S&P Global
Ratings

RatingsDirect®

Summary:

Parker Water & Sanitation District, Colorado; Water/Sewer

Primary Credit Analyst:
Malcolm N D'Silva, Centennial + 1 (303) 721 4526; malcolm.dsilva@spglobal.com

Secondary Contact:
Jaime Blansit, Centennial + 1 (303) 721 4279; jaime.blansit@spglobal.com

Table Of Contents

Summary:

Parker Water & Sanitation District, Colorado; Water/Sewer

Credit Profile		
US$81.52 mil wtr and swr enterprise rfdg and imp rev bnds ser 2022 due 11/01/2041		
Long Term Rating	AA+/Stable	New
Parker Wtr & San Dist wtr & swr		
Long Term Rating	AA+/Stable	Affirmed
Parker Wtr & San Dist wtr & swr (AGM)		
Unenhanced Rating	AA+(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rating Action

S&P Global Ratings assigned its 'AA+' long-term rating to Parker Water & Sanitation District, Colo.'s anticipated $81.5 million series 2022 water and sewer enterprise refunding and improvement revenue bonds. At the same time, S&P Global Ratings affirmed its 'AA+' rating on the district's existing water and sewer enterprise revenue bonds. The outlook is stable.

The series 2022 bond proceeds will refund a portion of the district's series 2012 bonds and finance capital improvements to the system, including a new headquarters facility, construction and equipping of an advanced filtration system, and the installation of a tank and water line extension. Post-issuance, the district will have approximately $282 million of debt outstanding, including about $176 million of enterprise revenue bonds, $81 million of general obligation (GO) bonds, and about $25 million of loan obligations. Approximately 30% of the total debt outstanding represents the district's GO bonds, payable from separate unlimited ad valorem property taxes and other available district funds. For more information on the GO bonds, see analysis published May 1, 2020, on RatingsDirect.

We view the bond provisions as credit neutral. The bonds are secured by a pledge of the district's net revenues of the water and wastewater system. Key bond provisions include a rate covenant set at 1.1x annual debt service and an additional bonds test set at 1.1x maximum annual debt service. The series 2022 bonds will not have a debt service reserve, but we view this as credit neutral given the system has historically maintained a robust liquidity position.

Credit overview

The district has exhibited considerable growth in its service area, and its strong financial performance reflects a corresponding reliance on tap fees and other growth-related revenue, which we view as a potential vulnerability if such revenues materially decline without being mitigated by increased recurring operating revenues. The district is in the middle of a large capital cycle to meet growth needs, and we view the district as having strong financial capacity to absorb these future costs. The district's current five-year capital improvement program (CIP) is an extension of its master planning process, which indicates an aggregate project cost of approximately $260 million. We understand that a portion of its CIP is growth related, and management notes that the district has flexibility relating to project timing of various capital equipment and growth-related projects. The district's financing plan estimates additional borrowing of approximately $30 million in 2025 along with excess revenues and cash reserves to fund its CIP. The district's financial outlook is achievable, in our view, despite the layering of additional debt to fund its CIP. We believe that strong management of long-term financial and capital planning will be a key factor supporting rating stability.

The stable outlook reflects our anticipation that the district will continue to operate its enterprise system in a manner that will sustain its very strong financial profile and all-in coverage metrics while addressing its long-term CIP and growth needs.

Environmental, social, and governance

We view the district's environmental, social, and governance (ESG) risks as not being significantly different from those of its peers. Like peers in the western U.S., the district faces challenges from population growth, climate change, and drought conditions. Based on its financial plan, officials are making several investments across its facilities to mitigate the district's environmental risks. The district has sufficient water supply rights to meet long-term demand and it has been investing in water supply diversification and storage to realize its goal of reaching 75% renewable water sources by buildout. The district has formal long-term financial and capital planning, and updated master plans to ensure environmental compliance, which is supportive of our view that governance is in line with its peers. Management also maintains robust emergency planning, including cyber policies. We understand that management will continue to adjust its service rates to meet future revenue sufficiency, and we do not believe this will significantly increase affordability pressures or social risks, given very strong local incomes.

Stable Outlook

Downside scenario

We do not anticipate any downward rating pressure in the next two years, given the district's strong cash balances. However, because of the dependence on annual growth fees and other growth-related revenue to generate stronger all-in coverage, the rating or outlook could be negatively affected if significant reductions in these revenues result in substantially lower all-in coverage or liquidity ratios. We could also lower the rating, if any new potential environmental regulations lead to increased debt obligations beyond current expectations that significantly alter related financial metrics.

Upside scenario

We could raise the rating in the long term if the district sustains all-in coverage without growth-related fees at a level that we consider good, representing less reliance on one-time revenue to meet stronger coverage and if the district sustains liquidity at extremely strong levels during the life of the capital plan mitigating any evolving potential environmental regulations or unanticipated capital needs.

