S&P Global
Ratings

RatingsDirect®

Summary:

San Buenaventura, California; Water/Sewer

Primary Credit Analyst:
Chloe S Weil, San Francisco + 1 (415) 371 5026; chloe.weil@spglobal.com

Secondary Contact:
Malcolm N D'Silva, Englewood + 1 (303) 721 4526; malcolm.dsilva@spglobal.com

Table Of Contents

Summary:

San Buenaventura, California; Water/Sewer

Credit Profile		
San Buenaventura 2020 rfdg wtr rev bnds (federally taxable) due 01/01/2044		
Long Term Rating	AA/Stable	Affirmed
San Buenaventura Pub Fac Fing Auth, California		
San Buenaventura, California		
San Buenaventura Pub Fac Fing Auth (San Buenaventura) wtr rev bnds		
Long Term Rating	AA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings affirmed its 'AA' rating on the city of San Buenaventura (Ventura), Calif.'s outstanding water revenue bonds.
- The outlook is stable.
- As of Dec. 31, 2022, the water system had $63.7 million of water revenue bonds outstanding. Our rating reflects the potential costs associated with a forthcoming $63.6 million Water Infrastructure Finance and Innovation Act (WIFIA) loan. This loan will be administered by the Environmental Protection Agency (EPA).

Security

We view the water revenue bond provisions as adequate. The bonds are secured by net revenues of the city's water system. Covenants include a rate covenant set at 1.20x current year debt service on all senior lien debt and an additional bonds test (ABT) set at 1.20x annual debt service for the next three years, including the new issue of parity debt. We note that operations and maintenance costs are defined in the indenture to exclude the city's state water contract payments during the period that it is not taking delivery of that water, although the city currently treats those payments as operating expenses in its audited financial statements. For the ABT, the city may include an allowance for additional revenues related to any increase in service charges that was in effect for less than the full 12-month test period. There is no debt service reserve for the bonds.

Credit overview

In our opinion, the water system's recent financial performance is a key credit strength, as is its stable and primarily residential customer base. Credit risks center on the system's constrained water supply and its rising service costs, which could challenge overall affordability over time. While we believe the city's approved rate plans set an achievable trajectory for near-term financial performance, negative economic headwinds and continued recessionary pressures could pressure operating margins and costs of service during the outlook period. Given the water system's significant capital needs, which total $341 million during the next decade, we believe that strong management of long-term financial and capital planning will be a key factor supporting rating stability. Near-term credit drivers center on the city's execution of the capital improvement plan (CIP).

The upcoming CIP will improve Ventura's water supply reliability, water quality, and disaster resiliency. Key projects include VenturaWaterPure, which will divert treated wastewater effluent to a new proposed Advanced Water Purification Facility (AWPF) for potable reuse, and a new State Water Project (SWP) interconnection that will allow the city to access this water and implement a blending strategy to improve its groundwater quality. We recognize that the first phase of the WaterPure project is not expected to be complete until fiscal 2026, which gives the city some time to phase in rate increases as the project comes online, however, the water system's financial metrics could weaken as the debt associated with the project begins amortizing thereafter.

We do not expect the VenturaPureWater project's production costs to be materially out of line with those of other recycled water projects currently under development across the state, which we consider credit supportive. Nevertheless, any political pushback related to the city's proposed rate plans or an erosion in the city's social capital due to revenue raising constraints in the context of the community's economic factors, would add downside risk to the rating.

The VenturaPureWater project is a joint undertaking with the city's wastewater fund. For more information on the wastewater system, please see our report published Jan. 17, 2023, on RatingsDirect.

Environmental, social, and governance

The city is faced with several ongoing ESG risk factors that affect our analysis. Considering near-term recessionary pressures, we believe there is heightened risk that the city's rates will rise faster than wealth and income levels for the area, which could create affordability risks. We consider this a key risk as the city forecasts that approximately 40% of its population is "low" income per the definition provided in Senate Bill 1087.

Given its location in Southern California, we believe the city also faces elevated environmental risk due to the region's inherent water supply scarcity, sea level rise and seismic exposure. Recent wildfires have affected the city's service area, and all damage to the water system's assets has been repaired. The electrical components that were damaged have been relocated to increase the distance to any vegetation, and we believe the city has well-defined emergency preparedness plans, including a multi-level cyber protection scheme.

