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City Manager's Office

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR, CITY COUNCIL, AND AGENCY BOARD

FROM: RICHARD KEIT
DEBRA FIGONE

SUBJECT: SEE BELOW

DATE: December 14, 2011

INFORMATION

SUBJECT: UPDATE ON THE REDEVELOPMENT AGENCY'S BOND RATINGS FROM S&P, MOODY'S AND FITCH

This information memorandum provides an update on the current credit ratings of the Redevelopment Agency's outstanding debt as summarized in the table below.

Rating Agency	Rating Action Date	Agency 80% Senior Bonds	Agency 80% Junior Bonds (JPM)	Housing Set-Aside 20% Bonds
S&P	11/21/11	BBB Negative Outlook	AA-/A-1+	A Outlook Stable
Fitch	10/05/11	BBB- Negative Watch	N/A	A Outlook Stable
Moody's	4/18/11	Baa1 (cash reserves) Baa2 (surety reserves) Negative Outlook	N/A	A2 Negative Outlook

On November 21, 2011, Standard & Poor's (S&P) took rating actions on the Redevelopment Agency's outstanding bonds and downgraded the 80% Senior Bonds to 'BBB' rating with 'Negative Outlook' from 'BBB+', and reaffirmed the 20% Housing Set-Aside Bonds at 'A' rating with 'Stable Outlook'.

In early October, S&P had placed both credits on "CreditWatch negative" given the Agency's work with JPMorgan to explore financing options on the letter of credit ("LOC") and a reflection "on the fact the agency has less room to maneuver." The action on November 21 was related to the removal of the "CreditWatch negative" and to make changes to the ratings reflecting the current financial position of the Agency subsequent to JPMorgan's extension of the LOC to July 1, 2012.

Copies of the rating reports for the Agency Senior Bonds and the Housing Set-Aside TABs are attached to this memo and in summary, the rating actions taken by S&P on November 21 reflect the following:

- ***Senior 80% bonds*** – "The rating change reflects [S&P's] view of the tighter maximum annual debt service (MADS) coverage, as a result of assessed value (AV) declines in the past few years…The outlook is negative, reflecting [S&P's] view of outstanding assessed value (AV) under dispute in the fiscal 2011 that represents 20.9% of fiscal 2012 incremental AV."

- ***Housing Set-Aside TABs*** – "The ratings reflect [S&P's] view of…Strong 1.8x maximum annual debt service (MADS) coverage based on fiscal 2012 tax increment"

A frequently asked question with respect to ratings in the "B" category is *"at what level are bonds considered 'junk bonds'?"* Given the current credit ratings, the Agency's 80% Senior Bonds are in the lower medium grade investments category which is two notches above the non-investment grade or speculative ("junk") category of "BB+" for S&P and "Ba1" for Moody's, and one notch above the junk status of "BB+" for Fitch. The 20% Housing Set-Aside Bonds are in the upper medium grade investments category.

Cost Implications

The terms of the Reimbursement Agreement with JPMorgan for the letter of credit on the Agency's variable rate debt sets the LOC fees based on the ratings of the Agency's 80% Senior Bonds. The rating downgrade by S&P results in an increase in the Agency's letter of credit fee for the 80% Junior Bonds secured by letters of credit from JPMorgan from the current fee of 2.25% (~$2.1 million/year) to 2.40% (~$2.2 million/year), or an increase of approximately $140,000 per year.

DEBRA FIGONE
City Manager

RICHARD KEIT
Managing Director

Attachments

Ratings On San Jose Redevelopment Agency, CA's TABs Lowered To 'BBB'; Outlook Negative

Publication date: 21-Nov-2011 11:53:17 EST

View Analyst Contact Information

SAN FRANCISCO (Standard & Poor's) Nov. 21, 2011--Standard & Poor's Ratings Services lowered its long-term rating and underlying rating (SPUR) to 'BBB' from 'BBB+' on San Jose Redevelopment Agency, Calif.'s senior nonhousing tax allocation bonds (TABs) outstanding. Standard & Poor's also removed the outlook from CreditWatch with negative implications and assigned a negative outlook.

