

RatingsDirect®

Summary:

Oxnard Financing Authority, California; Water/Sewer

Primary Credit Analyst:

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

Secondary Contact:

Tim Tung, San Francisco (415) 371-5041; tim.tung@standardandpoors.com

Table Of Contents

Rationale

Outlook

Related Criteria And Research

Summary:

Oxnard Financing Authority, California; Water/Sewer

Credit Profile

Oxnard wtr rev rfdg bnds

Long Term Rating

A+ / Negative

Outlook Revised

Oxnard Fincg Auth wtr

Unenhanced Rating

A+(SPUR) / Negative

Outlook Revised

Oxnard Fincg Auth, California

Oxnard, California

Oxnard Fincg Auth wtr rev proj bnds (Oxnard) ser 2010A

Long Term Rating

A+ / Negative

Outlook Revised

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services revised its outlook to negative from stable on Oxnard, Calif.'s and Oxnard Financing Authority, Calif.'s water revenue and revenue refunding bonds. At the same time, we affirmed our 'A+' long-term rating and underlying rating (SPUR) on the city's and authority's obligations secured by the net revenues of its water system. The negative outlook represents our view of the system's declining coverage levels due to lower system revenues resulting from decreases in water consumption.

The ratings reflect our view of the water system's:

- Established, diverse economic base that participates in the western portion of the Los Angeles region;
- Historically adequate to good debt service coverage (DSC), which management projects will rebound during the outlook period if rate increases are adopted; and
- Strong liquidity position, with cash equivalent to 281 days' operations at the end of fiscal 2014.

Partly offsetting these credit strengths is our view of the water system's:

- Need to implement significant rate increases to improve and maintain its coverage levels, and
- Significant capital improvement plan (CIP) and the city's plans to issue additional debt in the near term.

The bonds are secured by a pledge on the water system's net revenues excluding one-time connection fees associated with development. Legal provisions are, in our opinion, permissive, as they allow a rate covenant of 1.0x as long as there is at least 25% of maximum annual debt service (MADS) of cash available. The additional bonds test allows for the same restrictions as the rate covenant. A debt reserve requires the least of 10% of par, MADS, or 1.25x average annual debt service.

Oxnard, with a population of approximately 205,000, is situated approximately 62 miles west of Los Angeles in

Ventura County. Historically, the city served as a processing and service center for a surrounding agricultural region, but the city's economic base now includes a diverse mix of industrial and commercial activity, along with a base of regional commuter neighborhoods. Income indicators for the city are strong, in our view, with 2014 median household effective buying income (EBI) at 113% of the national median. However, per capita EBI is significantly lower, at 68% of the national median. Unemployment rates for the city over the past three years have been higher than the county and national rates and marginally lower than the state rate. According to August 2015 data, the unemployment rate is 6.3%. The customer base is stable, with water accounts having grown less than 1% annually during the past five years. At the end of fiscal 2014, there were 41,319, about 88% of which were residential.

The city's water supply comes from three sources: local groundwater, purchased groundwater from United Water Conservation District, or imported surface water from Calleguas Municipal Water District, a member of the Metropolitan Water District of Southern California. In fiscal 2014, local and purchased groundwater represented approximately 50% of supply while purchased surface water represented the other half. Although local groundwater is the city's least expensive option, this source is constrained by a regulation-driven agreement with neighboring agencies. The city has also indicated that, because imported surface water costs have continued to increase, it is considering increasing the use of recycled water that is generated from the city's wastewater treatment plant. Management expects that the recycled water system can produce approximately 7,000 to 8,000 acre-feet of water to offset existing potable water use by the end of the calendar year. Pursuant to the state's water conservation mandate, the city is required to reduce consumption by 12% compared to 2013. As of the state's August report, the city has reached 20% reduction.

Residential customers currently pay a base charge dependent on meter size and a volumetric charge depending on water use. The 2014 base charge for a 3/4-inch meter was \$15.61, and after adding the volumetric charges, we calculate a monthly bill of \$44.65 for our benchmark use of 1,000 cubic feet per month. When annualized, this represents about 1.1% of 2014 median household EBI, which we consider affordable. Management has historically passed through imported water rate increases to its customers and in fiscal 2013 and 2014, water rates increased by 8% and 2.4% over the previous year, respectively. Rates were not changed in fiscal 2015, and based on the most recent cost-of-service study, management is seeking council approval to raise rates by 15% for fiscal 2016, 12% in fiscal 2017, and 8% annually through fiscal 2020. Following the requisite Proposition 218 public hearing process, management hopes to implement these rate increases by February 2016.

The system's total DSC has been adequate to good during the past three years through fiscal 2014, with coverage levels consistently above 1.2x when excluding one-time connection fees, which are not pledged to the bonds. When including connection fees, coverage levels are, in our view, good. However, based on unaudited 2015 data, coverage has fallen to 1x for 2015 and is insufficient, at 0.95x, when excluding one-time connection fees. This was due to the decline in water consumption, and subsequently lower water revenues without the appropriate rate increase to make up for the revenue decline. Based on management's forecast, we expect coverage to rebound to at least a good level going forward although these projections rely heavily on the city's ability to raise rates according to its plan.

System liquidity has been strong over the past three years, with days' operating cash increasing to an estimated 338, or \$35.4 million of unrestricted cash, based on unaudited 2015 data from 284 in fiscal 2013. Based on the city's current

projections, there will be some drawdown in cash during the outlook horizon due to capital needs. Also, according to management's forecast, which is dependent on the implementation of the rate increases, liquidity will continue to be strong through the outlook period.

The city has identified approximately \$210 million in projects for the water system's CIP through fiscal 2020 with increasing expenditures for the recycled water system. Major capital projects include automatic meter reader replacements, water treatment plan upgrades, advanced water purification facility improvements, and aquifer storage and recovery and indirect potable reuse facilities construction. Management indicated that some CIP projects may be delayed depending on available resources and that the recycled water projects may be prioritized if drought conditions were to occur. Under the current CIP, the city expects to issue an additional \$245 million in debt during the next five years.

Outlook

The negative outlook reflects our view of the recent decline in coverage levels resulting from a decline of water consumption and subsequently a decline in water revenues. Further limiting the rating is the city's expectation to issue additional debt in the near term to fund its extensive capital program.

Upside scenario

We could revise the outlook back to stable if the city successfully raises rates to the levels specified in the current plan and is able to improve its coverage metrics.

Downside scenario

We could lower the rating if the city is unable to implement its rate increases and the additional borrowing or other circumstances continue to cause a decline in financial performance.

Related Criteria And Research

Related Criteria

- USPF Criteria: Water And Sewer Ratings, June 25, 2007
- USPF Criteria: Key Water And Sewer Utility Credit Ratio Ranges, Sept. 15, 2008
- USPF Criteria: Standard & Poor's Revises Criteria For Rating Water, Sewer, And Drainage Utility Revenue Bonds, Sept. 15, 2008
- 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, July 22, 2015
- U.S. Municipal Water And Sewer Utilities 2014 Sector Outlook: Learning To Do More With Less, Jan. 9, 2014
- 2014 Review Of U.S. Municipal Water And Sewer Ratings: How They Correlate With Key Economic And Financial Ratios, May 12, 2014

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.

Copyright © 2015 Standard & Poor's Financial Services LLC, a part of McGraw Hill Financial. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription) and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.