Summary:
New York City Transitional Finance Authority; Miscellaneous Tax

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Credit Highlights

• S&P Global Ratings assigned its 'AAA' long-term rating to the New York City Transitional Finance Authority's (TFA) approximately $1.03 billion future tax secured (FTS) subordinate bonds fiscal 2023 series B, consisting of tax-exempt subseries B-1 (approximately $980.3 million) and taxable subseries B-2 (approximately $54.0 million).

• At the same time, we assigned our 'AAA' long-term rating the TFA's approximately $50.3 million FTS subordinate bonds fiscal 2023 series C, consisting of tax-exempt subseries C-1 (approximately $6.9 million) and taxable subseries C-2 (approximately $43.4 million).

• The long-term rating on TFA’s senior and subordinate FTS bonds outstanding is 'AAA'.

• The outlook is stable.

Security

Personal income tax (PIT) revenue and, if needed, sales and use tax revenue generated within the City of New York secure the subordinate (second-lien) FTS bonds. Proceeds will refund TFA bonds outstanding.

Credit overview

Coverage and liquidity metrics supporting the AAA/Stable rating remain very strong, including PIT, which are expected to reach a record $16.6 billion in fiscal 2022. Two back-to-back years of remarkable collections reflect record Wall Street profits and higher bonus income, income tax withholdings on individual unemployment federal stimulus payments, and an economic recovery that began earlier than projected. However, with economic uncertainty stemming from the unknown duration of high inflation, supply chain issues, higher energy prices, and equity markets volatility, the June 2022 financial plan shows PIT declining in fiscal 2023 to $15.3 billion (7.6% below that of fiscal 2022). We believe the city's conservative estimate is largely based on projections that Wall Street profits will decline to $19 billion, or about historical averages, in calendar 2022 (down from $58 billion in 2021) and likely underscore more modest bonus income and lower PIT collections in fiscal 2023.
After a stall in the city’s economic recovery during the winter months of 2021 into 2022, spring and summer travel activity, acceleration of hybrid work schedules by major employers, and the federal government’s lifting of COVID-19 testing requirements for inbound international tourists spurred hiring in the leisure and hospitality sector, helping the city recover 79% of the jobs lost during the pandemic. In addition, a better-than-forecast job recovery pushed the city's unemployment rate to its lowest since the onset of the pandemic, though the rate remained higher than that of the U.S. at 6.1% in June 2022 (down from 10.6% in June 2021; rates not seasonally adjusted). Leisure and hospitality struggled to recover, but employment in this sector appears to be stabilizing, as is particularly evident in officials' reporting that tourism trends are 90% of 2019 activity, which exceeds NYC & Co.'s 2022 forecast for 56.4 million visitors (85% of 2019). That said, we believe that the emergence of a new infectious or more lethal COVID-19 variant or the monkeypox public health emergency could dampen activity.

Also supporting the high rating is the city's transfer of its rights, title, and interest in pledged revenue to the authority that enhances the statutory and legal mechanisms that separate control of the revenue from the city, supporting an obligor linkage we view as remote. However, risks remain that tether the priority lien rating to the city's obligor's creditworthiness, which is equivalent to the general obligation (GO) rating. The City of New York GO rating is 'AA' and is constrained by the city's very weak debt and contingent liability profile, which strong and well-embedded management practices offset.

Other key credit considerations include:

- Consistent expansion and diversification of New York City's economy, which has shown resilience as the pandemic waned following the abrupt contraction in 2020 (although we believe that macroeconomic conditions may slow the recovery in the second half of calendar 2022);
- Fiscal 2022 pledged revenue forecast of nearly $25 billion (15.5% above actual fiscal 2021 collections) that provides very strong 7.8x coverage of estimated annual actual debt service due in fiscal 2022 and our expectation for maintenance of at least 4x maximum annual debt service (MADS) coverage on subordinate-lien debt service over the outlook period;
- Strong bond provisions, including what we consider a conservative additional bonds test (ABT) of at least 3x MADS and maximum MADS of $1.32 billion for the senior-lien bonds, well in excess of current MADS of $73.8 million (calculated at the maximum variable rate), and at least 3x the sum of covenanted MADS of $1.32 billion on senior-lien debt plus annual debt service on subordinate debt for the subordinate-lien bonds;
- Our view that nationwide income and sales use taxes have historically demonstrated low-to-moderate volatility, with the breadth of the city's sales and use tax base offsetting cyclical volatility associated with PIT; and
- The city's general creditworthiness, which does not constrain the rating but will remain a consideration, as we see risks that could impair pledged revenue if the City of New York were to become pressured.

