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Summary:

Metro, Oregon; General Obligation

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Summary:

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Credit Profile		
US$12.68 mil full faith and credit rfdg bnds ser 2013 due 08/01/2022		
Long Term Rating	AAA/Stable	New
Metro GO		
Long Term Rating	AAA/Stable	Affirmed
Metro GO bnds (Zoo and Natural Areas Proj)		
Long Term Rating	AAA/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'AAA' long-term rating to Metro, Ore.'s $12.7 million series 2013 full faith and credit refunding bonds. In addition, Standard & Poor's affirmed its 'AAA' long-term rating on Metro's previously issued GO obligations. The outlook on all ratings is stable.

The rating reflects our view of Metro's:

- Very large and diverse tax base, encompassing most of the Portland region;
- Relatively low level of funding interdependencies with the federal government;
- Strong operational performance and financial reserves;
- Strong financial policies and practices; and
- Low debt burden relative to market value.

The bonds are secured by Metro's full faith and credit, including the obligation to levy ad valorem property taxes within constitutional restrictions, which include limits on the growth of assessed value and maximum levy rates. We understand that Metro will use the series 2013 bond proceeds to refund all or a portion of its series 2003 full faith and credit refunding bonds to achieve interest savings over the same amortization period.

Encompassing 1.5 million residents in the urbanized portions of Clackamas, Multnomah, and Washington counties, Metro serves the bulk of the Portland region within the State of Oregon. An elected council representing districts within the service area governs Metro, and its areas of responsibility include:

- Regional planning for population growth;
- Metropolitan transportation planning (including distribution of federal transportation funds);
- A regional park system;
- The Oregon Zoo;
- A collection of civic facilities in central Portland, including the Portland Center for the Performing Arts and a convention and exposition center; and
- A regional solid waste and recycling utility.

The economic recovery in the Portland region appears to have found traction. Metro's three counties experienced

year-over-year growth in the number of employed residents during April 2010-September 2012 (although they declined in October and November 2012), and their combined unemployment rate was 7.1% for November 2012, which was down from a peak of 10.6% in February 2010. Likewise, as measured by the Standard & Poor's/Case-Shiller Home Price Index, the region's housing market has started to recover, with positive seasonally adjusted growth since February 2012, although it would need to grow by 31% to return to its peak in 2007. Within Metro's taxing area, market value is down 17% from its peak in 2009 but fell by just 2% in fiscal 2013 to $182.1 billion. We view Metro's income profile as good, with the median household effective buying income of the three counties at about 106% of the national level.

Metro exhibits a relatively low level of funding interdependencies with the federal government. For 2012, capital and operating grants, a portion of which the state also provides, represented 10% of total governmental expenses.

Metro has maintained a very strong financial position, in our view, for more than a decade, but the often project-specific nature of its operations can lead to fluctuations. Since fiscal 2006, when Metro consolidated most of its funds into its general fund in advance of Government Accounting Standards Board (GASB) Statement No. 54 guidelines, its available general fund balance has ranged from 38.2% to 64.9% of expenditures. The balance was at the low end of this range, $27.3 million, at the end of fiscal 2012 but we consider it to be very strong in relative terms. Management reports that one recent source of revenue pressure was a decline in solid waste tonnage, which drives both its solid waste enterprise revenue and an excise tax that flows to the general fund. We understand that Metro responded with targeted expenditure reductions in most activities, small fee increases, a freeze on management compensation, and a slowdown in staff salary growth. Nevertheless, Metro's available balance declined in fiscal years 2011 and 2012, partly because of accelerated grant disbursements for planned transit-oriented development projects.

Metro's most recent midyear financial report, based on the first three-months of actual figures, projects an after-transfer operating deficit of 6% of expenditures on a budgetary basis. In response to its baseline forecast of continued operating balances through fiscal 2016 even with an expected 4% full-time equivalent employee decline between fiscal years 2012 and 2015, management has indicated that Metro is developing a plan for additional spending reductions to structurally balance its operations. Encroachment by parks expenses and declining federal support for planning are key challenges but increased revenues for zoo operations decreases the need to use unrestricted revenues for this function. We understand that voters in May 2013 will consider a temporary property tax increase to fund improvements and deferred maintenance of Metro's parks and natural areas assets, which could address part of Metro's operating challenges.

Helping Metro to maintain a pattern of very strong reserves, in our view, is its inclusion of a current-year contingency of 4% of operating expenses in its budget to address unanticipated costs or a downturn in revenues and an additional 3% "stabilization" reserve from which Metro can draw to absorb revenue losses or unplanned expenditures. Metro's policy is to replenish the funds within two years should it draw from the reserve.

We note that the state property tax framework, which, on average, creates a gap between assessed value (AV) and market value by limiting AV growth to 3% per year excluding new construction, largely insulates Metro's property tax revenue (14% of budgeted fiscal 2012 general fund revenue) from real estate market declines. For fiscal 2013, total AV was 72% of market value.

We consider Metro's management practices "strong" under our Financial Management Assessment methodology. An FMA of "strong" reflects our view that practices are strong, well embedded, and likely sustainable.

We consider Metro's combined direct and overlapping debt to be moderate, at 3.1% of market value and $3,785 per capita. Amortization is rapid, with 66% of principal retired within the next 10 years, and virtually all of Metro's debt consists of GO bonds, which have a dedicated tax levy specific to each series. However, we believe that this retirement speed and the organization's limited operations translate into elevated carrying charges, at about 45% of noncapital total governmental funds expenditures, adjusted for its series 2012A GO bonds the debt service, which started in fiscal 2013. We understand that Metro retains about $40 million in authorization for GO debt for zoo projects, which it plans to exercise next in 2015, and about $28 million in authorization for GO debt for natural areas purchases, which management reports will depend on real estate market conditions.

Metro makes its full annual required contribution to the state-managed defined-benefit and hybrid defined-benefit and defined-contribution pension plans that cover its employees. The annual pension cost for these expenses totaled 3.8% of total governmental funds expenditures in fiscal 2012 and may gradually decline in relative terms over time, as management reports that Metro's employees have agreed to require that employees hired after fiscal 2012 cover the employee portion of the state contribution. However, this ratio is likely to climb in fiscal years 2014 and 2015 as contribution rates increase in response to investment performance for the state pension system. Its other postemployment benefits (OPEB) liability consists of an implicit subsidy of health care benefits, which allows former employees to participate in its health plan until age 65. Its unfunded actuarially accrued liability at the end of fiscal 2011 was $2.9 million and its annual OPEB cost was $427,000 (0.3% of total governmental funds expenditures), both assuming a 15-year amortization. We understand that Metro does not anticipate setting aside reserves for this liability.

Outlook

The stable outlook reflects our view that Metro's very strong financial position and operational revisions in response to recent operating imbalances will allow it to absorb additional revenue pressures, should they occur. We could lower the rating if Metro substantially draws down its reserves, although we believe that outstanding GO authorization to address capital needs makes this unlikely during our two-year outlook horizon.

Related Criteria And Research

- USPF Criteria: GO Debt, Oct. 12, 2006
- State And Local Government Ratings Are Not Directly Constrained By That Of The U.S. Sovereign, Aug. 8, 2011

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