

## RATING ACTION COMMENTARY

# Fitch Rates Massachusetts Clean Water Trust's \$405MM SRF Bonds 'AAA'; Outlook Stable

Fri 18 Nov, 2022 - 9:08 AM ET

Fitch Ratings - Austin - 18 Nov 2022: Fitch Ratings has assigned a 'AAA' rating to the following bonds issued by the Massachusetts Clean Water Trust (MCWT) under its 2015 Master Trust Agreement (MTA):

--Approximately \$143 million state revolving fund (SRF) bonds, series 24A (Green Bonds);

--Approximately \$150 million SRF bonds, series 24B (Sustainability Bonds);

--Approximately \$112 million SRF refunding bonds, series 2022.

The series 24A and 24B bond proceeds will be used to finance or refinance certain wastewater and drinking water projects within the state and pay issuance costs. The refunding bond proceeds will be used to refund certain series of previously issued bonds and to pay costs of issuance. The bonds are expected to sell via negotiation the week of November 28.

In addition, Fitch has affirmed the 'AAA' rating on the following obligations:

--Approximately \$1.3 billion in outstanding parity MTA bonds;

--Approximately \$834.0 million in outstanding prior pool-program bonds;

--Approximately \$7.4 million in outstanding prior single-obligor bonds.

The Rating Outlook is Stable.

## RATING ACTIONS

ENTITY / DEBT ⚡	RATING ⚡			PRIOR ⚡
Massachusetts Clean Water Trust (MA) [State Revolving Fund]				
Massachusetts Clean Water Trust (MA) /Massachusetts Water Resources Authority Program - Subordinated Obligations/1 LT	LT	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
Massachusetts Clean Water Trust (MA) /Massachusetts Water Resources Authority Program Revenues/1 LT	LT	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable
Massachusetts Clean Water Trust (MA) /Revolving Fund Revenues/1 LT	LT	AAA Rating Outlook Stable	Affirmed	AAA Rating Outlook Stable

[VIEW ADDITIONAL RATING DETAILS](#)

**SECURITY**

Bonds are secured by pledged loan repayments, Commonwealth of Massachusetts (the commonwealth) contract assistance payments (CAPs), rights and interest of the MTA, and certain other funds including the equity fund.

**KEY RATING DRIVERS**

Sound Financial Structure: Fitch's cash flow modeling demonstrates that the combined SRF programs can continue to pay bond debt service even with loan defaults in excess of Fitch's 'AAA' liability rating stress hurdle, as produced using Fitch's Portfolio Stress Model (PSM).

Highly Rated Borrower Pool: Approximately 97% of the aggregate programs consist of borrowers exhibiting investment-grade ratings. Loan security is also strong as underlying borrowers are secured by general obligation pledges of city and towns, local utility revenue pledges, or a combination of both.

Moderate Concentration: Single-borrower and top-10 concentration are moderate, with each at around 20% and 48% respectively. Together these metrics are generally consistent with sector peers.

Strong Program Management: MCWT manages one of the largest SRF programs in the nation. To date, there have been no pledged loan defaults in MCWT's pool programs.

## **RATING SENSITIVITIES**

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

--The ratings are at the highest level on Fitch's scale and cannot be upgraded.

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

--Inability to pass Fitch's 'AAA' liability rating stress hurdle due to any of the following;

--Increased leveraging;

--Significant deterioration in aggregate borrower credit quality.

## **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**

MCWT's SRF programs provide subsidized financing and grants to local government entities within the commonwealth for eligible clean water and drinking water projects. As typical for SRFs, bond proceeds are combined with federal grants, a required state match, and other recycled funds on hand to fund loans to borrowers.

The series 24A and B bonds and series 2022 refunding bonds will be the ninth and tenth series of bonds issued under the 2015 MTA. MCWT also administers the clean water and drinking water SRF programs under the 1993 program resolution including the prior pool program and the prior single-obligor bonds to Massachusetts Water Resource Authority (MWRA; together, the prior programs). These programs are closed for new-money issuances.

