

# **Bond Case Briefs**

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## **U.Municipal Water Utilities: No News is (Probably) Good News; The Outlook is Stable**

As we noted in our recently released criteria, we view the municipal waterworks and sanitary sewer sector as one with very low risk. The sector:

- provides essential services in a monopolistic manner;
- uses proven technology; and
- is characterized by risk-averse management.

It remains a very highly rated sector, and upgrades continue to outnumber downgrades. But that does not mean the sector itself is without risk.

Utilities by nature are extraordinarily capital-intensive, and that capital is generally raised by borrowing; there is no such thing as a municipal initial public offering or equity cushion. Furthermore, the inherent stability does not completely insulate particular issuers from their own unique challenges. We have observed that most of our downgrades in 2015 were associated with weakened finances, not economic deterioration, and we believe that will continue to be the case. Utility managers and elected officials continue to have to manage the “triple bottom line,” balancing a utility’s revenue requirements and financial commitments versus social policies versus the utility’s role as an environmental steward. If at one end of the scale drinking water is viewed by users as a human right that should be free of price, versus being viewed as a commodity, the United States is somewhere in between. We believe that in the U.S. we are moving in the direction of commodity pricing as Americans slowly gain appreciation for the true value of water, usually only if there is temporary scarcity such as a drought. We also view 2016 as a turning point that will potentially mark the beginning of the first wave of new regulations in a number of years.

### **Overview**

- Utility ratings should remain stable for 2016, but the new criteria may introduce some volatility
- Regulatory risks are looming and could be expensive, but are not necessarily imminent.
- The rate of increase of water and sewer bills continues to be larger than comparable services and even the rate of real personal income growth.

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