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Ratings

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Washington Suburban Sanitary District, Maryland; General Obligation

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Table Of Contents

Washington Suburban Sanitary District, Maryland; General Obligation

Credit Profile		
US$315.95 mil cons pub imp bnds ser 2025 dtd 02/20/2025 due 06/01/2054		
Long Term Rating	AAA/Stable	New
Washington Suburban San Dist GO		
Long Term Rating	AAA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'AAA' rating to Washington Suburban Sanitary District (WSSD), Md.'s $287.2 million series 2025 consolidated improvement bonds and $28.7 million 2025 (second series) consolidated public improvement bonds (green bonds).
- At the same time, S&P Global Ratings affirmed its 'AAA' rating on the district's existing debt.
- The outlook is stable.
- Total debt outstanding (including the current issuance and Maryland Water Quality Bonds) is $4.4 billion.

Security

Debt service has been paid from revenues generated from fees, charges, rates and assessments, and other available funds. In the event of a deficiency, the Montgomery County and Prince George's County councils are required to impose ad valorem taxes on all the assessable property within the district. To date, neither county has been required to levy any ad valorem taxes to pay debt service on any of WSSD's outstanding bonds.

We understand proceeds from this issue will be used to fund capital projects, some of which are designated as "green projects," as well as the payment of costs of issuance related to the sale.

We consider the financial metrics supportive of the 'AAA' rating, with all-in coverage being just strong but with extremely strong liquidity levels in the past three fiscal years. We view the unlimited ad valorem property taxes, which could be levied should district operating levels decline, as supportive of the district's debt service (in theory), given the extremely strong liquidity levels and that timing issues are mitigated; this provides the rating additional support.

The issuer bonds are eligible to be rated above the sovereign because we believe the district can maintain better credit characteristics than the U.S. in a stress scenario. Under our criteria "Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions" (published Nov. 19, 2013, on RatingsDirect), the district has full rate-setting authority, in addition to independent taxing authority and independent treasury management from the U.S. government.

Credit overview

WSSD's credit quality is anchored by the extremely strong management team that has historically demonstrated an ability and willingness to reduce expenditures and increase rates to maintain sufficient coverage and liquidity, as well as the large and mostly affluent tax base that ultimately secures the bonds if user fees are insufficient. Management has numerous and formal prudent financial, operational, and capital policies, which we view as critical to the 'AAA' rating. We recognize that coverage and cash is narrower than those of its commensurately rated peers; however, the additional security provided by the tax base and management's history of rate increases and cost containment offset this risk.

Environmental, social, and governance

Overall, we believe WSSD has above-average exposure to regulatory risks given the existing consent decree and associated large capital improvement plan (CIP). However, management's strong practices and commitment to support environmental restorative and resiliency policies somewhat offset these risks. We believe WSSD has a better social and governance profile than its utility peers, which is reflected in the 'AAA' rating. Furthermore, the district expects to be completed with consent decree projects over the next 1-2 years. Implementing the increased levy requires approval from two governmental entities, which could increase the risk of delays. Liquidity is an important mitigant to this timing risk factor and management recently increased its liquidity target, which we view favorably.

Outlook

The stable outlook reflects our view of the large, diverse, and mostly affluent service area, which remains strong. Credit stability also rests with our view that management has a meaningful track record in managing volatility in revenues through significant expense reductions to maintain healthy coverage and liquidity. Despite substantial capital needs, we believe rates will remain affordable and financial metrics will meet forecasts.

Downside scenario

If management is unable to effectuate necessary rate increases or contain costs, which results in a reduction in reserves or a failure to meet forecast projections, while managing the sizable capital plan, we could lower the rating. While management has been prudent in reducing its expenditures historically, there is a point at which there will be fewer discretionary expenditures to reduce, which could necessitate greater rate increases and pressure rate affordability. Given income levels and affordability relative to peers, we believe this is unlikely but if political pressures or economic weakness results in willingness issues, we could also consider lowering the rating.

