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Summary:

Metropolitan Water Reclamation District of Greater Chicago, Illinois; General Obligation

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Credit Profile

US\$166.865 mil GO ltd tax rfdg bnds ser 2021C due 12/01/2032		
<i>Long Term Rating</i>	AA/Stable	New
US\$113.555 mil GO unlted tax rfdg bnds taxable ser 2021E due 12/01/2033		
<i>Long Term Rating</i>	AA/Stable	New
US\$111.585 mil GO ltd tax cap imp bnds (green bnds) ser 2021A due 12/01/2051		
<i>Long Term Rating</i>	AA/Stable	New
US\$46.28 mil GO unlted tax rfdg bnds (alternate rev source) taxable ser 2021F due 12/01/2041		
<i>Long Term Rating</i>	AA/Stable	New
US\$31.715 mil GO unlted tax rfdg bnds ser 2021D due 12/01/2031		
<i>Long Term Rating</i>	AA/Stable	New
US\$30.0 mil GO unlted tax cap imp bnds (green bnds) ser 2021B due 12/01/2036		
<i>Long Term Rating</i>	AA/Stable	New

Rating Action

S&P Global Ratings assigned its 'AA' long-term rating to Metropolitan Water Reclamation District of Greater Chicago (MWRD), Ill.'s anticipated \$500 million general obligation (GO) debt issuance, consisting of:

- \$111.585 million 2021 series A GO limited tax capital improvement bonds (green bonds);
- \$30.00 million 2021 series B GO unlimited tax capital improvement bonds (green bonds);
- \$166.865 million 2021 series C GO limited tax refunding bonds;
- \$31.715 million 2021 series D GO unlimited tax refunding bonds;
- \$113.555 2021 taxable series E million GO unlimited tax refunding bonds; and
- \$46.280 2021 taxable series F GO unlimited tax refunding bonds (alternate revenue source)

All amounts are anticipated and subject to change. At the same time, S&P Global Ratings affirmed its 'AA' rating on the MWRD's existing general obligation (GO) debt. The outlook is stable.

The 2021 series A and B bond proceeds will fund various capital projects that the obligor defines as "green" that involve pollution and flood control, open space restoration, and implement other sustainable and resilient practices with respect to water, phosphorus, biosolids and energy regulations and usage. The MWRD's designation of the notes as "green" is self-designated and immaterial to our credit rating analysis. We do not review or monitor use of proceeds, the process for project evaluation and selection, the management of proceeds, or any ongoing reporting related to the

eligible "green" projects in the assignment or surveillance of our credit ratings. We do not believe the "green" designation alters the transaction's credit risk profile. The various refunding bonds will allow the district to shorten the average life of the bonds slightly while smoothing out future debt service, achieve interest cost savings, and allow for flexibility for future issuance. Officials plan to fund capital needs with bond proceeds from this issue as well as through the state revolving loan program. Officials do not plan another bond issuance until 2025, tentatively estimated at \$111 million.

We rate the MWRD's limited-tax GO debt on par with the obligor's general creditworthiness as reflected in the rating on the unlimited-tax GO bonds under our linked ratings criteria, "Criteria FAQ: S&P Global Ratings' Approach To Rating U.S. Local Government Bonds Secured By Dedicated Limited Ad Valorem Tax Pledges", published Feb. 5, 2018, on RatingsDirect. The fungibility of resources, and the ability to manage those resources, determine our view of the obligor's ability and willingness to pay.

The MWRD's GO alternate revenue source bonds are secured by its unlimited-tax GO pledge and revenue from its stormwater management tax revenue fund. The bonds are rated based on the MWRD's GO pledge.

Credit overview

MWRD provides flood control and wastewater treatment in a treatment area encompassing roughly 882 square miles. This consists mostly of Cook County, including Chicago and 128 suburbs, with a population of over 5 million. MWRD's primary challenge in its budget, in our view, is absorbing continuing pension contributions in a climate of tepid revenue growth, given that its budget is mainly property tax funded. While the MWRD is not seeking revenue increases that go beyond statutory limits, we note that local taxpayers are facing growing tax burdens from a variety of jurisdictions, which may contribute to future revenue softness and taxing considerations.

