FitchRatings

Fitch Rates Washington Metropolitan Area Transit Authority's $496.5MM Gross Revenue Bonds 'AA-'

Fitch Ratings-New York-24 July 2017: Fitch Ratings has assigned a 'AA-' rating to the following bonds to be issued by the Washington Metropolitan Area Transit Authority (the Authority or WMATA):

--$496.5 million gross revenue transit bonds, series 2017B.

The Rating Outlook is Stable.

Proceeds will be used to fund various capital costs of the Authority. The bonds are scheduled for sale via negotiation during the week of July 31.

SECURITY
The bonds are payable from a gross lien on all transit system operating revenues and jurisdictional allocations received by the Authority from the District of Columbia, and the participating local governments within the WMATA transit zone. The participating local governments, within the Commonwealth of Virginia, are: the cities of Alexandria, Falls Church and Fairfax, the counties of Arlington and Fairfax, and political subdivisions located within those counties; and, within the state of Maryland: the counties of Montgomery and Prince George's, and political subdivisions of the state located within those counties.

KEY RATING DRIVERS
Analytical Conclusion: The 'AA-' rating reflects the Authority's strong legal and regulatory framework resulting from its creation through an interstate compact, which grants it sovereign-like powers and exemption from all laws and orders of its signatories, except those pertaining to inspection of equipment and facilities, safety and testing; use of streets, highways, and vehicular facilities; traffic control and regulation; zoning; signs and buildings.

Although the Authority does not have a dedicated tax revenue source and has suffered from a failure to adequately fund system maintenance, Fitch believes that WMATA's revenue structure is inherently strong. This is highlighted by the fiscal support of its operating and capital budget from highly rated state and local governments pursuant to the interstate compact. Other strengths center on WMATA's quasi-monopolistic provision of highly essential transit services and an underlying economy that supports a solid long-term ridership base. The Authority's financial leverage is very low, with net debt and other long-term liabilities to gross pledged transit revenues measuring 1.7x after this sale and exceptionally high coverage of projected maximum annual debt service (MADS).

Rating weaknesses center on the Authority's significant unfunded capital needs. WMATA has identified $1.5 billion in annual investment over the next 10 years solely to maintain system reliability and safety. WMATA has been plagued by internal control and management weaknesses, an inability to make sufficient investment in system infrastructure, and a series of rail accidents that have led to lower ridership and fare revenue. While WMATA has worked to correct these weaknesses, they combine to create a weak overall budget position that has resulted in the use of capital funds to cover operating expenses and an increase in jurisdictional subsidies.

REVENUE DEFENSIBILITY - STRONGER: WMATA's revenue framework is underpinned by the fiscal support provided by various state and local governments for its operating and capital budget. The obligation of these entities is framed in the multijurisdictional compact but ultimately subject to annual appropriation. Fitch's rating assumes continuation of financial support by the participating jurisdictions given the critically important nature of WMATA transit assets to the regional economy and the respective jurisdictions' high credit quality.

The remainder of WMATA's operating resources is largely derived from passenger fares over which the Authority has full legal rate control. Current fares are considered economical but future increases may be subject to increasing political and passenger resistance as the Authority deals with a loss of confidence in system reliability and safety and recent ridership declines. The strength of the underlying economy combined with the region's significant congestion problems should support ridership over the long term.

OPERATING RISK - MIDRANGE: Labor and fringe benefit costs consume the bulk of WMATA's budget. The Authority retains full legal control to reduce its workforce but it is otherwise constrained by collective bargaining agreements and a labor framework featuring binding arbitration. The cost of labor and fringe benefits has outpaced growth in fare revenues, requiring higher subsidy support. Capital needs are significant with an estimated $15.5 billion needed over the next 10 years to maintain system reliability and safety. The capital plan faces a funding gap of more than $6 billion which could result in a material increase in long-term liabilities and fixed budgetary costs.

FINANCIAL PROFILE - STRONGER: WMATA's leverage position is very low, which provides capacity to fund its substantial capital program at the current rating level. Fitch's financial profile assessment reflects the protection afforded bondholders from the gross lien on revenue and the Authority's status as an interstate compact, the effect of which, in Fitch's opinion, is to make the Authority not subject to bankruptcy or other insolvency proceedings.

Net debt and other long-term liabilities to gross pledged revenues was measured at 1.3x in FY2016 (and 1.7x following this issuance) and roughly 2.1x (or 2.4x) in Fitch's rating case scenario. Gross pledged revenues in FY2016 were approximately $1.7 billion, or more than 11x MADS on outstanding parity debt.

WMATA is required to annually adopt a balanced operating budget where operating revenues and subsidies equal expected operating expenses for the fiscal year. Financial results have been variable in recent years and the Authority has addressed recent years' funding gaps with increased subsidy support, significant staff reductions, and use of capital funds for preventative maintenance activities, among other management initiatives.

RATING SENSITIVITIES
Governmental Support: Evidence of decline in the level of fiscal support to WMATA by the participating jurisdictions would accentuate other areas of revenue and operating risk and likely result in a rating downgrade.

Capital Investment Outlook: WMATA's ability to fund and execute its substantial capital program and maintain the system in an ongoing state of good repair would alleviate the Authority's long-term operating risk and be viewed as a positive rating factor.

System Essentiality: Shifts in our view of WMATA's essentiality to the regional economy driven by sustained declines in ridership, loss of political support, or other factors would pressure the rating.

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In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis and InvestorTools.

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Additional information is available on www.fitchratings.com

Applicable Criteria
Rating Criteria for Public Sector Revenue-Supported Debt (pub. 05 Jun 2017) (https://www.fitchratings.com/site/re/898969)

Additional Disclosures
Solicitation Status (https://www.fitchratings.com/site/pr/1026946#solicitation)
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