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Hudson Yards Makes Muni-Bond Market History for New York Agency.

New York's transit agency is cashing in on the massive development rising from an industrial landscape on Manhattan's far west side.

The Metropolitan Transportation Authority, which typically uses fare-box revenue and bridge and tunnel fees to secure its debt, raised $1.06 billion Wednesday by selling its first bonds backed by real-estate. The securities will be repaid from money the agency receives from leasing land in Hudson Yards, a 26-acre site whose development has triggered a surge of construction in residential towers, office space and retail near the riverside west of Eighth Avenue.

Goldman Sachs & Co., the lead underwriter on the deal, priced the bonds — which have 5 percent coupons and mature in 2046, 2051 and 2056 — at yields of 1.88 percent, 2.38 percent and 2.63 percent, respectively, according to data compiled by Bloomberg.

"People like larger names in high-tax states that are unique in their credit story," said Sean Carney, head of municipal strategy at BlackRock Inc., which manages about $124 billion of municipal debt.

The Hudson Rail Yards Project, developed by affiliates of Related Cos and Oxford Properties Group, is transforming Manhattan's largest tract of undeveloped land. When completed by 2029, it will have three office towers, nine residential buildings, 1 million square feet of retail anchored by Neiman Marcus, a luxury hotel, 15 acres of public space and a cultural center. Monthly rent payments will cover the bonds. Time Warner Inc., KKR & Co. and Wells Fargo & Co. are among the future occupants.

The new bonds, called Hudson Rail Yards Trust Obligations, may be a draw to New York investors looking to diversify their portfolios, said Scott Richman, chief investment officer at Whitehaven Asset Management, which oversees $110 million of assets, the bulk of which is municipal debt.

"For the mutual funds, this entity will count as a different name and for better or worse a different name is actually worth a lot in the municipal market," Richman said. "So even though it might have a similar credit backing to a much larger issuer, that will create demand within the space."

The sale comes amid strong demand for municipal bonds that has kept yields — which move in the opposite direction as price — near record lows. The MTA's most actively traded securities — revenue bonds with a 4 percent coupon that mature in 2036 — changed hands Wednesday at an average yield of about 2.6 percent, down from a 2.67 percent yield when they were first sold on June 23, according to data compiled by Bloomberg.

MTA's rail yards run from 30th to 33rd streets and between Tenth and 12th Avenues. The MTA leased the airspace above the above the rail yards to Related and Oxford. The developers are almost finished building a platform over the eastern half of the site and will do the same on the western half.

The rail yards are the center of a larger rehabilitation of the once-decrepit area, called the Hudson Yards District. A new 7 subway line station, financed by $2 billion of city bonds, opened on the site a year ago to connect the area to midtown Manhattan. To the south is the High Line, a landscaped promenade on a former elevated rail line that extends from Greenwich Village through part of Chelsea.

The MTA's real estate consultant Jones Lang LaSalle Americas, Inc. has valued the Western Rail Yards at $3.2 billion to $3.7 billion, according to bond documents.

"With this transaction MTA is taking advantage of significant value of the Hudson Rail Yard assets and low interest rates to monetize the ground leases on the Eastern and Western Rail Yards," Pat McCoy, the agency's finance director, said in an e-mail.

The bulk of the bond proceeds will repay notes the MTA sold to finance capital projects ahead of the sale, according to McCoy. In the event a tenant defaults on lease payments, the agency agrees to pay interest on the bonds for up to seven years, according to McCoy. The MTA also has the option to take over a defaulted lease and make the full payments.

Moody's Investors Service rates the bonds A2, its sixth-highest investment grade and one step below MTA's transportation revenue bonds, citing the stability provided by the escalating ground rent payments, given the high value of the real estate. Kroll Bond Rating Agency assigned its A- rating, one step lower.

The bonds may be redeemed early if Related and Oxford elect to prepay their leases, which could leave debt due in 2056 paid off by 2026, under one scenario.

"All of a sudden you don't have a long bond in your portfolio, you have a 10-year security," said Robert Amodeo, head of municipals in New York for Western Asset Management Co., which holds $25 billion of the securities.

There's also a risk that development of the Western Rail Yards may fall behind schedule and real estate values could fall, he said.

Those risks are offset by the structure of the lease payments, which are senior to mortgage payments paid by Related and Oxford and the MTA's willingness to step in to pay interest payments if there's a default. The developers and lenders have a strong motivation to avoid default, said Rachael McDonald, a Moody's analyst in New York.

"Given the high potential value of the properties once completed, we believe there are strong incentives in place for the tenants to pay," McDonald said.

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