

## **FITCH RATES SAN ANTONIO STARBRIGHT CONTRACT REV BONDS 'AA+'; OUTLOOK STABLE**

Fitch Ratings-Austin-29 May 2013: Fitch Ratings assigns an 'AA+' to the following San Antonio, Texas bonds:

--\$21.1 million Starbright Industrial Development Corporation (IDC) contract revenue refunding bonds, taxable series 2013 (Starbright Project).

The bonds are scheduled to sell via negotiation during the week of June 3, 2013. Bond proceeds will be used to refund all outstanding Starbright IDC contract revenue bonds for interest cost savings.

In addition, Fitch affirms the following ratings:

--\$972.2 million limited tax bonds at 'AAA';

--\$328.4 million combination tax and revenue certificates of obligation (COs) at 'AAA';

--\$27.7 million tax notes at 'AAA';

--\$21.3 million (Starbright IDC) contract revenue bonds, series 2003 at 'AA+';

--\$35.8 million San Antonio municipal facilities corporation (MFC) lease revenue bonds at 'AA+';

--\$550.4 million public facility corporation (PFC) improvement and refunding lease revenue bonds (convention center refinancing and expansion project) at 'AA'

The Rating Outlook is Stable.

### **SECURITY**

The contract revenue bonds are special obligations of the San Antonio Starbright Industrial Development Corporation and are payable from pledged contract payments from the city comprised of payments from its electric and gas utility, CPS Energy. The city is unconditionally obligated to pay debt service on the contract revenue bonds from the revenues it receives from CPS. The limited tax bonds, COs, and tax notes are secured by an annual property tax levy, limited to \$2.50 per \$100 taxable assessed valuation (TAV). The COs are additionally payable from a limited pledge of net revenues of the city's municipal parks system. The MFC lease revenue bonds are secured by annually appropriated lease payments made by the city to the MFC. The PFC lease revenue bonds are secured by annually appropriated lease payments made by the city to the PFC.

### **RATING DRIVERS**

**HIGH STARBRIGHT DEBT SERVICE COVERAGE:** CPS (electric and gas system revenue bonds rated 'AA+' by Fitch) payments to the city provide very high debt service coverage for the Starbright IDC's contract revenue bonds. Additionally, the source of the electric and gas payments to the city are considered strong, the bonds' contract terms and legal covenants are sound and no additional leveraging is planned.

**STRONG FINANCIAL RESERVES:** San Antonio's favorable financial performance has been aided by management's focus on increasing efficiency and conservative budgeting, enabling the city to preserve its progress in implementing enhanced financial reserve policies during the economic slowdown. Fitch favorably views the city's two-year budget strategy, which has expanded its planning horizon.

**LARGE CAPITAL PLANS:** The city's debt profile is mixed, characterized by its above average overall debt burden, balanced against rapid limited tax bond amortization and ample debt service capacity within the current tax rate enabled by a declining debt service schedule. The city's capital

plan is aggressive but will allow the city to address its sizeable deferred capital needs.

**MILITARY REMAINS KEY SECTOR:** Although the local economy has diversified notably, the military remains a major economic factor. This is evidenced by very large ongoing investments and planned additions to troop strength resulting from base realignment and closure decisions that have benefited the city.

**STABLE ECONOMY:** The recessionary contraction of the local economy has reversed course, enabling the city's unemployment rate to remain well below state and national averages. The city's population growth remains rapid, aided by affordable home prices and ample developable land.

**RATING SENSITIVITIES:**

**SHIFT IN FUNDAMENTALS:** The rating is sensitive to shifts in fundamental credit characteristics including the city's strong financial management practices. The city's history of maintaining solid reserve while addressing operating and capital needs indicates continued rating stability.

