Fitch Rates Seacoast Utility Auth (FL)'s Water & Wastewater Ref Revs 'AA'; Outlook to Positive

Fitch Ratings-New York-26 October 2016: Fitch Ratings has assigned a 'AA' rating to the following Seacoast Utility Authority, Florida (the authority) bonds:

--Approximately $7,700,000 water and sewer utility system revenue refunding series 2016A;
--Approximately $43,210,000 water and sewer utility system revenue refunding bonds, series 2016B.

The bonds are expected to sell the week of October 31 via negotiation. Bond proceeds will be used to refund all of the authority's series 2009A bonds maturing after March 1, 2020, refund a portion of the series 2009B Build America Bonds (BABs), pay interest coming due on the series 2016B bonds through March 1, 2020, and to pay costs of issuance. No debt service reserve fund will be established for the series 2016 bonds.

In addition, Fitch Ratings has affirmed the authority's 'AA' rating on the following bonds:

--$87.5 million (pre-refunding) water and sewer revenue bonds, series 1989A, 2009A and 2009B (BABs).

The Rating Outlook has been revised to Positive from Stable.

SECURITY

The bonds are secured by a first-lien pledge of net revenues of the authority's water and sewer system (the system) and investment income.

KEY RATING DRIVERS

POSITIVE OUTLOOK: The Positive Outlook is driven by the system's strong financial flexibility, improving financial forecasts, and rapidly declining debt burden.

FINANCIAL FLEXIBILITY: The system financial position is solid, with debt service coverage (DSC) at or near 2x for the last four years. Management forecast point to continued strong DSC in line with historical norms. The system's liquidity position should remain robust for the rating level, despite modest anticipated declines due to cash defeasance and pay-go capital funding.

DECLINING DEBT PROFILE: Existing debt metrics compare favorably to Fitch's 'AA' rating category median, but the current crossover refunding transaction results in a short- term increases the authority's debt profile until the crossover date. The structure of the series 2016 refunding bonds coupled with the cash defeasance, provide for rapid amortization and it is expected that following the crossover date, debt ratios will swiftly decline.

AFFORDABLE RATES: Rates remain very affordable and provide ample financial flexibility for the authority.

ADVANCED TREATMENT AND ADEQUATE SUPPLY: Recent facilities upgrades and renewed water use permits provide the system with sufficient water supplies and treatment capacity to meet demand requirements for the near to intermediate term.

DIVERSE SERVICE AREA: The economic base of the service area is very stable and diverse and characterized by high wealth levels.

RATING SENSITIVITIES

CONTINUED STRONG FINANCIAL PERFORMANCE: Continuation of the system's sound financial performance, in line with management's projections, coupled with strong cash balances and the rapidly declining debt profile could result in upward rating movement.

CREDIT PROFILE

The authority was established in 1988 when it acquired the assets of a private water and wastewater utility. Created by an inter-local agreement between Palm Beach County, the city of Palm Beach Gardens, the village of North Palm Beach, and the towns of Juno Beach and Lake Park, the authority serves a 65-square-mile service area in northeastern Palm Beach County.

DECLINING DEBT BURDEN

Existing debt ratios have been trending downward with debt per customer of $1,614 comparing favorably to Fitch's 'AA' category median of $2,050. Similarly, debt to net plant for fiscal 2015 was 39%, compared to Fitch's 'AA' rating category median of 47%.
The current transaction will traditionally refund the series 2009A bonds, while the series 2016B will crossover refund the series 2009B bonds. The crossover date coincides with the March 1, 2020 optional redemption date on the series 2009B bonds and at that time a majority of the 2009B bonds ($59 million) will be called using the escrowed proceeds of the 2016 bonds. The authority anticipates cash defeasing the remaining $6 million in series 2009B bonds, leaving only the series 2016B bonds outstanding. Utilizing the crossover refunding, while adding to the overall debt burden in the short-term, preserves the eligibility of the BABs subsidy.