Credit Opinion

Enterprise Profile

WSSD serves a population of about 1.9 million in the Washington-Baltimore metropolitan area, the fourth largest in the nation. The local economy's depth and diversity, in our opinion, contribute to the district's below-average unemployment and above-average income and wealth. Unemployment has trended down for both counties indicating robust and ample employment opportunities. Montgomery County and Prince George's County median household effective buying incomes were 146% and 119%, respectively, of the national average, which we view as extremely strong. Market value for the district is $381 billion or $200,500 per capita, which we consider extremely strong and supportive of the 'AAA' rating.

The six-member Washington Suburban Sanitary Commission governs the district. The commission has full rate-setting ability; it levies a variety of charges and fees, the most significant of which are consumption charges – which accounted for roughly 79% of revenues in fiscal 2024. It typically provides the counties with a consumption-rate forecast annually. Rates are affordable, relative to both incomes and regional peers. The six-year rate forecast includes an 8.5% increase in 2025, followed by projected annual rate increases ranging from 9.8% in 2026 declining to 5.8% in 2031--equating to an average annual increase of 7.9%. In addition, fiscal 2025 rates included increased fixed fees as a proportion of water and sewer revenues to enhance revenue stability. We see these higher percentage of fixed charges as a credit positive and beneficial as it provides increased revenue stability as the district carries out its capital plan. Projected rate increases, above what has recently been proposed, is a direct result of the commission making the decision to do more pay-go funding for capital projects than in previous years. The district has affordability program and customer assistance programs for lower income customers, which have been recently reviewed and adjusted given the pressures related to the recent pandemic and associated economic downturn. The approach to addressing affordability is extremely comprehensive relative to its peers, in our opinion. We believe the rate increases in the long-range financial plan are prudent and will support the substantial CIP and the increased liquidity and coverage targets.

Financial Profile

Debt service coverage (DSC) is narrow relative to that of 'AAA' rated peers. However, management is sophisticated and has demonstrated an ongoing ability to recover costs and adjust expenditures as needed to meet revenue volatility. Through the pandemic, it has mitigated revenue losses through aggressive cost-containment "savings plans," which targeted reductions in operating expenses as well as pay-as-you-go and debt service savings. We believe management has demonstrated a willingness to raise rates and reduce costs to meet challenging operating and economic environments.

Debt service has always been paid by user fees, but the commission can levy an ad valorem property tax, if needed, which is a positive credit factor in our analysis. The commission sets the budget to ensure full cost recovery, including necessary infrastructure investment. Annual DSC, excluding capital contributions, has been at or slightly above sum sufficient and there is no rate covenant. Coverage for fiscal 2025 is expected to be somewhere between 1.2x and 1.3x, ultimately ramping up to 1.5x by fiscal 2027, which is the district's informal target.

The commission previously suspended all water turnoffs and late penalties due to the pandemic. As a result, payment delinquencies grew to $64 million as of June 30, 2021. As the economy improves, WSSD's delinquencies continue to decline(at $49.9 million in first-quarter 2025) and benefit from an increased number of payment plans preventing further account turnoffs. Management has effectively employed several methods to reduce the delinquencies, including consistent expansion of its customer assistance program in addition to the ongoing set up of payment plans.

WSSD's liquidity has remained healthy throughout the past decade, in our view. There have not been any draws on the reserve during fiscal years 2021-2024. If water or sewer operating revenues do not reach budgeted amounts, the commission first reduces expenditures, then draws on the reserve. If the reserve is inadequate, the commission may implement a midyear rate increase, although this has never been required. Finally, if all revenues are insufficient, the commission may levy a tax on the two-county area for debt service payment, which would be requested and effectuated annually. Liquidity is critical in a distressed scenario, given that there would be timing considerations associated with any tax levy. Management reports that cash on hand would be used as well as a line of credit, if needed. In fiscal 2024, liquidity was extremely strong with $452 million, or 306 days' cash on hand. On May 30, 2024, the commission executed a three-year maturity extension to extend their standby note purchase program through June 1, 2027 with the ability to issue up to $600 million of bond anticipation notes (BANs), if necessary.

