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Whitewater (City of) WI Water Enterprise

Update to credit analysis

Summary

The Whitewater (City of) Water Enterprise (A1) benefits from increased rates that support strong net revenue and a solid cash position. The debt burden is moderate relative to the system's small operating size and annual debt service coverage is strong. The enterprise's largest ratepayers are a gas power plant and the University of Wisconsin-Whitewater, which have provided stable water sales in recent years. Coronavirus related shutdowns could negatively affect water sales at the university over the coming months. Legal protections on the system's water revenue debt are adequate, and its revenue debt is additionally secured by the city's pledge to cure debt service deficiencies (subject to annual appropriation).

We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. We do not see any material immediate credit risks for Whitewater's Water Enterprise. However, the situation surrounding coronavirus is rapidly evolving and the longer term impact will depend on both the severity and duration of the crisis. If our view of the credit quality of the water enterprise changes, we will update our opinion at that time.

Credit strengths

» Strong liquidity and days cash on hand

» Demonstrated willingness and ability to raise regulated rates

Credit challenges

» Small system with limited service area growth

» Below average demographic profile

Rating outlook

Outlooks are typically not assigned to local governments with this amount of debt.

Factors that could lead to an upgrade

» Significant expansion to the customer base

» Material debt burden decline

Factors that could lead to a downgrade

» Deterioration in liquidity

» Sustained decline in debt service coverage

Key indicators

Exhibit 1

Whitewater (City of) Water Enterprise, WI					
System Characteristics					
Asset Condition (Net Fixed Assets / Annual Depreciation)	29 years				
System Size - O&M ($000)	$1,073				
Service Area Wealth: MFI % of US median	71.60%				
Legal Provisions					
Rate Covenant (x)	1.20x				
Debt Service Reserve Requirement	DSRF funded at the lesser of the standard 3-prong test (Aa)				
Management					
Rate Management	A				
Regulatory Compliance and Capital Planning	Aa				
Financial Strength					
	2014	2015	2016	2017	2018
Operating Revenue ($000)	$1,709	$1,712	$1,803	$1,739	$1,850
System Size - O&M ($000)	$901	$917	$937	$964	$1,073
Net Revenues ($000)	$810	$798	$869	$833	$809
Net Funded Debt ($000)	$1,978	$1,596	$2,026	$1,776	$2,726
Annual Debt Service ($000)	$474	$511	$257	$195	$235
Annual Debt Service Coverage (x)	1.7x	1.6x	3.4x	4.3x	3.4x
Cash on Hand	403 days	355 days	378 days	469 days	447 days
Debt to Operating Revenues (x)	1.2x	0.9x	1.1x	1.0x	1.5x

Source: Audited financial statements, US Census Bureau, Moody's Investors Service

Profile

The Whitewater Water Enterprise is owned by the City of Whitewater (A1) and provides municipal water service within the city limits. The water system has 3,839 water meters, 5 wells and 7 employees. The system pumps into distribution about 1.6 million gallons per day (mgd). The system provides services to city's residential population of 14,750, various commercial and industrial entities and the University of Whitewater with its 11,586 students.

Detailed credit considerations

Service area and system characteristics: small system size; below average socioeconomic profile

We do not expect material declines in water system revenue, however revenues from commercial customers and the University of Wisconsin at Whitewater are likely to decline in the short-term. The water enterprise's service area benefits from the institutional presence of the university and location 45 miles southeast of Madison (Aaa stable) and 55 miles southwest of Milwaukee (A1 negative). The water system provides service to the city's stable population of 14,750 through 3,758 metered customers. As is common among cities with a large university presence, rate payer income metrics are below average with the city's median family income at 72% of national medians. The system size is below the US median, as measured by operating and maintenance expenses at $964,000.

A study of the water system demonstrated sufficient ability to meet demand in 2017 with estimated well capacity at about 6.7 million gallons per day (mgd), average daily pumpage at 2mgd and maximum domestic pumpage at 3.9mgd. The system's customer base is primarily residential at 34% of revenue, as estimated from the city's 2019 actual estimated budget. Revenue is concentrated among the top two rate payers, LS Power and the university. LS Power is a natural gas fire power plant that uses water for steam generation and makes up 23% of the water system's revenue. The university makes up about 10% of revenue. Water system revenue will likely be negatively affected from university closures though the system benefits from ample liquidity and strong days cash on hand.