Program metrics are stable over time. At this review, minimum annual loan-to-bond debt service coverage (DSC) inclusive of the combined programs is approximately 1.2x, falling within the historical range of 1.1x-1.3x registered since 2018. The PSM's liability stress hurdle, a measure of pool quality, shows a 'AAA' hurdle of 15%, an increase from 11.3% yoy, but remaining very favorable in comparison to Fitch's 'AAA' median of 31%. Lastly, single-borrower concentration has improved from about 25% historically to less than 20% at this review.

Sound Financial Structure

Due to the enhancement described below, Fitch's cash flow modeling demonstrates that the programs can continue to pay bond debt service even with hypothetical loan defaults of 100% in any four-year period of the outstanding bonds' expected life (per Fitch criteria, a 90% recovery is also applied in its cash flow model when determining default tolerance). This result is well in excess of Fitch's 'AAA' liability stress hurdle of 15.0% as produced by the PSM. The liability rating stress hurdle is calculated based on overall pool credit quality as measured by the ratings and concentration of underlying borrowers and loan size and term.

In addition to its modelling analysis, Fitch measures the financial strength of pools by calculating the program asset strength ratio (PASR). The PASR, an asset-to-liability ratio, includes total scheduled pledged loan repayments from both programs, CAP payments, pledged accounts and account earnings divided by total scheduled bond debt service. MCWT's pool program PASR is 1.7x, compared to Fitch's 2022 'AAA' median level of 1.9x but still considered sound. Minimum annual DSC is also below median levels at 1.2x, although lower minimum annual coverage is typical, and less of a concern for SRF structures enhanced with large reserve-fund balances.

#### Pledged Accounts Provide Substantial Loss Protection

The series 24 and other SRF bondholders are primarily protected from losses by surplus loans made in excess of bond debt service. Bondholders of the prior pool program bonds are also protected from losses by pledged reserves of approximately \$284 million, equal to about 34% of all prior pool program bonds. As the prior program bonds amortize, related loan repayment surpluses and reserves are released to the deficiency fund before being released to program equity. The equity fund balance currently approximates about \$1.0 billion, or about 37% of outstanding bonds.

The 2015 MTA program pledges amounts available in the equity fund to all bondholders on a parity basis. In light of this feature, Fitch combines all of MCWT's SRF programs in its cash flow model analysis.

#### High-Quality Loan Pool with Moderate Concentration

Fitch estimates that at least 97% of the aggregate SRF program participants exhibit investment-grade credit quality, with the large majority rated 'A+' or higher. This drives the 'AAA' liability stress of 15%, which compares favorably to Fitch's 'AAA' median of 31% (lower liability stresses correlate to stronger credit quality). Loan security is also solid as the programs are secured by general obligation pledges of cities and towns, local utility revenue pledges or a combination of the two.

The combined programs consist of 258 borrowers, the top 10 of which comprise about 48% of total outstanding loan obligations. After MWRA's 20% (senior and subordinate lien revenue bonds rated AA+/Stable and AA/Stable, respectively), the remainder of the top 10 borrowers range in size from 2% to 5.3%.

#### Strong Program Management

MCWT is an interagency management team composed of officials from the commonwealth treasurer's office, the executive office of administration and finance. The commonwealth's Department of

Environmental Protection (DEP) administers Massachusetts' SRFs in an arrangement typical of such programs nationwide. DEP staff members review and monitor projects for several water and wastewater programs, including the pool program. MCWT exhibits strong program management, having never experienced a pledged or leveraged loan default across any of its SRF programs.

## **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.

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## **APPLICABLE CRITERIA**

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

[State Revolving Fund and Municipal Finance Pool Program Rating Criteria \(pub. 27 Sep 2021\) \(including rating assumption sensitivity\)](#)

## **APPLICABLE MODELS**

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

Portfolio Stress Model, v1.11.1 ([1](#))

State Revolving Fund Cash Flow Model, v1.18.2 ([1](#))

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Massachusetts Clean Water Trust (MA)

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