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Ratings

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Summary:

Albuquerque-Bernalillo County Water Authority, New Mexico; Water/Sewer

Primary Credit Analyst:
Theodore A Chapman, Dallas (1) 214-871-1401; theodore.chapman@spglobal.com

Secondary Contact:
Jose E Razo, Dallas 2147655877; jose.razo@spglobal.com

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Credit Profile		
US$89.49 mil sr lien jt wtr and swr sys rfdg and imp rev bnds ser 2017 due 07/01/2034		
Long Term Rating	AA+/Stable	New
Albuquerque (Albuquerque Jt Wtr & Swr Sys)		
Long Term Rating	AA+/Stable	Affirmed

Rationale

S&P Global Ratings assigned its 'AA+' long-term rating to Albuquerque-Bernalillo County Water Authority, N.M.'s (the authority) series 2017 senior-lien joint water and sewer system refunding and improvement revenue bonds. The rating reflects, in our opinion, the combination of an extremely strong enterprise risk profile and a very strong financial risk profile. In addition, we affirmed our 'AA' rating on the authority's series 2014B subordinate-lien system refunding revenue bonds. The outlook on all debt is stable.

We have applied the utility revenue bond criteria to determine the authority's general creditworthiness (issuer credit rating) and have applied this rating to the senior-lien issues. Because of the open nature of the senior lien, meaning additional parity debt could still be issued in the future, we continue to make a rating distinction between the two liens. We expect management to primarily use the senior lien for its capital market debt.

The enterprise risk profile reflects our opinion of the authority's:

- Service area that includes the state's primary economic center, with an employment base that was resilient through the recession and continues to exhibit stability;
- Robust planning efforts that ensure that operational and financial requirements are well-aligned, including resource management and sustainability, financial policies that establish strong levels of pay-as-you-go funding and operations that reflect a long-term water supply from a mix of surface and groundwater; and
- Combined water and sewer rates that remain very affordable even with a number of recent and planned rate adjustments.

The financial risk profile reflects our view of the system's:

- Financial performance that has seen a sustained recovery. Immediately following the introduction of a new raw-water supply source and the corresponding treatment facilities, the authority's coverage and cash positions dipped measurably but have since rebounded very well;
- Rapid roll-off of its existing long-term debt, allowing additional debt funding of projects without pressuring rates or financial results; and
- Strong financial management practices and policies, which in our view makes it likely that recent financial performance will perpetuate into the future.

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We understand that the proceeds of the series 2017 bonds will be used to refund eligible maturities of the authority's series 2009A-1 senior lien revenue bonds for savings purposes as well as funding $71 million in new projects. The bonds are secured by a first- lien pledge on the net revenues of the authority's retail waterworks and sanitary sewer system. The authority has about $497 million in senior-lien debt, $85 million in subordinate-lien bonds and loans, and $1 million in super-subordinate state loans. The authority has no direct purchase obligations or what we would deem as less traditional debt instruments that could expose it to contingent liquidity risks.

Additional senior-lien bonds may be issued so long as senior-lien debt service coverage (DSC) is at least 1.33x maximum annual debt service (MADS), whereas the test for additional subordinate-lien debt is 1.2x MADS. Debt service reserve funds are established on a series by series basis.

Enterprise risk

Albuquerque-Bernalillo County Water Authority serves nearly 210,000 metered accounts, or an estimated 95% of the total residents of the county, although aside from annexations or other one-time system expansions, the annual growth rate has moderated greatly since the recession and subsequent recovery. The Albuquerque metropolitan statistical area (MSA) has a broad and diverse economy and is the largest economy in the state. With a population of more than 658,000, employment opportunities in the MSA are led by the federal and local government, the flagship campus of the University of New Mexico, a robust health care sector, and Sandia National Laboratories. In addition, financial services and technology are growth sectors, including larger new additions by Fidelity Investments and Facebook. As such, the November 2016 unemployment rate for the MSA of 5.8% is better than the state's although slightly higher than that of the U.S. The county's median household effective buying income is roughly on par with the nation's. The authority has no concentration concerns from its principal customers relative to its total operating revenues.

The authority derives its raw water from a diverse supply that includes both ground and surface water. In 2016, surface water supplied 55% of the total raw water, mainly from the Rio Grande and Colorado rivers by way of direct water rights or firm bilateral agreements. Authority management believes that the current supply will be sufficient to support a total population of at least one million given the decades of successful resource management by way of voluntary and mandatory water conservation measures. Water levels vary in the reservoirs that impound the surface water. At the end of 2016 in the Rio Grande basin, Abiquiu Reservoir was over 80% full and relatively healthy, although the Heron Reservoir is less than 25% full. The system has not suffered any curtailments or other limitations in its surface water allocations.