For our latest U.S. economic forecast, see "Economic Outlook U.S. Q4 2021: The Rocket Is Leveling Off", published Sept. 23, 2021, on RatingsDirect.)

The 'AA' rating also reflects our view of the MWRD's:

- Participation in the deep and diverse Chicago metropolitan area economy, with good incomes and extremely strong per capita market value;
- Limited purpose nature with inherent expenditure flexibility; and
- Moderate debt burden with limited future debt needs.

Environmental, social, and governance factors

We believe MWRD's capital plans and mission to improve water quality, protect properties from flood damage, and sustainability and resiliency plans, as they are implemented, set it on the path to mitigate environmental risk and we view its social risk as in line with those of the sector. We believe that the MWRD's governance risk is elevated compared to sector standards due to its weakly funded pension plan.

Stable Outlook

Downside scenario

Should the MWRD draw down on its reserves significantly, to levels below its target, or it amends or pauses its policy with respect to funding its pensions, and we believe its financial operations are compromised, we could lower the rating.

Upside scenario

If the MWRD's future pension contributions remain manageable, while it maintains or improves on other relevant credit factors, we could raise the rating.

Credit Opinion

Large and stable service area that encompasses Cook County

MWRD's tax base has a value of \$170.9 billion in levy year 2020, and it is very diverse and steadily growing. Property tax revenue is trending steadily upward and collections are strong. Due to COVID-19 and related stay-at-home orders, unemployment peaked at a very high 18.1% in April 2020, and ended the year with an average 11.1% unemployment rate, which we consider high. As of July 2021, the unemployment rate was 8.8%.

Finances are sound, but fitting pension contributions into the budget could prove challenging

MWRD's fiscal year end is Dec 31. For the 2021 fiscal year, officials anticipate ending the year with an estimated \$48.7 million corporate fund surplus. Officials plan to adopt a 2022 budget calling for a modest \$28.3 million deficit, or 7% of the budget.

About 67% of fiscal 2020 general fund revenue, or \$252 million, is from property taxes, which remain sound through fiscal 2021. The general fund collects user charges from tax exempt entities and heavy users, and land rentals, both of which are steady and account for 20% of annual revenue, followed by personal property replacement taxes (PPRT) of \$22.5 million or 6%, which are more economically sensitive in nature. As a non-home rule entity, the MWRD's revenue raising capability is fairly limited; property tax revenue growth is subject to the property tax extension limitation law, which allows for year-over-year revenue growth of 5% or the rate of inflation, whichever is less. Officials forecast overall revenue growth will be sizeable at roughly 5% in 2022 and 2023, followed by steady 4% year-over-year growth through 2026. MWRD is not eligible for CARES Act or American Rescue Plan Act (ARPA) federal stimulus funding. After a large 7% increase in 2022, expenses follow a slower rate of growth of 2% or less after 2023.

We believe these trends position the MWRD to continue to meet its pension funding policy, which calls for contributions in excess of the actuarially determined contributions. The supplemental contributions were incorporated in the 2021 budget and \$30 million is planned for 2022. Given the funding levels of the pension plan, we anticipate contributions will continue to rise and could pressure the budget, especially since revenue raising flexibility is limited. However, MWRD officials have a history of managing discretionary expenditures and we expect fiscal balance will be maintained in 2021 and 2022.

Fiscal 2020 ended with a positive, \$20.6 million net change in general corporate fund balance. The available fund

balance (which excludes nonspendable reserves but includes restricted reserves) of \$256 million at the close of fiscal 2020 is equal to a very strong 74% of expenditures. We expect general fund reserves will remain very strong in 2021 given the expected surplus, which will be partly offset by a subsequent use of reserves in the 2022 budget.

Sound financial management

The budget is constructed using historical information and forecasts from external sources. The board receives quarterly updates of revenue and expenditure performance. The annual budget includes a five-year forecast and capital improvement plan. Long-term capital planning looks out five years and 30 years. MWRD has policies that guide reserve levels in the corporate fund, working cash fund, and reserve claim fund, all geared toward ensuring cash flows in the event of unanticipated revenue fluctuations.

