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S&P: Could The Western U.S. Drought Threaten Municipal Credit Stability?

Key Takeaways

- Water supply challenges could create credit pressure for municipal utilities, irrigation districts, and local governments resulting from either a materially unfavorable shift in cost or if the service area economy stagnates due to insufficient supply.
- Managing water demand, procuring drought-resistant supply, and maintaining storage will be critical to managing fluctuations in hydrology. Issuers with prudent rate structures and strong balance sheets will be best positioned to absorb disruptions in operations or revenue collections from hydrological variability.
- Drought-related credit pressures for local governments include potential limits on economic growth, heat waves that require assistance for residents, and climate change-induced hydrological volatility that weakens levees and leads to flash flooding and mudslides.
- Extreme hydrological variability has been a pervasive challenge across the West. As droughts become more prolonged or expansive, there could be credit pressure. We expect well-defined climate adaptation policies, credible long-range resource plans, and achievable supply and demand management strategies will support stable credit quality. Many of these plans will be part of issuers' ESG planning as they address what could become the "new normal" across the West.

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