

FITCH RATES MASSACHUSETTS WATER RESOURCES AUTHORITY'S \$368MM REVS 'AA'; OUTLOOK STABLE

Fitch Ratings-New York-26 January 2009: Fitch Ratings assigns an 'AA' rating to the Massachusetts Water Resources Authority's (MWRA or the authority) approximately \$98 million general revenue bonds, 2009 series A and \$270 million general revenue refunding bonds, 2009 series B. The bonds are scheduled for negotiated sale the week of Feb. 2, 2009. Proceeds from the 2009 series A bonds will fund new capital projects and proceeds from 2009 series B bonds will refund outstanding commercial paper as well as outstanding parity debt for savings. In addition, Fitch affirms the 'AA' rating on MWRA's \$3.1 billion of outstanding general revenue bonds and the 'AA-' rating on MWRA's \$1.4 billion of subordinated general revenue bonds. The Rating Outlook for all bonds is Stable.

The long-term 'AA' and 'AA-' rating on MWRA's senior and subordinate lien bonds, respectively, is based on MWRA's sound financial operations and operating track record. Effective financial management is demonstrated by the authority's ability to achieve favorable operating results despite volatility in Commonwealth debt service assistance. Furthermore, the authority maintains prudent budgetary practices, comprehensive long-term planning, and vigilant project oversight and prioritization of its capital improvement program (CIP). Leveraging associated with the authority's historical capital spending is high and will remain so for some time. However, the rate of future leveraging is expected to slow considerably as the authority's CIP continues to transition from court-mandated projects to ongoing rehabilitation. Reserves are expected to remain strong despite amendments to the bond indenture, and strong debt service coverage is expected to continue. Rates charged by the authority are among the highest in the urban U.S. and remain one of the most significant credit vulnerabilities. However, this credit risk is mitigated somewhat by the above-average wealth levels of the service areas and the impeccable collections rates at 100% since the authority's inception.

MWRA provides wholesale water and wastewater services to 61 communities located primarily in eastern Massachusetts. Approximately 2.8 million people (or 43% of the total population of the commonwealth) reside in the authority's service areas, the largest of which is the city of Boston which contributes nearly one-third of MWRA's revenue derived from rates and charges. The service areas are economically diverse generally, and wealth levels are above state and national averages.

Although partially mitigated by higher income levels throughout much of the service area, MWRA's elevated rates continue to be a credit concern. Due in large part to annual increases in commonwealth debt service assistance from fiscal years 2004-2008, rate hikes have been moderate ranging from 4%-5% annually over the period. The fiscal 2009 adopted budget included a manageable 4.5% increase assuming the anticipated receipt of \$11.2 million in debt service assistance from the state. However, mid-year cuts in the state's budget eliminated the expected appropriation for MWRA. While state assistance typically accounts for less than 4% of total operating revenues, projected annual rate increases of 5.7% through fiscal 2014 are likely to be slightly higher assuming the revenue enhancement from the commonwealth is not restored.

Despite the volatility in the state assistance, financial operations are healthy and historical debt service coverage is solid. Senior lien debt service coverage in fiscal 2008 was slightly better than 2.0 times (x), and equal to 1.2x with the inclusion of subordinate-lien debt obligations. Financial projections through fiscal 2014 indicate comparable debt service coverage. Prudently, the authority maintains multiple reserve funds used to minimize rate increases and redeem outstanding bonds. Overall, the authority maintains ample liquidity.

Following the massive capital investments undertaken during the 1990s, MWRA's focus is now increasingly on combined sewer overflows (CSOs), regulatory compliance, and system rehabilitation and maintenance. The adopted fiscal years 2009-2013 CIP totals approximately \$1.1 billion and addresses substantially all current regulatory compliance issues. The current CIP is

significantly lower than in prior years, partially reflecting the notable scale of capital spending utilized for the clean-up of Boston Harbor and the completion of over 50% of the CSO master plan. Fitch believes future capital costs should remain manageable given MWRA's vigilant project oversight and its board's existing self-imposed spending cap.

Contact: Christopher Hessenthaler +1-212-908-0773, New York, or Doug Scott +1-512-215-3725, Austin.

Fitch issued an exposure draft on July 31, 2008 proposing a recalibration of tax-supported and water/sewer revenue bond ratings which, if adopted, may result in an upward revision of this rating (see Fitch research 'Exposure Draft: Reassessment of the Municipal Ratings Framework'.) At this time, Fitch is deferring its final determination on municipal recalibration. Fitch will continue to monitor market and credit conditions, and plans to revisit the recalibration in the first quarter of 2009.

Media Relations: Cindy Stoller, New York, Tel: +1 212 908 0526, Email: cindy.stoller@fitchratings.com.

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