



## Financial Policies FY2022 Updates Response to Questions

**QUESTION NUMBER:** 3

**REQUESTED BY:** Grant Rabon

**DATE REQUESTED:** 2/09/2021

**QUESTION:** Is there anything preventing Austin Water from getting improved bond ratings from the rating agencies with the current financial policies?

**RESPONSE:**

Austin Water's goal is to maintain its current bond AA bond rating from all three major rating agencies. However, improvement or deterioration in days cash on hand or debt service coverage would not necessarily result in a rating upgrade or downgrade since there are a variety of factors that influence the bond rating process.

One of the biggest driving factors for the proposed financial policy changes, is the lessons learned during the drought from 2011 to 2015. Austin Water saw drought related revenue shortfalls totaling \$96 million from 2012 to 2015. As a result of those revenue shortfalls, debt service coverage, which measure the amount of revenues available to cover debt service as a multiple of annual debt service requirements, dropped to 1.27 times annual debt service requirements in 2014, which was slightly above the bond covenant level of 1.25. Had Austin Water experienced a larger revenue shortfall in 2014, it could have been in technical default and likely would have had its bond rating downgraded. In addition, Austin Water saw its days cash on hand financial metric drop to 53 days, which was below the financial policy level of 60 days.

As a result of the low debt service coverage and days cash on hand levels, two of the three major rating agencies placed Austin Water on a negative rating outlook, which signaled to the investor community that a downgrade was a possibility. As liquidity and debt service coverage improved, the negative rating outlook was removed, and Austin Water's bond ratings stabilized. However, it became



clear that Austin Water's current financial policy targets were too low to provide the strategic guidance needed to maintain minimum levels of financial performance to ensure compliance with bond covenants and to maintain Austin Water's AA credit rating.