Financial Services Update

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Greetings from Financial Services:

Beginning this month, Financial Services will provide updates on financial and economic topics of interest to ODOT managers and stakeholders.

The focus of this first issue is the Oregon Transportation Investment Act (OTIA I, II and III) borrowing programs.

Decisions ODOT makes about how and when to issue ODOT's debt can result in savings of millions of dollars in debt service costs.

Future updates will include information about ODOT's budget, revenue forecast and improvements we are making to the services we offer to ODOT.

We welcome your comments or suggestions. Please email me at:

dennis.strachota@odot.state.or.us

Dennis Strachota,
Chief Financial Officer

Combined OTIA spending excludes $300 million OTIA III Local Bridge Bonds distributed as grants in 2004.

Timing of the Next OTIA Bond Issue

Financial Services expects to issue the next OTIA bonds in May 2006. Past and future projected spending will help us establish the size of the next bond issue.

Past Spending

Spending for the three OTIA programs exceeded $505 million in November 2005, excluding the local bridge bonds. This spending has been funded by about $250 million in OTIA bond proceeds and interest earnings and $255 million in existing State Highway Fund cash balances. Spending from the Highway Fund for later reimbursement with bond proceeds has cash management and investment advantages for ODOT. Spending will be reimbursed with each bond issue and the cash balance will be restored to a higher level.

Projected Spending

OTIA spending for the 12 months beginning May 2006 is expected to be about $240 million.

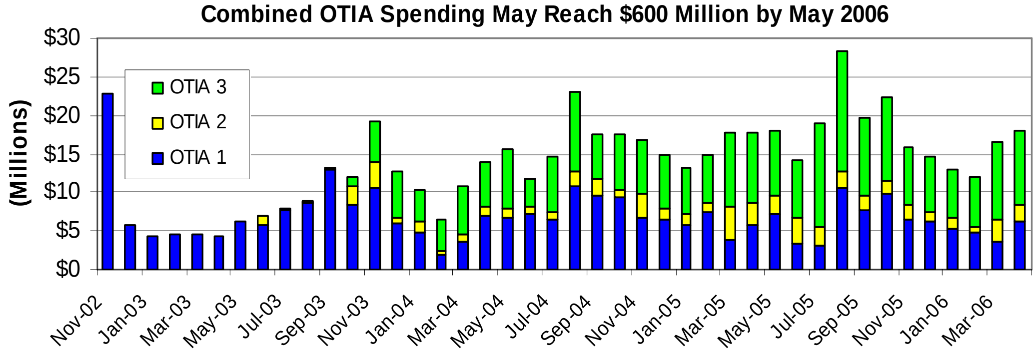
Both the reimbursement amount and the anticipated next year's spending provide indicators of an appropriate amount ODOT should borrow in May 2006. Actual sizing of the issue will be determined in the last month or two prior to the bond issue.

Financial Services will recommend issuance of new bonds annually to provide funds needed for construction during the ensuing year. Annual bond sales will help the Department better manage its cash balances and reduce issuance costs.

In addition, Financial Services will work with State Treasury to establish a short term borrowing option that would allow the Department to provide accelerated funding if project delivery occurs faster than estimated for planned bond issues.

The graph below shows actual and projected OTIA spending from 2002 through May 2006. Spending shown for November 2002 includes all prior months.

Combined OTIA Spending May Reach $600 Million by May 2006



Saving Money for ODOT

Financial Services has the opportunity to save money for ODOT through the OTIA borrowing program. Savings translate to more funding available for construction programs.

Two of the key cost-saving strategies are described at right:

STRATEGY #1

Reduce ODOT's Cost of Borrowing

and

STRATEGY #2

Preserve ODOT's Debt Capacity

Financial Services is a branch of ODOT's Central Services Division. Financial Services provides centralized accounting, financial reporting, payroll and benefits, budget development, economic and financial analysis, business planning, debt administration, cash management, the Oregon Transportation Infrastructure Bank, tax collection and auditing, revenue forecasting, tax policy analysis and cost allocation services.

ODOT Financial Services
355 Capitol Street NE
Room 434
Salem, OR 97301-3872
Phone: 503-986-3900
Fax: 503-986-3906

STRATEGY #1

Reduce Bonding Costs

Various factors affect ODOT's cost of borrowing. Market conditions – in particular, interest rates – are important but are beyond our control. Issuers are advised not to base decisions on interest rate predictions. However, we can influence other factors. Below are some examples:

- **Timing of borrowing**

  ODOT should only borrow when programs need funding. Management has set a threshold of $100 million in the State Highway Fund as the point where it makes sense to borrow. Borrowing in the spring also makes sense, since spending is heaviest in the summer.

- **Structure of each bond issue.**

  Many tools are available in the bond market which can potentially save money for ODOT. For example, Financial Services plans to include a component of variable rate debt with future bond issues. We will provide more details in future updates.

- **Investment of bond proceeds.**

  A key goal identified by Financial Services is to improve the investment return on the State Highway Fund. By law, balances are currently invested in short term liquid assets. If a portion could be invested longer term, ODOT would gain access to higher yields. Financial Services will seek a legislative change that would allow greater investment flexibility.

STRATEGY #2

Preserve Debt Capacity

Investors buy ODOT bonds to earn tax-exempt interest in a secure investment. This security is reflected in the Department's high bond rating – AA or higher from all 3 rating agencies. One factor rating agencies consider is debt capacity – the amount of bonds we issue compared to revenues available to pay debt service. For each bond issue, we are required to show that projected revenues will be at least 3 times as high as projected debt service.

The graph below shows ODOT's debt capacity projected through FY 2011. Because debt is growing at a much faster pace than revenues, debt capacity is projected to shrink each year.

Better timing of bond issues and refunding (refinancing) prior bond issues can help preserve debt capacity. In a future update, we will provide more information on steps we are taking to preserve ODOT's debt capacity.

Debt Capacity Will Decline Steadily Without Savings or New Revenue