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RATING ACTION COMMENTARY

Fitch Affirms San Francisco BART's IDR and Sales Tax Revs at 'AA'; Outlook Neg; Affirms GOs at 'AAA'

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Fitch Ratings - San Francisco - 28 Mar 2024: Fitch Ratings has affirmed the ratings on San Francisco Bay Area Rapid Transit District, California (BART or district) as follows:

--$686.7 million general obligation (GO) bonds series 2022D-1 at 'AAA';

--$590.8 million sales tax revenue bonds series 2015A, 2016A, 2017A, 2019A, 2019B at 'AA'; and

--The district's Issuer Default Rating (IDR) at 'AA'.

The Rating Outlook for the GO bonds is Stable. The Outlook for the IDR and sales tax bonds remains Negative.

RATING ACTIONS

ENTITY / DEBT	RATING		PRIOR
San Francisco Bay Area Rapid Transit District (CA) [General Government]	LT IDR Affirmed	AA Rating Outlook Negative	AA Rating Outlook Negative

San Francisco Bay Area Rapid Transit District (CA) /General Obligation - Unlimited Tax - Dedicated Tax/1 LT	LT	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
San Francisco Bay Area Rapid Transit District (CA) /Issuer Default Rating - General Government/1 LT	LT	AA Rating Outlook Negative	Affirmed	AA Rating Outlook Negative
San Francisco Bay Area Rapid Transit District (CA) /Sales Tax Revenues/1 LT	LT	AA Rating Outlook Negative	Affirmed	AA Rating Outlook Negative

VIEW ADDITIONAL RATING DETAILS

SECURITY

The sales tax revenue bonds are payable from a first lien on 75% of the 1/2 cent BART sales and use tax (sales tax) levied in the BART counties.

The GO bonds are secured by a voter-approved unlimited ad valorem property tax levied on all taxable properties within Alameda and Contra Costa counties, and the city and county of San Francisco (collectively, the BART counties).

The sales tax revenue bonds are payable from a first lien on 75% of the 1/2 cent BART sales and use tax (sales tax) levied in the BART counties.

IDR ANALYTICAL CONCLUSION

The 'AA' IDR incorporates BART's superior gap closing capacity, low long-term liabilities and manageable capital spending pressures in the context of an unusually broad and deep economic resource base. The Negative Outlook reflects Fitch's view of BART's challenging post-pandemic revenue recovery environment and the ongoing execution risks BART faces as it adapts to fundamental changes in commuter behavior and transit demand over the next several years.

Fitch believes BART, which has traditionally relied heavily on fares to support strong operating performance, will need additional revenues in future years. This revenue would require outside approval or budget reductions on a scale that are impractical given basic system capital maintenance requirements and longer-term plans for system expansion, absent a dramatic near-term increase in ridership.

The 'AA' IDR continues to reflect BART's superior gap closing capacity, low long-term liabilities and manageable capital spending pressures in the context of an unusually broad and deep economic resource base.

DEDICATED TAX ANALYTICAL CONCLUSION

The 'AAA' rating and Stable Outlook on the 2022 GO bonds is based on a dedicated tax analysis and reflects Fitch's assessment that the pledged revenues for repayment of the GO bonds meet the definition of "pledged special revenues" under the U.S. Bankruptcy Code. Fitch has been provided with legal opinions by district counsel that provide a reasonable basis for concluding that the tax revenues levied to repay the bonds would be considered 'pledged special revenues' in the event of a district bankruptcy.

Together with strong statutory and constitutional provisions, the pledged special revenue status provides both the ability and incentive to continue paying debt service during the pendency of a bankruptcy. Therefore, pursuant to Fitch's Tax-Supported Rating Criteria, the GO bonds may be rated up to five notches above the district's IDR. The 'AAA' unlimited tax GO bond rating is based on a dedicated tax analysis that considers the strength and growth prospects of the tax base.

The 'AA' sales tax revenue bond rating reflects the system's operating risk, which caps the revenue bond rating at BART's IDR. The structure would be rated higher if not for the IDR cap, reflecting both solid growth prospects for pledged revenues and very strong resilience to cyclical sales tax declines.

