S&P Global
Ratings

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Summary:

Woodbridge Irrigation District, California; Water/Sewer

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Credit Profile		
US$11.615 mil rev bnds (2022 Water System Refunding Revenue Bonds) ser 2022 dtd 04/05/2022 due 07/01/2043		
Long Term Rating	A+/Stable	New
Woodbridge Irr Dist WTRSWR		
Long Term Rating	A+/Stable	Outlook Revised
Woodbridge Irr Dist certs of part (2013 Refincg) (AGM)		
Unenhanced Rating	A+(SPUR)/Stable	Outlook Revised

Many issues are enhanced by bond insurance.

Rating Action

S&P Global revised its outlook to stable from negative and affirmed its 'A+' rating on Woodbridge Irrigation District, Calif.'s outstanding series 2013 water revenue certificates of participation (COP), which will ultimately be refunded with the proceeds of the series 2022 bonds. At the same time, S&P Global Ratings assigned its 'A+' long-term rating to the district's series 2022 water system refunding revenue bonds.

The outlook revision reflects the importance of the district's primary water supply to regional demand, its very strong financial position, and the predictability of revenues from its two largest customers--the cities of Stockton and Lodi. Nevertheless, we believe these strengths are partially offset by the heightened business risks from drought and water scarcity challenges that its agricultural customers increasingly face, which we consider a constraining credit factor. Although these customers contribute a relatively modest proportion of overall revenue, we understand the district has more flexibility to increase agricultural rates than it does to modify its municipal contracts.

We view the bond provisions as credit neutral. The bonds are payable from net revenue of the district's water system. Key bond provisions include a rate covenant set at 1.2x annual debt service and an additional bonds test set at 1.2x maximum annual debt service. The bonds will not be issued with a debt service reserve fund, which we do not consider to be a limiting credit factor given the district's extremely strong cash position. The district will have no other debt outstanding following this issuance.

Credit overview

The district is a supplemental water purveyor serving a small portion of San Joaquin County. The district has no direct retail customers and provides raw water primarily to agricultural customers. We consider the service area relatively limited, although we understand land is increasingly being converted to residential and commercial uses as neighboring cities grow and spur new housing demand. Most of the district's service area consists of vineyards for wine production and orchards.

The district has entered into agreements with East Bay Municipal Utility District (EBMUD), which operates major reservoirs on the Upper Mokelumne, which acknowledge the priority of some of the district's senior rights, such that in years with low forecasted runoff, EBMUD may curtail a portion of the district's water, a development that occurred in 2014, 2015, and 2021, and which we believe may occur with heightened frequency should the current drought remain prolonged.

Although low water years can adversely affect its agricultural customer base, only about 13% of the district's annual revenue comes from irrigation water fees, water standby and recharge fees. Most of the district's revenue (approximately 80%) comes from the combined water sales to the cities of Lodi and Stockton under long-term take-or-pay contracts. These contracts extend through 2047 and 2049, respectively, which we consider a stabilizing credit factor. Moreover, the Stockton water sales agreement will allow total diversions to Stockton to potentially double by 2025-2030, which would further bolster the district's financial position. We consider the existence of the two municipal contracts to be a key credit strength as both cities are required to pay their full contracted obligation (even under a drought scenario where deliveries to them are partially curtailed).

The rating further reflects our view of:

- The generally favorable characteristics of the district's primary water supply. It diverts water (up to 60,000 acre-feet a year) from the Mokelumne River under senior, pre-1914, appropriative rights. We consider this supply to be relatively low cost, and we believe it will rise in importance to its customers as groundwater pumping restrictions are adopted over time in the region. We also recognize that Mokelumne River is a comparatively more stable source than other regional surface water alternatives, such as the Central Valley Project or State Water Project.
- A relatively modest and concentrated customer base, with most of its water deliveries serving permanent crops within a 13,000-acre service area. The top 10 irrigation customers comprise approximately 51.9% of all irrigation water sales revenues for 2021. In our view, permanent crops represent a hardened demand for water that must be met each year, thus we believe its agricultural users may be exposed over time, especially to the extent implementation of the Sustainable Groundwater Management Act compels local groundwater markets to cap how much individual property owners can pump in the region, influencing both current and future supply reliability.
- Adequate credit quality of the district's municipal customers, Stockton and Lodi. Both municipal utilities have historically maintained very strong liquidity positions and pay their contractual obligations to the district quarterly. We consider Stockton's local economy to generally be weak, but broad and diverse in scope given that the city serves as the market center for the surrounding agricultural region. Although the city of Stockton filed for bankruptcy in 2012 (and emerged from bankruptcy protection on Feb. 25, 2015), we note that during the bankruptcy period, the court did not order a stay on water fund revenue and no water revenue was diverted to fund general government operations – moreover, payments to the district were not impacted by the bankruptcy.
- Extremely strong district-level financial performance as measured by debt service coverage (DSC) and liquidity, which we believe will be perpetuated at levels consistent with historical trends. DSC has surpassed 3.0x in each of the past five years and exceeds 1.8x even under a stress scenario that nets out revenue from either Stockton or Lodi. For the past five years, the district has kept unrestricted reserves of approximately 3.5x to 4.0x total expenses. The district's unofficial reserves policy is to maintain at least one year of total expenses in unrestricted reserves; and
- Lack of additional debt plans to fund capital projects, according to management.

The stable outlook reflects our believe that the district's municipal contracts will provide revenue stability despite the likelihood of future variability in water deliveries during drought conditions.

Environmental, social, and governance

As mentioned, the district faces several elevated environmental risk factors that influence our analysis. In our view, accelerating water shortages may broadly influence agricultural production in California and potentially lead to the permanent idling or conversion of farmland. While the district is the sole provider of surface water for irrigation within its service area, certain agricultural customers within the district can utilize pumped groundwater through their own groundwater wells. The California Department of Water Resources has identified the Eastern San Joaquin Groundwater Subbasin (which is where the district is located) as one of the state's 21 critically over-drafted subbasins and we understand the entire basin must achieve groundwater sustainability within 20 years. Given the complexities of supplemental water procurement and agricultural water conservation to meet this goal, having robust planning and a management team with commensurate skill and experience in the water industry will be important to credit quality. Despite the environmental risks, we believe social and governance risks are neutral considerations in our credit analysis.

Stable Outlook

Downside scenario

We could take a negative rating action if either the district's or its municipal customers' financial position deteriorates significantly, such as from unanticipated increase in water supply costs or an extraordinarily large change in capital plans (without timely rate adjustments).

Upside scenario

While unlikely to occur during the two-year outlook period, we could raise the rating if the service area demonstrates robust economic diversification.

Related Research

Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020