**CREDIT PROFILE**

**STARBRIGHT BONDS' HIGH COVERAGE LEVELS EXPECTED**

The contract revenue bonds, whose proceeds financed the acquisition and conveyance of the site for a Toyota manufacturing plant, comprise a modest part of the city's debt portfolio. The 'AA+' rating on these bonds reflects the strength of the revenue stream from which bond repayments are made, the very high debt service coverage, and the solid contract and legal covenants of the transaction. CPS' annual payment to the city's general fund is pledged for repayment of the contract revenue bonds. Audited fiscal 2012 pledged revenues totaled \$288.1 million and covered the bond's maximum annual debt service by a very high 173 times (x). Because the city relies on CPS payments (accounting for 30.9% of expenditures and transfers out in fiscal 2012) for operations, Fitch expects coverage to be very high regardless of pledged revenue performance.

Pursuant to an economic development contract between the city and the IDC, the city is unconditionally obligated to pay debt service on the contract revenue bonds. The payments are not subject to reduction and the corporation covenants it will maintain the contract in full force as long as bonds are outstanding. Although no additional leveraging is planned, Fitch notes that additional bonds are allowed under the indenture.

Payments to the city from CPS are net revenues of the utility systems in an amount not to exceed 14% of gross revenues of the utility systems less the value of the gas and electric services used for municipal purposes. Such payments are subject to the flow of funds and more specific terms of city ordinances authorizing bonds payable from the utility systems. Under the flow of funds for CPS utility revenue bonds, distribution of the 14% of gross revenues is the fifth priority, preceded by operations and maintenance expenses, payment of parity bonds and reserves, payment of inferior lien obligations, and a distribution to the repair and replacement account. Although legal provisions do not establish a minimum level of annual CPS payments to the city, Fitch believes their position within CPS' flow of funds will provide continued high debt service coverage of the contract revenue bonds.

**LARGE FINANCIAL RESERVES**

The city's financial profile remains solid as evidenced by the maintenance of unreserved fund balances in excess of 20% of spending since fiscal 2006, well above its 9% fund balance policy level. Additions to fund balance had been enabled by previously strong sales tax growth and positive CPS (electric and gas utility rated 'AA+' by Fitch) payment trends, along with management's aggressive cost controls in the form mainly of annual personnel reductions.

**TWO-YEAR BUDGET STRATEGY**

The city's two-year budget strategy, in which a portion of reserves in excess of its fund balance

policy are internally designated for the next year's spending (the two-year reserve), has expanded its planning horizon. A sizeable \$76.9 million of such reserves was budgeted for use in fiscal 2012, equal to 8.2% of spending, although greater than projected sales tax receipts and significant budget carry-forwards allowed the city to utilize only \$16.1 million (a large 79% reduction) of the allocation.

Sales tax receipts grew by a strong 9.7% in fiscal 2012, exceeding the budget's 6% growth estimate. In contrast, CPS payments decreased modestly due to a relatively mild summer. As a result of the partial use of the two-year reserve, the unrestricted fund balance declined to a still strong \$209.7 million or 22.5% of operating expenditures and transfers out. A portion of this fund balance, \$83.4 million, is designated as the city's 9% reserve. Another \$68.9 million of the fiscal 2012 fund balance is designated as the city's two-year reserve.

## CURRENT YEAR'S PROGRESS AND FISCAL 2014 BUDGET

The fiscal 2013 budget, aided by the appropriation of \$68 million of the two-year budget reserve (equal to 6.8% of appropriations), is balanced at a level property tax rate and is based on a modest sales tax growth projection of 1% above actual fiscal 2012 receipts. Sales tax receipts for the first seven months are 6.9% above the year prior. Although the city still projects it will still utilize the majority (\$62 million) of the two-year budget reserve, Fitch recognizes that the city typically outperforms its projections. In the event the projected amount of the two-year reserve is needed, the resulting unrestricted fund balance would total a still strong \$147 million or 15% of spending.

