FitchRatings

FITCH RATES NEW YORK CITY MUNI WATER FINANCE AUTH'S $475MM REVS 'AA+'; OUTLOOK STABLE

Fitch Ratings-New York-27 March 2015: Fitch Ratings has assigned an 'AA+' rating to the following water and sewer system second general resolution (SGR) revenue bonds for the New York City Municipal Water Finance Authority (NYW, or the authority):

--Approximately $475 million water and sewer system SGR revenue bonds, fiscal 2015 series GG.

The Rating Outlook is Stable.

The fiscal 2015 series GG bonds are scheduled for negotiated sale March 31. Proceeds will be used to retire outstanding First General Resolution (FGR) bonds for cost savings with no extension of maturity dates and to pay issuance costs.

SECURITY

The SGR bonds are special obligations of NYW, payable solely from and secured by a subordinate lien on gross revenues of NYW's combined water and sewer utility system (the system). FGR bonds are secured by a first lien on gross revenues of NYW. The bonds currently being issued will not have a debt service reserve fund (DSRF).

KEY RATING DRIVERS

SOUND LEGAL PROTECTIONS: NYW's primary credit strength is its legal structure, including its status as a bankruptcy-remote issuer, providing substantial protection to bondholders from potential operating risks associated with the system and New York City (the city).

REGIONAL PROVIDER OF AN ESSENTIAL SERVICE: The system provides an essential service to an exceptionally large, diverse and economically important service area. The system benefits from an abundant, high-quality water supply exempt from expensive filtration requirements and transmission costs.

DEMONSTRATED RATE-RAISING WILLINGNESS: Strong financial management and a proven ability and willingness to raise rates are reflected in consistently solid financial results, despite continued volatility in consumption.

WELL-MANAGED CAPITAL PROGRAM: Sophisticated capital planning efforts have helped achieve compliance with large and costly mandated regulatory projects and ensured the system's total assets are adequately maintained.

HIGHLY LEVERAGED SYSTEM: Debt levels are high as a result of having to comply historically with environmental mandates and maintain a large urban system and its aging assets. Declining but still sizeable debt issuances programmed into the current capital plan will keep debt levels elevated for the long term.

IMPROVED COLLECTIONS: Below-average current collection rates persist, although payment incentives and strong enforcement mechanisms have yielded positive results in recent years.

RATING SENSITIVITIES

MAINTENANCE OF SUFFICIENT RATES: Failure to establish rates sufficient to ensure the continuation of strong financial margins and currently robust debt service coverage (DSC) levels on senior and subordinate lien obligations would be viewed negatively.

RISING DEBT LEVELS: The continued escalation in the system's debt levels remains an increasing concern that could ultimately pressure the rating. Increases in leverage beyond what is currently forecast would likely place added pressure on the authority's current rating.

CREDIT PROFILE

SOUND LEGAL PROTECTIONS

Fitch believes NYW bondholders benefit from strong legal protections that include:

--Revenues collected in a lock box structure controlled by the trustee and used to pay debt service of FGR and SGR bonds before operations and maintenance (O&M) expenses;
--The bankruptcy-remote, statutorily defined nature of the authority;
--Ownership of system revenues by the bankruptcy-remote New York Water Board, which sets rates independently without city council approval.

These layers of legal protection serve to significantly shield FGR and SGR bondholders from the operational risks of the city's massive water and sewer enterprise as well as other city government operations. Consequently, Fitch does not make a rating distinction between FGR and SGR bonds. SGR bondholders' claim on gross revenues is subordinate only to FGR debt service deposits, NYW administrative costs, and FGR DSRF requirements.

Following such deposits, revenues flow from the subordinated indebtedness fund of the FGR revenue fund directly to the SGR revenue fund to pay SGR debt service deposits. Only after monthly required deposits under the SGR are satisfied and held by NYW's trustee are funds released from the lockbox to pay O&M expenses.

