December 7, 2017

Memorandum

To: STA Board of Directors

From: Peter Shellenberger, *PFM Financial Advisors LLC*

Re: STA 2009C Standby Purchase Agreement Extension and Swap Amendments

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Introduction

PFM Financial Advisors LLC ("PFM"), as the financial advisor to Sacramento Transportation Authority ("STA" or "Authority"), has worked with STA staff to prepare the recommended strategy of keeping the Series 2009C variable rate bonds in their current form and extending the existing Standby Bond Purchase Agreement ("SBPA") with the existing liquidity provider, US Bank, for 18 months. This memorandum discusses the rationale behind this recommendation.

PFM worked with STA staff to evaluate options to either refund the 2009C Bonds or keep the 2009C Bonds in their current form and extend the SBPA with US Bank. The benefit of refunding the 2009C Bonds is the Authority's ability to re-write a specific bond covenant and release approximately $8.1 million in bond proceeds that are currently deposited in the debt service reserve fund ("DSRF"). These proceeds will be available for projects upon release.

However, the tax reform bill currently negotiated in the US House and Senate creates uncertainty regarding the most cost-effective way to refund the 2009C Bonds. The two options for refunding include the use of publicly sold variable rate demand bonds ("VRDB") or floating rate notes ("FRN") that are directly purchased and held by a commercial bank. The pending tax reform bill may result in one strategy being lower cost than the other: currently they are very close to one another in terms of cost.

We expect negotiations on the tax bill to be complete in the coming weeks and the impacts of tax reform to be better understood over the following months. With this expectation, PFM recommends that the Authority maintain the current structure of the 2009C Bonds and extend the SBPA with US Bank for 18 months, with the option to refund in 12 months with no early termination fee under the SBPA agreement. This will allow STA's team to clearly understand the impact of tax reform and recommend the lowest cost option for refunding under the new tax regime. This strategy bides time without incurring the full cost of a refunding and positions the Authority to refund and release the proceeds in the DSRF in December 2018, should the Board decide to refund at that time.

In addition to extending the SBPA with US Bank, it is recommended that the Authority make amendments to the swap agreements to add Fitch Ratings as an eligible rating agency under those agreements and to effectuate certain technical changes to those agreements to allow for the potential refunding of the 2009C Bonds in the future. The Authority's Bond counsel has worked with the Authority's swap counterparties to amend the swap agreements and has provided forms of these documents for Board consideration and approval. Approval of these amendments will place the Authority in a state-of-ready to refund the 2009C Bonds when the Board deems it appropriate to proceed.

Commensurate with this recommendation are the following documents to extend the existing SBPA associated with the 2009C Bonds and amend the current swap agreements:

1. Authorizing Resolution
2. Amendment No. 4 to Standby Bond Purchase Agreement
3. Amendment No. 1 to Fee Letter Agreement
4. Forms of Amendment to the Swap Agreements

Debt Portfolio Overview and the SBPA Extension

The Authority currently has $364.6 million of debt outstanding, consisting of the Series 2009C VRDBs, the Series 2012 fixed-rate bonds, the Series 2014A FRNs, and the Series 2015A VRDBs. The Authority's bonds hold long-term credit ratings of AA+/AA+/Aa3 from Standard & Poor's, Fitch, and Moody's, respectively. The table below summarizes STA's existing debt portfolio:

Sacramento Transportation Authority Debt Summary

SERIES	OUTSTANDING PAR	FINAL MATURITY	MODE	SBPA/DIRECT PURCHASE	EXPIRATION/ TENDER DATE	REMARKETING AGENT
2009C	*$106,100,000*	*10/1/2038*	*Weekly VRDB*	*US Bank*	*1/7/2018*	*US Bank*
2012	$46,315,000	10/1/2027	Fixed-Rate	N/A	N/A	N/A
2014A	$106,100,000	10/1/2038	FRN	Wells Fargo	8/10/2020	N/A
2015A	$106,100,000	10/1/2038	Weekly VRDB	Mizuho	3/12/2018	JP Morgan
Total	$364,615,000					

Of the Authority's $364.6 million of debt, $212.2 million are VRDBs supported by SBPAs – Series 2009C Bonds and Series 2015A Bonds. The SBPAs are agreements in which commercial banks agree to purchase and hold the bonds if there is insufficient investor demand in the public capital markets. Since inception, there has always been strong investor demand for the STA's bonds and there has been no need to draw upon the SBPA. That said, SBPAs are necessary to insure liquidity for investors under the VRDB structure.