Credit Opinion

The district's service area encompasses about 27,900 acres in the northeastern portion of Douglas County, about 20 miles southeast of the city and county of Denver. The district serves the Town of Parker, a portion of Lone Tree, Castle Pines North, and an unincorporated portion of the county. The district continues to see population growth, reaching about 60,000 in 2021. The district expects buildout of more than twice this population by 2050. It currently serves about 22,600 single-family equivalents, which is about 46% of the total projected system buildout. We view the service area's income levels to be very strong based on Parker's (majority of the service area) median household effective buying income (MHHEBI), which was 161% of the national median. Parker's unemployment rate has historically been below both the state and national levels.

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

- Service area participation in the strong Denver-Aurora-Lakewood metropolitan statistical area (MSA) supported by very strong income indicators, and diversifying and growing customer base;
- Affordable combined service rates (at 1.7% of MHHEBI) in the context of the service area's very strong income levels and low poverty rate;
- Very low industry risk as a monopolistic service provider of an essential public utility; and
- Good Operational Management Assessment, represented by sufficient water supply to meet long-term demand, continued maintenance to ensure integrity of the system, and expansion of its facilities to meet continued demand.

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

- Extremely strong all-in coverage above 2.0x during the past three fiscal years, although we understand strong metrics are heavily reliant on growth-related fees;
- Extremely strong liquidity, with approximately $170 million of unrestricted cash in fiscal 2021 (unaudited), equivalent to about six years of operating expenses;
- Large capital plan that consists of growth-related projects, with a pro forma debt-to-capitalization ratio at about 34% that we expect will rise but stay manageable given future debt plans; and
- Good Financial Management Assessment, represented by regularly updated long-term financial and capital plans, a formal investment policy, and other, less formalized financial guidelines.

Enterprise risk: Solid economic fundamentals supported by strong growth and water supply diversification to meet long-term demand

The district's customer base is primarily residential and very diverse, in our view. During the past five years, customer growth ranged between 3% and 5% annually. Residential customers account for about 70% of the district's annual usage. We consider the customer base to be very diverse based on the leading 10 customers contributing about 11% of total operating revenues in 2021, with the leading customer representing less than 2%. The district reviews rates annually, works with an external rate consultant, and has modestly increased rates annually during the past five years. On average, rate increases for both water and sewer have been slightly less than 3% annually. The district recently completed a full cost-of-service study in 2020 with continued projected modest rate adjustments (average of 3% annually for the foreseeable future).

The district obtains water supply from a variety of sources including wells in the Denver basin, Cherry Creek water rights, Water Infrastructure Supply Efficiency (WISE) water, and Reuter Hess Reservoir water. The district plans to decrease the amount of groundwater pumped from wells and increase renewable supply in the Reuter Hess Reservoir water treatment facility. Denver basin wells can supply 16 million gallons per day (mgd), and alluvial wells 3 mgd, Reuter Hess Water Purification Facility can treat 10 mgd, and WISE water can supply 1 mgd. Total current system water supply capacity is 30 mgd, which exceeds the peak daily demand of about 17 mgd. Management has ample water supply and enough treatment capacity to meet demand. In addition, the district operates two advanced wastewater treatment plants with a recent expansion that provides for sufficient treatment capacity in the long term.

Financial risk: Very strong financial metrics with some reliance on one-time growth-related fees

We view the district's all-in coverage as healthy but dependent on one-time developer fees and growth-related revenue. All-in coverage is our internally adjusted debt service coverage metric that we believe best tracks the use of every dollar of utility operating revenue, regardless of lien, accounting treatment, or ultimate purpose and includes a fixed minimum payment for WISE water. In addition, we analyze both total all-in coverage, excluding property tax revenue and corresponding GO debt service payments, as well as including property tax revenue and GO debt service. In both scenarios, historical all-in coverage was very strong at above 2.0x. In addition, we performed a stress test by excluding all one-time developer and growth-related tap fees, with all-in coverage averaging 1.2x during the past five fiscal years. This reflects our view that growth-related fees continue to drive stronger coverage metrics. In 2021, one-time growth-related fees were slightly above 50% of total revenue. Based on our analysis of management-provided projections, which we view as reasonable, we do not expect coverage metrics will deviate materially from historical trends during the next five fiscal years.

The district has historically maintained an extremely strong liquidity position, and we anticipate it will likely remain so. The liquidity position has been sufficient to cushion volatility and provide manageable rate increases. At the end of fiscal year 2021, the district held unrestricted cash and investments, including about $6 million from the rate stabilization fund, of about $170 million, or over six years of operating expenses. Based on management's cash flow projections, we understand that the district plans to deploy capital reserves to supplement its capital needs. However, we anticipate relatively nominal draws on internal operating cash to fund future capital needs, and we anticipate management will continue to maintain sufficient liquidity to meet operations.

Related Research

Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020