

FITCH RATES MASSACHUSETTS WATER RESOURCES AUTHORITY'S \$337MM REVS 'AA+'; OUTLOOK STABLE

Fitch Ratings-New York-28 October 2011: Fitch Ratings assigns an 'AA+' rating to the following Massachusetts Water Resources Authority's (MWRA or the authority) bonds:

--\$336.8 million general revenue bonds, 2011 series C, rated 'AA+'.

The general revenue bonds, 2011 series C are scheduled for negotiated sale the week of Nov. 7, 2011. Bond proceeds will refund outstanding parity bonds for cost savings.

In addition, Fitch affirms the following ratings:

--\$3.4 billion general revenue bonds at 'AA+';

--\$1.1 billion subordinate general resolution revenue bonds at 'AA'.

The Rating Outlook is Stable.

SECURITY:

MWRA's debt is secured by senior and subordinated liens on net authority revenues derived largely from wholesale rates and charges assessed on local units of government.

KEY RATING DRIVERS:

--MWRA provides an essential service to a large and diverse service area with strong economic underpinnings.

--The wholesale system benefits from an ample long-term water supply and sufficient excess water and sewer treatment capacity.

--Local governments served by the authority are required to pay for MWRA services as a general obligation, and non-payment is subject to a tested state aid intercept.

--MWRA maintains independent rate-setting authority, prudent budgetary practices, comprehensive long-term planning, and vigilant project oversight and prioritization of its capital program.

--Financial flexibility has diminished over time due to significant leveraging and notably high user charges.

--The authority's capital program continues to transition from costly court-mandated projects to ongoing rehabilitation.

--MWRA has achieved strong collection rates of 100% since its inception.

CREDIT PROFILE:

MWRA provides wholesale water and wastewater services to 61 communities located primarily in eastern Massachusetts. Almost 2.8 million people (or 43% of the population of the commonwealth) reside in the authority's service areas, the largest of which is the city of Boston, which contributes one-third of MWRA's revenue derived from rates and charges (Fitch rates the Boston Water and Sewer Commission's general revenue bonds 'AA+' with a Stable Outlook). The service areas are generally economically diverse, and wealth levels are above state and national averages.

The 61 local communities included in the service area are required to pay for MWRA services as a general obligation and rate-setting is not subject to any limitations, including the state's Proposition 21/2. These protections, coupled with the authority's ability, pursuant to its enabling act, to utilize a local aid intercept to recover amounts unpaid by one of its member communities provide significant operating flexibility and credit strength.

MWRA's rates are among the highest in the urban U.S. and an ongoing credit concern, somewhat mitigated by the above average area income levels. However, the size of needed rate hikes has trended downward as annual capital spending has declined over time. Over the last five years the authority boosted rates on average by a moderate 3.6% annually. For fiscal 2011, the board adopted

a nominal 1.5% rate hike in order to give rate payers some degree of rate relief amid the economic downturn. Going forward, rates are forecast to rise by an annual average of 6% through fiscal 2016 to keep pace with rising debt service. The adopted budget for fiscal 2012 included a 3.5% increase.

The authority's financial operations have remained relatively stable despite escalating debt service and the eventual elimination of Commonwealth debt service assistance. Fiscal 2011 ended with a sizeable operating surplus that was prudently applied to the defeasance of approximately \$22.6 million of senior lien obligations and redemption of about \$7 million in subordinate bonds. Historical coverage on senior lien annual debt service (ADS) has been strong, averaging 1.9 times (x) over the prior five fiscal years, and all-in coverage has been adequate at just above the 1.1x threshold established by bond resolution. Audited results for fiscal 2011 show coverage of 1.7x and 1.1x on senior lien and all-in ADS, respectively. Liquidity is good, with unrestricted cash remaining at just above 300 days cash.

Following the massive capital investments undertaken during the 1990s, MWRA's capital program is now increasingly focused on completion of combined sewer overflow (CSOs) projects, regulatory compliance, and system rehabilitation and maintenance. The fiscal years 2012-2016 capital improvement plan (CIP), which totals approximately \$1.2 billion and addresses substantially all current regulatory compliance issues, is significantly reduced from prior CIPs, reflecting the significant scale of capital spending on the cleanup of Boston Harbor in the 1990s and the completion of the majority of the CSO master plan. Fitch believes future capital costs should remain manageable given MWRA's vigilant project oversight and its board's self-imposed spending cap. Funding for capital needs will continue to come almost entirely from long-term borrowings, including revenue bonds and state loans.

Because of the size of historical capital investments, the authority's debt levels have been and will remain high for the foreseeable future. Debt to net plant is notably high at 93%, and debt per capita equals almost \$1,900. However, the authority's capital cycle has declined substantially over the last several years with annual spending equal to about half the amount expended each year in the 1990s. Fitch expects this trend to continue.

Exposure to variable rate debt and derivatives is fairly sizeable, although management's demonstrated ability to prudently monitor debt portfolio performance offsets this risk. Of the total amount of debt outstanding, approximately 21% is variable rate with each series of variable rate bonds backed by liquidity agreements from a diverse pool of liquidity providers. Almost two-thirds of outstanding variable rate debt is hedged through floating-to-fixed rate swaps. The outstanding notional amount totals \$714.3 million, and the most recent (October 2011) mark-to-market value of the swaps totaled negative \$163.5 million. Regular swap payments are on parity with subordinate lien bonds.

Contact:

Primary Analyst
Christopher Hessenthaler
Director
+1-212-908-0773
Fitch, Inc.
One State Street Plaza
New York, NY 10004

Secondary Analyst
Doug Scott
Managing Director
+1-512-215-3725

Committee Chairperson
Karen Ribble
Senior Director

Media Relations: Sandro Scenga, New York, Tel: +1 212-908-0278, Email: sandro.scenga@fitchratings.com.

Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

In addition to the sources of information identified in Fitch's Revenue-Supported Rating Criteria, this action was additionally informed by Creditscope.

Applicable Criteria and Related Research:

- 'Revenue-Supported Rating Criteria'(June 20, 2011);
- 'Water and Sewer Revenue Bond Rating Guidelines' (Aug. 10, 2011);
- '2011 Water and Sewer Medians' (Jan. 18, 2011);
- '2011 Outlook; Water and Wastewater Sector' (Jan. 18, 2011).

Applicable Criteria and Related Research:

Revenue-Supported Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=637130

U.S. Water and Sewer Revenue Bond Rating Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=647331

2010 Water and Sewer Medians

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=509146

2011 Outlook: Water and Wastewater Sector

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=593286

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTP://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](http://fitchratings.com/understandingcreditratings). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE 'WWW.FITCHRATINGS.COM'. PUBLISHED RATINGS, CRITERIA AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE 'CODE OF CONDUCT' SECTION OF THIS SITE.