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Camrosa Water District Financing Authority, California Camrosa Water District; Water/Sewer

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Camrosa Water District Financing Authority, California

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Credit Profile		
US\$14.0 mil wtr and wastewtr rfdg rev bnds (Camrosa Water District) ser 2016A dtd 10/12/2016 due 01/15/2046		
<i>Long Term Rating</i>	AA/Stable	New
Camrosa Wtr Dist Fincg Auth, California		
Camrosa Wtr Dist, California		
Camrosa Wtr Dist Fincg Auth (Camrosa Wtr Dist) wtr rev bnds		
<i>Long Term Rating</i>	AA/Stable	Upgraded

Rationale

S&P Global Ratings raised its long-term rating to 'AA' from 'AA-' on the Camrosa Water District Financing Authority, Calif.'s water and wastewater refunding revenue bonds outstanding, issued on behalf of Camrosa Water District. At the same time, S&P Global Ratings assigned its 'AA' long-term rating to the district's series 2016A revenue bonds. The outlook is stable.

The rating action reflects the district's very strong enterprise risk profile and very strong financial risk profile, based on the application of our revised criteria, "Rating Methodology And Assumptions For U.S. Municipal Waterworks And Sanitary Sewer Utility Revenue Bonds," published Jan. 19, 2016 on RatingsDirect.

The bond proceeds will refund water and wastewater bonds outstanding for debt service savings, and also generate \$6 million of new money proceeds to support upcoming capital needs of the water system. The bonds are secured by installment sale payments made by the district to the authority under separate water and wastewater installment payment agreements, which in combination provide sufficient revenue to pay debt service on the bonds. Key bond provisions include a rate covenant set at 1.15x annual debt service and an additional bonds test set at 1.15x maximum annual debt service (MADS). The bonds additionally have a reserve fund, funded at the least of 10% of par, 125% of average annual debt service, or MADS. As neither the water or wastewater system is obligated to cover the other's obligations under the installment sale agreements, the credit quality of the bonds would suffer if the credit quality of either system were to deteriorate.

Although the district's risk profile maps to an indicative rating of 'aa-/aa' in our revenue debt criteria matrix, we have selected the 'aa' anchor based on the individual credit quality of the water and sewer systems both of which have consistent financial performance, relatively low leverage (even with the addition of the series 2016A bonds), and strong economic indicators.

The enterprise risk profile reflects our view of the district's:

- Service area participation in the broad and diverse Ventura-Oxnard-Thousand Oaks metropolitan area economy,
- Very low industry risk as a monopolistic service provider of an essential public utility,
- Affordable service rates in the context of the service area's very strong income levels and a track record of annual rate adjustments, and
- Comprehensive operational management practices and policies.

The financial risk profile reflects our view of the district's:

- Very strong historical all-in coverage (averaging over 1.3x for the water enterprise and over 2.0x for the sewer enterprise, as calculated by S&P Global Ratings) that we believe is sustainable based on management's six-year financial forecast;
- Sound liquidity position with total unrestricted cash on hand of \$11 million at the end of fiscal 2016 (unaudited);
- Manageable five-year capital plan that does not require additional debt issuance through fiscal 2022 following the issuance of the series 2016 bonds; and
- Robust financial management practices and policies.

Outlook

The stable outlook reflects our expectation that the district will continue to manage both water and sewer enterprises expenses, pass through rising imported water costs, and produce very strong DSC and liquidity as it progresses through its capital improvement plan. The district will begin a comprehensive water rate study in July 2017 and implement new rates in July 2018. In addition, we understand the district will begin an in-house wastewater rate review in October 2016, to lead to a Proposition 218 hearing in January 2017.

Upside scenario

Although we are unlikely to do so, we could raise the rating if liquidity grows to a level we consider extremely strong and financial performance of both enterprises becomes commensurate with a higher rating.

Downside scenario

We do not anticipate taking a negative rating action during the outlook period, but could do so if coverage deteriorates or cash reserves are spent down to levels inconsistent with the district's track record.

Enterprise Risk

The district is located between Los Angeles and Santa Barbara along Highway 101 in Ventura County. The district serves unincorporated Santa Rosa Valley and the eastern portion of the City of Camarillo (population: 68,100). The district provides water service to over 30,000 people through approximately 10,932 connections, while providing wastewater service to 8,811 connections in Camarillo and a small portion of the neighboring City of Thousand Oaks.

District residents have easy access to jobs countywide and in Los Angeles. The region also has a very large military population at the nearby Point Mugu Naval Air Station and Port Hueneme, which adds stability. The district participates in the broad and diverse Oxnard-Thousand Oaks-Ventura metropolitan statistical area (MSA) economy. Camarillo's household income levels are strong, in our view, with median household effective buying income (EBI) at 142% of the U.S. average and 125% of the state average. According to June 2016 data, Ventura County's

unemployment rate was 5.4%.

The district's customer base is primarily residential and very diverse. Residential customers make up approximately 91% of the district's customer base and consume approximately 41% of the water provided annually. The top 10 water customers account for 17% of water service revenue. The largest customer at 4.5% of water revenue, Leisure Village, is a stable retirement community of approximately 2,100 single-family, occupant-owned dwellings. The second-largest customer is the California State University, Channel Islands (CSUCI; 2.5%), which opened in 2002. The current enrollment of CSUCI is 7,367 students and management expects an additional 15,000 students by 2025. With the exception of growth at CSUCI, the service territory is built out and minimal customer growth is anticipated for both the water and sewer enterprises. On the sewer side, customer concentration is greater, largely because Leisure Village is billed under one meter. Leisure Village accounts for approximately 24.6% of sewer revenue, followed by CSUCI at 8.9%. In aggregate, the 10 largest wastewater customers account for 43% of sewer revenue.

