

## **FITCH RATES NEW YORK CITY MUNI WATER FINANCE AUTH'S \$340MM REVS 'AA+'; OUTLOOK STABLE**

Fitch Ratings-New York-13 November 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 \$340 million water and sewer system SGR revenue bonds, fiscal 2016 series BB consisting of:

--\$317 million fiscal 2016 subseries BB-1;

--\$23 million fiscal 2016 Subseries BB-2.

The Rating Outlook is Stable.

The fiscal 2016 series BB bonds are scheduled for negotiated sale November 17. Proceeds will be used to retire outstanding commercial paper notes, refund outstanding SGR bonds 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). 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:** New York City Municipal Water Finance Authority's inability 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 fifth consecutive year in fiscal 2015, increasing to 12.0x and 5.x, respectively. Reflecting the gross lien on system revenues, DSC grew to 19.7x and 8.5x, respectively. The trend of favorable operating results reflects primarily the authority's continued ability and willingness to raise rates and realize positive budget variances as a result conservative budgeting practices.

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 290 days of cash on hand in fiscal 2015, 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 2015 (measured on a cash basis) totaled \$1.01 billion, up from the \$985 million generated in fiscal 2014.

Results through the first four months of the current fiscal year are positive, with consumption up about 3.5% and year-to-date revenues reportedly up by nearly 2% compared to prior forecast results. The authority adopted modest rate increases of 5.6% and 3.4% in fiscals 2014 and 2015, respectively, following several years of more sizeable increases. For fiscal 2016, the authority recently adopted a modest 2.97% rate increase, its lowest increase in fifteen years. Despite the continued 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 2020 are based on what Fitch believes to be reasonable assumptions. The forecast generally 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 2016 through fiscal 2019, and by 1% in 2020. As a result, all-in DSC from net revenues is projected to remain at a strong level of no less than 2.2x through the current planning period and annual surpluses are forecast to remain in excess of \$900 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 2016 -2025 includes an estimated \$14.9 billion in water and sewer projects, up approximately 15% from the prior year's plan, but still 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 new money bond issues through fiscal 2019 totaling \$6.8 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 108%, and, measured on a per capita basis, leverage approximates nearly \$3,300. By comparison, Fitch's median ratios for the rating category 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.

Contact:

Primary Analyst  
Christopher Hessenthaler  
Senior Director  
+1-212-908-0773  
Fitch Ratings, Inc.  
33 Whitehall Street  
New York, NY 10004

Secondary Analyst  
Andrew DeStefano  
Director  
+1-212-908-0284

Committee Chairperson  
Doug Scott  
Managing Director  
+1-512-215-3725

Media Relations: Sandro Scenga, New York, Tel: +1 212-908-0278, Email:  
sandro.scenga@fitchratings.com.

Additional information is available at 'www.fitchratings.com'.

#### Applicable Criteria

Revenue-Supported Rating Criteria (pub. 16 Jun 2014)

[https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=750012](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=750012)

U.S. Water and Sewer Revenue Bond Rating Criteria (pub. 03 Sep 2015)

[https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=869223](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=869223)

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTP://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](http://fitchratings.com/understandingcreditratings). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE 'WWW.FITCHRATINGS.COM'. PUBLISHED RATINGS, CRITERIA AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE 'CODE OF CONDUCT' SECTION OF THIS SITE. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.