(SEE BELOW FOR DEDICATED TAX ANALYSIS)

Economic Summary

BART provides essential public transportation services to the San Francisco Bay Area and benefits from one of the strongest economic resource bases in the U.S notwithstanding the recent slowdown in employment growth in the technology sector. The region is home to the world's largest information technology industry cluster, which has driven extraordinary wealth creation and sustained population growth for many years. The Bay Area also has large health care, biotechnology, higher education, retail, professional services, finance, tourism and governmental sectors. Incomes and educational attainment are far above national averages, while poverty rates are well below average.

However, the Bay Area's economic recovery lags that of other localities emerging from the pandemic as a result of a multiple rounds of lay-offs at local tech companies, above average hybrid and remote work labor profile, and reduced traffic in the downtown central business district, evidenced by an above average office vacancy rate.

Fitch expects BART to continue to play a key role in connecting the region's workers to employment centers and in meeting the region's environmental and congestion management goals. However, the transit district will continue to face a challenging revenue environment because of the persistence of remote and hybrid work patterns, which have fundamentally changed commuter patterns and demand for mass transit.

IDR KEY RATING DRIVERS

Revenue Framework: 'a'

Fitch expects the district to experience an extended period of revenue weakness due to reduced ridership. The assessment reflects both a significant and persistent downward adjustment in demand and Fitch's expectation that the district's revenues will grow faster than inflation from its reduced baseline given the resilience of the regional economy and BART's essential role in connecting the region's workers to jobs.

BART's independent legal ability to raise revenues is satisfactory relative to typical cyclical pressures, due to the system's control over fares. However, Fitch believes fare flexibility is not sufficient to fully offset the extraordinary downward shift in long-term commuter demand that is emerging post-pandemic. The district is likely to need new revenue sources in the next several years, and BART's board does not have the authority to raise taxes without outside approval.

Expenditure Framework: 'a'

Fitch expects spending growth to be above revenues at least over the medium term, reflecting weakened long-term revenue trends and preexisting wage and capital pressures. Expenditure flexibility is solid with moderate fixed costs, strong control over service levels and significant pay-go capital spending offsetting a restrictive labor environment.

Long-Term Liability Burden: 'aaa'

Combined debt and pension liabilities are low at 7.5% of personal income. Debt is expected to rise as the district uses voter-approved general obligation bonds to address its backlog of capital spending needs, but the liability burden is expected to remain noticeably below 10% of personal income.

Operating Performance: 'aaa'

The district is well positioned to withstand typical cyclical revenue variability due to healthy reserves relative to historical revenue volatility, consistently positive margins and the ability to offset reasonable revenue losses with spending adjustments and fare increases. Budget management in times of recovery is somewhat mixed with healthy funding of retirement liabilities and conservative, thorough financial planning offset by some historical deferrals of needed capital spending.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--A robust ridership recovery to 65% of pre-pandemic levels or a permanent shift in the revenue structure that provides the district a broader revenue base and returns revenue growth to its prior solid levels;

--Spending adjustments that support long-term structural budget balance in the face of lower near-term revenues and ridership levels;

--For the sales tax revenue bonds positive rating action on the IDR;

--For the GO bonds an upgrade is not applicable given the 'AAA' rating.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A failure to make progress in aligning expenses with existing revenues and/or an inability to secure new ongoing revenue sources well ahead of the expiration of extraordinary federal stimulus measures, leading to structural imbalances that decrease financial resilience;

--A weaker than expected recovery in ridership and revenues that is materially lower than the agency's current 40% to 50% of pre-pandemic ridership levels;

--For the sales tax revenue bonds negative action on the district's IDR;

--For the GO bonds a decrease in the district's IDR below the 'A' level.

CURRENT DEVELOPMENTS

Near-Term Pressures Addressed by Federal and State Aid

BART and other fare-dependent U.S. public transit agencies were among the hardest hit local governments during the pandemic due to the loss of riders and fare revenues through the extended period of shelter-in-place orders and the shift by corporate employers to remote work schemes. To date, the resulting revenue gaps have been filled through a combination of Federal and State Aid, spending reductions, salary savings from vacant positions, as well as modifications to service levels.

BART's financial performance remains strong due more than $1.6 billion of extraordinary federal aid awarded through fiscal 2022 (FYE June 30), which equals more than three years of pre-pandemic fare revenues. The level of aid reflects the acuity of the need among large fare-dependent urban transit providers, their environmental and economic essentiality and an enduring federal commitment to public transportation that has included substantial ongoing support for both capital investments and operations.

