18 SEP 2023

Fitch Rates New York City Muni Water Finance Auth's Revs 'AA+'; Outlook Stable

Fitch Ratings - New York - 18 Sep 2023: Fitch Ratings has assigned a 'AA+' rating to the following New York City Municipal Water Finance Authority's (NYW or the authority) revenue bonds.

Approximately $629 million water and sewer system second general resolution (SGR) revenue bonds fiscal 2024 series AA consisting of the following:

--Approximately $257.2 million fiscal 2024 subseries AA-1;

--Approximately $160.9 million fiscal 2024 subseries AA-2; and

--Approximately $210.9 million fiscal 2024 subseries AA-3.

The fiscal 2024 series AA bonds are scheduled to sell the week of September 25. Proceeds of the bonds will be used to (i) pay costs of system improvements; (ii) refund certain outstanding bonds; and (iii) to pay costs of issuance.

Fitch has also affirmed the following ratings:

--Approximately $455.7 million first general resolution (FGR) revenue bonds and various related bank bonds at 'AA+' (pre-refunding);

--Approximately $28.1 billion SGR revenue bonds and various related bank bonds at 'AA+' (pre-refunding);

--$400 million authorized extendable municipal CP (EMCP) notes, series seven and eight at 'F1+'.

The Rating Outlook is Stable.

The 'AA+' rating reflects the combined credit quality of the authority and the New York City Water Board (the water board), as well as the authority's role as the issuer of revenue bonds on behalf and in support of the expansive New York City (the city) water and sewer system (the system). The financial profile is very strong and assessed at 'aa' in the context of historically very low leverage, measured as net adjusted debt to adjusted funds available for debt service (FADS) on a gross revenue basis. The 'F1+' short-term rating primarily reflects the 'AA+' long-term rating and adequate liquidity.

Bondholders are afforded strong protections through a statutory framework providing a gross lien on pledged water and sewer revenues, along with Fitch's expectation of the remoteness of either the authority or water board filing for bankruptcy protection, or being included in a city bankruptcy proceeding if one were to ever occur. The credit profile is further supported by the very strong revenue defensibility and operating risk profile, both assessed at 'aa'.

Leverage was in the mid-7.0x range through fiscal 2020 (FYE June 30). The adverse impact of the pandemic on the service area drove leverage to 8.3x in fiscal 2021. Fiscal 2021 results reflect reduced overall revenues and higher expenses, as the acute effects of pandemic-driven closures were realized for a full year. Additionally, the system's previously projected rate increase was not adopted that year in light of the widespread economic strain, further reducing revenue-generating capacity.

In fiscal 2022, leverage improved to 8.0x, reflecting an increase in revenues driven by the 2.76% rate increase combined with a higher rate of consumption, slowing rate of delinquencies and the elimination of the lease payment to the city. Total debt service was lower in fiscal 2022, the result of prior years' cash defeasance and the benefit of the low interest rate environment on certain variable rate debt service.

The authority's five-year projections, assume annual rate increases of the already enacted 4.42% in fiscal 2024, and projections of 5.4%, 5.9% and 6.6% in each of the fiscal years 2025, 2026 and 2027. The authority's forecast assumes the execution of an average of $2.2 billion in annual capital spending over the next five years, including an estimated $1.7 billion in fiscal 2023, supported by ongoing new debt issuance, as well as continued expectations for sizeable annual surplus revenues. These projections also assume the continued waiver of the city lease payment (discussed in more detail below).

Based on the authority's projections, leverage is anticipated to remain stable at 8.0x into fiscal 2023, and rise in Fitch's stress case to 8.3x in fiscal 2024, remaining stable through fiscal 2027. A resumption of the lease payment to the city, absent off-setting actions, would likely move leverage to a level no longer consistent with the rating.

Fitch does not differentiate between the FGR and SGR liens as they are both afforded strong support from gross revenue pledge and benefit from the subordination of O&M payments. Since 2020, the authority historically prefunded in excess of $1.0 billion of debt service, further reducing risk to subordinate lien bondholders.

SECURITY

SGR bonds are special obligations of NYW issued under the SGR and payable solely from and secured by a subordinate lien on gross revenues of NYW. Outstanding FGR bonds are payable solely from and secured by a first lien on gross revenues of NYW.

KEY RATING DRIVERS

Revenue Defensibility - aa

Very Strong Rate Flexibility, Favorable Service Area with Unique Economic Profile

The water board retains the legal authority to adjust rates as needed without external oversight. Revenue defensibility is further supported by the system's monopolistic provision of water and sewer services to its favorable service area. The service area is characterized by a stable customer base, median household income that approximates the nation and weaker, but improving unemployment rates relative to the nation.

Fitch also considers the city's unique economic profile as an international center for numerous industries as an anchor for the service area. Rates are considered affordable for almost 80% of the service area population, using Fitch's standard monthly usage of 7,500 gallons for water and 6,000 gallons for sewer.

Operating Risk - aa

Very Low Operating Cost Burden, Elevated Capital Needs

In fiscal 2022, the system's operating cost burden was considered very low approximating $3,300 per million gallons (mg), consistent with the operating risk assessment. The life cycle ratio was a low 36% in fiscal 2022. Capex outpaces annual depreciation, with a five-year average of 180% for the five years ended fiscal 2022.

The system's capital improvement plan (CIP) for fiscal 2023 through fiscal 2027 approximates $15.3 billion, with associated estimated actual spending of $10.9 billion for the same period. Approximately 44% of the CIP is related to water pollution control projects, including plant upgrades and reconstruction. Water distribution approximates 21% of the CIP, sewer programs approximately 17% and water supply and transmission approximately 15%. Estimated capital spending averages $2.2 billion annually during these five years, in excess of historical depreciation, supporting a continued low life cycle ratio.

