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RATING ACTION COMMENTARY

Fitch Upgrades Seacoast Utility Auth, FL's Water & Wastewater Rfdg Revs at 'AAA'; Outlook Stable

Tue 24 Nov, 2020 - 1:06 PM ET



Fitch Ratings - Austin - 24 Nov 2020: Fitch Ratings has upgraded the ratings on the following Seacoast Utility Authority, FL (SUA) bonds to 'AAA' from

'AA+':

--Approximately \$44.4 million water and sewer revenue bonds, series 2016A and 2016B.

Fitch also assigns an Issuer Default Rating (IDR) of 'AAA' to SUA.

The Rating Outlook is Stable.

ANALYTICAL CONCLUSION

The upgrade of the bonds to 'AAA' and the assignment of a 'AAA' IDR reflect SUA's very low leverage, which has experienced a downward trend over the last five years due to continued strong financial performance supported by regular rate increases and rapidly amortizing debt. SUA completed a crossover refunding in March 1, 2020, which fully defeased the series 2009B bonds, leaving only the series 2016A and 2016B bonds outstanding. The ratings reflect the combined water and sewer system's very low leverage, as measured by net adjusted debt to adjusted funds available for debt service (FADS), in the context of its very strong revenue defensibility and very low operating risk profile, both assessed at 'aa'. SUA's financial operations are very strong. Leverage registered at a negative 0.7x in fiscal 2019 and is expected to decline further over the forward look. SUA will fully pay off its debt by March 2024, freeing \$13 million annually for capital projects. This is expected to allow SUA to cash fund its capital plans via pay-go with no additional debt issuances expected.

CREDIT PROFILE

SUA was created through an inter-local agreement by the City of Palm Beach Gardens, Palm Beach County, the Village of North Palm Beach, the Town of Lake Park and the Town of Juno Beach. The retail water and sewer system serves primarily residential accounts in a 65 square-mile service area in northeastern Palm Beach County and serves approximately 100,000 people through around 36,000 and 31,700 water and wastewater connections,

respectively. SUA acquired the utility assets of Seacoast Utilities on Dec. 20, 1988 by eminent domain.

Recent facilities upgrades and expansion of wells provide the system with sufficient water supplies and treatment capacity to meet demand requirements until build out, which is expected in the next 10 to 15 years. SUA recently completed construction of a new water treatment plant with 30.5 million gallons per day (mgd) capacity to replace two existing plants. SUA has entered the final phase of its water supply wellfield renovation initiative. By the end of 2020, all 36 surficial aquifer wells will have been renewed or replaced to membrane system standards. As the wastewater treatment plant approaches 30 years in service, scheduled renewal and replacements to major mechanical, electrical, biosolids treatment, pumping and control systems are in progress.

Coronavirus Considerations

The recent outbreak of coronavirus and related government containment measures worldwide create an uncertain global environment for the water and sewer sector. While the system's performance through most recently available data has not indicated material impairment, changes in revenue and cost profile are occurring across the sector. Fitch's ratings are forward-looking in nature. Fitch will continue to monitor developments in the sector as a result of the virus outbreak and incorporate any revised expectations for future performance and assessment of key risks as appropriate.

KEY RATING DRIVERS

Revenue Defensibility 'aa'

Very Favorable Service Area Characteristics; Affordable Service Costs

Revenues are derived entirely from SUA's exclusive right to provide retail water and sewer service within the service area. SUA's service area characteristics are favorable with moderate growth and above-average incomes. SUA has independent rate-setting authority and rates are

affordable for the vast majority of customers.

Operating Risks 'aa'

Very Low Operating Risks

The operating risks assessment is supported by SUA's very low operating cost burden and a moderate life cycle ratio. Average annual capital spending over the next five years of \$140.6 million is significantly above historical average spending and focuses primarily on renewal and replacement (R&R). Planned spending should outpace annual depreciation and keep the life cycle below 45%.

Financial Profile 'aaa'

Exceptionally Strong Financial Profile

SUA's exceptionally strong financial profile reflects continued financial performance supported by regular rate increases and rapidly amortizing debt, which have lowered leverage to approximately negative 0.7x. Leverage is expected to decline further in the forward look. Liquidity is expected to remain robust and neutral to the assessment.

ASYMMETRIC ADDITIVE RISK CONSIDERATIONS

No asymmetric additive risk considerations affected this rating determination.

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:

--A sustained increase in leverage closer to 5.0x due to either significant unexpected borrowing or a decrease in FADS.

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>].

SECURITY

The bonds are secured by a first-lien pledge of net revenues of the SUA's system and investment income.

REVENUE DEFENSIBILITY

Revenue defensibility is considered to be very strong, assessed at 'aa'. All revenues are derived from the system's monopolistic business lines providing retail water and sewer services. Customer growth is midrange reflected by the five-year CAGR of 0.4% as of fiscal 2019. Income levels are stronger in relation to the nation at 133% of the national average while the unemployment rate was about 73% of the national average.

Water rates consist of a base facility charge and a commodity charge. The base facility charge is a fixed monthly charge traditionally kept high at approximately 71% of a customer's total water bill (based on 7,500 gallons usage) and is designed to cover most fixed costs such as R&R, payroll, insurance, etc. The commodity charge is designed to recover variable operating costs and is based on a 3-tiered structure that increases with increasing consumption. SUA continues to increase rates per its 2010 ordinance that allows CPI rate adjustments, approximately 2% to 3% annually. The resulting bill of about \$69 (fiscal 2019 rates) is considered to be affordable for the vast majority of customers (almost 90%).

