

MOODY'S

RATINGS

Rating Action: Moody's Ratings upgrades City of Madison, WI's sewer revenue and water revenue bonds to Aa1; outlook stable

06 Nov 2024

New York, November 06, 2024 -- Moody's Ratings (Moody's) has upgraded the City of Madison, WI's outstanding sewer revenue bonds and outstanding water revenue bonds to Aa1 from Aa2. We have also assigned a Aa1 to the city's Sewer System Revenue Bonds, Series 2024-E, with a proposed par amount of about \$16 million. At the close of 2023, the city had about \$168 million in water revenue debt and \$51 million in sewer revenue debt outstanding. The outlook is stable.

The upgrades for both the water and sewer revenue debt are driven by improved financial metrics at each system, including growing liquidity and strengthening debt service coverage.

RATINGS RATIONALE

The upgrade of the sewer revenue bonds to Aa1 reflects sustained growth in the sewer enterprise's liquidity and improved debt service coverage as a result of recent rate increases. The system closed fiscal 2023 with 228 days cash on hand and annual debt service coverage of 2.3x. The financial strength of the sewer enterprise is also bolstered by its relationship to the City of Madison (Aaa stable), which owns and operates the system and maintains much larger financial operations with healthy reserves. The system's debt burden will remain low at about 1.1x revenue because of modest borrowing plans and the limited scope of the system, which only handles collection. Wastewater treatment is performed by a separate entity, the Madison Metropolitan Sewerage District. Median family income is strong at 120% of the US, and the large customer base includes the Wisconsin state capital and the University of Wisconsin's flagship campus.

The upgrade of the water revenue bonds to Aa1 reflects rate increases that have resulted in improved debt service coverage and healthy liquidity for the water enterprise. Annual debt service coverage grew to 2.4x in 2023 following an 18% water rate increase. Liquidity is expected to remain strong at over 300 days cash on hand.

The financial strength of the water enterprise is also bolstered by its relationship to the City of Madison, which owns and operates the system and maintains much larger financial operations with healthy reserves. The system's debt burden is 2.7x revenue and unlikely to grow substantially because management intends to fund more projects from annual revenue surpluses, which currently exceed planned annual capital investments after paying debt service. Median family income is strong at 120% of the US, and the large customer base includes the Wisconsin state capital and the University of Wisconsin's flagship campus.

RATING OUTLOOK

The stable outlook reflects the expectation that the credit quality will remain strong, supported by continued economic growth, long-standing government and higher education presences within the city and continued financial stability.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- Expansion of operating size that leads to continued strengthening of debt service coverage and liquidity closer to Aaa medians, which are well over 3x coverage and 365 days of cash

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Weakening of annual debt service coverage to consistently below or near 1.7x
- Narrowing of system liquidity to consistently below 200 days cash on hand
- Material increase in debt burden

LEGAL SECURITY

Debt service on the sewer system's revenue debt is payable from net revenue of the sewer utility. Legal provisions include a 1.25x rate covenant, an additional bonds test of 1.25x maximum annual debt service (MADS) coverage, and a debt service reserve fund funded at the lesser of 10% of principal amount or MADS.

Debt service on the water system's revenue debt is payable from net revenue of the water utility. Legal provisions include a 1.25x rate covenant, an additional bonds test of 1.25x MADS coverage, and a debt service reserve fund funded at the lesser of MADS, 10% of original principal amount, or 125% of average annual debt service for all outstanding bonds.

USE OF PROCEEDS

Proceeds of the Series 2024-E bonds will fund improvements to the sewer system from the city's annual capital improvement plan, including pipe replacement, lining projects and lift station improvements.

PROFILE

Madison is the state capital of Wisconsin (Aa1 stable) and is home to the flagship campus of the University of Wisconsin. It is the state's second largest city with an estimated population of about 287,000.

The Madison water system and sewer system are enterprises of the city. The sewer system provides wastewater collection to about 71,000 customers within the City of Madison. The water system provides water treatment and distribution to over 71,000 customers within the City of Madison, as well as the adjacent villages of Maple Bluff and Shorewood Hills, and a portion of the City of Fitchburg (Aaa).

METHODOLOGY

The principal methodology used in these ratings was US Municipal Utility Revenue Debt published in March 2024 and available at <https://ratings.moodys.com/rmc-documents/416489>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

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Ryan Patton
Lead Analyst
Regional PFG Chicago
Moody's Investors Service, Inc.
100 N Riverside Plaza
Suite 2220
Chicago 60606
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

Gera McGuire
Additional Contact
Regional PFG Chicago
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

Releasing Office:
Moody's Investors Service, Inc.
250 Greenwich Street
New York, NY 10007
U.S.A
JOURNALISTS: 1 212 553 0376
Client Service: 1 212 553 1653

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