S&P Global Ratings

RatingsDirect®

Summary:

South Dakota Conservancy District; State Revolving Funds/Pools

Primary Credit Analyst:
Gregory Dziubinski, Chicago + 1 (312) 233 7085; gregory.dziubinski@spglobal.com

Secondary Contact:
Scott D Garrigan, New York (1) 312-233-7014; scott.garrigan@spglobal.com

Table Of Contents

Summary:

South Dakota Conservancy District; State Revolving Funds/Pools

Credit Profile		
US$77.985 mil st revolving fd prog bnds ser 2020 due 08/01/2042		
Long Term Rating	AAA/Stable	New
South Dakota Conserv Dist (State Revolving Fd Prog)		
Long Term Rating	AAA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AAA' rating and stable outlook to South Dakota Conservancy District's (SDCD) roughly $77.985 million series 2020 state-revolving-fund program bonds and affirmed its 'AAA' rating, with a stable outlook, on SDCD's existing state-revolving-fund program bonds.

Officials intend to use series 2020 bond proceeds to fund new and existing loans to Sioux Falls under the clean water program and pay issuance costs.

Because we view securitizations backed by pools of public-sector assets as highly sensitive to national risk, we cap the rating on the securitization at two notches above the U.S. sovereign rating. We, however, do not apply any specific sovereign default stress because the U.S. sovereign rating is 'AA+'.

Repayments made under pledged loan agreements and other various funds pledged under the master indenture secure the bonds. SDCD does not issue separate state-match and leveraged series bonds for each program, but it separates each series into a state-match and leveraged portion for each program as applicable. SDCD segregates principal-and-interest payments from loan agreements: Interest payments secure the bonds' state-match portion with principal payments and excess interest payments after SDCD pays state-match debt service securing the bonds' leveraged portion.

Credit overview

Following mobility restrictions and the closure of large segments of the economy due to COVID-19 and the swift onset of a related recession, all of S&P Global Ratings' U.S. public finance sector outlooks are now negative. (For further information, please see the article, titled "All U.S. Public Finance Sector Outlooks Are Now Negative," published April 1, 2020, on RatingsDirect.)

For long-term municipal pools, the majority of underlying cash flow, either pledged for bond repayment or guaranteed by the programs, originates from U.S. public-finance-asset classes. Excess cash flow, however, well beyond what SDCD needs to pay state-revolving-fund bond debt service currently acts as a cushion to downside pressure.

The rating reflects our opinion of the combination of extremely strong enterprise- and financial-risk scores, reflecting

SDCD's:

- Market position, reflecting support from multiple levels of government that creates growing equity;
- Collateralization that allows the program to absorb very high borrower defaults, resulting in extremely strong loss coverage;
- Extremely low historical borrower defaults and delinquencies; and
- Strong financial management policies and practices under our Financial Management Assessment (FMA) methodology.

The stable outlook reflects S&P Global Ratings' expectation that the pool's diversification will likely continue and that SDCD will likely manage its loan-origination process to provide sound protection against loan-default risk. We think debt service coverage (DSC) and available reserves will likely continue to provide substantial protection against loan delinquencies or defaults. The outlook also reflects S&P Global Ratings' expectation that SDCD's strong loan-portfolio management will likely continue and that collateralization will likely sustain very high DSC of potential defaults and delinquencies.

Environmental, social, and governance (ESG) factors

We have analyzed SDCD's overall ESG risks relative to its economy, management, budgetary outcomes, and debt-and-liability profile and determined all are in-line with our view of the sector standard.

Stable Outlook

Downside scenario

We do not currently expect to lower the rating because DSC solely from loan revenue provides a strong cushion for potential defaults.

Credit Opinion

Enterprise risk

We consider SDCD's enterprise-risk score extremely strong due to the combination of low industry risk and extremely strong market position. Ongoing support from state and federal sources leads to growing equity available for additional loan activity.

The state created SDCD in 1959 for planning, developing, and managing the use and conservation of water resources. A seven-member Board of Water And Natural Resources governs SDCD; the board sets certain policies for South Dakota Department of Environment & Natural Resources, including water policies and the state water plan. The governor appoints board members. South Dakota Department of Environment & Natural Resources employees serve as SDCD's staff, performing administrative functions.

Financial risk

We consider SDCD's financial-risk profile extremely strong. SDCD achieves overcollateralization through annual revenue structured well in excess of annual debt-service costs and surplus revenue generated from prior-year cash flow. For clean and drinking water, minimum annual DSC just from loan revenue exceeds 1.3x in all years; it generally grows stronger during the course of the debt-amortization schedule. SDCD currently has about $254 million of available cash and investments in various funds. If it cannot draw cash from various investments to make timely debt-service payments, available cash flow from annual loan repayments provides enough of a cushion, in our view, that bond payments would not necessarily be impaired. SDCD uses portions of these funds to make additional loans, so loan revenue recycles back into the program to provide additional DSC.

The pool's cross-collateralization mechanism helps cushion the pool further from loan-default risk. If loan interest payments are insufficient to pay debt service on the bonds' state-match portion, SDCD can use excess interest payments from the clean- or drinking-water program. If loan principal payments are insufficient to pay debt service on the bonds' leveraged portion, SDCD can use excess principal-and-interest payments from the clean- or drinking-water program. Federal law does not allow the use of loan principal payments for the bonds' state-match payments; this is why the cross-collateralization mechanism does not permit excess loan principal payments for the bonds' state-match debt service.

Including the series 2020 bonds, SDCD has roughly $386 million of state-revolving-fund bonds outstanding; 575 loans, either outstanding or pending, with more than $800 million of principal due support this. The borrower portfolio includes loans to 192 separate entities, but some entities have loans with different pledges. The largest borrower is Sioux Falls with $229 million of existing and future loans payable, accounting for 29% of all loans. There have been no loan defaults or delinquencies for the past 12 months. Loan agreements require the borrowers using utility revenue pledges to maintain 1.1x DSC and a 1.1x rate covenant. Sales tax pledges require 1.2x DSC.

Management

We consider SDCD's financial management policies and practices strong under our FMA methodology, indicating financial practices are strong, well embedded, and likely sustainable.

SDCD management prepares and updates its intended use plan annually, including the project priority list. It ranks projects and funds them in order of priority. SDCD staff evaluates the creditworthiness of potential borrowers, and borrowers must meet minimum DSC depending on the security. Once funded, annual reporting loan requirements include financial statement and DSC certificates.

SDCD has an investment-management policy in its master-trust indenture. The policy generally restricts investments to U.S. treasuries and agencies, certificates of deposit, money-market funds, and other investments either collateralized or with investment-grade counterparties.

Related Research

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