Financial Profile - aa

Leverage Remains Elevated for the Rating; Gradual Declines Anticipated

The authority's leverage (on a gross lien basis) was 8.0x in fiscal 2022, compared to 8.3x in fiscal 2021, reflective of the modest rate increase and improved consumption and reduced expenditures that in part reflect the suspension of the lease payment to the city. The liquidity profile is neutral to the assessment and reflects coverage of full obligations (COFO) of 1.7x and current cash on hand of 335 days, when incorporating carry forward revenues.

Fitch's Analytical Stress Test (FAST) considers the potential trend of key ratios in a base case and stress case over a five-year period. The stress case is designed to impose capital costs 10% above expected base case levels and evaluate potential variability in projected key ratios.

In the base case, leverage approximates 8.2x in fiscal 2024 and modestly declines to 8.1x in fiscal 2027. In the stress case, leverage reaches 8.3x in fiscal 2024 and remains stable through the five-year horizon. Although near-term leverage has declined from previous estimates, a sustained pause in the trend of declining leverage, or a reversal of this trend, is likely to have negative rating implications. The liquidity profile is anticipated to remain neutral to the assessment.

Asymmetric Additional Risk Considerations

No asymmetric additive risk considerations affected this rating determination.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

--Reversal in the trend of declining leverage through the five-year horizon;

--Leverage that stabilizes around 8.5x in Fitch's base or stress cases;

--Sustained weakness in FADS stemming from a delay in rate-setting or an increase in expense that weaken the authority's operating margins.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

--A sustained decline in leverage to below 5.0x in Fitch's base and stress cases within the context of current revenue defensibility and operating risk assessments.

PROFILE

The authority was created as a public benefit corporation in 1984 in order to issue bonds, notes and other financing instruments to fund capital improvements to the city's system. Fitch considers the authority to be an issuer that benefits from a contractual framework in which revenues and costs are largely balanced. The water board leases the system from the city and is responsible for setting, levying and collecting customer rates and system revenues to transfer to the authority for bond repayment and to the city for O&M reimbursement.

The city is entitled to an annual lease payment, although it has not received one since fiscal 2021, and the city had not requested the payment in several of the years prior to fiscal 2020. The maximum annual lease payment is 15% of the authority's annual debt service; should the city request the maximum lease payment, it would range from about $280 million in fiscal 2024 to about $330 million in fiscal 2027.

Further, the authority has the power to require the water board to charge and collect sufficient rates to pay the costs of operating and financing the system, as well as to enforce that the city adequately operate and maintain the system. The authority may not file for bankruptcy without state legislative approval and Fitch views the authority as bankruptcy-remote from the city. Fitch also views the water board as bankruptcy-remote from the city.

The system is the country's largest municipally owned water and sewer utility. It is operated by the NYC Department of Environmental Protection (DEP, a city agency) and provides retail water and sewer service to approximately 835,700 accounts and about 8.3 million residents within the city. It also provides wholesale service to an approximately one million residents in communities north of the city. The service area includes over 300 square miles across NYC's five boroughs (the Bronx, Brooklyn, Manhattan, Queens and Staten Island) as well as communities within Westchester, Putnam, Orange and Ulster counties.

The DEP performs day-to-day system O&M and is responsible for executing the system's multi-billion-dollar capital program. Capital and maintenance needs are expected to remain significant over the long-term given the demand placed on system assets in an expansive urban setting.

The water system provides an average of approximately 1 billion gallons per day (bgd) from three upstate aqueducts that span as far as 125 miles north of the city. Demand has steadily declined over time due to water efficiency measures, and has been a stable 75% of dependable yield from three city-owned upstate reservoir systems. The sewer system collects and treats an average of approximately 1.2 bgd of wastewater at 14 in-city wastewater treatment plants for virtually the entire city. Average annual flows approximate 70% of the 1.8 bgd design capacity.

Structural and Legal Protections

Fitch believes NYW bondholders benefit from strong legal protections that include the statutorily defined nature of the authority, bankruptcy remoteness and the gross pledge of system revenues. While these layers of legal protection do not completely shield FGR and SGR bondholders from the operational risks of the city's massive water and sewer enterprise, they limit diversion of revenues to general city operations.

A large portion of annual debt service obligations is consistently funded well in advance of scheduled payment dates by the restricted revenue fund, which consists of both current year revenues and carry-forward surplus cash. The authority carried forward nearly $1.1 billion into fiscal 2022, enough to pre-pay approximately 75% of fiscal 2022 combined FGR and SGR debt service of nearly $1.4 billion.

Only after monthly required deposits under the SGR are satisfied and held by NYW's trustee will funds be released for other purposes, including the cash-defeasance of additional debt service, reimbursement to the city for O&M expenses and the lease payment (if any).

Sources of Information

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
New York City Municipal Water Finance Authority (NY) [Water, Sewer]					
• New York City Municipal Water Finance Authority (NY) /Water & Sewer Revenues (2nd Lien)/1 LT	LT	AA+	Affirmed		AA+
• New York City Municipal Water Finance Authority (NY) /Water &	LT	AA+	Affirmed		AA+

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Sewer Revenues/1 LT					
• New York City Municipal Water Finance Authority (NY) /Water & Sewer Revenues/1 ST	ST	F1+	Affirmed		F1+

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

Public Sector, Revenue-Supported Entities Rating Criteria (pub.27 Apr 2023) (including rating assumption sensitivity)

U.S. Water and Sewer Rating Criteria (pub.03 Mar 2023) (including rating assumption sensitivity)

Additional Disclosures

Solicitation Status

Endorsement Status

New York City Municipal Water Finance Authority (NY)	EU Endorsed, UK Endorsed

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