Overall net debt (including overlapping debt) remains low, in our view, at about 1.5% of market value at the end of fiscal 2024. Debt to capitalization is moderate at 45%. All of the commission's debt is self-supporting. Despite the commission's history of annual debt issuances to fund WSSD's sizable CIP, the commission's overall net debt levels have remained low given the size of the customer and tax base. The 2026-2031 CIP is $4.8 billion, 68% of which will be debt-financed. Capital needs consist primarily of rehabilitation or replacement of the older portion of water and sewer mains, as well as ensuring compliance with the Potomac Water Filtration Plant and Sanitary Sewer Overflow consent decrees, which are currently on target. In our view, the near-term capital needs are substantial, but the income levels and customer base are sufficient to keep rates relatively affordable in the near term (relative to income and peers).

Management has a very strong, institutionalized asset management plan, and it builds ongoing rehabilitation into the annual budget. Asset management is innovative and has improved operational performance and, in many cases, building resiliency into the system and reducing costs, which we view favorably. Emergency response planning assesses enterprise-wide risk and plans for emergency response. Given the effects of climate change and the increased frequency of significant storms, we believe this level of planning is critical to credit quality. The commission continues to update cyber-security policies following a cyber-attack in May 2021. The attack did not result in any financial or operational issues. Limited data on the commission's internal network were accessed and the commission followed the appropriate notification steps. We understand that no information was publicly disclosed. Existing policies and protective measures are in place. We believe management has prudent cyber policies in place and in addition to cyber insurance, is taking sufficient steps to enhance its cyber-protective measures.

Washington Suburban Sanitary District, Maryland--economic and financial data

		Fiscal year-end			
	Most recent	**2024**	**2023**	**2022**	**Median (AAA)**
Economic data					
MHHEBI of the service area as % of the U.S.	133.3				114.0
Unemployment rate (%)	2.6				3.4
Poverty rate (%)	9.3				10.3
Water rate (6,000 gallons or actual) ($)	44.4				33.3
Sewer rate (6,000 gallons or actual) ($)	59.4				37.2
Annual utility bill as % of MHHEBI	1.4				1.0
Operational management assessment	Good				Good

Washington Suburban Sanitary District, Maryland--economic and financial data (cont.)

		Fiscal year-end			
	Most recent	**2024**	**2023**	**2022**	**Median (AAA)**
Financial data					
Total operating revenues ($000s)		947,067	884,792	833,602	73,371
Total operating expenses less depreciation ($000s)		538,473	512,750	475,942	53,231
Net revenues available for debt service ($000s)		490,934	463,026	425,355	--
Debt service ($000s)		228,621	278,504	285,668	--
S&P Global Ratings-adjusted all-in DSC (x)		2.1	1.7	1.5	2.6
Unrestricted cash ($000s)		451,944	382,348	297,379	90,711
Days' cash of operating expenses		306	272	228	713
Total on-balance-sheet debt ($000s)		4,431,430	4,328,372	4,102,568	140,491
Debt-to-capitalization ratio (%)		45.0	45.1	44.5	26.0
Financial management assessment	Strong	--	--	--	Strong

Note: Most recent economic data available from our vendors. MHHEBI--Median household effective buying income. DSC--Debt service coverage.

Ratings Detail (As Of January 24, 2025)

Washington Suburban Sanitary Dist consolidated pub imp bnds		
Long Term Rating	AAA/Stable	Affirmed
Washington Suburban Sanitary Dist consolidated pub imp bnds of 2023		
Long Term Rating	AAA/Stable	Affirmed
Washington Suburban Sanitary Dist cons pub imp rfdg bnds		
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