



RATING ACTION COMMENTARY

Fitch Rates Massachusetts Clean Water Trust's \$355MM SRF Bonds 'AAA'; Outlook Stable

Mon 12 Apr, 2021 - 8:07 PM ET

Fitch Ratings - Austin - 12 Apr 2021: Fitch Ratings has assigned an 'AAA' rating to the following bonds issued by the Massachusetts Clean Water Trust (MCWT):

--Approximately \$143.2 million state revolving fund (SRF) bonds, series 23A (Green Bonds);

--Approximately \$212.3 million SRF bonds, series 23B (Sustainability Bonds).

The bonds are expected to sell via negotiation the week of April 25. Bond proceeds will be used to finance or refinance costs related to certain wastewater and drinking water projects within the state and pay issuance costs.

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

--\$2.1 billion in outstanding parity SRF and Pooled Loan Program bonds.

The Rating Outlook is Stable.

Feedback

SECURITY

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

KEY RATING DRIVERS

Sound Financial Structure: Fitch's cash flow modeling demonstrates that the MCWT's combined SRF and pooled loan programs (together, the pool program) 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 99% of the pool program consists of borrowers exhibiting investment-grade ratings. Loan security is also strong as borrowers are secured by general obligation pledges of city and towns, local utility revenue pledges, or a combination of both.

High Single-Borrower Concentration: Single borrower concentration is high, with the Massachusetts Water Resources Authority (MWRA) representing 24% of total outstanding loan principal.

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 program.

RATING SENSITIVITIES

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

--Not applicable given the 'AAA' rating.

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

--Significant deterioration in aggregate borrower credit quality, increased pool concentration or increased leveraging resulting in MCWT pool programs' inability to pass

Fitch's 'AAA' liability rating stress hurdle.

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 provides subsidized financial assistance to local governments and other eligible borrowers in the commonwealth under its SRF programs. The series 23 bonds will be the eighth issuance of bonds issued under the 2015 master trust agreement (2015 MTA). MCWT also administers clean water and drinking water SRF programs under the 1993 program resolution (the pooled loan program) which is now closed.

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

In spite of the challenges created by the coronavirus, MCWT has preserved its financial and operational strength. While loan accommodations have been extended to borrowers, if necessary, to address the effects of the coronavirus, MCWT has not entered into any accommodations thus far. Given the financial strength of the SRF sector, Fitch is not expecting any meaningful impairment, if any, for either the sector or MCWT at this time.

SOUND FINANCIAL STRUCTURE

Fitch measures the financial strength of the pool by calculating the program's asset strength ratio (PASR). The PASR includes total scheduled pledged loan repayments, CAP payments, excess releases from the standalone SRF programs, plus any reserve balances and account earnings divided by total scheduled bond debt service.

MCWT's pool program PASR is 1.6x, which is below Fitch's 2020 'AAA' median level of 2.1x but still considered sound. Minimum annual debt service coverage--excluding reserve deallocations--is also below median levels at 1.3x, although lower minimum annual coverage is typical for SRF structures enhanced with large reserve fund balances.

Cash flow modeling demonstrates that the pool program 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 in excess of Fitch's 'AAA' liability stress hurdle of 11.3% as produced by the PSM. The liability rating stress hurdle is calculated based on overall pool credit quality as measured by the rating of underlying borrowers, loan size and term, and concentration.

CAPS AND DEALLOCATIONS SUPPORT BOND DEBT SERVICE

CAPs provide support for approximately 8% and 5% of debt service in the 1993 program and single-obligor SRF programs, and the 2015 MTA program, respectively, on behalf of certain borrowers. CAPs constitute a general obligation of the commonwealth (GOs AA+/Stable), for which the commonwealth's full faith and credit are pledged. Additional enhancement equal to approximately 19% of combined program debt service is provided by scheduled releases from the 1993 and single-obligor SRF programs. Both the CAPs and the releases from the 1993 and standalone programs were stressed in Fitch's cash flow model analysis.

HIGH-QUALITY LOAN POOL WITH SIGNIFICANT SINGLE-BORROWER CONCENTRATION

Fitch estimates that at least 99% of SRF program participants exhibit investment-grade credit quality, with the large majority rated 'A+' or higher. In aggregate, pool credit quality is strong versus similar municipal pools as reflected by the commonwealth pool programs' low 'AAA' liability stress of 11%, which compares favorably to Fitch's rating category median of 32% (lower liability stresses correlate to stronger credit quality). Loan security is also solid as the loan portfolio in the program is secured by general obligation pledges of cities and towns, local utility revenue pledges or a combination of the two.

The pool program consists of 253 borrowers, the top 10 of which comprise about 50% of total outstanding loan obligations. After MWRA's 24% (senior and subordinate lien revenue bonds rated 'AA+' and 'AA', respectively, with a Stable Outlook), the remainder of the top 10 borrowers range from 2% to 4%. Fitch's concern with MCWT's high single-borrower concentration is somewhat mitigated by the high rating of MWRA. Overall, MCWT's pool program composition is consistent over time.

ENHANCEMENT PROVIDED BY OVERCOLLATERALIZATION AND RESERVES

The series 23 and certain prior series of bonds are primarily protected from losses by surplus pledged direct loan repayments funded from program equity made in excess of bond debt service. As bonds enhanced by overcollateralization amortize, excess amounts are eventually released to the MTA's pledged equity fund and are therefore available to other SRF program borrowers.

Although no reserves are being funded with this issue, combined series' reserves from previous pool program issuances equal approximately \$466 million, or 32% of outstanding bonds. This compares very favorably with the 'AAA' rating category median of 3.3%.

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.

RATING ACTIONS

| ENTITY/DEBT | RATING | PRIOR |
|-------------|--------|-------|
|-------------|--------|-------|

| ENTITY/DEBT | RATING | | PRIOR | |
|---|--------|---------------------------|----------|---------------------------------|
| Massachusetts Clean Water Trust (MA) [State Revolving Fund] | | | | |
| ● Massachusetts Clean Water Trust (MA) /Revolving Fund Revenues/1 LT | LT | AAA Rating Outlook Stable | Affirmed | AAA Rating Outlook Stable |

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

[Public Sector, Revenue-Supported Entities Rating Criteria \(pub. 23 Feb 2021\) \(including rating assumption sensitivity\)](#)

[State Revolving Fund and Municipal Finance Pool Program Rating Criteria \(pub. 03 Mar 2021\) \(including rating assumption sensitivity\)](#)

APPLICABLE MODELS

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

Portfolio Stress Model, v1.11.0 ([1](#))

State Revolving Fund Cash Flow Model, v1.18.1 ([1](#))

ADDITIONAL DISCLOSURES

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