The preliminary fiscal 2014 budget allocates the remaining \$6.8 million of the two-year reserve, reducing the projected budget gap to \$35 million-\$50 million, equal to a manageable 3.6% to 5.1% of planned fiscal 2014 expenditures. The city expects the projected budget gap to narrow as the fiscal year advances, which Fitch considers reasonable given past experience. Despite the sound reserves, Fitch would be concerned if the city relied on fund balance for annual spending to more than a modest degree given the high rating level.

## LARGE CAPITAL NEEDS

In 2012, the city issued the first installment of the \$596 million general obligation bond authorization approved by voters in May 2012. As the largest bond authorization in the city's history, it is intended to address the city's substantial deferred capital needs. According to management, all future debt will be sized and timed to maintain the city's current debt service tax rate assuming modest tax base growth.

## OVERALL DEBT PROFILE PRESSURED

The impact of the 2012 bond program on the city's direct debt profile should be manageable given its declining debt service schedule, favorable pay-out rate, and expansive tax base. The rapid pay-out rate, at 66% of limited tax bond principal in 10 years, is reflected in sizable annual debt payments, which in fiscal 2012 were above average at 13.5% of total government spending (net capital outlays).

However, the city's overall debt burden is high at \$5,800 per capita and 9.4% of market value, without consideration of state support for school district debt. In July 2013, the city plans to issue \$126 million from its 2012 bond program and \$16 million in non-voted COs. Subsequently, the city's remaining bond authorization will total \$398 million.

## WELL-FUNDED PENSION PLANS

Civilian and certain public safety employees participate in an agent multiple employer defined benefit pension plan administered by the Texas Municipal Retirement System (TMRS). Recent changes to TMRS' valuation methodology and the elimination of automatic repeating cost of living adjustments increased the pension's funded ratio to a high 91.6% as of Dec. 31, 2011. TMRS' valuation is based on a 7% discount rate which Fitch considers reasonable. Fire fighters and police participate in a single employer defined benefit pension plan which was similarly well-funded at

83% as of Oct. 1, 2011 using a Fitch-adjusted 7% investment return.

Annual contributions for both pension plans comprised a manageable 6.5% of governmental spending (net capital outlays) in fiscal 2012. Retiree health benefits for civilians are also provided through TMRS and are funded on a pay-go basis. Retiree health benefits for fire fighters and police have been financed on a pre-funded basis since 1989, resulting in a notable funded position of 37% as of Oct. 1, 2011.

#### MILITARY STILL KEY WITHIN BROAD ECONOMY

San Antonio is the second largest city in the state and seventh largest in the U.S., with an estimated population of 1.4 million for 2013. Prominent sectors in the local economy are military and government employment, domestic and international trade, convention and tourism, medical and health care, financial services, and telecommunications. Aided by considerable growth in energy sector jobs, the city's unemployment rate declined to 5.8% in March 2013, down from the 6.6% level recorded in March 2012.

The city's unemployment rate compares favorably to state and national averages of 6.3 % and 7.6%, respectively, for the same period. The city's construction sector has benefited from several large projects, including the recent completion of the \$3.2 billion San Antonio Military Medical Center, which was accompanied by approximately 12,500 additional military personnel to the city. After posting strong annual gains through fiscal 2009, the city's taxable values have flattened through fiscal 2013 as new improvement values have been offset by reappraisal losses in existing values. Preliminary indications for the fiscal 2014 AV points to a modest 2% increase.

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Additional information is available at '[www.fitchratings.com](http://www.fitchratings.com)'

In addition to the sources of information identified in Fitch's Tax-Supported Rating Criteria, this action was informed by information from CreditScope, University Financial Associates, S&P/Case Schiller Home Price Index, HIS Global Insight, Zillow.com, and National Association of Realtors.

Applicable Criteria and Related Research:

--'Tax-Supported Rating Criteria', dated Aug. 14, 2012;

--'U.S. Local Government Tax-Supported Rating Criteria', dated Aug. 14, 2012.