Environmental, social, and governance

We view the environmental, social, and governance factors that could affect TFA's economic base on which pledged revenue is collected as somewhat similar to those of the city, particularly should exposure to severe weather events and other chronic physical climate risks disrupt economic activity or pledged revenue collections. A potential resurgence of the pandemic still presents a health and safety social risk that could stall the city's economic momentum and pose greater uncertainty for sales tax collections, though resilient PIT collection mitigates the risk. We also view
the governance structure of the TFA's FTS statutory and legal mechanisms positively, as it protects the rights of bondholders and limits the city's ability to divert revenue prior to debt service payment.

**Outlook**

The stable outlook reflects our view of growth in TFA's pledged revenue, which has shown resiliency through multiple economic cycles, including the most recent shock from the pandemic. As a result, TFA annual debt service coverage and MADS coverage remain extraordinarily strong, and we expect this to continue.

**Downside scenario**

We could lower the rating or revise the outlook to negative in the unlikely event that pledged revenue falls substantially short of the forecast or that TFA accelerates borrowing that leads to materially lower MADS coverage of less than 4x.

**Credit Opinion**

**Economic fundamentals: Very strong**

The sheer size of the economic base supports our very strong view of economic fundamentals despite the effects on the region from COVID-19. For example, the city's population across Bronx, Kings, Queens, Richmond, and New York counties is larger than that of 39 U.S. states and increased to 8.8 million with the 2020 census data. In addition, in 2020 the New York City metropolitan area's GDP remained the highest across the 10 largest metropolitan areas at $1.8 trillion. Although GDP declined 3.4%, it remains more than 50% larger than that of the next-largest metro area (Los Angeles-Long Beach-Anaheim).

The June 2022 financial plan revised PIT up for fiscal 2022 from actual fiscal 2021 collections to $16.6 billion, which incorporates nearly $1.8 billion received year to date compared with the April 2022 financial plan. The updated forecast for fiscal years 2023 through 2026 reflects collections of $15.3 billion, $14.9 billion, $15.5 billion, and $15.9 billion, sequentially. We believe the city's forecast is realistic and reflects slower U.S. growth in the next 12 months, consistent with S&P Global Economics' baseline scenario in the report "Economic Outlook U.S Q3 2022: The Summer Of Our Discontent," published June 27, 2022, on RatingsDirect. In addition, with the city's largest employers in the financial services and technology sectors announcing the phaseout of remote work status in first quarter 2022, we believe subway ridership and demand for restaurants and retail establishments will increase and influence pledged revenue trends. We expect that the city's economy will expand, as occurred following the events of Sept. 11, 2001, and the Great Recession in 2009, bolstered by employment diversification from companies such as Meta, Amazon, TikTok, and Google signing large leases in midtown Manhattan. Finally, the city's excellent universities, access to first-class health care providers, investments by venture capitalists in technology startups, and attractiveness as a leisure and business travel destination support the city's resilient PIT and sales tax trends.

The city levies a 4.5% sales tax on a broad range of economic activity, including retail sales (also from online sales), utilities, communication sales, services, and manufacturing. In addition, it levies a 6% tax on receipts from parking, garaging, or storing motor vehicles. Taxable sales within the city doubled from 2004 to 2020 and, after declining in
2021, rebounded to the pre-pandemic level of $182 billion in 2022 (data from March 1, 2021, to Feb. 28, 2022).

**Coverage and liquidity: Very strong**

Our view of TFA's coverage and liquidity is very strong. Pledged revenue is forecast to increase to nearly $25 billion, or 15.5%, in fiscal 2022, largely reflecting a nearly 10.0% increase in PIT and 28.2% increase in sales tax collections. The fiscal 2022 sales tax trends indicate robust recovery in economic and tourist activity, job growth, and return-to-office trends. Pledged revenue also provides extraordinarily strong annual debt service coverage in fiscal 2022 of 7.8x as well as MADS coverage of 6.7x based on the maximum rate on the variable-rate bonds and 7.0x based on the 4.25% budgeted adjustable rate (when reflecting the refunding executed with the series 2023 B and C transaction). These coverage trends are consistent with our view of the 'AAA' credit rating.

While recent suggestions for increasing the city's debt capacity limits could result in materially more TFA issuance, the change would require various hurdles before coming to fruition. Should this ultimately occur, we believe management would structure debt plans to ensure that pledged revenue continues to provide very high coverage in line with historical trends.

We do not view the TFA's variable-rate portfolio as a negative credit factor given the TFA's management of associated liquidity risk, which we incorporate into our analysis. In addition, given the TFA's historical and projected MADS coverage, we do not view the lack of a fully funded debt service reserve as a negative credit factor.

