

Research Update:

McKinney, TX Series 2025 Waterworks And Sewer System Revenue Bonds Rated 'AA+'; Outlook Stable

April 24, 2025

Overview

- S&P Global Ratings assigned its 'AA+' rating to McKinney, Texas' roughly \$26.4 million series 2025 waterworks-and-sewer-system revenue bonds.
- At the same time, S&P Global Ratings affirmed its 'AA+' rating on the city's existing waterworks-and-sewer-system revenue bonds.
- The outlook is stable.

Rationale

Security

Net water-and-sewer-system revenue secures all revenue debt.

Officials intend to use series 2025 bond proceeds to finance various water-and-wastewater improvements citywide. Post series 2025 issuance, the combined system will have roughly \$289.7 million of utility revenue-supported debt outstanding as of fiscal year-end 2025.

Credit highlights

The rating reflects our opinion of the systems' strong and diverse economy, in one of the nation's fastest-growing regions; this has boosted the utility's improved finances, underpinned by consistent customer growth and sound financial prudence. On a senior-lien basis, not including fixed costs from the city's wholesaler, debt service coverage (DSC) has averaged 2x during the past three years.

McKinney has been proactively updating its rate study annually for the past several years to primarily account for increasing pass-through costs from North Texas Municipal Water District (NTMWD). The city adopted rate increases of 2% and 9% for the water-and-wastewater systems, respectively. Management updates the rate study every year, and it intends to complete the rate study update in fiscal 2025. During the next few years, management plans to adopt rate increases between 7% and 10% to pass through wholesale rate increases and

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maintain all-in DSC in-line with current levels. The utility's solid liquidity supports its finances with 241 days' operating cash on hand in fiscal 2024, coupled with no plans for significant draws during the coming years. We believe management's oversight of costs from NTMWD and the potential effect on system operations and all-in DSC will likely be imperative to sustain the rating at the current level.

The water-and-sewer systems' five-year capital improvement program (CIP), which totals \$477 million for fiscal years 2025-2029, is due primarily to growth projects. McKinney expects to issue about \$175 million of water-and-sewer revenue bonds to fund its CIP with near-term debt plans of \$85 million and \$45 million for fiscal years 2026 and 2027, respectively. The current CIP also identifies about \$150 million of grant funding. We understand management will likely fund the remainder of the CIP with cash, but management communicates it does not currently plan to spend down liquidity significantly.

The rating also reflects our view of the systems':

- Rapidly growing, predominantly residential customer base, characterized by above-average income and consistently growing population and customer accounts, albeit with relatively affordable, but slightly elevated, utility rates compared with its peers--We think this will likely continue to increase modestly since we expect additional rate increases;
- Recently improved finances, guided by annual rate increases, resulting in three years of all-in DSC of more than 1.2x, further supported by steadily growing liquidity, which we expect it will likely sustain--Our all-in DSC metric incorporates the city's take-or-pay agreement with NTMWD, which we consider debtlike in nature;
- Low debt load--However, we expect the system will likely become increasingly leveraged as it issues debt to fund its growth-driven CIP; and
- Good operational and financial management practices, highlighted by its well-embedded asset-adequacy-identification program and appropriate drought-contingency and conservation plans, as well as its formal policies, rate-setting autonomy, and robust long-term operating and capital planning--We believe the distribution-only water system and collection-only wastewater system decrease operational risk.

Environmental, social, and governance

Overall, we consider environmental, social, and governance factors neutral in our credit analysis. McKinney adopts; adheres to; and adjusts operating and financial policies and procedures, including state and federally mandated. The utility has had neither fines nor penalties nor has it received any regulatory actions. Social factors surrounding rate affordability and governance risk surrounding rate-raising autonomy are heightened in that the systems' depend on NTMWD for potable water and sewage treatment; however, current affordable rates, in the context of the service area's above-average income, provide some cushion before affordability is likely to become a concern. Governance for the city is above average, including a high level of planning; risk management; and robust state oversight, which mitigate potential operating and financial risk for both systems. Managerial practices include cybersecurity protocols.

Outlook

The stable outlook reflects S&P Global Ratings' opinion that the system's overall credit characteristics will likely remain consistent with historical trends, including sustained all-in DSC

improvement based on appropriate rate increases to offset increasing NTMWD costs, coupled with stability in the systems' economic fundamentals and rate affordability.

Downside scenario

We could lower the rating if rate increases were to insufficiently provide the necessary revenue to sustain improved all-in DSC, particularly if fixed costs from NTMWD or capital expenses were to become unmanageable, leading to deteriorated all-in DSC or liquidity.

Upside scenario

While unlikely, we could raise the rating if there were strong and sustained all-in DSC growth higher than historical trends, coupled with the maintenance of current liquidity and an extremely strong enterprise-risk profile.

McKinney, Texas--economic and financial data

	Most recent	Fiscal year-end			
		2024	2023	2022	Median (AA+)
Economic data					
MHHEBI of the service area as a % of the U.S.	144				112
Unemployment rate (%)	3.2				3.4
Poverty rate (%)	4.8				10.2
Water rate (6,000 gallons or actual) (\$)	99.2				33.9
Sewer rate (6,000 gallons or actual) (\$)	86.3				38.6
Annual utility bill as a % of MHHEBI	2.4				1
Operational management assessment	Good				Good
Financial data					
Total operating revenue (\$000s)		152,544	137,793	123,385	41,982
Total operating expenses less depreciation (\$000s)		122,112	106,980	92,379	31,740
Net revenue available for debt service (\$000s)		51,915	44,104	31,006	--
Debt service (\$000s)		23,619	21,009	19,170	--
S&P Global Ratings-adjusted all-in DSC (x)		1.4	1.4	1.2	2.5
Unrestricted cash (\$000s)		80,471	62,642	53,240	55,536
Days' cash of operating expenses		241	214	210	650
Total on-balance-sheet debt (\$000s)		317,717	265,701	235,709	74,352
Debt-to-capitalization ratio (%)		32	30.2	31.2	25
Financial management assessment	Strong	--	--	--	Good

Note: The most recent economic data available from our vendors. MHHEBI--Median household effective buying income. DSC--Debt service coverage.

Ratings List

New Issue Ratings

US\$26.405 mil wtrwrks and swr sys rev and rfdg bnds ser 2025 dtd 05/15/2025 due 03/15/2045

Long Term Rating AA+/Stable

Ratings Affirmed

Ratings List

Water & Sewer

McKinney, TX Water and Sewer System	AA+/Stable
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The ratings appearing below the new issues represent an aggregation of debt issues (ASID) associated with related maturities. The maturities similarly reflect our opinion about the creditworthiness of the U.S. Public Finance obligor's legal pledge for payment of the financial obligation. Nevertheless, these maturities may have different credit ratings than the rating presented next to the ASID depending on whether or not additional legal pledge(s) support the specific maturity's payment obligation, such as credit enhancement, as a result of defeasance, or other factors.

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