"The rating change reflects our view of the tighter maximum annual debt service coverage, as a result of assessed value declines in the past few years," said Standard & Poor's credit analyst Matthew Reining.

The removal of the CreditWatch negative reflects the fact that JPMorgan Chase Bank N.A. amended the subordinate, nonhousing TABs' existing letters of credit (LOCs) with the trustee, which extended the termination dates of the agency's LOCs to July 1, 2012 from Nov. 25, 2011. This action affects the agency's subordinate series 2003A and 2003B bonds, as well as its subordinate series 1996A and 1996B bonds. With the extension, the agency's principal outstanding of $93.5 million (as well as related interest) delays the need to refinance this debt while the California Supreme Court has stayed various redevelopment agency activities including debt issuance. Had the LOC not been extended or otherwise been resolved, under the reimbursement agreement, the full principal and accrued interest would be due to JPMorgan from the agency. The agency's outstanding TABs are secured by a senior lien in both the case of the housing and nonhousing tax increment revenues, and we understand from bond counsel that there are no provisions in the bond documents for cross default on the nonhousing bonds.

The outlook is negative, reflecting our view of outstanding assessed value (AV) under dispute in fiscal 2011 that represents 20.9% of fiscal 2012 incremental AV.

RELATED CRITERIA AND RESEARCH

- USPF Criteria: **Special-Purpose Districts**, June 14, 2007
- **Assessing The Credit Impact Of California's Redevelopment Agency Legislation**, Oct. 24, 2011

Complete ratings information is available to subscribers of RatingsDirect on the Global Credit Portal at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.

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'A' Ratings On San Jose Redevelopment Agency, CA's Housing TABs Removed From CreditWatch; Outlook Stable

Publication date: 21-Nov-2011 00:00:59 EST

View Analyst Contact Information

SAN FRANCISCO (Standard & Poor's) Nov. 21, 2011--Standard & Poor's Ratings Services removed the 'A' long-term rating and underlying rating (SPUR) on San Jose Redevelopment Agency, Calif.'s housing tax allocation bonds (TABs) outstanding from CreditWatch with negative implications. At the same time, Standard & Poor's assigned a stable outlook to the rating.

"The stable outlook reflects our anticipation that the project area will maintain at least good coverage of maximum annual debt service based on the broad project area tax base over the two-year outlook horizon," said Standard & Poor's credit analyst Matthew Reining. "If assessed value continues to decline, leading to further decreases in coverage, we could lower the ratings."

The removal of the rating from CreditWatch negative reflects the fact that JPMorgan Chase Bank N.A. amended the subordinate, nonhousing TABs' existing letters of credit (LOCs) with the trustee, which extended the termination dates of the agency's LOCs to July 1, 2012 from Nov. 25, 2011. This action affects the agency's subordinate series 2003A and 2003B bonds, as well as its subordinate series 1996A and 1996B bonds. With the extension, the agency's principal outstanding of $93.5 million (as well as related interest) delays the need to refinance this debt while the California Supreme Court has stayed various redevelopment agency activities including debt issuance. Had the LOC not been extended or otherwise been resolved, under the reimbursement agreement, the full principal and accrued interest would be due to JPMorgan from the agency. The agency's outstanding TABs are secured by a senior lien in both the case of the housing and nonhousing tax increment revenues, and we understand from bond counsel that there are no provisions in the bond documents for cross default on the nonhousing bonds.

The ratings reflect our view of:

- The large size and depth of the merged project area, which includes more than 8,000 acres throughout San Jose;
- The project area's central position in the Silicon Valley economy;
- Strong 1.8x maximum annual debt service coverage based on fiscal 2012 tax increment; and
- A very low volatility ratio of 0.06, indicating only modest sensitivity to declines incremental assessed value, as well as a relatively mature area.

RELATED CRITERIA AND RESEARCH

- USPF Criteria: **Special-Purpose Districts**, June 14, 2007
- **Assessing The Credit Impact Of California's Redevelopment Agency Legislation**, Oct. 24, 2011

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