lease Revenue Bonds, Series 2012A and B, via negotiation the week of June 18; Approximately $141,000,000 Convention Center Expansion Financing Authority Lease Revenue Refunding Bonds, Series 2012A, via negotiation the week of June 4.

Security: San Diego's lease rental payments that the city covenants to budget and appropriate annually, subject to abatement, which is mitigated by standard rental interruption insurance.

Purpose: San Diego Public Facilities Financing Authority (SDFFA) Lease Revenue Bonds, Series 2012A, to fund deferred capital improvement program projects; SDFFA Lease Revenue Refunding Bonds, Series 2012B, and Convention Center Expansion Financing Authority (CCEFA) Lease Revenue Refunding Bonds, Series 2012A, for economic refundings.

Final Maturity: SDFFA Lease Revenue Bonds, Series 2012A: April 1, 2042; SDFFA Lease Revenue Refunding Bonds, Series 2012B: April 1, 2032; CCEFA Lease Revenue Refunding Bonds, Series 2012A: April 1, 2028.

Key Rating Drivers

Fundamental Credit Strengths: The city benefits from a diverse economy, a variety of revenue streams, and its desirable location as a place to live and work or visit. While taxable assessed valuation (TAV) trends have performed relatively well, Fitch Ratings expects relatively stagnant performance over the near term.

Elevated Unemployment Rate: The city's unemployment rate rose significantly during the economic downturn and remains elevated.

Solid Financial Operations: The city ended fiscal 2011 essentially breaking even and maintaining an adequate unrestricted general fund balance. The city projects similar performance for fiscal 2012.

Administrative Challenges Remain: Fitch expresses some reservations about the city's ability to fully implement disclosure initiatives, given recent system implementation problems that delayed audits. The city's plan to resume timely audit reporting in November 2012 is an important positive step.

Significant Liabilities: The overall debt burden is moderate and expected to remain so despite planned debt issuances to address what the city reports as significant unmet infrastructure maintenance needs.

What Could Trigger a Rating Action

Potential Areas of General Fund Exposure: Additional general fund support for debt currently reimbursed by redevelopment moneys, the city's storm water program, and construction projects if state funding ceases due to possible voter approval of a ban on project labor agreements, could place downward pressure on the city's bond ratings.

Rating History — GOs

Rating	Action	Outlook/ Watch	Date
AA–	Affirmed	Stable	5/29/12
AA–	Affirmed	Stable	4/13/12
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	3/27/08
BBB+	Downgraded	Negative	5/27/05
A	Downgraded	Negative	2/16/05
AA	Affirmed	Negative	9/23/04
AA	Downgraded	Negative	2/27/04
AAA	Upgraded	—	5/28/02
AA+	Assigned	—	4/3/98

Rating History — COPs and Lease Revenue Bonds

Rating	Action	Outlook/ Watch	Date
A+	Affirmed	Stable	5/29/12
A+	Affirmed	Stable	4/13/12
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	3/27/08
BBB–	Downgraded	Negative	5/27/05
A–	Downgraded	Negative	2/16/05
AA–	Affirmed	Negative	9/23/04
AA–	Downgraded	Negative	2/27/04
AA+	Assigned	—	5/28/02

Related Criteria

Tax-Supported Rating Criteria, Aug. 15, 2011

U.S. Local Government Tax-Supported Rating Criteria, Aug. 15, 2011

Credit Profile

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 significant ongoing economic development, its socioeconomic characteristics are somewhat mixed, and its unemployment rate was still elevated at 9.5% in March 2012.

Relatively Mild Tax Base Fluctuations

The city's tax base has survived in relatively good shape despite the pressures on the wider county's property market during the economic downturn. Two years of small TAV declines (0.6% in fiscal 2010 and 2.1% in fiscal 2011) were followed by a slight rebound in fiscal 2012 (up 0.8%). The city recently adjusted its projection for fiscal 2013 TAV to a 1.1% decline from the 2.3% increase estimated earlier this year. The change reflects the county's revised projections in light of unexpected further median house price declines. The county's ongoing elevated levels of appeals, foreclosures, and delinquencies suggest that the city's tax base could continue to experience stress despite ongoing construction and a positive housing price trend.