Also, the authority is contributing $13 million to the transaction to reduce debt levels and principal repayment on the series 2016B bonds will be accelerated. The shortened repayment schedule provides for rapid debt amortization while keeping annual debt service costs near historical norms through fiscal 2025. Fitch believes the current structure of the series 2016 bonds positively demonstrates the system's financial flexibility and is a beneficial use of the authority's ample cash balances.

STRONG LIQUIDITY AND GOOD COVERAGE PROVIDE FINANCIAL FLEXIBILITY

Financial metrics continue a positive trend with robust liquidity and stable DSC. Senior-lien DSC (excluding connection fees) for fiscal 2015 was over 2x. Fitch calculated coverage based on management revenue and expense forecasts point to continue strong DSC of 2.2x to 2.4x through the fiscal 2022 forecast period. These recently revised projections, based on increased connections and consumption, are an improvement over the prior forecasts, which pointed to coverage levels of 1.8x to 1.9x through 2019.

Authority liquidity is very strong, averaging over 900 days of cash on hand for the last five fiscal years. The authority's exceptional liquidity will see some decline due to the $13 million contribution towards the current refunding transaction and the authority's plan to cash-fund its CIP. Realization of higher forecasted DSC levels, coupled with liquidity levels that remain at or above Fitch's 'AA' medians could result in positive rating movement.

INCREASED CAPITAL SPENDING PLANNED

The authority's 2017 - 2022 CIP totals $113 million, or $1,711 per customer, and is up 30% from the prior budget cycle. The notable increase in capital spending reflects management's desire to increase the authority's investment in system infrastructure. Annual capital expenditures range from $15 million to $18 million in the first three years and over $20 million in out-years. Cash balances are very robust and able to handle the increased costs. The focus of the CIP remains on renewal and replacement of system assets.

NEW TECHNOLOGY AND RENEWED PERMIT PROVIDE ADEQUATE SUPPLY

The authority recently completed construction of a new water treatment plant with 30.5 million gallons per day (mgd) capacity to replace two existing lime softening plants. Treatment plant capacity exceeds the 2015 demand of 15 mgd by over 50%.

The new plant improves the quality of water delivered and represents a more efficient alternative to renewal and replacement of the other two facilities. Furthermore, the new plant, along with accompanying wells, diversifies the authority's water supply to include brackish Floridan aquifer water supplies, helping to reduce pressure on fresh groundwater supplies. The authority's water use permit for freshwater supplies is expected to meet demand through at least 2032.

Wastewater is treated at a system-owned and operated plant. The majority of effluent from the wastewater system is sold as recycled water. A deep injection well disposes of the small portion of effluent that is not recycled. Current wastewater treatment capacity exceeds demand by over 50%.

AMPLE RATE AFFORDABILITY

Fitch views the authority's rate structure and flexibility as positive credit factors. Rates are structured with a substantial fixed component which provides for stable revenue to support operations. The authority also has a history of raising water and sewer rates as needed. Following three years of above average rate increases, adopted in fiscal 2010, the authority's governing board voted to adjust rates annually based on the consumer price index.

Management did not adjust rates in fiscal 2013 due to favorable financial results and cost containment but resumed indexed increases in fiscal 2014. On average, rates are increased by 3% and the authority continues to budget for 3% annual rate increases for at least the next five years. Rates maintain flexibility, registering 1.2% of median household income (MHI) and well below Fitch's 2% MHI affordability threshold.

STABLE, WEALTHY SERVICE TERRITORY

The system provides retail service to over 35,000 and 31,000 water and wastewater connections, respectively, with the majority being residential connections. Economic prospects within the authority service area are favorable due to low unemployment rates and high wealth levels.

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Applicable Criteria
Revenue-Supported Rating Criteria (pub. 16 Jun 2014) (https://www.fitchratings.com/site/re/750012)
U.S. Water and Sewer Revenue Bond Rating Criteria (pub. 03 Sep 2015) (https://www.fitchratings.com/site/re/869223)

Additional Disclosures
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