

RatingsDirect®

Summary:

Texas Water Development Board; State Revolving Funds/Pools

Primary Credit Analyst:

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

Secondary Contact:

Lisa R Schroeer, Charlottesville + (434) 529-2862; lisa.schroeer@spglobal.com

Table Of Contents

Rating Action

Stable Outlook

Credit Opinion

Summary:

Texas Water Development Board; State Revolving Funds/ Pools

Credit Profile

US\$264.595 mil state revolving fd rev bn ds ser 2022 due 08/01/2043

Long Term Rating

AAA/Stable

New

Texas Wtr Dev Brd SFRP

Long Term Rating

AAA/Stable

Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' rating to the Texas Water Development Board's (TWDB) anticipated \$264.595 million series 2022 state revolving fund (SRF) revenue bonds. At the same time, we have affirmed our 'AAA' rating on the board's SRF revenue bonds outstanding. The outlook is stable.

Bond proceeds will be used to fund the purchase of additional local political subdivision bonds, and may also fund the state match requirements for clean water and drinking water SRF programs. Local bond repayments flowing into the SRF programs from the board's portfolio of pledged political subdivision bonds are the primary source of security for SRF revenue bonds.

The stable outlook on the 'AAA' long-term rating reflects the program's financial strength and conservative management and S&P Global Ratings' expectation that the board will maintain strong coverage levels. We do not anticipate changing the extremely strong enterprise and financial risk profiles and, therefore, a lower rating is not likely.

Credit overview

Following the series 2022 issuance, TWDB will have approximately \$4.8 billion of political subdivision bonds outstanding pledged to secure about \$2.0 billion of state-revolving loan fund debt service payable. Board officials have funded the purchase of political subdivision bonds with a combination of state-match and revenue bonds, federal capitalization grants, and surplus cash flows from the program. The program's capitalization sources have allowed the board to maintain very strong debt service coverage (DSC).

The 'AAA' rating reflects the combination of extremely strong enterprise and financial risk profiles, which, in turn, reflect the board's:

- Low industry risk score and extremely strong market position;
- Ongoing federal and state support, with strong state oversight;
- Extremely strong loss coverage score due to annual coverage generated from program participant payments, which is bolstered by the excellent history of borrower repayment, with no defaults; and

- Generally strong financial policies and practices.

Given these enterprise and financial risk profiles, the final rating is 'AAA' because we did not make any negative overriding adjustments.

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+'.

Stable Outlook

Downside scenario

Although highly unlikely, a lower rating could be warranted should there be a combination of excessive leveraging that creates stress on annual coverage levels or should there be a sudden increase in borrower payment defaults or delinquencies.

Credit Opinion

Enterprise risk

The extremely strong enterprise risk profile reflects the program's low industry risk, coupled with an extremely strong market position. The market position is an indication of TWDB's governance structure, along with the ongoing support of the program, and our expectation of continued federal and state equity contributions. The board was established in 1957 by constitutional amendment and provides financial assistance by purchasing bonds issued by entities in the state. It is governed by three governor-appointed members. An executive administrator and an experienced, industry-recognized staff are responsible for managing the board's programs, including the SRF. The state has historically met the federal matching requirement through the issuance of general obligation (GO) bonds but has used SRF revenue bonds to fund the state match since 2018.

The pledged TWDB bond portfolio consists of more than 600 obligations to more than 300 distinct entities across the state. We consider the portfolio diverse, though the top 10 borrowers represent approximately 52% of total par outstanding. Significant borrowers include Houston Combined Utility System (13% of bonds held by the board), the North Texas Municipal Water District (NTMWD; 10%), and the San Antonio Water System (6%). A multiyear commitment to fund projects at NTMWD suggest concentration may increase somewhat in the coming years. Officials conveyed that the program is not making other new multiyear commitments at this time.

Financial risk

The financial risk profile reflects the program's ability to absorb a very high level of loan defaults or delinquencies, coupled with an extremely strong payment history and strong financial management practices.

TWDB is projecting to receive approximately \$6.0 billion of loan payments through 2052 to support the clean and drinking water SRF bonds and obligations related to the state GO bonds previously used to fund the state match requirements. A new master resolution was authorized on March 1, 2018. All bonds under the prior clean water SRF

master resolution have been defeased to the call date, leaving only the series 2018, 2019, 2020, and 2021 SRF revenue bonds under the new master resolution outstanding.

TWDB can use pledged revenues from existing clean water and drinking water SRF subdivision bonds to pay annual debt service related to the outstanding revenue bonds and state GO bonds issued to fund state match. The pledge of SRF loan repayments to the state GO bonds is subordinate to the pledge of those loan revenues to the SRF bonds. However, our cash-flow analysis includes the debt service on the state GO bonds, as in practice those are repaid from the SRF loan revenue. This all-in coverage produces a still very strong annual DSC no lower than 1.6x during the life of the bonds under our stress scenarios evaluating the influence of certain levels of borrower defaults. Annual coverage under our stress scenarios on the SRF bonds alone projects at no less than 2.0x during the life of the bonds.

Positive credit features also include the board's policies regarding origination and monitoring of bonds it purchases. Prior to the purchase of political subdivision bonds, the TWDB staff reviews financing applications received. The applications include an engineering review, along with certain legal and fiscal information. Once bonds are purchased, the TWDB financial compliance group annually reviews each issuer. There are multiple levels of review, from a general desktop review to a more thorough analysis if needed.

To guard against cash-flow uncertainties, local bond payments are received throughout the year so that TWDB receives funds well in advance of revolving fund bond payment dates. To help gauge future demand for financing assistance, it completes an annual capacity evaluation, with the annual funding level included in the required intended-use plan. Regarding investments, the board follows the guidelines set forth in the state's public funds investment act and public funds collateralization act. The primary objectives are security and liquidity.

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.