We view the district's service rates as affordable in the context of the service area's very strong income levels. In 2012, the district undertook a water and wastewater rate study to evaluate the existing water and sewer rates and to make projections for a five-year period. As a result of the study, on April 24, 2013 the board adopted a five-year rate schedule that included increases in the commodity and meter service charges for the water enterprise through fiscal 2018 and charges for the wastewater enterprise through fiscal 2017, to reflect increasing operational costs. The district's water rates also reflect price adjustments to pass through import water purchases. Water customers pay a flat monthly fee, plus a tiered usage-based charge. Currently, a residential customer pays about \$67.59 per month for 1,800 cubic feet of water. Wastewater customers are charged a flat fee based on the number of equivalent dwelling units (EDUs). The current monthly rate per EDU is \$31.32. We consider these service rates affordable, at about 1.1% and 0.5%, respectively, of Camarillo's median household EBI.

Based on our operational management assessment, we score the district a '2' on a six-point scale on which '1' is the strongest. The district provides three classes of water to its customers: potable, nonpotable, and recycled. Potable water is a blend of imported water purchased from Calleguas Water District, the local member agency of the Metropolitan Water District of Southern California (MWD), and accounts for approximately 55% of potable supplies; the remaining 45% is groundwater that the district treats at the wellhead. The district's main aquifer (Santa Rosa Basin) is not in overdraft and management reports that the district has enough supply in the basin without a need for recharge. The nonpotable water the district serves is a combination of surface water diverted from the Conejo Creek and local groundwater, while recycled water is a tertiary treated product from the Camrosa Water Reclamation Facility (CWRP) The district's total water sales volume decreased during the past two fiscal years to 12,867 acre-feet in fiscal 2016, from 14,843 acre-feet in fiscal 2015 and 16,978 acre-feet in fiscal 2014, primarily as a result of voluntary or mandatory water conservation measures during a significant drought period. The CWRP is capable of treating an average daily wastewater flow of 1.5 million gallons per day (mgd) and a peak flow of approximately 2 mgd. Management reports that the facility has adequate treatment capacity to serve its current connections, but the district is in the process of re-rating the CWRP to treat a maximum of 2.25 mgd.

The district's operational contingency plans include an adopted drought management plan that is incorporated into its urban water management plan. As of June 2016, approximately 7,025 of the district's 7,912 active potable water

meters have been automated with radio-read meters to facilitate meter reading and improve customer service. Management regularly communicates its strategic goals internally and to outside parties, such as by engaging in public outreach regarding water conservation to comply with recent state mandates. We understand that the district uses both supervisory control and data acquisition (SCADA) and graphical information systems for tracking the maintenance and condition of the system's assets.

Consistent with our criteria "Methodology: Industry Risk," published Nov. 19, 2013, we consider industry risk for utilities covered under these criteria a '1' on a six-point scale, with '1' being the best.

Financial Risk

Our assessment of the system's financial risk profile as very strong reflects the district's very strong all-in coverage, very strong liquidity position, low leverage, manageable capital needs, and robust financial management framework. The district's financial disclosure is a credit weakness, in our view, because water and sewer fund information as reported in the audit are combined, although revenue from each enterprise is not pledged to bondholders of the other enterprise, under the installment sale agreements for the bonds.

In our view, the district's financial performance has been historically very strong, and based on management's forecast we anticipate that this range of performance will be sustainable over the medium term. Based on the district's audited financial statements, for the water enterprise we calculate all-in debt service coverage (DSC) of 1.4x for fiscal years 2015 and 2014, and 1.3x for fiscal 2013. Based on a one-time receipt of \$1.5 million in connection fees in fiscal 2016, all-in DSC is expected to improve to 1.8x in fiscal 2016 (unaudited) and remain in the 1.4x-1.6x range through fiscal 2021. Our calculation of all-in coverage takes into consideration the district's direct debt service as well as imputed debt service from the Calleguas Water District, the local member agency of the MWD. DSC for the sewer enterprise has historically exceed 2.1x, but following an improvement to 3.3x in fiscal 2016 (unaudited) is expected to tighten to about 1.6x through fiscal 2020. Thereafter, as a significant portion of the district's sewer system debt outstanding matures in 2020, coverage is expected to rise to surpass 6x. The debt-to-capitalization ratio is low, in our view, at 20.1% on a combined basis for the two enterprises.

Liquidity is, in our view, strong. As of June 30, 2016, unrestricted cash and investments totaled \$11.0 million, with about \$5.4 million (or 159 days' operating expenses) available to the water enterprise and \$4.8 million (or 999 days' operating expenses) available to the sewer enterprise. Management reports that the district has modest capital needs on the sewer side, and we expect unrestricted sewer enterprise cash to rise to about \$6.9 million through 2021 because the water system is expecting to cash fund about \$3.8 million of capital expenditures in fiscal 2017, unrestricted water cash balances to decline to about \$3.4 million in fiscal 2017, then rebound to \$7.9 million by fiscal 2021. Based on our financial management assessment, we rate the district a '2' on a six-point scale on which '1' is the strongest. We believe that the district's practices are strong, comprehensive, and supportive of high credit quality. Revenue and expenses assumptions are reasonable, and interim financial reporting is regularly provided to the district's board throughout the year. The long-term planning process is rigorous, and the detailed multiyear forecast is annually updated. The district has an adopted reserve policy that we believe supports sound liquidity and articulates the rationale for maintaining its various reserves. Financial planning and operational information are relatively easily obtained, as the district's budget,

financial statements, and other important operational and financial information are readily available on its website.

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