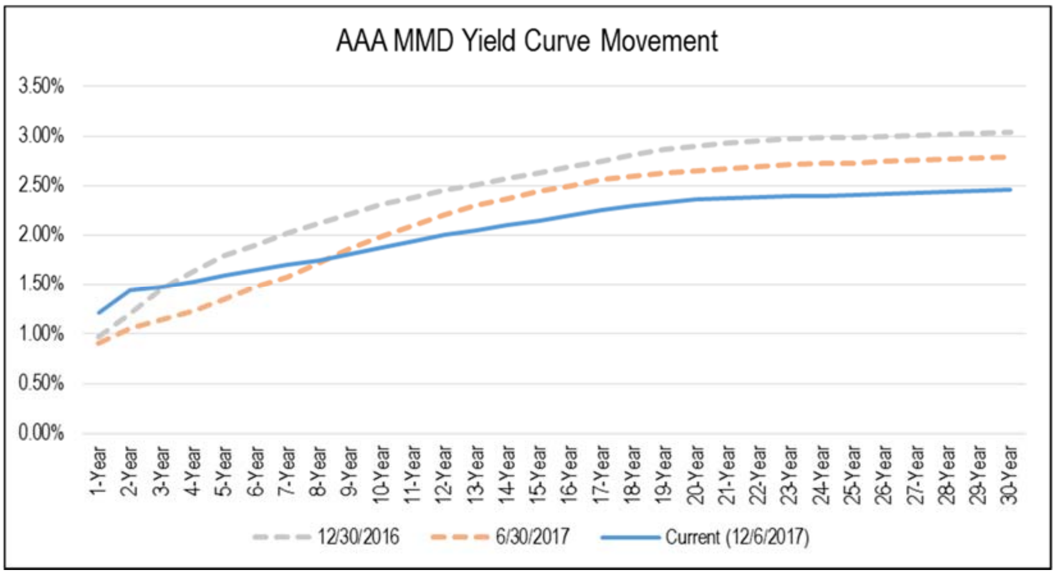
The proposed SBPA extension with US Bank is an 18-month agreement that costs 0.38% annually. The extension proposal has a 12-month make-whole provision, which allows the Authority to terminate the agreement after 12 months at no additional cost. Furthermore, this extension does not add any additional debt. This structure is conservative enough to weather the uncertainties of tax reform, yet flexible enough to adjust course once the impacts are known.

Swap Amendments

The proposed amendments to the STA swap agreements are not considered material and have been agreed to by the Authority's swap counterparties. The amendments allow the Authority to add Fitch Ratings as an eligible rating agency under those agreements. Fitch Ratings has already been added under relevant bond documents and they will now be included in the swap agreements. Additionally, the proposed amendments effectuate certain technical changes within the definition of outstanding bonds which will allow for the potential refunding of the 2009C Bonds in the future. The Authority's Bond counsel has worked with the Authority's swap counterparties to amend the swap agreements and has provided forms of these documents for Board consideration and approval. Approving these amendments at this point in time will place the Authority in a state-of-ready to refund the 2009C Bonds when the Board deems it appropriate to proceed in the future.

Market Update

Demand for municipal bonds continues to be strong, resulting in low long-term borrowing rates. As of December 6, 2017, the 30-year interest rate of the AAA Municipal Market Data ("MMD") index, the benchmark index for long-term tax-exempt bonds, was 2.46%. Over the course of the previous five trading days, it declined 0.29% as investor demand remains strong. Conversely, short-term tax-exempt rates have risen, as the market anticipates the Federal Open Market Committee increasing the Federal Funds target rate range to 1.25% - 1.50% at its December meeting. Importantly to STA, as short-term rates increase, both the payments on STA's bonds as well as receipts on the STA's swap will increase, offsetting one another and providing a hedge against the increase from a cost perspective. Currently, the 1-year interest rate for tax exempt bonds (based on the AAA MMD Index) is 1.21%, and hasn't been this high since 2008. The graph below illustrates how the AAA MMD yield curve has moved over the past year.



In November and December, the House and the Senate passed separate tax reform bills that will have sweeping impact, including impact to the municipal bond market. The House's version of the bill eliminates private activity bonds ("PABs"). The Senate's version retains PABs. STA has not used PABs as part of their financing strategy and this change should not have a direct impact to STA. Both the Senate and House version of the bill eliminates the use of tax-exempt bonds for advance refundings – refunding existing bonds more than 90 days before their call date. While advance or early refundings would be eliminated under the new tax bill, the Authority still retains the ability to refund existing fixed rate bonds upon their call date on a tax exempt basis. This change should not have significant impact to STA.

The uncertainty around tax reform is expected to boost bond issuance in December as many issuers advance refund bonds before that provision is potentially eliminated. Going forward, if advance refundings and PABs are eliminated this could reduce bond supply available to investors in the coming years. The effect of reduced supply could have a positive impact on the issuers by reducing interest rates. That said, the proposed reduction of the corporate tax rate from 35% to 20% would reduce the benefit/value of tax exemption and could put increased pressure on tax-exempt municipal interest rates. With the sweeping nature of this proposed tax reform bill and the many variables impacted, the end result on interest rates and the municipal bond market will take several months, after implementation, to be fully comprehended. PFM is continually monitoring these developing changes and will keep STA's staff and Board fully informed along the way.