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1 May 2017

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Mass Transit - US

Proposed Federal Budget Would Compound Mass Transit Capital Funding Shortfall

The Trump Administration's fiscal year 2018 budget blueprint proposes ending approvals for certain types of mass transit capital grants, which would widen public transportation's $90 billion capital investment gap. Transit agencies rely on federal funding for almost half of their capital funding (see Exhibit 1).

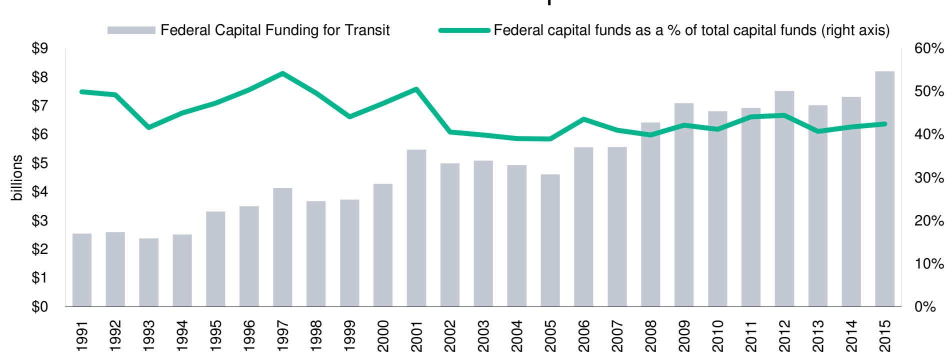
The cuts, which focus on programs representing nearly one-fifth of federal transit funding, would be credit negative if enacted as proposed in the budget blueprint. The most vulnerable credits are transit agency bonds secured by fares or general revenues; bonds secured by taxes or federal grants have some insulation from capital funding shortfalls.

» **Mass transit enterprises would struggle to replace lost federal funds.** If the proposal passes, transit agencies would have to delay or cancel capital projects; otherwise, the agencies would struggle to replace federal funds with higher fares, more debt, or more state and local subsidies.

» **Proposal raises prospect of future cuts for transit grant anticipation revenue vehicles (GARVEEs)**. An environment in which the federal government cuts transit funding could eventually hurt bonds secured by future federal transportation funding.

» **Tax-backed transit bonds are most insulated from federal cuts.** Bonds issued to finance transit enterprises that are secured directly by a tax are most insulated from federal cuts. Transit enterprises that utilize this type of financing will have to decide whether to cancel capital projects or leverage their tax revenues with more debt.

Exhibit 1
Federal Government a Paramount Source of Transit Capital Funds



Source: Federal Transit Administration

What does President Trump's budget blueprint propose for transit?

The blueprint proposes to stop approving new grants under the Federal Transit Administration's Capital Investment Program, which distributes $3.5 billion of grants annually (18% of the FTA's budget). However, it is likely that there will be modifications to the proposal.

Projects in this program fit into two categories: those that have been approved for full grant funding and those that have not. The president's proposal would continue distributing grants for projects with funding approval, but not award new grants for projects that are still awaiting approval for full funding. Projects still awaiting approval for funding have not entered construction yet; however, many are phases of multiphase projects, and significant investments have been made in earlier project phases and in readying the current phase for construction.

There are three types of grants under the Capital Investment Program: New Starts, Small Starts and Core Capacity.[1] President Trump's proposal specifically calls for eliminating new New Starts grants, which represented $2.33 billion of grants in fiscal 2017, or 12% of the FTA's budget (see Exhibit 2). The proposal does not specifically address Small Starts or Core Capacity, but we think all Capital Investment Program projects without full funding agreements are at risk (see Exhibit 3).[2] The FTA lists more than 50 projects with more than $10 billion of grant requests without full funding agreements in its Capital Investment Program.

