

Tax Supported
New Issue

Oakland, California

Ratings

New Issue	
2008–2009 Tax and Revenue Anticipation Notes, Series A and B (Taxable)	F1+
Outstanding Debt	
City of Oakland	
General Obligation Bonds	A+
Pension Obligation Bonds	A
Oakland Joint Powers Financing Authority	
(City of Oakland General Obligation Bond Program)	
Refunding Revenue Bonds, Series 2005	A+
Revenue Bonds, 2005 Series A-1, A-2, and B	A
Lease Revenue Refunding Bonds (Oakland Administration Buildings), 2008 Series A-1, A-2, and B	A

Rating Outlook

Stable

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New Issue Details

Sale Information: \$155,000,000
2008–2009 Tax and Revenue Anticipation Notes, consisting of approximately \$70,000,000 Series A and approximately \$85,000,000 Series B (Taxable). Series A to sell competitively on or about June 25, series B to sell June 26 via negotiation.
Security: Both series secured by taxes and other unrestricted revenue received by the city of Oakland during fiscal 2009.
Purpose: Assist the city's cash flow.
Final Maturity: Tentatively June 30, 2009.

Rating Rationale

- Projected coverage of note set-asides is strong, particularly when borrowable resources are included.
- Cash flow holds up well to stress scenarios, including modeling the impact of slower tax growth than budgeted and a labor cost increase.
- Cash flow projections are based on a proposed budget that includes optimistic tax performance and no allowance for additional costs of labor contract renewals.
- Oakland's 'A+' general obligation bond rating reflects a deep and diverse economic base and consistently strong financial position with above-average unreserved general fund balances, balanced by above-average debt ratios and vulnerability to the economic and financial effects of a downturn in residential real estate.
- The 'A' rating on the lease revenue bonds reflects the transactions' sound structures and essential leased assets.

Key Rating Drivers

- For the tax and revenue anticipation notes (TRANS), the city's willingness and ability to adjust spending in response to negotiated labor agreements and variations in tax revenue performance and/or state receipts are key to this short-term rating.
- For the long-term ratings, the city's ability to retain fiscal balance in light of a slowing economy, personnel costs increases, and likely state funding reductions is paramount.

Credit Summary

Fitch Rating's 'F1+' rating is the highest for short-term debt and reflects sound coverage of note principal and interest by available revenue, repayment set-asides made in April and June, and the sufficient cushion provided by borrowable resources at note maturity. Also, the projected cash flow holds up well to stress scenarios that envision weaker tax revenue and higher labor costs.

Oakland's 'A+' general obligation bond rating also is a factor in rating the notes. The long-term rating reflects the city's above-average unreserved general fund balances and adherence to many conservative financial management policies. While the city has benefited from very healthy assessed valuation (AV) growth, the area's property market slowdown will create financial pressure given the importance of property tax revenues. Fitch views the city's tax revenue projections for fiscal 2009 as optimistic. Debt is moderate to high and the city has a sizable unfunded actuarial accrued liability in its pension system, which it will need to start paying down in fiscal 2012.

The TRANS are secured by unrestricted revenue projected to be received in fiscal 2009, which totals \$789.5 million and covers TRAN principal and interest a high 4.85 times (x). The city covenants to set aside one-half of the principal payment in April, and the second half, plus interest, in June. These set-asides are covered 2.2x and 1.74x, respectively. Also, the city consistently has about \$75 million in funds at year end that can be borrowed from to meet note repayment if the cash flow varies significantly from the forecast.

Related Research

- *Oakland Joint Powers Financing Authority, California, March 27, 2008*
- *Rating Municipal Short-Term Debt, Oct. 18, 2007*

Rating History — GO Bonds

Rating	Action	Outlook/ Watch	Date
A+	Affirmed	Stable	4/2/08
A+	Assigned	Stable	4/8/97

Oakland’s projected cash flow continues to show strength under various stress scenarios, including two that project property, sales, business license, and real estate transfer taxes at one-half of the growth budgeted by the city. Fitch views these stress scenarios as important given the optimistic assumptions regarding tax gains and the ongoing labor negotiations with all city unions except police.

