

RatingsDirect®

Summary:

Texas Water Development Board; State Revolving Funds/ Pools

Primary Credit Analyst:

Adam Torres, New York + 1 (212) 438 1141; adam.torres@spglobal.com

Secondary Contact:

John Kennedy, CFA, Chicago +1-312-233-7088; john.kennedy@spglobal.com

Table Of Contents

Credit Highlights

Outlook

Credit Opinion

Summary:

Texas Water Development Board; State Revolving Funds/Pools

Credit Profile

US\$915.545 mil st wtr implementation rev fd for texas, rev bnds ser 2022 due 04/15/2039

<i>Long Term Rating</i>	AAA/Stable	New
Texas Wtr Dev Brd SFRP		
<i>Long Term Rating</i>	AAA/Stable	Affirmed
Texas Wtr Dev Brd SRFP		
<i>Long Term Rating</i>	AAA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'AAA' rating to the Texas Water Development Board's (TWDB) anticipated \$916 million series 2022 State Water Implementation Revenue Fund for Texas (SWIRFT) revenue bonds.
- At the same time, S&P Global Ratings affirmed its 'AAA' rating on the TWDB's SWIRFT bonds outstanding.
- The outlook is stable.

We borrowed elements of our criteria "Commercial Paper, VRDO, And Self-Liquidity," published July 3, 2007, specifically the adoption of asset discount factors, to stress the market value of certain SWIFT fund holdings, namely equities, that may be used for SWIRFT purposes.

Security

Bond proceeds will be used to purchase 17 political subdivision obligations (PSOs) from 13 different entities. The bonds are secured by the repayment of those PSOs, along with funds transferred from the State Water Implementation Fund for Texas (SWIFT) to the SWIRFT.

Credit overview

We assessed SWIRFT's enterprise risk profile as very strong, given that the program was established through the passage of a constitutional amendment, was capitalized via a direct equity contribution, and is managed by a governmental agency. We believe the program's financial risk profile is extremely strong, reflected by the loss coverage score (LCS), operating performance, and financial policies.

The combination of the risk profiles scoring, along with a positive overriding factor due to the lack of any default or delinquency in all TWDB programs for an extended period, leads to the 'AAA' rating. Key to the rating is that, if necessary, the SWIFT account may address PSO delinquencies and defaults; we have stressed these funds during our loss coverage analysis and our evaluation of the financial risk profile.

Outlook

The stable outlook reflects our expectation that, in line with historical trends, embedded policies and procedures will remain consistent; proactive financial management will ensure stable cash flows that meet program goals and objectives; and the SWIFT funds, while established to provide for growth in the fund, will also provide for a high level of potentially available funds for SWIRFT programs, including addressing any potential defaults or delinquencies. The stable outlook also incorporates our expectation that TWDB management will maintain the ability and willingness to address any SWIRFT account shortfalls through additional bond-enhancement agreements as required.

Downside scenario

We could lower the rating if the SWIFT is leveraged to the point of creating a stress level for which the fund is unable to compensate. A change in the policies, procedures, or governing legislation that allows for, or creates significant dilution of available SWIFT balances could pressure the rating. Finally, if management demonstrates an unwillingness to take appropriate steps to cure any revenue shortfalls in the respective SWIRFT accounts, we could also take a negative rating action.

Credit Opinion

SWIRFT program

In November 2013, voters approved an amendment to the state constitution, which created the SWIFT and the SWIRFT. To initially capitalize the SWIFT, \$2 billion was transferred from the state's economic-stabilization fund and placed in the SWIFT. Funds held in the SWIFT are managed by the Texas Treasury Safekeeping Trust Co. The SWIFT was established to provide financial assistance for state water plan projects and had a market value of \$1.8 billion as of March 31, 2022.

Although the balance in the SWIFT is not pledged to the bonds, the use of the funds in the SWIFT is highly restricted and they can be used only for state water plan projects. Although these projects could include other TWDB programs, it remains the board's intent that the corpus of the SWIFT be available to make annual transfers to the SWIRFT to fund local water projects. The availability of the S&P Global Ratings-stressed SWIFT balance and the board's willingness to approve additional transfers to cover any shortfalls in the SWIRFT accounts remain, collectively, a critical factor in our assignment and maintenance of the 'AAA' rating.