OPERATING RISKS

SUA's operating risks are very low and assessed at 'aa'. The operating cost burden is similarly very low at \$4,746 per million gallons of water produced and sewer flows treated. The operating risk also benefits from a favorable life cycle ratio at 42% and a five-year average ratio of capex to depreciation of 85% as of fiscal 2019.

The current capital program spanning 2020-2024 totals \$140.6 million with capex focusing on R&R, including pipeline infrastructure replacement and water plant improvements. There are no significant new projects in the five to 15-year time horizon. All SUA debt will be fully paid by March 2024, freeing \$13 million annually for capital projects. This is expected to allow SUA to cash fund its capital plans via pay-go, with no additional debt issuances expected for the foreseeable future. Cash balances and yearly free cash are robust, and consequently cash funding capex should not pressure the system.

FINANCIAL PROFILE

The financial profile is exceptionally strong and assessed at 'aaa'. SUA's leverage ratio was a negative 0.7x at the end of fiscal 2019, which has continuously improved since fiscal 2015 as a result of ongoing increases in revenues resulting from regular rate adjustments as well as rapidly amortizing debt. The liquidity profile, while neutral to the assessment, has also improved over the last five fiscal years with available cash increasing to its highest level in fiscal 2019. At the close of fiscal 2019, current days cash on hand and the liquidity cushion ratio equaled 1,136 days. For the same period, coverage of full obligations was 2.5x; Fitch-calculated debt service coverage for the period was also 2.5x.

Fitch Analytical Stress Test (FAST)

The FAST considers the potential trend of key ratios in a base case and a stress case. The stress case is designed to impose capital costs 10% above expected levels and evaluate potential variability in projected key ratios. Base case assumptions includes SUA's unaudited 2020 figures and the 2021 budget five-year plan. In addition, no new debt is included over the next five years as capital spending will be funded entirely from existing and projected cash reserves. Finally, escrowed 2016 refunding bond proceeds totaling around \$59 million which were used on March 1, 2020 to refund the 2009 bonds were included in fiscal 2020 principal repayments. Based on these assumptions leverage declines further over the forward look to a negative 1.6x by year five and to a negative 1.2x under the stress case. The liquidity profile remains neutral to the assessment.

Given the overriding economic uncertainty related to the coronavirus, Fitch has also considered an additional sensitized downside scenario that assumes a 4% revenue decline in fiscal 2021 with a recovery stretched over the following three years. Leverage did not materially change in this scenario and was not a consideration in the final rating.

ASYMMETRIC ADDITIVE RISK CONSIDERATIONS

No asymmetric additive risk considerations affected this rating determination.

SOURCES OF INFORMATION

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

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.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY/DEBT	RATING		
Seacoast Utility Authority (FL) [Water, Sewer]	LT	AAA	New Rating
	IDR	●	
● Seacoast Utility	LT	AAA	Upgrade
		●	

Authority
(FL) /Water
& Sewer
Revenues/1
LT

[VIEW ADDITIONAL RATING DETAILS](#)

Additional information is available on www.fitchratings.com

APPLICABLE CRITERIA

[Public Sector, Revenue-Supported Entities Rating Criteria \(pub. 27 Mar 2020\) \(including rating assumption sensitivity\)](#)

[U.S. Water and Sewer Rating Criteria \(pub. 03 Apr 2020\) \(including rating assumption sensitivity\)](#)

ADDITIONAL DISCLOSURES

[Dodd-Frank Rating Information Disclosure Form](#)

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[Endorsement Policy](#)

ENDORSEMENT STATUS

Seacoast Utility Authority (FL)

EU Endorsed

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US Public Finance

Infrastructure and Project Finance

North America

United States

ENTITIES

Seacoast Utility Authority (FL) [Water, Sewer]

Seacoast Utility Authority (FL)

ISSUER CONTENT

Seacoast Utility Authority (FL) [Water, Sewer] - ESG Navigator

Fitch Upgrades Seacoast Utility Authority, FL's Water & Wastewater Ref Revs 'AA+';

Outlook Stable

Seacoast Utility Authority, Florida

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

Fitch Affirms Seacoast Utility Authority, FL's Water & Wastewater Revs at 'AA'; Outlook Stable

Fitch Affirms Seacoast Utility Authority, FL's Water & Wastewater Revs at 'AA'; Outlook Stable

Fitch Upgrades Seacoast Utility Authority, FL Water & Wastewater Revs to 'AA'; Outlook Stable

Fitch Affirms Seacoast Utility Authority, FL Water & Wastewater Revs at 'AA-'; Outlook

RECOMMENDED CONTENT

Delayed Draw Risk in Infrastructure Projects Makes Investor Credit Quality Critical

Delayed Draw Risk in Project Finance - Investor Credit Quality and Sophistication Are Critical

Fitch Takes Various Rating Actions on U.S. Enhanced Municipal Bonds and TOBs

Fitch Affirms Fellowship Senior Living's (NJ) Rev Bonds at 'BBB+'; Outlook Negative

Fitch Rates California Infrastructure & Econ Dev Bank's 2020A ISRF Bonds 'AAA'; Outlook Stable

Waverly Heights, Ltd. (PA) - ESG Navigator

Royal Oaks Life Care Community, Arizona

Fitch Affirms Mount Sinai Hospital (NY) Revs at 'A'; Outlook Stable

Fitch Affirms Rosalind Franklin University's (IL) Revs at 'BBB+' and Assigns IDR; Outlook Negative

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RATINGS KEY

POSITIVE

NEGATIVE

EVOLVING

STABLE

OUTLOOK



WATCH



* **Long Term/Short Term Issuer Default Rating** displayed in orange denotes EU Unsolicited and Non-Participatory Ratings

Where there was a review with no rating action (Review – No Action), please refer to the “Latest Rating Action Commentary” for an explanation of key rating drivers

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