FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms Washington Metropolitan Area Transportation Authority; Outlook Remains Negative

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Fitch Ratings - New York - 12 May 2022: Fitch Ratings has affirmed the Washington Metropolitan Area Transportation Authority's (WMATA) outstanding dedicated capital revenue bonds and gross transit revenue bonds (series 2017A-1, 2017A-2, 2017B, 2020A and 2021A) at 'AA'. Fitch has also affirmed WMATA's outstanding gross transit revenue bonds, series 2018 and Issuer Default Rating (IDR) at 'AA-'.

The Rating Outlook Remains Negative.

The rating distinction amongst the outstanding gross revenue transit bonds reflects the additional pledge of dedicated capital funds for the series 2017A-1, 2017A-2 and 2017B bonds (see below for more information on the bonds' security provisions).

SECURITY

The dedicated revenue bonds are backed by a lien on the dedicated capital funding established under the 2020 bond resolution. The dedicated capital revenues are payable to the authority pursuant to statutes enacted by the District of Columbia (the district), the

Commonwealth of Virginia and the State of Maryland (collectively, the states), subject to annual appropriation.

The statutory dedicated capital funding revenue allocation is as follows: $178.5 million from the district payable from its general sales tax revenue, $167 million from Maryland payable from the Maryland Transportation Trust Fund (TTF), and $154.5 million from Virginia (approximately $30 million of which is not available for debt service) payable from various regional taxes on transient accommodations, wholesale fuel purchases, real property transfers, and sales and use taxes.

The pledge of the dedicated capital revenues is subordinate to approximately $640 million of outstanding gross revenue transit bonds, series 2017AB. The series 2017AB bonds are backed by a pledge of the trust estate established pursuant to the 2003 gross revenue bond resolution, which includes all transit system operating revenues (fares, rents, etc.) and operating subsidies received from the states and participating local governments within the WMATA transit zone.

The 2003 gross revenue bond resolution was amended prior to the issuance of the authority's gross revenue transit bonds, series 2018 so that all bonds issued under the 2003 gross revenue bond resolution on or after Nov. 15, 2018 (including the series 2018 bonds) do not have a lien on the dedicated capital funding revenues.

KEY RATING DRIVERS

Analytical Conclusion: The 'AA' rating on the authority's dedicated revenue bonds is based on a dedicated tax bond (DTB) analysis of the underlying revenue streams that support each state's capital funding commitment, and the general credit quality of the authority, as expressed through its IDR. Each state is allowed, but not required, to proportionally reduce its dedicated capital funding contribution if another does not pay its full amount. The rating reflects a weak link approach to the dedicated tax analysis.

Each state's dedicated capital funding contribution is subject to appropriation establishing a cap at one notch below the lowest of the district and the states' IDRs. Fitch's IDR for the district is 'AA+'/Stable and 'AAA'/Stable for both Maryland and Virginia.

Rating Link to WMATA's IDR: Fitch views the security for the dedicated revenue bonds as linked to, but not capped by, the general creditworthiness of the authority. The authority was created by an interstate compact through legislation passed by the district, Maryland, Virginia and the U.S. Congress, the effect of which, in Fitch's opinion, is to grant the authority sovereign-like powers and to make it ineligible for bankruptcy or other insolvency proceedings.

Since the dedicated capital funding revenues are segregated from the authority's operations and statutorily restricted for "state of good repair" projects (and prohibited from being used for operating expenses) Fitch's criteria allow for the rating on the dedicated revenue bonds to be above the authority's IDR. However, Fitch believes the flow of dedicated capital funding revenues to the authority could be vulnerable to impairment in a fiscal emergency, which limits the degree of notching above the authority's IDR. The Negative Outlook on the dedicated revenue bonds reflects the Outlook assigned to the authority's IDR.

Authority IDR Analysis: WMATA's Outlook remains Negative, reflecting the risk from continued low ridership (about 30% of pre-pandemic levels) and passenger revenues and uncertainty about the authority's ability to realign spending with federal stimulus accounting for approximately 30% of the nearly $2.3 billion fiscal 2023 operating budget. The authority expects to exhaust its remaining federal stimulus ($314 million) in fiscal 2024, heightening risk to a rating downgrade within the next 12 months absent improvement in ridership and revenue trends and a plausible plan to address the authority's structural budget gap.

The authority's 'AA-' IDR reflects its general credit quality, including a 'stronger' revenue defensibility assessment underpinned by the strength and stability of financial support provided by highly rated participating jurisdictions, which are obligated (subject to certain restrictions) to cover the operating and capital costs of the transit system from its legally available funds, subject to annual appropriation. The assessment also reflects the authority's strong pricing characteristics including its full rate-setting authority, strong market position, and the essentiality of mass transit service within a large and diverse economy.

The 'midrange' assessment of the authority's operating risk profile reflects its significant capital needs and track record of system performance and safety issues, rapidly rising but still manageable pension costs, and constraints imposed by collective bargaining agreements and a labor framework featuring binding arbitration. Service reductions and layoffs represent the most meaningful of the authority's cost-cutting tools, but Fitch views these as difficult to implement given prospects for significant consumer, political and labor push back.

