

29 JAN 2024

## Fitch Rates Washington Suburban Sanitary District, MD's GO Bonds 'AAA'; Outlook Stable

Fitch Ratings - New York - 29 Jan 2024: Fitch Ratings has assigned a 'AAA' rating to the following Washington Suburban Sanitary District, MD (WSSD) general obligation (GO) bonds:

--Approximately \$299.3 million consolidated public improvement bonds of 2024;

--Approximately \$29.9 million consolidated public improvement bonds of 2024 (Second Series) (Green Bonds).

The bonds are anticipated to price competitively on Feb. 8; proceeds will be used to fund capital improvements to the system and pay costs of issuance.

The Rating Outlook is Stable.

The 'AAA' bond rating considers WSSD's very strong utility fundamentals reflected in its revenue defensibility and operating risk profiles, both assessed at 'aa'. The financial profile, also assessed at 'aa', reflects Fitch's expectations for continued financial profile improvement leading to a trend of declining leverage (measured as net adjusted debt to adjusted funds available for debt service [FADS]) to about 8.0x over the next five years. This trend is dependent upon continued healthy rate adjustments over the five-year horizon generating FADS in support of ongoing capital spending and increasing operating costs.

The district's financial performance improved into fiscal 2022 (FYE June 30) and continued into fiscal 2023 with leverage of 8.9x and 8.1x, respectively. Improved leverage reflects rate adjustments and improved collections along with curbs on the rate of expenditure growth. Liquidity also improved, although it remains neutral to the financial profile assessment.

Fitch also considers the district's financial profile in the context of the service area's (Prince George's and Montgomery Counties) resource base. From this vantage, its long-term obligations approximate 2.8% of total personal income (2022 data) of the service area. When combined with the district's authority to levy taxes to pay debt service and operations, this expanded view of the resource base supports the 'AAA' bond rating.

However, Fitch notes that ad valorem taxes are not currently levied, and the authority to do so is subject to a review process that, while serving to prevent default, limits the benefit of this additional resource at the current rating level. Fitch's view regarding the incremental benefit of the district's authority to levy taxes would be unlikely to support the current rating if the trend of declining leverage is interrupted or reversed.

### SECURITY

Debt service is expected to be paid from revenues generated by district fees, charges, rates and assessments and other available funds. In the event of a deficiency of such revenues, the bonds are payable from ad valorem taxes levied within the district (Montgomery County and Prince George's County).

### KEY RATING DRIVERS

## **Revenue Defensibility - 'aa'**

Very Favorable Service Area, Affordable Rates for the Vast Majority of the Population

WSSD serves an expansive and very favorable service area that encompasses parts of Prince George's and Montgomery counties. The district retains the legal authority to adjust rates as needed without external oversight. Using Prince George's County as proxy, Fitch considers the monthly residential water and sewer bill affordable for approximately 87% of the service area population based on standard monthly usage of 7,500 gallons for water and 6,000 gallons for sewer.

The very favorable service area is characterized by stronger income levels, a moderate unemployment rate relative to the nation and midrange customer growth. Customer growth registered a five-year CAGR of 0.5% as of fiscal 2023; the district's customer base is primarily residential and there is no customer concentration.

## **Operating Risk - 'aa'**

Very Low Operating Cost Burden, Moderate Investment Needs

In fiscal 2023, the system's operating cost burden was very low at \$5,470 per million gallons (mg) of flows, consistent with the operating risk assessment. The life cycle ratio was very low at 32% in fiscal 2023. Annual capital spending relative to depreciation has been robust, and was a five-year average of 205% for the five years ended fiscal 2023. Planned capital spending for the next five years should generally outpace historical depreciation, supporting a continued very low life cycle ratio.

The district's anticipated capital spending for fiscal years 2024 through 2028 approximates \$3.0 billion. The estimated spending includes approximately \$2.1 billion of bond proceeds, including those from prior sales, as well as \$746.3 million of pay go funds. The remaining sources primarily are derived from grants and capital contributions. The district continues to refine its capital plan to improve efficiencies and execution.

## **Financial Profile - 'aa'**

Leverage to Decline, Neutral Liquidity

The district had very low leverage of 8.1x as of fiscal 2023. As noted, this has been on a declining trend for the last several years, largely driven by improving FADS, and is down from the peak of 11.1x in fiscal 2020. The liquidity profile is neutral to the overall assessment with current days cash on hand of 229 and coverage of full obligations (COFO) of 1.8x. Fitch-calculated total debt service coverage for fiscal 2023 was 1.9x, which excludes fixed service expense.

The Fitch 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. The FAST reflects Fitch's view of a reasonable scenario, which is generally informed by publicly available and/or management provided information with respect to capex, user charges and rate of revenue and expenditure growth.

In the base case scenario, the leverage ratio is projected to increase to 9.4x in fiscal 2024, then decrease to 7.5x through fiscal 2028. In the stress case, the leverage ratio is expected to increase to 9.5x in fiscal 2024, then decline to 7.9x through fiscal 2028. Liquidity is expected to remain neutral to the assessment over the five-year horizon.

## **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**

- Failure to maintain leverage comfortably below 10.0x through the five-year horizon;
- Failure to secure rate increases that satisfactorily support operations and continued robust capital investment, including progress toward consent decree milestones;
- Contraction in the economic base that no longer supports an enhancement to the ratings.

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

- The rating is at the highest level on Fitch's scale and cannot be upgraded.

## **PROFILE**

The district provides retail water and sewer services to Montgomery and Prince George's counties along the north and east borders of Washington, D.C. In addition to utility charges, the district has the authority to levy ad valorem taxes without limit for debt service. The district's very favorable service area includes a broad and economically diverse customer base that spans nearly 1,000 square miles and serves over 1.9 million residents through approximately 479,000 water and 449,000 sewer customer accounts.

The commission consists of six members (three from each county and all residents of the district) who are appointed by respective county executives. The commission's responsibilities include, but are not limited to, planning for the operating and capital improvements of the district; establishing water and sewer usage rates, connection charges, and other charges and fees; causing ad valorem taxes to be levied; and approving new debt.

Water production at the district's two treatment plants averages in excess of 160 million gallons per day, well below the district's available supply. The district's sewer conveyance and treatment capacity are also ample. Treatment is shared among the district's six plants and the Blue Plains Advanced Wastewater Treatment Plant (owned and operated by the District of Columbia Water and Sewer Authority; IDR AA/Stable) with whom the district maintains a cost-sharing agreement.

### **Date of Relevant Committee**

18 January 2024

### **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
Washington Suburban Sanitary District (MD) [Water, Sewer]	LT AAA 	Affirmed	AAA 
<ul style="list-style-type: none"> <li>Washington Suburban Sanitary District (MD) /General</li> </ul>			

ENTITY/DEBT	RATING	RECOVERY	PRIOR
	Obligation		
	-		
	Unlimited		
	Tax/1 LT		

## RATINGS KEY OUTLOOK WATCH

<b>POSITIVE</b>		
<b>NEGATIVE</b>		
<b>EVOLVING</b>		
<b>STABLE</b>		

## Applicable Criteria

[U.S. Public Sector, Revenue-Supported Entities Rating Criteria \(pub.12 Jan 2024\) \(including rating assumption sensitivity\)](#)

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

## Additional Disclosures

[Solicitation Status](#)

## Endorsement Status

Washington Suburban Sanitary District (MD) EU Endorsed, UK Endorsed

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