S&P Global Ratings

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Summary:

Oakland, California; Appropriations; General Obligation

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Credit Profile		
US$63.0 mil GO bnds (Measure Kk) ser 2017A-1 due 01/15/2047		
Long Term Rating	AA/Stable	New
US$50.3 mil GO bnds (Measure KK) ser 2017A-2 due 01/15/2035		
Long Term Rating	AA/Stable	New
Oakland GO		
Long Term Rating	AA/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA' long-term rating to Oakland, Calif.'s series 2017 A-1 and A-2 (Measure KK) general obligation (GO) bonds. At the same time, S&P Global Ratings affirmed its 'AA' long-term rating on the city's existing GO bonds, and its 'AA-' rating on the city's existing pension obligation bonds (POBs) and lease revenue bonds. The outlook on all ratings is stable.

Security

Revenue from unlimited ad valorem taxes levied on taxable property within the city secures the city's GO bonds. The Alameda County Board of Supervisors has the power and obligation to levy these taxes at the city's request for the bonds' repayment. The POBs are payable from any legally available revenue of the city, including special ad valorem tax override revenue that the city may levy through 2026 to fund the city's Police and Fire Retirement System (PFRS) obligations. The city's lease revenue bonds are secured by lease payments made by the city, as lessee, to the authority, as lessor.

The 'AA-' long-term lease revenue bond rating reflects our view of:

- The city's covenant to budget and appropriate lease payments in its annual budgets, and
- The risk associated with appropriation-backed obligations.
- The 'AA' long-term GO rating reflects our assessment of the following factors for the city:
- Very 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;
- Adequate budgetary performance, with operating results that we expect could deteriorate in the near term relative to fiscal 2016, which closed with operating surpluses in the general fund and at the total governmental fund level;
- Very strong budgetary flexibility, with an available fund balance in fiscal 2016 of 19% of operating expenditures;
- Very strong liquidity, with total government available cash at 43.3% of total governmental fund expenditures and 4.3x governmental debt service, and access to external liquidity we consider strong;
- Very weak debt and contingent liability position, with debt service carrying charges at 10.1% of expenditures and

net direct debt that is 136.5% of total governmental fund revenue, and a large pension and other postemployment benefit (OPEB) obligation and the lack of a plan to sufficiently address the obligation, but rapid amortization, with 68.3% of debt scheduled to be retired in 10 years; and
- Strong institutional framework score.

Very strong economy

We consider Oakland's economy very strong. The city, with an estimated population of about 426,000, is located in Alameda County in the San Francisco-Oakland-Hayward MSA, which we consider to be broad and diverse. The city has a projected per capita effective buying income of 117% of the national level and per capita market value of $121,000. Overall, the city's market value grew by 7.5% over the past year to $55 billion in 2017. Alameda County's unemployment rate was 4.2% in 2016, though recent seasonally unadjusted figures are lower.

In many respects, the city of Oakland is a political, cultural, and economic center on the West Coast and the city is a cornerstone community for the San Francisco-Bay Area regional economy. The city is the county seat of Alameda County, the seventh-most populous county in the state. As the city is deeply embedded within the regional economy, its economic trends mirror that of the region.

The city's assessed value (AV) trend is in the midst of a period of long-term growth as the average annual growth figure was 6.5% for each of the past four years. Driving the trend is a combination of local development, continued strong demand for single- and multifamily dwellings, and relatively strong commercial growth. Looking ahead, we continue to build optimism in the local economy, particularly in the city's AV trend, as a series of large development projects will soon hit the local tax rolls. These projects include the Brooklyn Basin Project ($1.5 billion for all phases), commercial and infrastructure improvements, an office tower, and an estimated $600 million for housing projects, among others. In addition to new development within the city, a variety of economic indicators that include building permits, taxable sales, and employment trends have been markedly positive in recent years. Overall, we are forecasting stable to positive growth for the urban centers in California as continued home price appreciation has helped boost local government tax receipts throughout much of the region, including the city of Oakland. As a result, we expect the broader macroeconomic forces to support our view and expectation of a local economy that we consider to be very strong. For additional information, please refer to our report, titled "U.S. State And Local Government Credit Conditions Forecast," published April 18, 2017 on RatingsDirect.