Exhibit 2

New Starts Projects Would Lose Funding Under Blueprint

New Starts Projects Expressly Targeted for Federal Grant Elimination

Applicant	Project	Total Project Cost (millions)	Total Grant Request (millions)
Central Puget Sound Regional Transit Authority (Aaa stable)	WA Seattle, Lynwood Link Extenstion	$2,345.9	$1,172.7
Maryland Transit Administration	MD Maryland National Capital Purple Line	$2,448.2	$900.0
Metropolitan Council of Minneapolis (Aaa stable)	MN Minneapolis, Southwest Light Rail Transit	$1,774.4	$887.2
Fort Worth Transportation Authority	TX Fort Worth, TEX Rail	$996.1	$498.0
Orange County Transportation Authority (A1 stable)	CA Santa Ana, Santa Ana/Garden Grove Streetcar Project	$288.7	$144.4

Sorted by the size of the grant request

Sources: US Department of Transportation, Moody's Investors Service

Exhibit 3

Other Significant Projects At Risk of Losing Funding

Other Large Projects without Full Funding

Applicant	Project	Total Project Cost (millions)	Total Grant Request (millions)
Peninsula Corridor Joint Powers Board (A1 stable)	CA San Carlos, Peninsula Corridor Electrification Project	$1,758.5	$447.0
NY MTA (A1 stable)	NY New York City, Canarsie Line Power and Station Improvements	$273.6	$100.0
Valley Metro Regional Public Transportation Authority	AZ Tempe, Tempe Streetcar	$182.9	$75.0
Sacramento Regional Transit District (A3 stable)	CA Sacramento, Downtown Riverfront Streetcar	$150.0	$75.0
City of Seattle (General Obligation Aaa stable)	WA Seattle, Seattle Streetcar Center City Connector	$134.9	$75.0
Indianapolis Public Transportation Corp.	Red Line All-Electric BRT	$96.3	$75.0

Sorted by the size of the grant request

Sources: US Department of Transportation, Moody's Investors Service

In addition to those listed above, the proposal would have a longer-term impact on the entire transit sector, which relies on federal funding for many major transit projects and might not be able to fund them without federal grants. In some cases, the loss of federal funds could threaten the viability of projects already under way. For example, Maryland's Purple Line light rail system is being financed as a public-private partnership (P3). The loss of federal funding could jeopardize the financing for the entire $5.6 billion project. Many transit projects would not proceed without federal funding, which often represents 50% or more of major projects' costs.

The blueprint would also eliminate funding for a discretionary grant called the Transportation Investment Generating Economic Recovery (TIGER) program. TIGER grants for all types of transportation are authorized at a total level of $499 million annually, of which transit and rail projects combined have generally gotten about half.

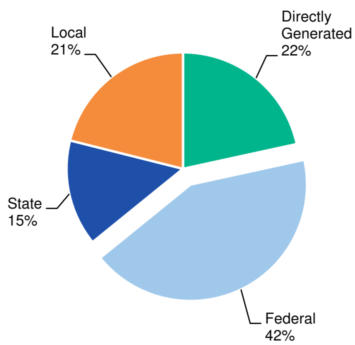
Transit enterprises would struggle to replace their largest source of capital funding

The federal government is the most important source of capital funding for mass transit enterprises in the US, and a curtailment of federal funding would exacerbate a $90 billion transit capital investment gap.[3] The federal government provides about 42% of transit capital funding, according to the Federal Transit Administration (see Exhibit 4). The federal government also provides some operating grants, representing 8% of operating expenditures (see Exhibit 5). The Blueprint does not propose to reduce operating grants.

Exhibit 4

Federal Government is Crucial Source of Capital Funding

Capital Funding Sources: (Total in 2015: $19.3 billion)



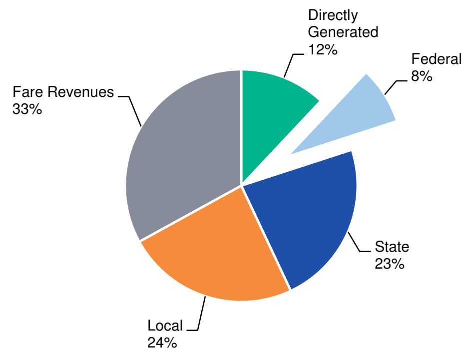
Directly generated funds are mostly taxes.

Source: Federal Transit Administration

Exhibit 5

Federal Government Also an Important Source of Operating Funds

Operating Funding Sources: (Total in 2015: $46.3 billion)



Directly generated funds are mostly taxes. Fare revenues here includes some non-fare funds generated by transit agencies.

