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Summary:

New York City Municipal Water Finance Authority; Water/Sewer

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Summary:

New York City Municipal Water Finance Authority; Water/Sewer

Credit Profile		
US$480.39 mil 2nd gen resolution rfdg bnds 2014 ser DD due 06/15/2039		
Long Term Rating	AA+/Stable	New

Rationale

Standard & Poor's Ratings Services assigned its 'AA+' rating to the New York City Municipal Water Finance Authority's (NYCMWFA) fiscal 2014 series DD second general resolution water and sewer system revenue bonds. We also affirmed our 'AA+' underlying ratings (SPURs) on the authority's existing second-resolution bonds, as well as our 'AAA' long-term rating on the system's first general resolution revenue bonds. The outlook on all the ratings is stable.

The difference between the long-term ratings on the first- and second-resolution debts reflects lien priority and the active use of both liens. The long-term ratings reflect the fundamental credit strengths of the NYCMWFA, which include, in our opinion:

- The bondholder protections provided by the issuer's legal and structural features, including a gross pledge of revenues that results in true separation from the utility's operating function when combined with the New York City Water Board's ability to raise rates (a true-up mechanism) and the segregation of funds;
- The system's fundamental credit strengths, characterized by a large and diverse customer base, very good financial profile, and strong management; and
- The capacity and demonstrated willingness to adjust rates when necessary, especially in the face of a sizable capital improvement plan (CIP) of $12.8 billion in forecasted capital commitments through fiscal 2024. Despite the large CIP, the authority has been extremely successful in managing a myriad of projects while still meeting or exceeding all deadline-certain benchmarks; as such, the level of mandated projects relative to the total CIP continues to decrease, providing greater flexibility in the capital budget.

Bond proceeds will be used to refund for savings various maturities of the system's outstanding revenue bonds. The NYCMWFA has about $7.3 billion of first-resolution debt and $23.1 billion of second-resolution debt. A first-lien pledge on the system's gross revenues secures the first-resolution debt. A debt service reserve (DSR) provides additional liquidity to the first-resolution debt. The second resolution bonds are subordinate and do not benefit from a DSR.

Long-term financial planning, both for the operating budget and the capital program, remains an identified strength of the system. This continues to allow management to fund and complete major projects and mandates while maintaining the system; the recent 2014 update to the consulting engineer's report confirmed the system's good overall condition and management's adept handling of the large capital plan. The planning and conservatism to assumptions consistently lead to a favorable variance to budget. For fiscal 2012, for example, management saw a 7.2% year-over-year increase in operating revenues, even with a 2.3% decline in consumption. Fiscal 2013 result was even more pronounced, as a projected $665 million surplus ultimately ended up being $750 million.

Management has aggressively used surplus revenues for cash defeasance of debt. Between the carryforward cash and the unique nature of certain of the customer billings, the system's fiscal 2014 debt service requirement was already completely funded only four months into the fiscal year. The authority's leadership has also made dedicated efforts to contain costs and pursue operational and debt savings whenever possible, given the assumed 1.5% per year continued decline in consumption in the near term.

Given that, debt service coverage (DSC) of the senior and combined senior and subordinate debt is 10.3x and 3.6x, respectively, for fiscal 2013, a marked improvement from already extremely strong fiscal 2012 results. The authority projects combined senior and subordinate DSC, on a gross revenue pledge basis, to remain steady at a still-healthy 2.7x by 2018. Even when hypothetically calculating coverage on a net revenue pledge basis, total DSC across both liens is no worse than about 1.7x by Standard & Poor's calculations.

Liquidity remains a strength as well. Between the designated operations and maintenance reserve of one-sixth of projected operating expenses, and other available working capital, fiscal 2013 cash on hand of about $950 million equates to roughly eight months of operating expenses. In addition to providing robust working capital levels, it also serves as a hedge against interest-rate risk and other contingent liabilities. The authority does have some interest-rate swaps, several of which have unfavorable mark-to-market values. Over their lifetimes, however, the swaps – just as the unhedged variable-rate debt – have served to generally lower the authority's cost of borrowing and currently are not expected to be terminated.

The New York City Water Board has a long history of adjusting rates annually as necessary. Due to the conservatism in the budgeting, actual rate increases are typically less than originally forecasted. This includes the two most recent adopted rate increases -- 5.6% for fiscal 2014 and 7.5% in fiscal 2013 -- that several years ago were projected to each be about 1.5 percentage points higher. Because management continually updates its extensive long-term plans, we believe it will continue to exceed its forecast even if the implemented rate adjustments remain smaller than originally planned. The CIP remains the key driver behind the continued rate adjustments. Despite the large size of the capital program, key projects all remain within budget and on time. The main driver of the capital program is rehabilitation of assets, both on a discretionary basis as well as due to regulatory mandates. Despite the sheer number of large and ongoing projects, management has reduced mandated projects to just under one-fourth of total capital commitments. The planned capital expenditures from fiscal 2014 to 2023 are chiefly for water pollution control (37%), water distribution (27%), sanitary sewer projects (18%), and water supply and transmission (13%). Officials typically fund capital improvements through the $600 million commercial paper (CP) program before using long-term debt to retire the notes.