Strong management

We revised our view of the city's management policies and practices to strong from good under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable. Elements include a robust analysis of economic conditions and cost trends to build budget assumptions, as well as a formal 7.5% expenditures minimum reserve policy for emergencies in the city's "general purpose fund," which is its main operating fund on a budgetary basis and which, we understand, constitutes the bulk of its general fund on a generally accepted accounting principles (GAAP) basis. Recently, the city adopted and started to fund a "rainy day" reserve designation as a hedge against the revenue effects of economic cycles, which we believe could enhance the city's budgetary flexibility should it actively fund the reserve. Management provides quarterly budget-to-actual results and investments updates to the council, and the city annually updates its five-year capital plan, which identifies funding sources. Finally, the city maintains a five-year financial forecast that is integrated into decision making and is updated at least annually.

Adequate budgetary performance

Oakland's budgetary performance is adequate in our opinion. The city had operating surpluses of 6% of expenditures in the general fund and of 10.2% across all governmental funds in audited fiscal 2016. Our assessment accounts for our expectation that budgetary results could deteriorate somewhat from 2016 results in the near term, since we do not expect that the city will continue to produce adjusted general fund operating surpluses for the next two fiscal years.

The city's general fund revenue sub-categories are showing signs of a multiyear trend of unilateral growth. Specifically, the city's property tax revenue trend grew in three out of the past four years, with the two most recent periods posting more than 10% growth. We note that the city's property tax revenue, as is typical within California cities, is its largest revenue line at about 31% of the forecasted fiscal 2017 total general fund revenue. The remaining revenue mix includes the city's real estate transfer tax (14% of general fund revenue), business license taxes (13%), and the city's charges for services (10%). We note that the city's sales and use tax line represents about 10% of the city's general fund revenue.

Although the city's budgetary basis operating estimates and projections are not directly comparable with GAAP-basis accounting because of a slightly narrower definition of the city's main operating fund and because of different treatments of revenue and expenditures, the city's financial estimate for fiscal 2017 is showing a small use of fund balance and unspent carryover funds of about $66 million. We revised our opinion of the city's budgetary performance to adequate although we could revise our forward looking opinion to strong should the fiscal 2017 audit post stronger general fund operating performance than we anticipate. Further, we note that the city has a history of one-time general fund expenditures, including overtime expenditures related to the city's role as a focal point for civic protests in the region, the potential demand for one-time investments due to the high growth within the region, and the city's view of its long-term liabilities. Finally, we note that the city's fiscal 2018 budgetary expectations call for a balanced general fund result or a level that is indicative of at least adequate to potentially strong budgetary performance.

Very strong budgetary flexibility

Oakland's budgetary flexibility is very strong, in our view, with an available fund balance in fiscal 2016 of 19% of operating expenditures, or $123.3 million. Of the city's available general fund balance, about 47% of the recently released fiscal 2016 audit is listed as assigned for capital expenditures. We are not aware of any significant projects that could diminish the fund balances below a level that we would consider strong (or below 8% of general fund operating expenditures) since the city is working to finish capital projects funded by Measure DD. In addition, city voters recently approved Measure KK by 82%, which authorized up to $600 million for infrastructure improvements and will provide additional stability to the city's budgetary flexibility. As a result, we do not expect to change our view of the city's budgetary flexibility within our two-year outlook horizon since the city's general fund trend is expected to maintain at least stable reserves.

Very strong liquidity

In our opinion, Oakland's liquidity remains very strong, with total government available cash at 43.3% of total governmental fund expenditures and 4.3x governmental debt service in 2016. In our view, the city has strong access to external liquidity, if necessary. We believe the city has strong access to external liquidity, given its issuances of POBs, lease revenue bonds, and GO bonds in the past 20 years. We expect that the current liquidity levels will not likely fall below the threshold levels in the coming years. The city's investments are held in high-grade securities as regulated by the city's investment policy, and we do not consider its investment exposure aggressive. Finally, we note that fiscal 2017 did not require the city to issue a traditional tax and revenue anticipation note (TRAN) to support the city's total governmental fund cash.

Very weak debt and contingent liability profile

In our view, Oakland's debt and contingent liability profile remains very weak. Total governmental fund debt service is 10.1% of total governmental fund expenditures, and net direct debt is 137% of total governmental fund revenue in fiscal 2016 (with the addition of new debt data). Approximately 68% of the city's direct debt is scheduled to be repaid within 10 years, which is in our view a positive credit factor. Our assessment of the city's debt profile includes overlapping redevelopment property tax trust fund (RPTTF, formerly tax increment revenue) debt issued from the former redevelopment agency and successor agency to the former redevelopment agency. As previously mentioned, city voters recently approved Measure KK, or about $600 million of new GO authorization and the series 2017 bonds issued under Measure KK are included in our calculations with the base year of 2016.