Source: Federal Transit Administration

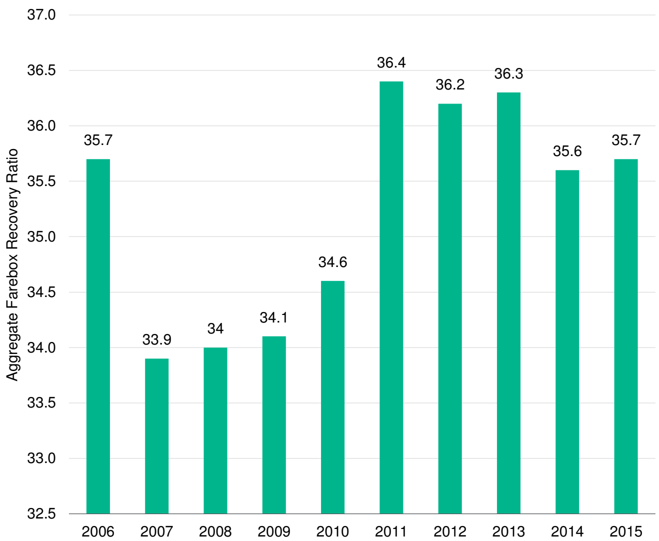
Most transit enterprises would be challenged to fully fund their capital programs with diminished federal support. Many projects likely would never proceed, and transit enterprises would struggle to fund those projects that do.

Transit enterprises are unable to independently support themselves financially and rely heavily on subsidies. Fares that transit agencies charged riders in 2015 only covered 35.7% of operating expenditures, , which totaled $46.3 billion, according to the Federal Transit Administration (FTA) (see Exhibits 6 and 7). Taxes or subsidies funded the remaining 64.3% of operating expenditures and 100% of capital expenditures, which totaled $19.3 billion. Total spending, both operating and capital, not funded by transit-generated revenues was $49 billion.

Exhibit 6

Transit Agencies Unable to Support Themselves

Farebox Recovery Ratio is the % of operating costs recouped from fares



Source: Federal Transit Administration

Exhibit 7

No Major Transit Agency Fully Supports Itself

Farebox Recovery Ratios for Moody's-rated Transit Enterprises

Transit	Farebox Recovery Ratio
Peninsula Corr Joint Pwrs Board (A1 stable)	75%
NY MTA (A1 stable)	57%
Washington Metro Area Transit Auth (A2 stable)	48%
San Joaquin Regional Rail Commission (A2 stable)	46%
San Diego Metro Transit System (Aa3 stable)	37%
San Francisco Municipal Trans Agency (Aa2 stable)	26%
Western Contra Costa Trans Auth (Aa3 stable)	24%
Minnesota Valley Transit Auth (A3 stable)	23%
North County Transit District (A1 stable)	21%
Sacramento RTD (A3 stable)	18%
Gold Coast Transit District (A2 stable)	17%
Alameda-Contra Costa Transit District (A1 stable)	16%
Victor Valley Transit Authority (A2 stable)	14%

Sources: Moody's Investors Service, Audited Financial Statements

Even to reach current spending levels, transits require large subsidies. The FTA estimates that in 2015 each mass transit trip cost an average of $4.16, and required a subsidy of $2.99.

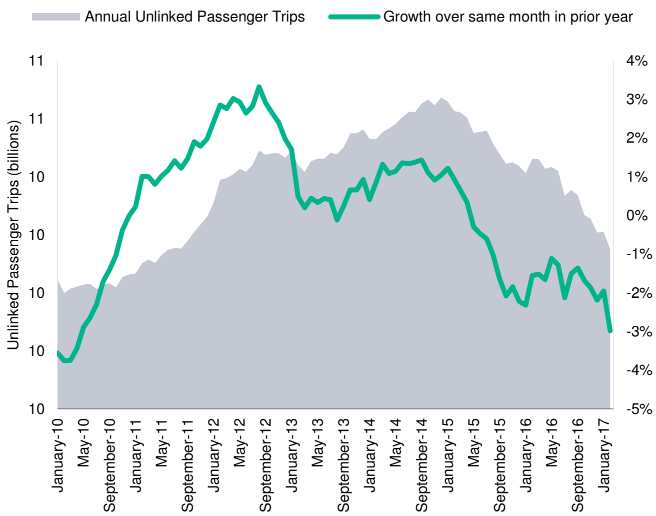
Current spending levels are not enough to maintain current transit assets and complete new projects. The US Department of Transportation in 2015 estimated a $90 billion backlog of capital projects just to preserve the existing state of transit infrastructure, let alone expand or modernize. If transit enterprises continued to invest in capital assets at the current inflation-adjusted pace, the backlog would grow to $122 billion by 2032 (in 2012 dollars).

