

14 Nov 2019 | New Issue

Fitch Rates Oklahoma Water Resources Board's Ser. 2019 SRF Revs 'AAA'; Outlook Stable

Fitch Ratings-Austin-14 November 2019: Fitch Ratings has assigned a 'AAA' rating to the following bonds issued by the Oklahoma Water Resources Board (OWRB):

--Approximately \$223.0 million revolving fund revenue refunding bonds, taxable series 2019 (2019 master trust).

The bonds will be used to refund certain outstanding series of clean water and drinking water state revolving fund bonds (CWSRF and DWSRF) issued under the 2003 master trust agreement (the 2003 master trust), and pay for the costs of issuance. The bonds are expected to price via negotiation the week of Dec. 2.

In addition, Fitch has affirmed the following:

--Approximately \$559.4 million (pre-refunding) outstanding revolving fund revenue bonds (2003 master trust) at 'AAA'.

The Rating Outlook is Stable.

SECURITY

The 2019 master trust bonds are secured by pledged loan repayments (excluding administrative fees), surplus and reserve releases from the 2003 master trust program, amounts in certain funds and accounts, and account earnings.

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KEY RATING DRIVERS

SOUND FINANCIAL STRUCTURE: Fitch's cash flow modeling demonstrates that OWRB's combined pool 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).

AVERAGE POOL DIVERSITY: The top-10 borrowers and the largest single borrower represent 59% and 23% of the pool, respectively. The top-10 concentration is mostly in line with Fitch's 'AAA' median, but the single obligor concentration is slightly higher.

LARGELY UNRATED PORTFOLIO: Approximately 67% of the pool obligors do not carry a public rating. In its PSM analysis, Fitch assumes unrated borrowers to be of below-investment-grade quality (BB). This assumption contributes to overall pool quality falling to below average compared with similar programs rated by Fitch.

STRONG PROGRAM MANAGEMENT: Management has demonstrated strength and capability in its underwriting and monitoring processes, as evidenced by the fact that the program has never experienced a pledged loan default.

RATING SENSITIVITIES

REDUCTION IN MODELED STRESS CUSHION: If the Oklahoma Water Resource Board's revolving fund programs were to experience significant deterioration in aggregate borrower credit quality, increased pool concentration, or increased bond leveraging resulting in an inability to pass Fitch's 'AAA' liability rating stress hurdle, negative rating pressure would be expected.

CREDIT PROFILE

OWRB was established in 1957 as an agency and department of the state of Oklahoma, and serves as the state's financing vehicle for local government water and wastewater capital funding. In addition to managing the state revolving fund (SRF) programs, the OWRB administers an additional state loan program and two grant programs.

The series 2019 bonds are the first issued under the 2019 master trust. In accordance with the recently amended 2003 master trust, excess funds released from the 2003 deficiency fund are transferred to the 2019 master trust's revenue fund on a semi-annual basis and available for debt service payments. Because of this feature and the cross-collateralization of the clean water and drinking water SRFs, Fitch combines the two funds and two master trust programs in its modelling analyses. The 2003 master trust will be closed with the issuance of the 2019 bonds.

FINANCIAL STRUCTURE EXHIBITS SOUND DEFAULT TOLERANCE

Fitch's cash flow modeling demonstrates that the availability of program resources allow for hypothetical loan defaults of 100% in the first, middle and last four years of the program's life (as per Fitch criteria, a 90% recovery is also applied in its cash flow model when determining default tolerance) while still paying bond debt service in full. This is in excess of Fitch's 'AAA' liability rating stress hurdle of 62%, thereby indicating a passing result under Fitch's quantitative analysis. The rating stress hurdle is calculated based on overall pool credit quality as measured by the rating of underlying obligors, obligation size, term and pool concentration.

As an additional measure of financial strength, Fitch calculates the program asset strength ratio (PASR). The PASR, an asset-to-liability ratio, includes total scheduled loan repayments plus any additional pledged funds divided by total scheduled bond debt service. The resulting PASR for OWRB's SRF program is sound at approximately 2.1x, besting Fitch's 2019 'AAA' median level of 1.9x. The PASR is slightly improved from the 1.8x measured at Fitch's review in February of 2018.

LOSS PROTECTION PROVIDED BY RESERVES AND OVERCOLLATERALIZATION

The series 2013B and 2014A bonds use a reserve-fund structure, wherein loss protection for bondholders is provided primarily by dedicated debt service reserve funds. All other outstanding bonds issued since 2010, including the series 2019 bonds, use a cash-flow structure, wherein loss protection is provided primarily by pledged loan repayments made in excess of bond debt service, or overcollateralization.

On an annual basis, aggregate loan repayments overcollateralize bond debt service by a minimum of 1.4x, which is mostly consistent with Fitch's 'AAA' rating category median of 1.5x. Debt service reserve funds from the series 2013B and 2014A bonds currently stand at approximately \$39 million, which equates to 7% of total projected bonds outstanding after this issuance.

The program is also enhanced by a cross-collateralization feature of the separate CWSRF and DWSRF programs, which allows for shortfalls in one program to be covered by surpluses in the other.

LARGELY UNRATED LOAN POOL WITH AVERAGE DIVERSITY

The combined loan pool is composed of 162 pledged obligors. Inclusive of one internal credit opinion assigned by Fitch, approximately 41% of the portfolio is considered to be investment-grade -- this compares unfavorably with Fitch's 'AAA' median of 62%. As a result of the largely unrated loan pool, the program's 'AAA' liability hurdle is an elevated 62% versus an 'AAA'

median of 32%.

At 23.4% of the pool total, the Oklahoma City Water Utilities Trust remains the pool's largest obligor (parity bonds not rated by Fitch but assessed to be of very high quality). The remaining top-10 borrowers range from 2.2% to 7.9% in size relative to the aggregate pool. Based on these characteristics, Fitch views the loan pool as having diversity similar to slightly worse than other 'AAA'-rated pooled programs.

EXPERIENCED PROGRAM MANAGEMENT AND SOUND UNDERWRITING

The OWRB is responsible for administering state laws related to water rights, promulgating state water standards and developing and updating the state comprehensive water plan.

The board's formal SRF underwriting procedures consist of approval of clean water or drinking water project feasibility, review of loan credit, and application and approval by OWRB. Borrower loan agreements typically must demonstrate 1.25x annual debt service coverage on outstanding loans, including any planned additional debt. Loans to smaller systems are secured further by a mortgage on the local borrower's system facilities.

In the event of a loan default, OWRB has the right to directly impose, enforce and collect charges on users of the defaulting system. OWRB has never experienced a default by any borrower within its pledged loan programs. It is the sole administrator of the CWSRF, while administration of the DWSRF is shared between OWRB and the state's Department of Environmental Quality.

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Applicable Criteria

[Public Sector, Revenue-Supported Entities Rating Criteria \(pub. 07 Nov 2019\)](#)

[U.S. Public Finance State Revolving Fund and Municipal Finance Pool Program Rating Criteria \(pub. 18 Sep 2019\)](#)

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