Applicable Criteria and Related Research:

Tax-Supported Rating Criteria

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## Summary:

# Starbright Industrial Development Corp., Texas San Antonio; Appropriations

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## Summary:

# Starbright Industrial Development Corp., Texas San Antonio; Appropriations

### Credit Profile

US\$21.135 mil contract revenue refunding bonds (San Antonio) (Taxable Starbright Proj) ser 2013 dtd 06/01/2013 due 08/15/2033

Long Term Rating

AA+/Stable

New

## Rationale

Standard & Poor's Ratings Services assigned its 'AA+' long-term rating to Starbright Industrial Development Corp., Texas' series 2013 contract revenue refunding bonds. At the same time, Standard & Poor's affirmed its 'AA+' rating on the corporation's contract revenue debt outstanding. The corporation's contract revenue is supported by San Antonio, Texas (AAA/Stable general obligation, or GO, debt rating). The outlook on all ratings is stable.

For more information on San Antonio's GO debt, please refer to the report published Oct. 1, 2012 on RatingsDirect.

San Antonio's portion of revenues received from City Public Service (CPS) secures the bonds. The revenue transfers from CPS to the city are subject to the availability of excess CPS funds, but according to its bond ordinance, the utility is required to transfer funds as long it has debt outstanding. The transfer of funds has occurred since 1963, and the city is reliant on these funds for operations.

The rating reflects our view of:

- The city's pledge of revenues it receives from CPS, which have historically been made in the maximum legal amount of 14% of the utility's gross revenues;
- The utility's legal requirement to make transfers to the city as outlined in its bond ordinance and supplemental ordinances;
- The city's control of CPS' transfer requirement and rate structure as outlined in the utility's bond ordinances; and
- Transfers that are subject to monthly appropriation.

San Antonio formed Starbright Industrial Development Corp. as a nonprofit industrial development corporation to issue bonds for the acquisition of land and other related costs to the city associated with the construction of a new Toyota Motor Corp. truck manufacturing facility south of downtown San Antonio. The city is issuing this debt through Starbright as contract revenue bonds, the debt service of which will be paid solely from revenues the city pledges from funds it receives from CPS. Bond proceeds will be used to refund the corporation's series 2003 bond outstanding for savings purposes.

Under CPS' bond ordinances, the utility is legally required to make monthly transfers to the city from funds available after meeting its own debt service and funding its own repair and replacement reserve fund. This legal requirement will be in effect as long as CPS has bonds outstanding. Current CPS debt extends out 28 years to maturity. Starbright's series 2013 revenue bonds mature on Aug. 15, 2033. The maximum amount CPS is required to transfer to the city is

14% of gross revenues less the city's costs for usage of gas and electric services from CPS.

Transfers to the city from CPS began in 1942. The 14% maximum amount was instituted in its bond ordinances and was phased in so that monthly transfers have been made at this maximum level each year since 1963. The transfer is expected to continue at the maximum level given that, by CPS' bond ordinances, the percent of gross revenues of CPS to be paid over to the city, within the 14% maximum amount, is determined by the city's governing body. In addition, the San Antonio city council sets CPS' rate structure. CPS' transfer to the city has represented roughly 30% of total revenues for many years. For fiscal 2012, the transfer from CPS totaled approximately \$260.7 million; as compared to the maximum annual debt service on the bonds, which was about \$1.6 million, we believe this provides very strong coverage.

In early 2003, San Antonio won its bid for a new Toyota truck plant to be built on land south of the downtown area; this industrial plant is the Starbright Project. Later that year construction began on the Starbright Project, and the plant came on line in November 2006. In 2010, Toyota expanded its production to include the Tacoma production, which added 1,000 new jobs to the plant. Currently Toyota has an estimated San Antonio workforce of about 2,900. The entire Toyota San Antonio campus, which includes several parts suppliers, has an estimated work force of about 6,000 and an estimated financial impact of \$1.7 billion on the local economy.