In its 2017 Infrastructure Report Card, the American Society of Civil Engineers (ASCE) assigned a grade of D- to US mass transit infrastructure. The ASCE found that 15% of transit facilities, 17% of systems, 35% of guideway elements and 37% of transit stations are not in a state of good repair. It also concluded that most transit capital investment was simply to preserve existing assets, rather than improve or expand them.

RIDERSHIP

Difficult as it is for transit agencies to fund operating expenses and capital programs already, transits are now facing another problem: ridership is down. Most of the transit agencies we rate reported ridership declines in fiscal 2016, with a median 2% drop (see Exhibit 9). The transit agencies in Exhibit 9 reported total ridership of 3.5 billion last year, or likely more than a third of all passenger trips in the US.

Exhibit 8
US Transit Ridership Peaked Two Years Ago



Unlinked passenger trips are the rolling sum of the previous 12 months.
Source: Federal Transit Administration

Exhibit 9
Most Transits Reported Declines in Ridership Last Year

Transit	Ridership Change in 2016
Washington Metro Area Transit Auth (A2 stable)	-6.4%
Sacramento RTD (A3 stable)	-5.6%
North County Transit District (A1 stable)	-5.0%
Gold Coast Transit District (A2 stable)	-2.8%
San Diego Metro Transit System (Aa3 stable)	-2.6%
Alameda-Contra Costa Transit District (A1 stable)	-2.6%
Western Contra Costa Trans Auth (Aa3 stable)	-2.0%
NY MTA (A1 stable)	-0.1%
Victor Valley Transit Authority (A2 stable)	1.1%
Minnesota Valley Transit Auth (A3 stable)	1.2%
Peninsula Corr Joint Pwrs Board (A1 stable)	3.6%
San Francisco Municipal Trans Agency (Aa2 stable)	5.9%
San Joaquin Regional Rail Commission (A2 stable)	7.1%

This is for fiscal year 2016, which ended June 30, 2016.
Sources: Moody's Investors Service, Issuers' Financial Statements

CHAIN EFFECT

In its report card, ASCE warned of a "chain effect" of deteriorating capital assets leading to less reliable service, in turn leading to lower ridership and lower support, and therefore less reinvestment. Although we believe transit ridership is mostly down because of low gasoline prices and not poor asset condition, a decline in federal capital funding coinciding with a decline in ridership would be a very difficult combination of pressures for transit agencies to overcome.

Federal cuts could eventually pressure GARVEEs

An environment in which the federal government cuts transit funding could eventually affect bonds secured by future federal transportation grants, known as grant anticipation revenue vehicles (GARVEEs). We rate $1.6 billion of GARVEEs issued by transits.

The budget blueprint does not immediately imperil any transit GARVEEs that we rate because the proposed cuts are from the Transportation Investment Generating Economic Recovery (TIGER) program or Section 5309 of the Capital Investment Program. The outstanding GARVEEs that we rate are all secured by grants issued under Section 5307 or Section 5337, which remain unaffected by the current budget proposal (see Exhibit 10).[4] Any cuts in the budget proposal would therefore not reduce pledged revenues for any transit GARVEE that we rate.

Exhibit 10
Proposed Cuts Do Not Immediately Threaten Transit GARVEEs

Transit	GARVEE Security	GARVEE Rating
Southeastern Pennsylvania Trans Auth	Sect 5337	A3 stable
Alaska Railroad	Sect 5307 and Sect 5337 (bonds secured by grants under both sections)	A3 stable
Chicago Transit Authority	Sect 5307 and Sect 5337 (separate bonds secured by grants under separate sections)	A3 stable
NJ Transit	Sect 5307	A3 stable
Tri-County Metropolitan Transportation District	Sect 5307	A3 stable

Source: Moody's Investors Service

A primary risk facing transit GARVEEs is the federal government's willingness to continue appropriating federal transit grants. If the budget blueprint is evidence of a diminishing willingness to fund transit at the federal level, it signals an elevated risk that all federal transit grants — including the ones that secure GARVEEs — could one day be on the chopping block.