BART entered the pandemic with strong liquidity and healthy financial margins. Net revenue coverage, a measure of the district's operating margins, equaled a very strong 2.0x in fiscal 2023 slightly lower than 2.4x debt service in fiscal 2022, but up from 1.6x the prior year. Unrestricted cash and investments increased to a strong $911.0 million, which equates to 348 days cash or 75% of fiscal 2023 spending.

BART's total restricted and unrestricted cash and investment balances equaled $1.69 billion in 2023 down slightly from $1.98 billion the year prior. Revenues rose 12% to just over $1.2 billion with largely as a result of a significant amounts of operating assistance from the various federal and state pandemic assistance programs. However, increased fare revenues (39%) and sales taxes (5%) also contributed to the overall increase noted above.

As Fitch expected, fiscal 2003 results to look similar to 2021 and 2022 results, but the improvement in fare revenue reported in fiscal 2023 is viewed as a credit positive notwithstanding the continuing support from federal and state sources. Fitch believes that fiscal 2021 was likely a low point in fare collections, given the slow but steady rebound in that revenue component. Additionally, the more moderate increases in sales tax revenue in fiscal 2023 belie the economic headwinds caused by high inflation and recently announced layoffs in the Bay Area's tech sector. In 2022, sales tax revenues were up 20%.

Federal and state aid appears sufficient to support revenues near pre-pandemic levels, the highest level of financial resilience and healthy overall financial margins through 2024 and into fiscal 2025 (assuming continued ridership gains and disciplined expenditure management. Longer term, the fundamental changes in commuting patterns will weaken BART's fare-dependent business model. Fare dependence was historically a strength for the district, providing the tools necessary to maintain strong financial performance across cycles through fare increases. Fares equaled about half of revenues excluding capital grants and GO bond levies in fiscal 2019 and equaled about 60% of BART's operating expenses excluding depreciation. The high level of fare revenue reflected the strong in office work culture and the relative strength of BART's business model in earlier periods, its essentiality to the region's commuters and its strong pricing power.

BART relied much less on taxes and other public subsidies than peers. Its West Coast counterparts in the Seattle and Los Angeles metropolitan areas, by comparison, received less than 10% of revenues from fares, depended overwhelmingly on broad, locally generated taxes, and did not experience severe revenue losses in the pandemic.

BART's system was extended to San Jose with revenue service beginning in June of 2020 following the completion of this extension by the Santa Clara Valley Transportation Authority. The expansion provides a direct rail link between relatively affordable East Bay housing markets and Silicon Valley in one of the region's most congested commute corridors, increasing BART's already high essentiality to the region.

Execution Risks in Period of Adaptation

A permanent or long-lasting reduction in transit demand would require fundamental changes in the district's revenue or expenditure frameworks, creating a new risk that far outweighs the offsetting benefit of shrinking the system's capacity. Fitch expects the district to reduce spending where possible but to also seek new revenues to resolve out-year budget gaps ranging between $78 million and $338 million beginning in fiscal 2025 through fiscal 2028 once the federal and state assistance has been exhausted.

Given BART's unclear revenue and ridership path we are maintaining our IDR rating at 'AA' with a Negative Outlook reflecting the ongoing execution risks BART faces as it works to adapt to an environment with reduced demand for core business of providing transportation to commuters to central business districts. Fitch believes the revenue risk associated with the expected loss of ridership and the need for outside approval of the additional taxes are inconsistent with an above-average IDR for the local government sector.

Fitch believes BART's revenue needs are modest relative to the Bay Area's economic resources, and the region's voters have historically demonstrated strong support for transit via earlier sales tax measures in the region. BART's current projected fiscal 2025 revenue gap in its downside ridership scenario equals $330 million excluding the last of its federal assistance dollars. Funding gaps increase to $315 million 2026 without intergovernmental aid. Gaps in 2027, 2028, and 2029 equal $318 million, $292 million and $281 million, respectively. This level of projected revenue losses exceeds the district's practical fare raising flexibility.

Fitch believes Bay Area voters and policymakers may be willing to provide greater subsidies to support mass transit system, but believes timing and political risks inherent in this effort are substantial, particularly given the fragmented nature of the Bay Area's multiple transit systems and overlapping political jurisdictions. Preliminary efforts to place a measure before the voters in 2026 are being weighed.