The authority's governing board in 2013 implemented additional rate increases for 2016 and 2018 with the goal of generating 5% operating revenue growth each time. Even with every-other-year rate increases since the beginning of the decade, rates in our view remain extremely affordable. Based on S&P Global Ratings' universal assumption of 6,000 gallons of water and sewer service, a monthly residential bill is currently about $40, or about 1.1% of median household effective buying income.

Based on our operational management assessment, we view the authority to be a '1' on a scale of 1-6, with '1' being the strongest. In our opinion, this indicates the strongest alignment of operations and organizational goals. The strong OMA includes a diversified and ample long-term raw-water supply, aggressive and well-embedded programs for both water conservation and reuse, and a comprehensive strategic vision for all divisions of the utility that includes benchmarking and high expectations across all facets of operations. In addition to having robust water conservation measures for decades, the authority in 2009 began an aquifer storage and recovery project that can inject as much as 10,000 acre-feet per year as underground storage. It has also been active in nonpotable water reuse, serving large irrigators and industrial customers since 2000.

In 2003, the state legislature created the Albuquerque-Bernalillo Water Utility Authority and transferred all functions, assets, and liabilities of the city of Albuquerque water and sewer system to the authority; separation of accounting functions, including audited financial statements, was completed in 2013. The authority is governed by a board consisting of three city council members, three county commissioners, the mayor of Albuquerque, and the village of Los Ranchos trustee (nonvoting). In 2005, the authority became a separate political subdivision of the state, rather than a joint agency of the city and county.

Financial risk

The authority's financial profile has historically been a strength, sustained by robust financial management policies and practices. This includes establishing rates to target a budgeted 1.5x senior-lien annual DSC, stronger than even its 1.33x senior-lien rate covenant. DSC and cash reserves, however, weakened for several years in 2010 as the authority adjusted operations to include treated surface water, as well as the related increase in annual debt service requirements. It was at this time that the board began implementing every-other-year rate adjustments, typically preapproving one future year increase at the same time as implementing one for the current budget. The authority has since rebuilt reserves substantially; as of the end of fiscal 2016, unrestricted cash stood at $101 million, and management has committed to budgeting a $2 million addition per year to build its rate stabilization reserve. All-in coverage has also rebounded; for fiscal 2016 it stood at 1.53x, and management's forecast--which we view as attainable--shows coverage consistently at or near 1.6x. All-in coverage is S&P Global Ratings' adjusted DSC metric that includes all recurring obligations of utility operating revenues, regardless of lien or accounting treatment. Total available cash reserves are now equivalent to almost one year of operating expenses, from as little as 12 days' cash on hand in 2010.

While the 10-year capital improvement plan (CIP) of $680 million assumes 41% debt funding, over 70% of the existing long-term debt will have been repaid over the same period. Management anticipates funding the remainder of the CIP with internally generated revenues. Therefore, we agree that additional periodic use of debt could be layered onto the existing capital structure without adversely affecting financial performance. The main project of the plan will be a comprehensive upgrade to the system's southside water reclamation plant, which already uses a methane capture system to generate enough electricity to run the entire plant.

Based on our financial management assessment (FMA), we deem the authority to be a '1' on a scale of 1-6, with '1' being the strongest. An FMA of 'strong' indicates that practices are strong, well embedded, and likely sustainable. The government maintains most of the best practices deemed critical to supporting credit quality and these are well-embedded in the government's daily operations and practices. Formal policies support many of these activities, adding to the likelihood that these practices will be continued into the future and transcend changes in the operating environment or personnel. This includes regularly updating its long-term financial forecast and capital improvement plan, constant budget monitoring, and a robust set of internal policies that make it likely that the recently improved financial performance will be sustainable over time.

Outlook

The stable outlook reflects our anticipation that the rebound in financial performance is sustainable over our two-year outlook horizon and probably beyond given the long-term view towards rate adjustments and commitment to maintaining its restored reserve levels.

Upside scenario

Given the inherent economic stability in the MSA, upward pressure on the rating would be driven primarily by attaining or exceeding its financial forecast for all-in coverage while sustaining strong reserves. While the timetable for such expectations could come within or beyond our two-year outlook horizon, we could raise the long-term senior-lien rating to 'AAA' from the current rating and stable outlook.

Downside scenario

Although we do not expect it, downward pressure on the rating would most likely come from a precipitous drop in financial performance, for example by way of aggressive use of debt that outstrips growth in the operating revenues, perhaps driven by a new unfunded environmental regulatory mandate.

Ratings Detail (As Of January 4, 2017)		
Albuquerque Bernalillo Cnty Wtr Util Auth jt wtr and swr sys imp rev bnds		
Long Term Rating	AA+/Stable	Affirmed
Albuquerque Bernalillo Cnty Wtr Util Auth WTRSWR		
Long Term Rating	AA/Stable	Affirmed

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.