Tax-backed transits most insulated from federal cuts

Transit agency bonds that are secured directly by a tax are most insulated from federal cuts. The legal structures that support these bonds typically provide for debt service payment from a local tax — such as a sales tax or payroll tax — prior to any excess revenues flowing to the transit enterprise that issued the bonds.

Many transit agencies in recent years have sought or expected to receive significant federal funding via expansion or modernization programs. To the extent that the federal government materially reduces grants, transit agencies will have to delay those projects or find new ways to fund them, including through increased tax-backed bond issuance.

If the federal government scales back its role in funding transit capital, transit agencies that have the authority to issue bonds secured by taxes may issue more tax-backed bonds to increase their available capital funds. Increased issuance could pressure coverage on existing tax-backed transit bonds, although all such bonds that we rate have legal provisions preventing issuance from depressing coverage beyond a certain threshold (see Exhibit 11).

Exhibit 11

Most Tax-Backed Transit Bonds Have Solid Coverage
(Five Largest Tax-Backed Transit Liens by Par Outstanding)

Five Largest Tax-Backed Transit Liens	Rating	Security	Coverage of Maximum Annual Debt Service by Pledged Revenues	Additional Bonds Test
Massachusetts Bay Transportation Authority (Sr lien)	Aa2 stable	1 cent statewide sales tax with floor	2.51x	1
Dallas Area Rapid Transit	Aa2 stable	1 cent sales tax in Dallas area	2.61x	2
Chicago Transit Authority	A1 negative	Share of regional sales taxes	2.63x	2
Regional Transportation Authority, IL	Aa3 negative	Share of regional sales taxes	2.60x	2.5
Metropolitan Atlanta Rapid Transit Authority (3rd lien)	Aa2 stable	Sales tax collected in Atlanta area	2.75x	2

Source: Moody's Investors Service

Appendix A

Exhibit 12

Transit Bonds by Type and Exposure
(Par outstanding rounded to nearest billion)

Transit Sector	Security	Number of Credits	Par Outstanding	Median Rating	Exposure to Federal Cuts
Enterprise	Fares or general revenues	13	$38 billion	A1	High -- transit enterprises are heavily subsidized and would struggle to replace lost funding
Tax-Backed	Tax (usually sales tax)	18	$28 billion	Aa2	Moderate -- legal structures protect the bonds, though transit agencies that issue tax-backed bonds still rely on federal capital funding
GARVEEs	Federal transit grants	5	$2 billion	A3	Moderate -- an environment of reduced federal funding increases the likelihood of cuts to pledged federal transit funds

Metropolitan Transportation Authority, NY (A1 stable) represents the vast majority of transit enterprise debt outstanding.
Source: Moody's Investors Service

Moody's Related Research

» US Budget Blueprint Proposes Credit-Negative Amtrak Restructuring - March 2017

» Increased Ridership, Sizable Expansion Signal Higher Taxpayer Subsidies - November 2015

» Government Relationships Put Debt and Revenues on Different Tracks - March 2016

» Congress Passes Long-Term Transportation and Funding Act, a Positive for GARVEEs and Transit Agencies - December 2015

» Potential Federal Shutdown Poses Little Risk for Municipal Credits - April 2017

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Endnotes

1 The New Starts and Small Starts categories both fund new systems or expand existing ones, with New Starts for bigger projects and Small Starts for smaller ones. The Core Capacity program category is for expanding capacity in existing corridors.

2 See full list here, excluding those labeled "FFGA"

3 2015 Status of the Nation's Highways, Bridges and Transit, US Department of Transportation

4 GARVEEs secured by grants under what is now called Section 5337 were originally secured by grants under Section 5309. Under 2012 legislation, many of these 5309 grants were reclassified as 5337, and therefore the pledged revenues for these bonds were reclassified as well. So, even though the president's proposed cuts are under what is now Section 5309, such cuts would not harm pledged revenues for bonds originally secured by Section 5309 grants. These are now all secured by Section 5337 grants.

REPORT NUMBER 1069024

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