Solid Financial Operations

As shown in the income statement table, the city ended fiscal 2011 with a solid unrestricted general fund balance (the sum of committed, assigned, and unassigned general fund balances under GASB 54) of $99.9 million, equaling 8.9% of spending. Excluding an $87.3 million transfer to the general fund of regional development authority (RDA) cash for projects not yet started (held in a separate trust account and subject to potential state claw back), fiscal 2011 operations were essentially break even.

The city projects a $17.8 million budget surplus for fiscal 2012 due to modest increases in property, sales, and hotel tax revenues, savings from previously implemented expenditure-reduction measures, additional personnel savings from a higher than anticipated number of retirements, and lower energy and utility expenses. No use of the projected $17.8 million is being recommended for the remainder of fiscal 2012. Instead, $12.8 million is included in the fiscal 2013 proposed budget (comprising $3.7 million for delayed expenses, $8.3 million for deferred capital projects, and $0.8 million for the general fund reserve), and $5.0 million is recommended to be added to reserves available for unforeseen circumstances or to mitigate the potential impact of the state denying redevelopment support for city debt. The city plans to adopt a final budget by June 15.

In addition to consistently exceeding its 8% general fund reserve goal, the city recognizes the need to bolster reserves for its public liability, workers' compensation, long-term disability, and enterprise funds and has concrete plans to incrementally build them up.

The city's five-year forecast shows general fund revenues offsetting known cost increases and benefitting from continued economic improvement as well as decreased annual pension contributions as a result of prior reforms. If realized, general fund operations would break even in fiscal 2013 and net surpluses after transfers would grow annually thereafter, gradually improving to a net surplus after transfers of $67 million in fiscal 2017. Given the recent adjustment of TAV projections to negative from positive and mixed economic indicators, Fitch believes certain revenue assumptions might prove aggressive but notes that projected overall revenue growth is modest.

Re-establishment of Timely Audits

Following pension disclosure failures that significantly delayed its audits for fiscal years 2003–2008, the city made significant investments in its financial reporting and accounting systems. However, after issuing its fiscal 2009 audit on a timely basis, problematic implementation of a new enterprise resource planning system delayed the fiscal 2010 audit by nine months and the fiscal 2011 audit by one month.

From a management and administration perspective, Fitch notes with concern the training weaknesses and inadequate management controls that led to the initial inaccurate data entry problem, the length of time taken to resolve the problem, and the failure to risk manage the implementation more successfully. The city expects to issue its fiscal 2012 comprehensive annual financial report (CAFR) on a timely basis in November 2012, ahead of the industry standard of December 2012.

Moderate Debt Burden, Significant Pension and OPEB Liabilities

Due to past market access impediments, the city's overall debt burden is moderate at $3,894 per capita, or 3.2% of fiscal 2011 market valuation. Debt amortization is average. In fiscal years 2011 and 2012, the city issued an elevated $161 million–$163 million in short-term tax revenue anticipation notes (TRANs) annually because of significant increases in the pension's annually required contributions for those years. However, fiscal 2013 TRANs will be lower at approximately $130 million due to improved fiscal 2012 year end balances and earlier timing of interfund transfers.

Debt Statistics

($000)

This Issue	229,575
Outstanding Debt Net of Refunding	518,827
Direct Debt	**748,402**
Overlapping Debt	4,342,563
Total Overall Debt	**5,090,965**
Debt Ratios	
Direct Debt Per Capita[a]	572
As % of MV[b]	0.5
Overall Debt Per Capita[a]	3,894
As % of MV[b]	3.2

[a]Population: 1,307,402 (2010). [b]Market value (MV): $185,306,329,000 (2011). Note: Numbers may not add due to rounding.

The city emphasizes its continued focus on funding its capital backlog of $898 million (excluding water and wastewater system needs). The city is considering issuing between $80 million–$90 million annually during fiscal years 2013–2017. The city might also act as conduit issuer for $520 million in bonds to expand its convention center, if all the required project approvals are granted, but it would be responsible for repayment of only a small portion of that debt.

Fitch believes the capital plan is manageable and should not dramatically alter the city's overall debt profile from both a tax base and budget burden perspective. However, in terms of overall funding for the city's capital needs, Fitch notes that voter approval of a June 5 ballot measure to prohibit project labor agreements could adversely affect the city's receipt of capital grant funding from the state ($194 million over the past two years), thereby creating more need for general fund support of capital projects.

