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Fitch: Federal Infrastructure Funds Lessen Public Utility Operating Risk

Fitch Ratings-New York/Austin-10 November 2021: The \$1.2 trillion Infrastructure Investment and Jobs Act (IIJA), which will soon be signed by President Joseph Biden, includes significant capital funding for utilities to address much needed remediation and resilience projects that will update and replace aging infrastructure and reduce operating risk, Fitch Ratings says. Access to grants and low-cost financing under the IIJA lowers a utility's cost burden and reduces the need to rely on rate increases to cover costs, which alleviates affordability pressures on the rate base.

With more resilient systems, utilities will be better positioned to mitigate increasing weather and cybersecurity threats and avoid more significant costs in the future. While increased capital spending generally improves a utility's lifecycle ratio and annual capex/depreciation, we do not expect ratings upgrades in the near-term based solely on any improvement in these metrics.

The total \$55 billion available to water utilities is unprecedented and addresses material infrastructure needs that accumulate as systems age. The IIJA adds over \$23 billion for both the Drinking Water State Revolving Fund (SRF) and the Clean Water SRF to fund water projects at lower interest rates, resulting in lower debt carrying costs. Funding will provide water and wastewater utilities essential capital funding for remediation of lead service lines (\$15 billion) and PFAS and other contaminants, including \$5 billion through SRFs and \$5 billion through the grant program for small and disadvantaged communities.

Many of the provisions in the IIJA are intended to broaden utilities' water portfolios, including \$100 million in competitive grant funds for water storage projects. Water infrastructure in the western US will receive a separate pool totaling \$8.3 billion. Over the medium to long term, these funds will help utilities in the west and southwest fund water storage and alternative water supply projects, such as water recycling, aquifer storage recovery and desalination, offsetting some of the supply pressures experienced due to prolonged drought conditions. The Drought Contingency Plan is also set to receive \$300 million under the IIJA to address drought risks to the Colorado River water supply.

IIJA moneys supplement Local Fiscal Recovery Funds for state, local, territorial and tribal governments under the American Rescue Plan Act that may be spent on broader needs and initiatives. A significant portion of these funds are expected to be spent on water and sewer infrastructure.

Water affordability is supported by the Low Income Water Assistance pilot program. This has limited benefit for most of our rated credits, which do not see material nonpayment or have a significant number of customers that would qualify.

Public power utilities will have access to funds that will provide necessary investment in grid resiliency, transmission and cybersecurity, allowing systems to limit incremental borrowings and moderate financial leverage. The most significant amount, \$10 billion, is dedicated to strengthening the electric grid's resilience against extreme weather events, and another \$3 billion is available to

help increase grid flexibility to respond to events that cause demand volatility. Hydropower projects will receive a boost, with incentive payments in the amount of \$628.6 million to help fund hydroelectric capital and efficiency improvements.

Funds are also available to assist public and private entities affected by cyberattacks, with an additional \$250 million specifically for rural electric cooperatives or county-owned utilities to boost cybersecurity and respond to cyber threats.

Congress will continue discussions on the broader Build Back Better Act (BBBA) later this month. The BBBA currently includes additional public utility funding, particularly for disadvantaged and rural communities to replace lead service lines. Expansion of clean energy tax incentives are also part of the proposal.