ECONOMIC RESOURCE BASE

Long-Term Pressures on Business Model

BART ridership and fare revenues remain well below pre-pandemic levels with many employers continuing to allow Bay Area employees to work remotely. Though the fiscal 2023 ridership recovery is confirmed by the higher fare box revenue, the district still lags that of other large urban transit agencies, reflecting its dependence on commuters. Less stringent return to office policies by regional employers and a shift to private vehicle usage will make for an elongated low-ridership period.

Fitch expects BART to adapt to protracted low ridership environment absent a return to pre-pandemic office culture. Fitch also believes the BART's substantial customer base of white-collar and high technology workers are particularly prone to more permanently adopt the changes in commute patterns, thereby reducing the district's ridership base during the traditional work week commuting hours. As a result, the recovery will continue to lag other regions, as ridership remains low through an extended period.

BART will remain essential to the Bay Area economy despite changing commute patterns as the Bay Area's highways and bridges remain capacity constrained. BART will likely remain the sole option for Cross bay travel as nearly half of current riders do not own private vehicles and system expansion projects bring in additional riders, albeit at a slower pace. Regional policymakers and employers remain committed to reducing the environmental impact of vehicle dependence via expansion of public transit and increases in housing density near transit.

IDR CREDIT PROFILE

Revenue Framework

BART's tax raising options -- including sales and parcel tax measures -- would likely require voter approval. Securing additional subsidies from state, federal and regional partners would require legislative approval from bodies outside BART's control, and any attempt to broaden the tax base to cover more of the service area could require state legislative changes.

DEDICATED TAX KEY RATING DRIVERS

Very Strong Resilience: The sales tax revenue bonds have the highest level of resilience at expected leverage levels. Fitch's rating assumes that the district does not significantly further leverage the sales tax revenue stream, reflecting both management plans and the issuer's need for residual sales tax revenues to support operations.

Solid Growth Prospects: The pledged sales tax revenues are expected to return to a pace of growth that exceeds inflation after the current disruption. The sales tax payer base is broad and diverse, and the district's economic resource base has very strong growth prospects.

DEDICATED TAX CREDIT PROFILE

The dedicated taxes pledged to the bonds do not meet the requirements set out in Fitch criteria for treatment as 'pledged special revenue' under section 902(2) of the bankruptcy code and are not otherwise insulated from the BART's operating risk. Therefore, the rating of the debt is capped at the IDR.

Sales taxes grew at CAGR of 4.6% for the 10-year period ending fiscal 2023. Fitch expects that revenue performance will continue to trend above long-term U.S inflation but below national GDP growth, consistent with historical performance, given solid economic and demographic growth within the BART counties.

Fiscal 2023 pledged revenues for the sales tax revenue bonds provided 5.52x coverage of maximum annual debt service (MADS) of $59.3 million. To evaluate the sensitivity of the dedicated tax revenue stream to cyclical decline, Fitch considers both a revenue sensitivity scenario and the largest decline in revenues over the period covered by the revenue sensitivity analysis. Based on the district's sales tax revenue history, the Fitch Analytical

Stress Test (FAST) generates a 5.7% decline in pledged revenues under the standard 1% U.S. GDP decline scenario. The largest cumulative revenue decline historically was 17.8% over two years in the aftermath of the Great Recession from fiscal years 2009-2010.

Assuming issuance up to the 1.5x additional bonds test (ABT), the structure could tolerate a 33% drop in revenues. However, Fitch does not expect material additional parity debt issuance. Given the district currently has no plans to further leverage the revenue stream and needs the excess cash flows to fund its ongoing operating and pay-go capital budget, Fitch assumes leverage will be limited to 4.0x MADS. At that leverage level, sales tax revenues could fall 75% before reaching 1.0x debt service coverage. The coverage cushion is roughly 13.2x the recessionary decline scenario produced by the FAST model and 4.2x the decline of the Great Recession, which Fitch views as consistent with a 'aaa' level of financial resilience.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

San Francisco Bay Area Rapid Transit District (CA) [General Government] has an ESG Relevance Score of '4' for Labor Relations & Practices due to {DESCRIPTION OF ISSUE/RATIONALE}, which has a negative impact on the credit profile, and is relevant to the rating[s] in conjunction with other factors.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

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APPLICABLE CRITERIA

U.S. Public Finance Tax-Supported Rating Criteria (pub. 04 May 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

San Francisco Bay Area Rapid Transit District (CA)	EU Endorsed, UK Endorsed

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The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. For more details on sector-specific best- and worst-case scenario credit ratings, please see Best- and Worst-Case Measures under the Rating Performance page on Fitch's website.

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