S&P Global Ratings

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Research Update:

New York City Municipal Water Finance Authority Series 2025DD Bonds Rated 'AA+'; Outlook Is Stable

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Overview

- S&P Global Ratings assigned its 'AA+' rating to New York City Municipal Water Finance Authority's approximately $600 million series 2025DD water-and-sewer-system second general-resolution revenue bonds, issued for New York Water (NYW).
- The outlook is stable.

Rationale

Security

All bondholders benefit from a gross revenue pledge and a statutory, perfected lien. The second-resolution bonds do not benefit from a debt service reserve fund.

NYW plans to use series 2025DD bond proceeds to refund existing debt for savings.

Current law does not authorize NYW or the board to declare bankruptcy. While we don’t rate to recovery, we consider the presence of a statutorily perfected lien and limitations around bankruptcy as positive structural provisions.

Credit highlights

The rating reflects our view of NYW's broad, diverse, and affluent service area and sophisticated management team that supports a highly complex operating profile and capital plan. The water and sewer system has used carry-forward cash balances to fund debt service well in advance of payment dates, which functions as a de facto set-aside payment for all bonds. The security structure provides significant bondholder security and robust system liquidity, which, in turn, create operating flexibility and mitigate potential financial pressure from event risk. Because of this strength, the rating incorporates a consideration for extraordinary financial strength related to lien-based debt service coverage (DSC) on all debt that is significantly higher than 3x and maintenance of unrestricted liquidity that has not decreased below $1 billion for, at least, the past five fiscal years; as of June 30, 2024, unrestricted cash and investments totaled $2.2 billion.

When accounting for all utility operating expenses--including those that are subordinate, such as base rental--we consider projected all-in DSC somewhat lower than similar-rated peers. On this all-in net revenue basis of coverage, our calculations indicate DSC equal to about 2x historically. Our review of management's projections indicates that to maintain this 2x DSC, management will likely need to outperform projections through some combination of positive operating variances through rate revenue or other revenue and expense line items, debt-refinancing opportunities, or a lower base-rental payment. Management's projections assume the maximum full base-rental payment request for future fiscal years, but the city has, to date, not requested these payments for future fiscal years.

NYW faces several challenges related to the macroeconomic-and-policy landscape, as well as the system's underlying infrastructure's age, size, and complexity. The authority's ability to balance rate affordability, financial health, and system investment is an important credit consideration, especially since economic recovery has been relatively slow and the city continues to face challenges.

In our view, the next several fiscal years will be critical from a financial perspective due to the effects of the restarting of lien sales, traction for efforts to reduce accounts receivable, sustainability of currently projected 8.5% annual rate increases, likelihood of future base-rental payment requests, and trajectory of the federal regulatory landscape; this will help indicate whether NYW's finances will likely be sustainable in a fashion that is consistent with historical trends and the current rating.

Additional key credit factors include our view of NYW’s:

- Broad and diverse economic and customer base, without comparable-sized peers. While economic recovery has begun, it remains slightly below the national level, with continued weakness in income and population growth.
- Affordable rates, with annual increases of 8.5% projected in 2026-2028, following an 8.5% approved rate increase for fiscal 2025; rate-setting is flexible, with the ability to increase rates within 30 days, which we view favorably.
- Seasoned and effective management team and board, with a strong sense of fiduciary duty and operational and financial acumen, supporting our credit view and confidence in management, despite the substantial complexities NYW faces during the two-year outlook, including a sizable capital plan; labor challenges; uncertainties related to collections and lien policy; and increasing climate-change pressure, all in a challenging economic environment.
- Extremely strong liquidity, both actual and on a days' cash on hand basis, which is critical to financial flexibility and credit strength. The ability to maintain significant cash balances directly influences DSC due to the annual carry forward of balances. This practice also allows for a more-level rate structure, but if the use of rolling cash balances results in postponed rate increases, we would view it as indicative of potential structural issues, which could pressure credit quality.

Environmental, social, and governance

New York Water is faced with numerous ongoing environmental, social, and governance factors that affect our analysis. We believe the system has outsized environmental risks, given the regulatory and climate resilience efforts that will be required to maintain its infrastructure at adequate levels.

The management and governance structure--with separate entities for operations, governance, and finance--has allowed for critical and apolitical decision-making, with an eye to both financial integrity and maintaining operations at a high level. We believe its governance efforts are sophisticated, which supports addressing long-term risks associated with asset adequacy.

Extreme weather events are becoming more common and ongoing sea-level rise will present system challenges. Emergency preparedness has improved, but climate resilience has taken on more urgency and is expected to require significant additional funding. NYW and the city have several planning initiatives, including resiliency planning, climate change modeling, and annual reporting to measure progress.

In 2021, the city released its "The New Normal" report, which addresses risk mitigation related to extreme storms. The report outlines efforts to reduce emissions, harden infrastructure to protect shoreline communities most vulnerable to storms, and to create a continuous line of protection against rising sea levels and storms. Specific to NYW, the report addresses its substantial need to rehabilitate and replace sewer pipes that were designed a century ago and are expected to be inadequate for current climate considerations. The report highlights the long- and short-term upgrades needed as well as innovative drainage solutions.

We believe management's approach to climate resiliency and sustainability is sound, and there is strong collaboration with the city. Given the age of the system and the regional climate risks, the capital plan addresses infrastructure projects that result in a more resilient system and have been enhanced to incorporate some of the projects associated with the recent report.

Further, management continues to refine and improve its asset-management program, including well-defined policies that provide a uniform methodology for a comprehensive evaluation of capital assets and a systematic approach to scheduling preventive maintenance and upgrades. This is a critical factor in our asset-adequacy assessment and our view of governance, given the advanced age of NYW's infrastructure and the potential risks for catastrophic failures.

Median household effective buying income varies widely from borough to borough. Given those differences, the city's Department of Environmental Protection (DEP) has a bill pay assistance program for low-income, senior, and disabled customers that we consider at least as robust as those of comparable peer cities in achieving social goals.

Outlook

The stable outlook reflects our belief that NYW will retain the financial capacity and management autonomy to navigate its near-term economic, infrastructure, climate, and regulatory pressures. Maintenance of the outlook relies on management's ability to successfully achieve positive financial variances as it has in the past, leading to stronger carry-forward revenue and DSC than current projections indicate.

Downside scenario

While we think NYW's budgeting practices are generally conservative and credit supportive at the current rating, a general misalignment between revenue and revenue requirements, or a reduction in enforcement ability that leads to consistently weaker finances than historical trends, could pressure the rating. We think management has the capacity and willingness to adjust rates to meet its capital and operating needs, evidenced by the board having a very long history of adjusting rates, usually annually, as needed. However, we will monitor the need for additional rate increases and any indication of reduced rate-setting flexibility or management autonomy.

Economic considerations for the city could also affect the rating, as evidenced by the city requesting base-rental payments for fiscal years 2024 and 2025, also indicating the economic impact on city finances.

Upside scenario

Consistent with the application of our “Assigning Issue Credit Ratings Of Operating Entities," criteria (published May 20, 2015), we do not consider there to be upward rating potential on the second general resolution debt.

Ratings List	
New Issue Ratings	
US$600.0 mil wtr and swr sys 2nd gen resolution rev bnds ser 2025 DD dtd 05/13/2025 due 06/15/2039	
Long Term Rating	AA+/Stable