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Summary:

Reedley Public Financing Authority, California Reedley; Water/Sewer

Primary Credit Analyst:

Aaron Lee, San Francisco (1) 415-371-5066; aaron.lee@standardandpoors.com

Secondary Contact:

Chloe S Weil, San Francisco (1) 415-371-5026; chloe.weil@standardandpoors.com

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Summary:

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Credit Profile

US\$3.395 mil wastewater rfdg rev bnds ser 2016 due 06/01/2037

Long Term Rating

A/Stable

New

Reedley Pub Fing Auth, California

Reedley, California

Reedley Pub Fing Auth Wastewtr Expansion Proj

Unenhanced Rating

A(SPUR)/Stable

Upgraded

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services raised its underlying rating (SPUR) on the Reedley Public Financing Authority, Calif.'s series 2007 wastewater revenue bonds, issued for the city of Reedley, to 'A' from 'A-'.

At the same time, Standard & Poor's assigned its 'A' long-term rating to the city's series 2016 wastewater revenue refunding bonds. The outlook on all issues is stable.

The upgrade is primarily due to continued improved financial performance as shown in the fiscal year-end 2015 audit, and our expectation that the city will continue to maintain improved coverage metrics through the outlook horizon. The upgrade is also due in part to the implementation of our updated criteria, "Rating Methodology And Assumptions For U.S. Municipal Waterworks And Sanitary Sewer Utility Revenue Bonds," published Jan. 19, 2016, on RatingsDirect.

The rating reflects our view of the city's strong enterprise risk profile and strong financial risk profile. The strong enterprise risk profile includes:

- The city's participation in the Fresno metropolitan statistical area, with a primarily agricultural economic base;
- A stable and diverse customer base; and
- Moderate rates that are reviewed annually and overall good operational management.

The strong financial risk profile includes:

- Improved coverage metrics that last stood at 1.3x at the end of fiscal 2015;
- Strong liquidity with nearly 790 days' of operating expenses;
- Moderately high debt-to-capitalization and no additional debt plans in the near future; and
- Good financial management.

The city's 2016 wastewater revenue refunding bonds are being issued to refund the 2007 bonds outstanding and are

secured by a pledge of net revenues of the city's wastewater system. Bond provisions are, in our view, adequate and credit neutral. Key provisions include a rate covenant of 1.2x annual debt service and an additional bonds test of 1.25x maximum annual debt service (MADS). A debt service reserve fund is to be funded at the lesser of MADS, 1.25x average annual debt service, or 10% of par. The city plans to apply for bond insurance for this issue and a surety to fulfill the reserve requirement.

Enterprise risk

The city is in central Fresno County and covers about 4.4 square miles approximately 25 miles southeast from the city of Fresno. The current population is about 25,500, which has remained relatively unchanged over the past five years. Agriculture represents a significant portion of the city's economic base, which results in cyclical unemployment figures. Income indicators are, in our view, adequate with 2014 median household effective buying income (MHHEBI) at 85% of the national median. The wastewater system is coterminous with the city limits and serves approximately 5,700 active accounts, of which 92% is residential. We view as the customer base as very diverse with the top 10 leading customers representing 12.4% of total revenues. Management does not expect any material changes to the customer base other than modest growth in wastewater accounts in the near future.

Single-family residential customers currently pay a flat monthly fee of \$49.35 for sewer service. Management reports that the last rate study was performed in fiscal 2013 during which there were significant rate increases. Since then, the city has implemented a 2.5% rate escalator that has taken effect during the past two fiscal years. Until a new rate study is performed, the city expects to maintain the automatic escalator, which the city council approves on an annual basis. Given the city's income levels and the county poverty rate, we view rates as moderately high, as they represent 1.6% of 2014 MHHEBI.

Based on our Operational Management Assessment, we view the city to be a '2' on a scale of 1-6, with '1' being the strongest. This indicates, in our view, that operational and organizational goals are generally well-aligned, even if some challenges exist. The wastewater treatment plant has capacity to treat 5 million gallons per day (mgd), which is ample for the current average dry weather flow of 1.7 mgd. Management also reported that it had recently installed a solar array that can meet all of the plant's electricity needs, which has helped the city buffer against electrical rate increases. The city does not have a formal succession plan, but has invested in training its operational staff for continuity. The city also offers educational and outreach programs for the local community.

Financial risk

The wastewater system's all-in coverage has improved to good levels from insufficient levels in fiscal 2011 and 2012. At the end of fiscal 2015, coverage was 1.3x compared with nearly 1.4x in fiscal 2014. The slight decline in coverage for fiscal 2015 resulted mainly from essentially flat operating revenues while operating expenses increased approximately 5% in fiscal 2015 compared to fiscal 2014. Based on management's forecast, coverage in fiscal 2016 is expected to reach 1.5x and will be maintained at these levels through the outlook horizon.

System liquidity has been strong during the past three fiscal years. At the end of fiscal 2015, the wastewater system had \$4.7 million in unrestricted cash, or about 789 days' operating expenses, compared with \$4.1 million in fiscal 2014. Given the city's anticipated capital expenditures and financial projections, we expect liquidity levels to be maintained at the historically strong levels through the two-year outlook horizon.

The wastewater system's debt-to-capitalization ratio is moderately high at 67.6%. Over the next five years, the city expects to spend about \$4.4 million in capital improvements, which will be funded on a pay-as-you-go basis. Management anticipates no additional borrowing at this time.

Based on our Financial Management Assessment (FMA), we view the city to be a '2' on a scale of 1-6, with '1' being the strongest. An FMA of '2' indicates our view that practices are good, but not comprehensive. The government maintains many best practices deemed as critical to supporting credit quality, particularly within the finance department. These practices, however, may not be institutionalized or formalized in policy, may lack detail or long-term elements, or may have little recognition by decision-makers outside of the finance department. The FMA of good includes reasonably conservative financial projections that are updated regularly, and semiannual financial reporting to the city council. The city also has adopted investment, liquidity, and debt management plans and produces GAAP (generally accepted accounting principle)-based audits.

Outlook

The stable outlook reflects our expectation that the sewer fund will continue to maintain its improved coverage metrics through the two-year outlook horizon due to the debt service savings from this refunding transaction and the lack of additional debt plans. We also do not expect any major changes to the customer base and wastewater operations that may cause financial stress.

Upside scenario

We may raise the rating if the city were to continue improving and sustaining its coverage metrics such that they are comparable to peers at a higher rating level.

Downside scenario

If for any reason there were a significant deterioration of the city's coverage metrics or unrestricted liquidity, we may lower the rating.

Related Criteria And Research

Related Criteria

- USPF Criteria: Rating Methodology And Assumptions For U.S. Municipal Waterworks And Sanitary Sewer Utility Revenue Bonds, Jan. 19, 2016
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- U.S. State And Local Government Credit Conditions Forecast, Jan. 11, 2016
- U.S. Municipal Water And Sewer Utilities 2014 Sector Outlook: Learning To Do More With Less, Jan. 9, 2014

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.

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