The authority's debt position will continue to rise sharply with incremental debt servicing costs expected to consume the bulk of the $470 million of dedicated capital funding. The FY23-28 capital investment plan totals $13.9 billion, of which approximately $5.0 billion will be funded by additional debt. Fitch expects the ratio of overall net leverage (inclusive of the authority's net pension liabilities) to gross pledged revenues to increase from approximately 2.8x in FY21 to 4.5x in FY26. The forecasted leverage ratio would remain consistent with the current rating assuming the stabilization of the authority's revenue profile. Fitch expects the authority will align the timing and amount of capital spend in response to available resources over time.

The rating continues to reflect the authority's strong legal and regulatory framework resulting from its creation through an interstate compact, which grants it sovereign-like powers and exemption from all laws and orders of its signatories, with limited exceptions.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--For the dedicated capital revenue bonds, positive action on the authority's IDR (assuming sustained high resilience of the structure to Fitch revenue scenarios).

--For the IDR, evidence of a sustainable recovery in ridership, new recurring revenue for operations and development of a credible cost savings plan that convincingly stabilizes authority finances.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--For the dedicated capital revenue bonds, a decline in dedicated capital funding below the statutorily prescribed amounts, or a weakening in the overall credit profile of the authority given the rating link to the IDR.

--For the IDR, a shift in Fitch's view of the mass transit system's essentiality to the regional economy, suggested by a lack of progress closing the ridership gap to pre-pandemic levels or evidence of weakened support for the authority's operating and capital budget by the states and/or participating jurisdictions.

--For the IDR, failure to develop a plausible plan that addresses the unwinding of federal fiscal stimulus and realigns recurring spending against forecast revenues.

--For the IDR, an outcome from the ongoing investigation of the authority's 7000-series railcars that prolongs or weakens its ridership recovery or adds material pressure to its liability and cost structure or capital plan.

--For the IDR, growth in long-term liabilities, including unfunded pensions, absent a commensurate increase in fiscal resources that constrains the authority's operating budget and spending flexibility.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

CREDIT PROFILE

IDR Developments

The operating budget for FY23 totals $2.25 billion, an increase of 7.0% from the FY22 budget. Principal funding sources for the budget include $1.2 billion in participating jurisdiction contributions (compliant with the 3% annual cap), $293.1 million in passenger revenue (about 43% of FY19 levels) and $680.8 million in federal stimulus (resulting in a balance of $314.3 million available for FY24).

WMATA was allocated $2.57 billion in federal stimulus that has been used to support the operating budget and avoid substantial service cuts and workforce reductions. Stimulus funds have also bolstered the authority's liquidity, which it estimates at $858.9 million as of 3QFY22 (or 145 days' operating expenses). Fitch's view of the authority's liquidity also considers $350 million in undrawn capacity under separate lines of credit.

Spending growth is driven by contractually bargained wage and step increases plus operating costs associated with increased service provision, including the commencement of the Silver Line Phase II operations. However, the system is operating below budgeted levels following the October 2021 derailment of the 7000-series railcars and ongoing National Transportation Safety Board investigation. The 7000-series trains, which accounted for close to 60% of the railcar fleet, remain offline. The authority has restored older series railcars into service, but the system has been operating at 44% to 64% of pre-pandemic levels depending on the service period.

Chronic service disruptions have plagued the authority, and this latest incident likely detracts from efforts to encourage ridership including new fare and pass offerings and discount programs. The authority does not expect to be able to return the 7000-series railcars to service until at least the summer of 2022.

The budgeted ridership (systemwide) for FY23 is 53% of pre-pandemic levels, and preliminary estimates target a return to 65% and 75% by FY24 and FY25, respectively. Rail ridership, which accounts for 52% of trips but 79% of budgeted passenger revenues (at $230.4 million), has averaged roughly 26% of pre-pandemic levels during the prior 6-month period, rising slightly to 32% in March as more federal government workers return to the office and resumption of tourism and group events. The substantial gap between budgeted and current ridership is a major credit risk, as the depth of spending cuts necessary to produce a balanced budget (as required under the authority's enabling act) as federal stimulus funds are depleted could ultimately worsen the ridership outlook.

Dedicated Capital Revenue Bond Profile

Given the legislative condition by which the states can proportionately reduce their dedicated capital funding commitment based on a payment reduction of another, Fitch's dedicated tax analysis is based on a "weak link" approach applied to the underlying revenue streams that support each state's respective dedicated capital funding revenues. The dedicated capital funding revenues are non-reverting once appropriated and statutorily authorized exclusively for the authority's capital program and the payment of debt service (with the exception of approximately $30 million from Virginia not available to pay debt service). Pursuant to the indenture, the revenues will be deposited into a restricted account of the authority and segregated from its transit operating revenues and the operating and capital subsidies it receives from the states and the participating jurisdictions.