This TRAN issuance is similar to Oakland’s sale for fiscal 2008, with the series A notes utilized to offset the uneven nature of property and other tax revenue and the series B proceeds used to make the city’s annual pension payment early in the fiscal year, with the city receiving a discount on the payment.

Note Structure and Coverage

The TRANs are secured by the city’s GO pledge payable from a first lien on unrestricted revenue received in fiscal 2009. According to fiscal 2009 cash flow projections, unrestricted revenue will be \$789.5 million. The total amount covers expected note principal and interest (\$162.8 million) a strong 4.9x.

To further ensure noteholder payment, the city covenants to deposit 50% of the principal due by April 2009; the remaining 50% of principal, as well as accrued interest, will be deposited in June 2009. This schedule is the same as was used in prior years’ TRANs.

The set-aside payments are restricted solely for note repayment. These payments have solid coverage by the cash flows during their respective periods. The April set-aside is covered 2.2x by cash available during that period. The June set-aside is also covered adequately at 1.7x.

The city’s borrowable funds add a strong cushion against unanticipated revenue or expenditure variances. The borrowable funds are substantial, estimated at roughly \$76 million for fiscal year-end 2009, about the same as in prior fiscal years. These funds include city revenue received but not yet credited to the general fund and separate revenue that belongs to other city funds but is legally available for lending to the general fund, if necessary. Additional flexibility is achieved in that the funds are unrestricted and do not require city council approval for use.

Cash Flow and Stress Scenarios

Like many California municipalities, Oakland issues TRANs to assist its annual cash flow by mitigating timing differences between property, state, and local tax receipts and expenditures. The city receives 43% of its property taxes, which make up slightly more than 30% of projected general fund receipts, in December and 35% in April and May combined. However, the city’s diverse revenue stream, including utility user, real estate, hotel, and parking taxes, assists the cash flow by leveling the revenue stream.

The city’s cash flow projections are based on the proposed fiscal 2009 budget. Fitch believes that the tax revenue forecast is optimistic, with property taxes expected to increase 7.9%, sales taxes 5.8%, business taxes 7.7%, and real estate transfer taxes 10.5%. While the city points to the recent completion of properties, including several condominiums, and better enforcement of business tax collections as reasons for the assumed tax gains, Fitch views these revenue sources as vulnerable to weak economic indicators evident nationally and in many parts of California. Nonetheless, the two note repayment set-asides remain well covered under a stress scenario assuming that tax revenue gains are only one-half of the projected figure.

Fitch’s stress scenarios, detailed in the following sections, are designed to address some of the uncertainties inherent in cash flow projections and TRANs borrowing. These scenarios test the cash flow’s resilience and the adequacy of borrowable funds to illustrate possible

outcomes and their attendant impact on the ability to repay noteholders. However, the scenarios are not meant to be predictions of forthcoming actions or city responses. In fact, the scenarios assume the city takes only the limited action described to cure revenue shortfalls. Other, likely more effective, options exist. Given this limited response, the ending deficits that occur in later months are well within the borrowable funds' range.

Stress Scenarios

Stress scenario I assumes that beginning in August, monthly receipts are delayed, and the prior month's ending balance must cover 25% of the following month's disbursements. This scenario also assumes that the receipt delay is corrected by month's end, so the effect on the balance is not cumulative.

Projected General Fund Cash Flow

(\$000, Fiscal 2009)