Recent severe weather events in and around New York City have also provided the opportunity for management to demonstrate its ability to maintain operations at a high level. For example, Hurricane Sandy's effect on the system's infrastructure in late October 2012 was material but far from crippling. As was also the case in August 2011 for Hurricane Irene, water levels at key upstate reservoirs were lowered prior to the storm so that there would be sufficient storage capacity to capture rainfall and runoff. The dams, therefore, retained their structural integrity and spill-control abilities throughout Sandy's aftermath. There was manageable damage to the drinking water system, although at its peak, NYCMWFA identified 9,800 accounts for which billing was delayed and without penalties until May 2013--even while charges accrued--as they were unoccupied. To date, billing has resumed to all but about 180 customers whose properties are not inhabitable. Some wastewater treatment plants did lose power during portions of the storm, but within days, 13 of the 14 wastewater plants were back to normal operations. The most recent estimate of system damage is $95 million, exclusive of any likely Federal Emergency Management Agency reimbursements.

Regardless, the authority's capital and borrowing needs remain significant, although the rate of increase in total debt is beginning to slow. In January 2013, the city released its most recent update to its capital plan; in the first five years through fiscal 2018, planned capital commitments average about $1.8 billion per year, funded mainly with debt (including bonds already sold). Management plans to continue to use existing CP programs and additional revenue bonds to fund the bulk of identified projects, although annual borrowings are projected to decline each year across the forecast.

The ratings also reflect our view of the pledged revenue stream and management's ability to adjust rates in a timely manner and without state regulation to provide adequate revenue sources to cover debt service and ongoing operating and capital expenditures. Water and sewer rates are affordable and, in general, lower -- on both an actual and a percentage-of-income basis -- than comparable urban systems. The abundant, low-cost water supply and delivery system is a major, unique advantage that has helped management maintain its rate-raising capacity despite the large capital program.

The rate covenant provides 1.15x aggregate annual DSC on the first-resolution bonds but just 1x on all subordinate debt. In addition, while the first-resolution debt has an additional bonds test (ABT) of 1.15x maximum annual debt service (MADS) and 1x operating expenditures, the second-resolution debt's ABT is a lower 1.1x aggregate debt service and 1x operating expenditures.

The authority includes its federal Build America Bonds (BABs) subsidy as revenue for both rate-setting and ABT purposes; the March 1, 2013, federal sequestration and associated interest-rate subsidy reduction had no material impact on NYCMWFA's cash flow, nor did the October 2013 federal government shutdown. Management's practice of budgeting conservatively for debt service and including large amounts of pay-as-you-go capital in its budget, coupled with historical net DSC well above 1x, all help offset any effects from the ongoing federal budget sequester. Additionally, the outstanding BABs contain make-whole call provisions, which for now limit the economics of refunding them with tax-exempt bonds. While the city rental payment is subordinate to the second-resolution bonds, providing additional liquidity at the date of debt service, the debt service funds are typically fully funded before the fiscal year is even halfway over, given the timing of operating cash flows and those certain accounts on fixed-rate, annual billings. The rental payment was about $210 million in fiscal 2013, as--on an escalating basis over time--a portion of the rental payment will be returned to the authority as per the lease provisions.

The system serves about 836,000 accounts, primarily in New York's five boroughs, all but 5% of which are metered. In addition, the authority provides water and sewer services to about 1 million customers in Westchester, Putnam, Orange, and Ulster counties. About 91% of the system is residential, with commercial and industrial users accounting for the balance.

Outlook

The stable outlook reflects Standard & Poor's expectation that the system's financial profile will remain commensurate with the ratings over our two-year horizon. The large CIP reflects the current regulatory environment and a large system that serves roughly 9 million people. We believe the strong management, including long-term planning and transparency regarding future rate adjustments, will continue to allow the authority to fund identified needs despite an expected rise in operating costs and significant additional debt.

Related Criteria And Research

Related Criteria

USPF Criteria: Standard & Poor's Revises Criteria For Rating Water, Sewer, And Drainage Utility Revenue Bonds, Sept. 15, 2008

Ratings Detail (As Of March 24, 2014)		
New York City Mun Wtr Fin Auth wtr & swr sys 2nd gen resol rev bnds fiscal 2008 ser DD due 06/15/2039		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth wtr & swr (FGIC) (SEC MKT)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth wtr & swr (MBIA) (FGIC) (National)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/A-2/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/NR/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AAA/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS		
Long Term Rating	AA+/A-1/Stable	Affirmed

Ratings Detail (As Of March 24, 2014) (cont.)		
Unenhanced Rating	NR(SPUR)	
New York City Mun Wtr Fin Auth WS VRD		
Long Term Rating	AAA/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (wrap of insured) (AGM & BHAC) (SEC MKT)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (AGM)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (AGM) (SEC MKT)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (AGM) (SEC MKT)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (BHAC) (SEC MKT)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (CIFG) (SEC MKT)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (MBIA) (AGM)		
Unenhanced Rating	AAA(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-2/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-2/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1+/Stable	Affirmed

Ratings Detail (As Of March 24, 2014) (cont.)		
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1+/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution)		
Long Term Rating	AA+/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution) ser 2008 BB-1		
Long Term Rating	AA+/A-1/Stable	Affirmed
New York City Mun Wtr Fin Auth WS (2nd gen resolution) (CIFG) (SEC MMKT)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth wtr & swr		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed
New York City Mun Wtr Fin Auth wtr & swr VRDB ser 1995A		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

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