

**Meeting Date:** 2/2/2016

**Report Type:** Staff/Discussion

**Report ID:** 2016-00072

**Title:** City Credit Ratings: Meaning and Implications

**Location:** Citywide

**Recommendation:** Receive and file.

**Contact:** Russ Fehr, City Treasurer, (916) 808-5832; Brian Wong, Debt Manager, (916) 808-5811, Office of the City Treasurer

**Presenter:** Russ Fehr, City Treasurer, (916) 808-5832, Office of the City Treasurer

**Department:** City Treasurer

**Division:** City Treasurer

**Dept ID:** 05001011

**Attachments:**

1-Description/Analysis

2-Credit Ratings Review

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**City Attorney Review**

Approved as to Form

Joseph Cerullo

1/27/2016 5:42:06 PM

**Approvals/Acknowledgements**

Department Director or Designee: Russell Fehr - 1/26/2016 1:46:40 PM

## Description/Analysis

**Issue Detail:** The City receives overall long-term ratings from three credit-rating agencies on a regular basis. These long-term ratings are not linked to specific projects and debt issues; they are, rather, assessments of the City's management of its fiscal affairs and longer-term financial issues.

**Policy Considerations:** A review of City's credit ratings and comments of the credit-rating agencies is appropriate at the start of the annual budget cycle.

**Economic Impacts:** The statements in the credit-rating reports assess the budget, the local economy, and longer-term fiscal issues.

**Environmental Considerations:** Not Applicable

**Sustainability:** Not Applicable

**Commission/Committee Action:** Not Applicable

**Rationale for Recommendation:** The consistent view of the credit-rating agencies and accompanying reports is relevant background information for the upcoming budget process.

**Financial Considerations:** The observation that the City has high levels of debt and employee-benefit liabilities suggests caution in taking on any new long-term liabilities.

**Local Business Enterprise (LBE):** Not Applicable

## The City of Sacramento's Long-Term Credit Ratings

Over the summer of 2015, as the City prepared to issue long-term debt, both for the Golden 1 Center Project and to refund existing debt, credit ratings were secured from three of the major credit-rating agencies. The City obtained project ratings for the specific debt issues as well as overall ratings for the City as a whole from Standard and Poor's Ratings Services; Moody's Investors Service, Inc.; and Fitch Ratings, Inc. All three rating agencies gave the City the same overall rating: AA-. And all three rating agencies made similar comments about the City, its leadership, its management, its economy, its budget, and its future challenges.

The reviews are holistic, pointing out strengths and weaknesses. They are not out-of-context criticisms, nor are the reviews focused on fault finding. The comments in the three credit-rating reports for the City reflect consistent themes:

- Elected policymakers have shown strong financial leadership through expenditure discipline and reserve building
- Strong management is in place
- Good financial policies and practices have been developed, approved, and put into practice
- The City has recent strong budgetary performance and increasing budgetary flexibility with increasing reserves and fund balance (increasing budget pressure in out years of budget forecasts is noted)
- The regional economy is improving with recovery in employment and the property and sales-tax bases
- The City has very strong liquidity and strong access to external liquidity if necessary
- There is budgetary risk if Measure A is not reapproved by the voters
- Budget forecasts indicate out-year operating deficits
- There is a weak combined debt, pension, and retiree medical position, and a plan to address the largely unfunded retiree medical benefit has yet to be developed
- Large pension and OPEB liability is a credit weakness

One report contained a general statement of the types of changes that could lead to a ratings upgrade or downgrade. Factors that could result in a rating upgrade to AA include the following:

- Material improvement to resident wealth

- Sustained, substantial fiscal improvement, including increases to reserves and fund balances
- Sustained, significant improvement to the local economy
- Reduction in general fund-supported debt

Factors that could lead toward a rating downgrade include the following:

- Deterioration in budget position
- Erosion of the local economy
- Increases in general fund-supported debt

Because the budget process is in its early phase, it is appropriate for the City Council to receive this overview of independent reviews of the City's collective conduct of its fiscal affairs and identification of longer-term issues. Throughout the Great Recession, the City maintained core services, liquidity, solvency, and planning for the future. Recovery has been guided by policy set by the City Council and included significant reserve building.

The warnings are simple and not at all news. As needs exceed resources, there is still budget pressure that will grow. Long-term liability levels are high. Prudence and caution must be exercised in taking on new long-term commitments.