Governance risk largely centers on litigation with the United Water Conservation District regarding the district's groundwater extraction charges. The city has challenged the district's groundwater extraction charges in court in each year since fiscal 2012. In 2020, a trial court ruled that the district's charges violated Proposition 26 and the district reached a settlement to pay the city $1 million. With the Supreme Court's August 2022 denial to review the district's appeal, the statute requiring the current three-to-one rate structure (municipal and industrial rates are three times that of agricultural users) has been ruled unconstitutional and the district must develop a new rate structure, which could result in additional refunds to the city.

Outlook

The stable outlook reflects our view that the city's pro forma financial metrics will remain credit supportive through the outlook period, despite a decline in debt service coverage (DSC) and negative economic headwinds.

Downside scenario

Should there be sustained deterioration in the water system's credit fundamentals, particularly a weakening in its financial capacity due to a significant increase in near-term capital needs that pressure the overall financial profile, we could revise the outlook to negative or lower the rating.

Upside scenario

We believe several factors constrain upward potential for the rating, including the system's planned large capital spending during the next decade, and a possible future reduction in groundwater production due to SGMA, seawater intrusion, or drought, absent the completion of the VenturaWaterPure and SWP projects.

Credit Opinion

San Buenaventura (population: 112,500), commonly referred to as Ventura, is approximately 65 miles northwest of Los Angeles and encompasses about 32 square miles. The water system's service area includes the entire city as well as certain adjacent unincorporated portions of the county. The water system provides service to a stable, primarily residential, and very diverse customer base. The city's population has been relatively stable during the past five years, and it is approximately 90% built out. Ventura has a diversified service economy, with employment opportunities in financial services, the nearby oil fields, and a well-developed food-processing industry. Although the city's agricultural presence adds some credit risk, the service area's mainly residential nature and very strong income indicators provide additional rating stability.

The city's water supply portfolio consists of a combination of pumped water from three groundwater basins, surface and subsurface water from the Ventura River, and water purchased from Casitas Municipal Water District, all of which has been adversely influenced by recent drought conditions. As certain city groundwater wells are located within groundwater water basins that are designated as high priority by the state of California due to overdraft conditions, we believe the city may be required to reduce its pumping to comply with the Sustainable Groundwater Management Act (SGMA). As such, the addition of the new VenturaWaterPure recycled water supply will mitigate this risk by providing a drought resilient source of supply that will (over time) comprise up to 20% of the city's overall supply. While the city has an annual entitlement to 10,000 acre-feet of water from SWP, it has never received water from the SWP because it has no direct connection to the SWP.

In our view, the city maintains good operational management practices and policies. We understand key utility staff is experienced in managing large-scale utility infrastructure projects. City procurement policies allow for construction manager at risk (CMAR) delivery, which mitigates risk-related to supply chain constraints, which we consider credit supportive.

The water system's historical financial metrics have been a key credit strength, with DSC exceeding 3.0x during the past three years. The city also maintained more than $95 million in cash on hand as of June 30, 2022; the strong cash balances help mitigate potential cost increases associated with the CIP. Our calculation of DSC includes fixed charges from the SWP and United Water's groundwater extraction charges. Our pro forma calculation of DSC indicates coverage falling to about 1.4x-1.5x through 2026, which we consider adequate for the rating level despite the decline from historical levels. Management expects unrestricted cash to exceed $50 million during this period, which we consider credit supportive.

Revenue and expense assumptions are reasonable, and management regularly tracks financial performance throughout the year, while presenting financial data to the city council on a quarterly basis. The city maintains formal policies relating to long-term capital planning as well as formal investment and liquidity policies. Financial and operational information is relatively easily obtained on an annual basis, as the city's budget and financial statements are readily available on the city's website.

We understand the city has adopted a rate plan in 2021, which incorporates 6%-7% per annum water rate increases through fiscal 2027, which incorporates reasonable cost assumptions. However, the combined water and wastewater CIP has increased in size and scope since the rate plan was adopted in 2022, and is up more than 40% from $469 million to $669 million, although we recognize that part of the increase is driven by management's conservatism.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022