Manageable and moderate debt burden with modest future capital needs

MWRD has \$2.8 billion of total debt outstanding. We consider the district's overall debt burden moderate at \$4,332 per capita and 4.3% of market value. Amortization is slower than average, with 47% of debt service due to be retired within 10 years. Debt service carrying charges are elevated at 34% of total governmental funds' expenditures, reflecting the limited-purpose nature inherent in an issuer of this type.

MWRD's primary operations revolve around operating and maintaining seven wastewater treatment plants (including one of the world's largest at Stickney, Ill.) and 560 miles of intercepting sewers and force mains. MWRD's five-year capital improvement plan totals \$787 million, with most funded from bonds and loans from the Illinois Environmental Protection Agency, the state revolving fund, and a planned \$111 million of general obligation issuance in 2025. The debt service extension base is currently \$175.5 million, and MWRD has capacity to issue additional limited tax debt.

Pension and other postemployment benefits liabilities are not bearing acute financial pressure, but longer-term risks exist

Pension and OPEB contributions accounted for 11% of total governmental funds expenses in fiscal 2020 and are likely to increase. We believe that pension and OPEB liabilities represent:

- A potentially worsening medium-term source of credit pressure that could weigh on its budget performance, particularly in light of the currently weak revenue climate.
- MWRD's single-employer defined benefit pension plan is poorly funded and growing pension contributions could add to budgetary stress each year, despite management's policies and efforts.
- OPEB costs are not currently pressuring the MWRD. We note MWRD has adopted a policy with the intention to fully fund the plan by 2026.

MWRD participates in the following plans as of its Dec. 31, 2020 audit:

- MWRD Retirement Fund: 57% funded, with a net pension liability of \$1.15 billion.
- MWRD Retiree Health Care Benefit Plan, a single-employer, defined benefit OPEB plan, which is 76% funded with a net liability of \$72.2 million.

MWRD's actuarially determined contributions (ADC) for its pension plan are sized to exceed the 90% state requirement; instead, the goal is to reach 100% funding by 2050. Since the MWRD adopted its pension funding policy

in 2013, it has contributed amounts in excess of the ADC. Most recently, in 2020, the total actual contribution was about \$87 million, which was \$22 million above the \$65 million ADC. However, despite these efforts, the actual minimum funding progress for the plan in 2020 was 70% and static funding was 97%, meaning contributions were not large enough to cover the present value of current-year benefits and interest on unfunded liabilities. The plan's somewhat long, 30-year closed amortization, a level 3% payroll growth assumption, and 7.25% discount rate, above our 6% baseline threshold, could lead to contribution volatility and slower than desired progress in improving funding levels. This indicates that despite the larger contributions made by the MWRD, its progress in improving funding levels will take time, and in the meantime, they face contribution volatility, even if smoothed over multiple fiscal years.

Related Research

- Through The ESG Lens 2.0: A Deeper Dive Into U.S. Public Finance Credit Factors, April 28, 2020
- Credit Conditions: U.S. Regions' Economies Perk Up As The Pandemic's Impact Ebbs, April 16, 2021
- Credit FAQ: Financial Management Assessment In U.S. Public Finance, June 27, 2006
- Criteria Guidance: Assessing U.S. Public Finance Pension And Other Postemployment Obligations For GO Debt, Local Government GO Ratings, And State Ratings, Oct. 7, 2019

Ratings Detail (As Of November 4, 2021)		
Metro Wtr Reclamation Dist of Greater Chicago GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Metro Wtr Reclamation Dist of Greater Chicago GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Metro Wtr Reclamation Dist of Greater Chicago GO cap imp bnds unlt'd taxser 2011C due 12/01/2038		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Metro Wtr Reclamation Dist of Greater Chicago GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Metro Wtr Reclamation Dist of Greater Chicago GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed
Metro Wtr Reclamation Dist of Greater Chicago GO		
<i>Long Term Rating</i>	AA/Stable	Affirmed

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