The senior-lien bonds maintain a conservative ABT of at least 3x covenanted MADS of $1.32 billion, well in excess of current MADS of $73.8 million (calculated at the maximum variable rate). The subordinate-lien bonds have an ABT of at least 3x the sum of covenanted MADS of $1.32 billion on senior-lien debt plus annual debt service on subordinate-lien debt. We believe the city's long-time target of maintaining debt service at less than 15% of tax revenue, along with its reliance on residual PIT and sales tax revenue to fund normal operations, provides bondholders assurance that leveraging pledged revenue up to the ABT for the subordinate bonds is unlikely to occur. Furthermore, the TFA has not issued parity senior-lien debt in recent years, and we expect that trend to continue. Although we do not include unpledged revenue in our calculation of coverage, New York City has prepaid a portion of TFA's debt service from the city's general fund, represented as a grant to the TFA that reached nearly $2.7 billion, to benefit fiscal 2022 results. By providing the grant from the general fund for payment of debt service, PIT revenue that the TFA retains is reduced, allowing the city a larger amount for operations.

**Revenue volatility: Very-low-to-low**

Pledged PIT and sales tax revenue are critical sources that fund city operations, collectively accounting for more than one-third of budgeted city tax revenue in fiscal 2021. We believe that nationwide PIT volatility is historically very low, while sales taxes have experienced low volatility, and this informs our view of the pledged revenue's combined volatility. However, we believe New York City's PIT revenue is cyclical and more sensitive to general economic and tourism trends as well as susceptible to certain market conditions. At the same time, we believe the breadth and diversity of the city's economy provide a broader base for sales and use tax collection, reducing its volatility compared with nationwide trends, even in the current economic environment.

Although each revenue source has experienced cyclical growth and decline, the overall growth trend for both is positive. Either tax source easily covers annual debt service in fiscal 2021, with PIT receipts providing 4.9x coverage
and sales tax collections 2.1x.

The PIT is the TFA bonds’ primary source of security, generating about 70% of statutory revenue in fiscal 2021. Since the TFA was established, PIT revenue has fully covered debt service without any use of sales taxes. In 1966 New York City imposed a PIT, and in 2006 the city returned to a lower schedule of base rates and a 14% surcharge, which resulted in a maximum rate of 3.648%. In 2010, the base rate increased, resulting in a maximum rate of 3.876%. The base rate and the 14% surcharge are scheduled to expire on Dec. 31, 2023. Unless legislation passes extending the base rate and the 14% surcharge, a lower rate schedule with a maximum rate of 1.48% will take effect. Previously scheduled to decline on several occasions since 1989, the base rate was always extended, most recently in April 2020.

**Obligor linkage: Remote**

The state legislature created the TFA under the New York City Transitional Finance Authority Act. The act authorizes TFA to issue debt secured by revenue that the state grants to the authority. The state collects pledged revenue, and PIT revenue is held in trust and transferred to the trustee by the state comptroller. Pledged revenue is not subject to appropriation by the city or state. The TFA indenture creates a lien for the benefit of bondholders that the city and state have covenanted not to limit or alter until the bonds are paid or discharged.

A board of directors manages TFA with the power to approve bond issuances. Five voting directors govern the authority: the director of the office of management and budget, the finance commissioner, the commissioner of design and construction, the comptroller, and the city council speaker. Two of the members are elected officials, the other three are appointed by the mayor, and all are in some way obligated to the residents of the City of New York.

We have also received a legal opinion that the pledged revenue is no longer property of the city under Section 902(1) of the bankruptcy code and would not be treated as such. In the event of a city bankruptcy, a plan of adjustment that contradicts this right and determination by the state would violate state law and thus should not be confirmable.

These factors inform our belief that the legal structure is an intended true sale of the pledged revenue that renders the revenue unavailable to fund operations, and contains other securitization features that segregate pledged revenue prior to the payment of debt service from the city's other revenue and cash balances. Therefore, we view pledged revenue as more insulated from potential operating shortfalls or budgetary pressure wherein it is neither legally nor practically available for operations. However, we believe risks remain that could result in the impairment of the revenue if the city were to become stressed, meaning bondholders cannot be completely isolated from the city's financial and economic condition.

**Rating linkage to New York City**

The City of New York GO rating serves as an assessment of the city's overall creditworthiness and is a key determinant of the authority's ability to pay bonds secured by revenue. While the high investment-grade rating denotes little risk of the city falling into distress, in our view, the potential for lowering the city GO rating cannot be disregarded.

For more information on New York City, see our report published Aug. 12, 2022.

**Ratings above the sovereign**

We rate the TFA bonds above the sovereign because we believe it can maintain better credit characteristics than the U.S. in a stress scenario, based on the locally derived pledged revenue for bondholders and our view that pledged
revenue supporting debt service on the bonds is at limited risk of negative sovereign intervention. The rating above the sovereign is based on our criteria "Ratings Above The Sovereign: Corporate And Government Ratings--Methodology And Assumptions," published Nov. 19, 2013.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.