With each issuance of bonds, a bond-enhancement agreement is executed and a transfer of funds from the SWIFT to the SWIRFT occurs. This transfer is sized to provide for the targeted subsidy amount determined by the TWDB. The corpus of the transfer, coupled with projected interest earnings and the scheduled repayments of the PSOs, is designed to provide 1.0x annual debt service coverage for each series of bonds. The transfer amount is determined in connection with each bond issue. Bonds projected to be issued in subsequent years will not be on parity with these, or with any previously issued, bonds. Each bond series is supported by a specific revenue stream, although that stream will always include certain PSO repayments and the related transfer from the SWIFT to the respective SWIRFT assistance account under that specific bond-enhancement agreement. The TWDB is authorized to execute no more than two bond-enhancement agreements each fiscal year.

Enterprise profile

The very strong market position score reflects the fact that the program was established through the passage of a constitutional amendment, was capitalized via a direct equity contribution, and is managed by a governmental agency. However, additional governmental support or contributions are not anticipated. The TWDB was created in 1957, with a mission of providing leadership, information, education, and support for planning, financial assistance, and outreach for the conservation and responsible development of water. It is responsible for long-term water planning and is primarily responsible for the state's financial programs associated with the water industry, including the establishment of policy for the financial programs.

We do not consider the program to be geographically concentrated, although densely populated areas of the state will likely require more funding.

Financial profile

Revenues from the PSOs do not initially provide 1.0x coverage of the annual bond principal and interest payments. The initial transfer of funds from the SWIFT is designed to cover that shortfall, which in effect creates a subsidy to the program participants. As the cash flows are currently structured, and assuming less than 100% recovery of any PSO defaults within the program, only a minimal level of defaults can be absorbed unless either projected interest earnings on any of the indenture accounts are significantly higher than projected or funds are accumulated in surplus accounts. Because of this, the rating is dependent on the mechanism that allows, but does not require, TWDB management to execute additional bond-enhancement agreements to address any SWIRFT shortfalls. TWDB management's ability and willingness to transfer funds if necessary is a key credit consideration.

Another factor that supports the extremely strong loss coverage score is the generally high credit quality of the participants. Following this round of funding, there will be 160 PSOs. Although there is some concentration in the SWIRFT program, with the top five borrowers representing 65% of PSOs by dollar amount, these borrowers are all rated at least 'AA-'. Furthermore, throughout the program, no single borrower exceeds 20% of PSO dollars; we expect diversification to continue.

Management's intent is to eventually provide financial assistance of more than \$27 billion, which would be supported by PSO repayments and future bond-enhancement agreements. Because of this, the investment strategy related to the SWIFT will become more critical as additional leveraging takes place. The SWIFT is actively managed by the Texas Treasury Safekeeping Trust Co., with many investment options available to maximize returns through a dynamic financial analysis model. In our view, a sufficient portion of the SWIFT is liquid, with a target allocation of 10% to be held in cash. This is in addition to the amount annually transferred to the SWIRFT program. Other investments include global equities, hedged equities, and global fixed income. The SWIRFT accounts are held at the trustee levels, and invested subject to the Texas Public Funds Investment Act.

Other factors supporting the extremely strong financial risk profile are the strong policies and procedures in place for administration of the SWIFT and SWIRFT. Management has an established application process for all of the board's financial assistance programs. Each year, TWDB staff review every SWIFT program participant's financial status. In addition, to guard against effects on future debt service payments, sufficiency of PSO revenue is required to be calculated at least 40 days in advance of the upcoming principal or interest payment date. Management also has

well-established investment policies and guidelines.

Rating above the sovereign

Because we view securitizations backed by pools of public-sector assets as highly sensitive to country risk, the rating on the securitization is capped at two notches above the sovereign. However, no specific sovereign default stress is applied, given that the U.S. sovereign rating is 'AA+'.

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.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

Copyright © 2022 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.