Fitch expresses concern regarding the general fund's potential exposure to additional debt burden (starting at up to $7 million in fiscal 2013 and $14 million annually thereafter) if the general fund has to pay for debt previously intended to be repaid by the now dissolved RDA. City officials advise that the impact on the general fund should be minimal, offset by projected property tax share revenue growth and moneys set aside to mitigate near-term impacts. Fitch believes that the city will likely be able to manage the additional exposure but remains concerned about potential negative financial effects as the RDA exposure represents approximately 80% of the projected fiscal 2012 $17.8 million net operating surplus after transfers.

General Fund Financial Summary

($000s, Fiscal Years Ended June 30)

	2007	2008	2009	2010	2011
Total Tax	749,219	775,176	757,858	722,514	744,289
Licenses and Permits	31,475	33,815	31,249	28,024	28,621
Fines and Forfeits	40,346	31,083	32,467	30,179	31,598
Charges For Services	85,026	87,263	133,117	127,536	181,006
Intergovernmental	21,710	18,322	13,183	8,866	10,204
Other Revenue	44,887	47,874	46,757	48,488	55,444
Total Revenues	**972,663**	**993,533**	**1,014,631**	**965,607**	**1,051,162**
General Government	189,203	225,570	243,057	230,270	259,782
Public Safety	517,522	562,975	584,986	563,475	574,248
Culture and Recreation	112,967	119,125	116,391	121,269	114,375
Capital Outlay	0	0	0	0	776
Debt Service	9,123	7,924	3,924	5,528	15,421
Other	117,246	133,720	157,757	152,190	134,791
Total Expenditures	**946,061**	**1,049,314**	**1,106,115**	**1,072,732**	**1,099,393**
Operating Surplus/(Deficit)	**26,602**	**(55,781)**	**(91,484)**	**(107,125)**	**(48,231)**
Transfers In	91,161	100,458	111,326	146,318	160,857
Other Sources	35	0	0	21	0
Transfers Out	47,391	51,828	30,074	38,583	25,453
Other Uses	0	116	157	0	0
Net Transfers and Other	43805	48514	81095	107756	135404
Net Operating Surplus/(Deficit) After Transfers	**70,407**	**(7,267)**	**(10,389)**	**631**	**87,173**
Total Fund Balance	132,048	124,781	114,392	115,023	245,748
As % of Expenditures, Transfers Out, and Other Uses	13.3	11.3	10.1	10.4	21.8
Unreserved Fund Balance	96,190	78,938	80,497	107,027	0
As % of Expenditures, Transfers Out, and Other Uses	9.7	7.2	7.1	9.6	0
Undesignated/Unreserved Fund Balance	95,031	75,339	78,347	105,014	0
As % of Expenditures, Transfers Out, and Other Uses	9.6	6.8	6.9	9.4	0
Unrestricted Fund Balance	0	0	0	0	99,868
As % of Expenditures, Transfers Out, and Other Uses	0	0	0	0	8.9

Note: Numbers may not add due to rounding.

San Diego City Employees Retirement System (SDCERS) is 68.5% funded using the city's 7.5% discount rate and 64.9% funded using Fitch's more conservative 7.0% discount rate, levels that Fitch views as less than adequate. The city has already worked to stem the growth in its pension costs by establishing second tier pension benefits for new hires starting in 2009–2012 (depending on job classification), reducing the rate of return for its deferred retirement option plan, and eliminating its contributions on behalf of employees.

On June 5, the electorate will also be asked to vote on further pension reform. A conservative analysis prepared by the city's independent budget analyst suggests that if successful, the considerable potential net savings from this reform ($963 million over 30 years) would come not from the proposed pension system changes that actually increase pension costs. Rather, the savings would result from proposed restraints to employee remuneration growth so long as they are not rescinded by majority city council vote. Nevertheless, in terms of the pension system, the ballot measure would benefit the city in the long term by shifting investment and longevity risks to future city employees.

In terms of OPEB, the city still has an unfunded accrued actuarial liability of roughly $567 million, or a low 0.4% of fiscal 2012 TAV, when including the benefit of recent reforms. The city negotiated a new city retiree health plan in 2012, which is projected to save $714.0 million in healthcare costs over 25 years and caps the city's annual OPEB contribution at $57.8 million (5.1% of budgeted fiscal 2012 spending) in fiscal years 2012–2015, with annual increases of up to 2.5% thereafter.

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.