	July	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	March	April	May	June	Total
Beginning Balance	62,626	110,464	47,165	44,429	36,372	17,222	104,181	98,202	107,877	112,245	92,763	102,910	—
Receipts	9,771	21,584	50,914	29,694	18,905	136,241	43,947	44,789	49,096	94,795	48,179	86,619	789,535
Note Proceeds	155,000	0	0	0	0	0	0	0	0	0	0	0	155,000
Total Receipts	164,771	21,584	50,914	29,694	18,905	136,241	43,947	44,789	49,096	94,795	48,179	86,619	944,535
Disbursements	116,932	84,883	53,651	37,751	38,055	49,282	49,926	35,115	44,728	36,777	38,032	54,654	794,785
Note Repayment	0	0	0	0	0	0	0	0	0	77,500	0	77,500	155,000
Total Disbursements	116,932	84,883	53,651	37,751	38,055	49,282	49,926	35,115	44,728	114,277	38,032	132,154	949,785
Ending Balance	110,464	47,165	44,429	36,372	17,222	104,181	98,202	107,877	112,245	92,763	102,910	57,376	—
Note Repayment Coverage	—	—	—	—	—	—	—	—	—	2.20	—	1.74	—
Stress Scenarios													
Adjustment SSI ^a	21,221	13,413	9,438	9,514	12,320	12,482	8,779	11,182	28,569	9,508	33,038	0	—
Ending Balance SSI	89,243	33,753	34,991	26,858	4,901	91,700	89,424	96,695	83,676	83,255	69,872	57,376	—
Adjustment SSII ^b	24	191	1,001	469	286	3,788	687	739	1,122	2,399	1,188	1,574	—
Ending Balance SSII	110,440	46,974	43,428	35,903	16,936	100,393	97,515	107,138	111,123	90,364	101,722	55,802	—

^aStress Scenario (SS) I assumes that monthly receipts beginning in August are delayed and that the prior month's ending balance must cover one-quarter of the following month's disbursements. ^bSS II assumes property, sales, business license, and real estate transfer tax revenue grows at one-half of projected gain over fiscal 2008 expected amounts.

Stress scenario II assumes that property, sales, business, and real estate transfer tax receipts rise at one-half of the amount assumed in the proposed budget, as detailed above. The impact on the cash flow is cumulative, affecting each month's and the year's total receipts.

Long-Term Rating Factors

The city's debt levels are moderate to high. Net direct debt totals \$1.4 billion, or \$3,519 per capita and 3.5% of taxable AV. Overall net debt is much higher at \$2.5 billion, or \$6,276 per capita and 6.3% of taxable AV. Principal amortization of long-term debt is above average at 68.4% retiring within 10 years. Total outstanding debt includes GO unlimited tax bonds issued to fund various public purposes such as open space development, emergency response, and seismic reinforcement, as well as capital improvements to senior centers, stables, gardens, parks, and recreational facilities. Debt also has been issued to support the civic improvement corporation, administration buildings, and the convention center. The city has a sizable unfunded actuarial accrued liability in its pension system, which the city will need to start paying down in fiscal 2012.

The city's financial position through fiscal 2007 was strong despite a \$9.4 million decline in its unreserved general fund balance between fiscal years 2006 and 2007. Its unreserved

general fund balance remained above-average at \$143.0 million, or 25.5% of total expenditures, transfers out, and other uses.

For fiscal 2008, the city's cash flow has had to absorb \$30 million, including a planned fund balance reduction (\$9 million), increased general fund transfers (\$12 million), and delayed parking meter lease revenues (\$4.5 million). This is likely to result in an operating deficit for fiscal 2008 and would decrease the unreserved general fund balance to \$117.5 million, which is still a high 24% of spending. While the city is projecting that it will maintain its high unreserved general fund balance in fiscal 2009, Fitch views the city's tax revenue projections for that year as optimistic.

Oakland is a major commercial and trade center in the San Francisco Bay area. The city's diverse economic base continues to expand. Oakland is home to Kaiser Permanente's headquarters, several large hospitals, Oakland International Airport, the Port of Oakland, and a regional federal government center. The economy has been growing in the high-technology, medical, government, construction, and service sectors.

The city's AV has posted impressive gains, with growth averaging 9.3% per year between fiscal years 2002 and 2008. Numerous large scale residential, commercial, and mixed-use developments are currently under construction or in the planning and approval process. However, the property market has been slowing in line with national trends. The city is experiencing this downturn most notably in new, lower-cost housing located in the city's eastern districts and in some multiphase developments. While the city's office vacancy rate is increasing, in part due to extra supply, its office rental rates are increasing. The property tax base is diversified, with the top 10 taxpayers accounting for 3.2% of total AV. TAV per capita is strong at almost \$100,000 per resident.

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