Debt service coverage and liquidity: sufficient coverage and strong liquidity

We expect the system's financial position to remain sound given strong net revenue, ample liquidity and likely rate increases. A large rate increase is expected in 2020 due to a complex rate study nearing completion with the Public Service Commission (PSC) of Wisconsin. As of April 2020, the PSC has submitted a letter to the city proposing a rate increase of over 20%. Fiscal 2018 operating revenue increased to $1.9 million in fiscal 2018 due to a moderate 3% rate increase.

We expect the system's strong annual debt service coverage to remain stable to remain mostly stable due to future planned rate increases, however coronavirus related shutdowns could result in moderate declines in water sales. Total annual debt service coverage was a strong 3.4x in fiscal 2018. Senior lien annual debt service coverage was a stronger 4.2x.

LIQUIDITY

We expect water system liquidity to remain strong due to upcoming rate increases. The system ended fiscal 2018 with a cash balance of $1.3 million, equal to a very strong 447 days cash on hand. Unrestricted liquidity is expected to increase in fiscal 2019 to $2.4 million, or a 127% of total operating revenues.

Debt and legal covenants: moderate debt burden, adequate legal provisions

The water enterprise's debt burden is likely to remain moderate based on moderate additional borrowing plans. Recent increases in net funded debt are largely from capital projects funded by GO debt issued by the city and supported by the city's enterprises including the water system. In 2020, the City of Whitewater expects to issue $5 million in long-term debt to refinance $2.3 million outstanding short-term notes and finance capital improvement projects across the city and its three business enterprises. Debt to operating revenue remained very strong at 1.5x. We expect the water systems gross debt burden to increase slightly due to manageable borrowing plans.

Legal provisions are satisfactory and include a rate covenant and additional bonds test of 1.2 times maximum annual debt service (MADS) for all outstanding revenue bonds. Additional security includes the city's pledge to cure deficiencies for reasonable costs and services should the enterprise's revenue falls below the pledge 1.2 times annual debt service requirement, though this pledge is subject to appropriation and levy limits.

DEBT STRUCTURE

All of the system's revenue debt is fixed rate and amortizes over the long-term. Debt service on the revenue bonds is secured by a senior lien on the water enterprise's net revenues. Amortization of revenue debt is fairly rapid with 73% of principal scheduled to retire within 10 years.

DEBT-RELATED DERIVATIVES

The system has no exposure to any debt-related derivatives.

PENSIONS AND OPEB

Employees of the water enterprise, like most city employees, participate in one multiple-employer cost-sharing plan, the Wisconsin Retirement System (WRS). In fiscal 2018, the enterprise contributed $29,000 to the plan, equal to a low 1.6% of city operating revenue. For more information on the City of Whitewater's pension obligations, please see our most recent credit opinion on the city.

ESG considerations

Environmental

Environmental considerations are not a primary credit driver. According to data of Moody's affiliate Four Twenty Seven, the City of Whitewater and its water enterprise are located in an area with high risk rainfall exposure and low risk to water stress exposure. The water enterprise are subject to extensive regulation pursuant to the federal Clean Water Act, the Clean Air Act, various administrative rules and State of Wisconsin regulations. The authority is in material compliance with all existing permits relating to the operation of the water and sewer systems.

Social

The water system provides an essential public service that is critical to community health and well-being. The system's largest rate payer includes a gas power plant and the University of Wisconsin-Whitewater. Water system revenue will likely be negatively affected in 2020 from university closures with the severity of these effects depending on the length of closure. However, the system benefits from strong days cash on hand and we expect revenue to recover following disruptions.

Governance

The water systems rate-setting is regulated by the Public Service Commission (PSC) of Wisconsin. However, the city has successfully passed rate increases in 2014 and 2018 to ensure revenue is sufficient to support debt service and cash reserves. In 2020, a large rate increase is expected. Management maintains a long-term capital improvement plan and currently has no outstanding consent decrees or other environmental regulatory violations.

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