STRONG FINANCIAL AND DEBT MANAGEMENT
NYW's strong financial management and conservative budgeting continue to yield sound financial metrics, despite ongoing volatility in consumption over the last several years and continued growth in debt service obligations. FGR and SGR DSC from net operating revenues improved for the fourth consecutive year in fiscal 2014, increasing to 7.7x and 3x, respectively. Reflecting the gross lien on system revenues, DSC grew to 12.6x and 4.8x, respectively. The authority's favorable operating results were driven in part by the adoption of a 5.6% rate increase that positively offset a nearly 1% decline in consumption.

Liquidity has also steadily grown in recent years to a more acceptable level. Unrestricted cash and investments together with O&M reserves increased to nearly 280 days of cash on hand in fiscal 2014, more than three times the amount on hand at the close of fiscal 2010. NYW's prudent practice of carrying forward and applying any operating surplus generated in the prior year to the payment of debt service in the coming fiscal year prevents the build-up of more robust cash balances but preserves rate flexibility. Fitch continues to view this strategy favorably. The net surplus generated in fiscal 2014 (measured on a cash basis) totaled $985 million, up from the $750 million generated in fiscal 2013.

Results through the first eight months of the current fiscal year are positive, with year-to-date revenues reportedly up by nearly 2.4% compared to the adopted budget. Consumption, while down about 1.7% to date, is almost in line with budgeted expectations. The authority adopted modest rate increases of 5.6% and 3.5% in fiscals 2014 and 2015, respectively, following several years of more sizeable increases, including double-digit rate hikes enacted in fiscals 2008 - 2011. Despite the escalation in rates, the average monthly residential bill remains relatively affordable in comparison to median household income levels for the service area.

PROJECTED FINANCIAL RESULTS REMAIN SATISFACTORY

Financial projections through fiscal 2019 are based on what Fitch believes to be reasonable assumptions. The forecast assumes the continuation of moderately sized rate hikes and incorporates sizeable annual debt offerings along with a 1.5% decline in consumption in each of fiscal 2015 through fiscal 2019. As a result, all-in DSC from net revenues is projected to remain at a strong level of no less than 2.1x through the current planning period and annual surpluses are forecast to remain in excess of $750 million, which will continue to be applied to subsequent year's annual debt service obligations.

LEVERAGED SYSTEM

Similar to many large urban utility systems, NYW's capital needs are significant, principally the result of state and federally mandated projects. The capital program for fiscals 2015 -2025 includes an estimated $12.8 billion in water and sewer projects, down significantly from a peak of $19.5 billion projected for fiscals 2008 - 2018.

Funding for capital projects will continue to come almost entirely from long-term debt issuance and an extensive commercial paper program. NYW's current forecast shows additional bond issues through fiscal 2019 totaling $6.6 billion, or an annual average of approximately $1.3 billion. Projected debt issuance, while sizable, is a marked decline from the amount of debt incurred over the previous five years.

Debt levels are high and escalation beyond what is currently forecast could pressure NYW's rating over the medium term. Debt-to-net plant now stands at about 106%, and, measured on a per capita basis, leverage approximates slightly more than $3,000. By comparison, Fitch's 'AA' category median ratios for debt-to-net plant and debt per capita are 50% and $521, respectively. Fitch believes the demonstrated commitment to raising rates as well as management's conservative budgeting will be key to preserving operating margins and meeting the continued growth in debt service costs included in NYW's financial forecast.

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In addition to the sources of information identified in Fitch's Revenue-Supported Rating Criteria, this action was additionally informed by information from Creditscope.

Applicable Criteria and Related Research:
--'Revenue-Supported Rating Criteria' (June 2014);
--'U.S. Water and Sewer Revenue Bond Rating Criteria' (July 2013);
--'2015 Water and Sewer Medians' (December 2014);
--'2015 Outlook: Water and Sewer Sector' (December 2014).

Applicable Criteria and Related Research:
2015 Water and Sewer Medians
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=818409
U.S. Water and Sewer Revenue Bond Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=715275
Revenue-Supported Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=750012
2015 Outlook: Water and Sewer Sector
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=818410