The dedicated capital funding revenues are derived from various sources identified in each state's dedicated capital funding legislation. The district has agreed to fund $178.5 million annually from its general sales tax revenue, payable semiannually on Oct. 1 and April 1. Fitch estimates the district's general sales tax revenues at $1.3 billion in FY21 or 7.2x the required contribution.

Maryland's legislation states that the governor is required to budget and seek an appropriation annually of $167 million from revenues in the TTF established to support the Maryland Department of Transportation. TTF revenues include a combination of fuel tax, motor vehicle titling tax, operating funds, motor fuel license and registration fees, and corporate income taxes, among other sources, are estimated at $3.3 billion in FY21 or 19.8x the required contribution.

Virginia's legislation directs a combination of regional revenues to be paid into the state treasury and credited to a WMATA capital fund to be released to the authority on a monthly basis pending certification of various capital and financial audits of the authority. Virginia's WMATA capital fund is to be funded annually with local transportation sales tax revenues, a regional recordation fee equal to $0.15 for each $100 of value of the related real property, a regional transient occupancy tax (TOT) equal to 2% on the amount of the charge for any dwelling or lodging room or space, and a regional wholesale fuel tax imposed on each gallon of fuel sold based on a rate established by the Commissioner of the Department of Motor Vehicles.

The local transportation sales tax revenues are fixed at $27.12 million per annum, whereas the other sources are variable. Fitch expects the regional taxes to narrowly cover Virginia's $154.5 million dedicated capital funding obligation (of which $30 million is restricted and unavailable for debt service).

The authority reports that it has received all dedicated capital funding revenues in full and on time. However, in FY21, the commonwealth allocated bond proceeds to remedy an estimated $17.6 million shortfall primarily due to declining TOT post-pandemic. The commonwealth also enacted a budget amendment to appropriate up to $32.4 million to address any deficiencies that might materialize in FY22.

Any deficiency in Virginia's full share of the dedicated capital funding revenue would have entitled, but not required, the district and Maryland to proportionately reduce their contributions. As such, Fitch views the commonwealth's actions as supportive to maintaining credit quality in the current environment without assuming a similar response in the future. Virginia is required to notify the authority if it determines at any time the amount held in its WMATA capital fund will not be sufficient to pay the contribution in full, and it will agree to meet with representatives from the authority, Maryland, and the district to determine an appropriate course of action, but there is no other legal recourse available to the authority to ensure full payment of the dedicated capital funding revenues from the other two states.

Dedicated Capital Revenue Growth Prospects

Fitch's 'a' assessment for revenue growth prospects is based on our view of Virginia's regional tax revenues, and more specifically the volatility inherent in the recordation and TOT revenues, pressure on fuel taxes from fuel efficiency technologies and regulatory standards, and the fixed dollar nature of the regional sales tax that offsets its solid historical growth.

Dedicated Capital Revenue Bond Resilience

Fitch's 'aa' resilience assessment reflects the significant cushion and tolerance for pledged revenue decline based on the expectation for an eventual increase in leverage to the 4x MADS ABT. Current MADS is approximately $101 million, resulting in 4.7x coverage from dedicated capital funding revenues of $470 million ($500 million total less approximately $30 million restricted contribution from Virginia). Dedicated capital funding revenues could decline by 79% before reaching 1.0x MADS, or 75% assuming an increase in MADS to the 4.0x ABT level.

District general sales tax revenues and Maryland TTF revenues exhibited modest revenue volatility with the largest cumulative pre-pandemic declines dating back to FY05 registering just 4.5% and 5.3%, respectively. Fitch's analysis of Virginia's regional taxes is based on a proxy analysis due to insufficient historical data, yielding a high historical stress of nearly 28% driven by large declines in recordation tax revenues from fiscal years 2007-2010 due to the Great Recession. Assuming MADS at the 4.0x ABT, the 75% coverage cushion would approximate 2.7x the 28% revenue decline, which Fitch considers consistent with an 'aa' resilience assessment.

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

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This 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. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT	RATING		PRIOR
Washington Metropolitan Area Transit Authority (DC) [General Government]	LT IDR	AA- Rating Outlook Negative Affirmed	AA- Rating Outlook Negative
Washington Metropolitan Area Transit Authority (DC) /Issuer Default Rating - General Government/1 LT	LT	AA- Rating Outlook Negative Affirmed	AA- Rating Outlook Negative
Washington Metropolitan Area Transit Authority (DC) /Transportation Revenues - Dedicated Revenues/1 LT	LT	AA Rating Outlook Negative Affirmed	AA Rating Outlook Negative
Washington Metropolitan Area Transit Authority (DC) /Transportation Revenues - Non Dedicated Revenues/2 LT	LT	AA- Rating Outlook Negative Affirmed	AA- Rating Outlook Negative
Washington Metropolitan Area Transit Authority (DC) /Transportation Revenues/1 LT	LT	AA Rating Outlook Negative Affirmed	AA Rating Outlook Negative

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Public Sector, Revenue-Supported Entities Rating Criteria (pub. 01 Sep 2021) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.0.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Washington Metropolitan Area Transit Authority	EU Endorsed, UK Endorsed

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