The city is responsible for 50% of the Oakland-Alameda County Coliseum Authority's (OACCA) operating costs and debt service requirements, pursuant to an agreement that originated in 1995 to manage a complex consisting of professional baseball/football (O.co Coliseum) and basketball (Oracle Arena) venues. Outstanding par for the OACCA obligations at the end of fiscal 2016 was $82.7 million, a portion of which included in our assessment of the city's total debt obligations. As reported in the fiscal 2016 audit, the city contributed about $11 million for debt service and operations, as the OACCA is running at an operating deficit. Looking ahead, the city continues to estimate about $12 million of appropriations for the OACCA in fiscal 2018. As a result of the uncertainty surrounding the Coliseum, the city identified a contingent liability in the amount of $45.5 million, which we have included in our calculation. We note that the city did not need to make a contribution for its share of the neighboring arena for fiscal 2016. Historical contributions ranged from $3.3 million (fiscal 2012) to $825,500 (fiscal 2015).

Finally, we anticipate future GO debt issuances, similar to the series 2017 under the previously discussed Measure KK. Altogether, voters approved $600 million of GO authorization that will address a variety of capital improvements in the city that include core infrastructure (streets and roads), emergency services, parks and recreation, seismic enhancements, and affordable housing. All components of Measure KK are managed under the city's capital improvement plan (CIP), and we expect the city to continue to issue under Measure KK in multiple series versus fulfilling the remaining authorization in one final series. Although the city's debt and contingent liability profile is very weak or the lowest rated profile within our local GO criteria, we do not expect that the issuance of the remainder Measure KK authorization over time will significantly constrain the city's balance sheet.

In our opinion, a credit weakness is Oakland's large pension and OPEB liability, without a long-term plan in place that we think will sufficiently address the budgetary implications of costs under these obligations. Oakland's combined pension and OPEB contributions totaled 13.2% of total governmental fund expenditures in 2016, which was a decline from 14.6% in fiscal 2014. Of the 13.2%, about 11.2% represents contributions to pension obligations and 2.1% represents OPEB payments. Looking ahead, we are anticipating increased contributions from the city and we have factored that into the rating.

The city participates in three defined benefit retirement plans that include the Oakland Police and Fire Retirement

System (PFRS), the California Public Employees' Retirement System (CalPERS) Safety Plan, and the CalPERS Miscellaneous Plan. We note that PFRS is a closed single-employer plan for employees hired prior to 1976. Using updated reporting standards in accordance with Governmental Accounting Standards Board Statement Nos. 67 and 68, the city's combined net pension liability (NPL) was about $1.4 billion, or about 142% of total governmental funds expenditures for the period, an above-average level for California cities. Of the total NPL, $1.2 billion, or about 85%, stems from the city's CalPERS plans. In July 2012, the city issued a POB and contributed $210 million to PFRS. As a result of the POB, the city entered into a funding agreement for the PFRS plan and is allowed to defer contributions into PFRS until July 1, 2017. Aiding the city's effort to support debt payments associated with, or direct contributions to, its closed public safety plan is a special ad valorem property tax that represents about 1% of total governmental fund expenditures.

Outlook

The stable outlook reflects our opinion of the city's very strong budgetary flexibility supported by at least adequate financial performance, which we expect will continue. As a result, we do not anticipate changing the ratings within the two-year outlook period.

Upside scenario

We could raise the rating if the city's economic indicators were to improve and thus raise our view of the city's debt profile. We could also raise the rating if the city's budgetary performance were to improve and remain at a level that we consider strong in light of the city's large pension and OPEB liability.

Downside scenario

Should the city reduce its available fund balances to a level we view as below strong, enter into a significant period of general fund operating imbalances, or constrain its balance sheet as a result of additional debt or contingent liability agreements, we could lower the rating.

Related Research

- U.S. State And Local Government Credit Conditions Forecast, April 18, 2017
- S&P Public Finance Local GO Criteria: How We Adjust Data For Analytic Consistency, Sept. 12, 2013
- Incorporating GASB 67 And 68: Evaluating Pension/OPEB Obligations Under Standard & Poor's U.S. Local Government GO Criteria, Sept. 2, 2015

Ratings Detail (As Of July 18, 2017)		
Oakland taxable POB		
Long Term Rating	AA-/Stable	Affirmed
Oakland POB (wrap of insured) (MBIA) (National) (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Oakland POB (wrap of insured) (MBIA, National & Assured Gty) (SEC MKT)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Oakland POB		

Ratings Detail (As Of July 18, 2017) (cont.)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Oakland Jt Pwrs Fing Auth, California		
Oakland, California		
Oakland Jt Pwrs Fing Auth (Oakland) lse rev bnds (Oakland Admin Buildings) 2008B (ASSURED GTY)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.