## Outlook

The stable outlook reflects our anticipation that CPS' maximum transfer amount to the city of 14% of gross revenues will continue and that the city will take any necessary action to see that the transfer is maintained as legally allowed under the utility's bond ordinances. As a result, we do not expect to change the rating within the two-year outlook time frame.

## Related Criteria And Research

USPF Criteria: Appropriation-Backed Obligations, June 13, 2007

### Ratings Detail (As Of May 24, 2013)

#### Starbright Indl Dev Corp, Texas

San Antonio, Texas

Starbright Indl Dev Corp (San Antonio) (Starbright Pro)

Long Term Rating

AA+/Stable

Affirmed

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# MOODY'S

## INVESTORS SERVICE

### **Rating Action: Moody's assigns Aa1 to the City of San Antonio (TX) Starbright Industrial Development Corporation's \$21.1 million Contract Revenue Refunding Bonds, Taxable Series 2013 (Starbright Project)**

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Global Credit Research - 24 May 2013

#### **Affirms Aa1 on \$21.3 million in previously issued bonds**

New York, May 24, 2013 --

Moody's Rating

Issue: Contract Revenue Refunding Bonds, Taxable Series 2013 (Starbright Project); Rating: Aa1; Sale Amount: \$21,135,000; Expected Sale Date: 05-28-2013; Rating Description: Revenue: Other

Opinion

Moody's Investors Service has assigned a Aa1 rating to the City of San Antonio (TX) Starbright Industrial Development Corporation's \$21.1 million Contract Revenue Refunding Bonds, Taxable Series 2013 (Starbright Project). Concurrently, we have affirmed the Aa1 rating on the Corporation's \$21.3 million in previously issued debt. Proceeds from the sale of the bonds will be used to refund the outstanding maturities of the Series 2003 bonds for an expected net present value savings in excess of 10%

#### SUMMARY RATING RATIONALE

The bonds are secured by pledged revenues including pledged contract payments under the Economic Development Contract. Under the contract, the city is obligated to pay to the trustee, on behalf of the corporation, from certain revenues it receives from the combined gas and electric utility system. The rating reflects the strength of the pledged revenues securing the bonds marked by strong debt service coverage ratios. The rating also incorporates the credit quality of the City Public Service electric and gas utility, which is the source of the pledged revenues. Additionally, the rating reflects weak legal provisions; there will be no debt service reserve on the bonds.

#### STRENGTHS

Strong credit quality of the Combined Utility System

Strong debt service coverage ratios

History of transfers to the City from the Combined Utility Fund

#### CHALLENGES

Weak debt provisions; no debt service reserve

#### WHAT COULD MAKE THE RATING GO UP

Strengthening of the legal security

#### WHAT COULD MAKE THE RATING GO DOWN

CPSs reduction or withholding of transfer payments to the city

#### PRINCIPAL METHODOLOGY

The principal methodology used in this rating was The City of San Antonio (TX) Starbright Industrial Development Corporation's Contract Revenue rating was assigned by evaluating factors believed to be relevant to the credit profile of the issuer such as i) the business risk and competitive position of the issuer versus others within its industry or sector, ii) the capital structure and financial risk of the issuer, iii) the projected performance of the issuer over the near to intermediate term, iv) the issuer's history of achieving consistent operating performance and

meeting budget or financial plan goals, v) the nature of the dedicated revenue stream pledged to the bonds, vi) the debt service coverage provided by such revenue stream, vii) the legal structure that documents the revenue stream and the source of payment, and viii) the issuer's management and governance structure related to payment. These attributes were compared against other issuers both within and outside of the City of San Antonio (TX) Starbright Industrial Development Corporation's core peer group and City of San Antonio (TX) Starbright Industrial Development Corporation's ratings are believed to be comparable to ratings assigned to other issuers of similar credit risk

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