

CREDIT OPINION

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Contacts

Lauren Dahan +1.212.553.4491
Vice President - Senior Analyst
lauren.dahan@moodys.com

Orlie Prince +1.212.553.7738
Associate Managing Director
orlie.prince@moodys.com

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Americas 1-212-553-1653

Asia Pacific 852-3551-3077

Japan 81-3-5408-4100

EMEA 44-20-7772-5454

Virginia Beach (City of) VA Water & Swr Ent

Update following assignment of positive outlook

Summary

[Virginia Beach, VA's water and sewer enterprise's](#) (Aa1 positive) credit profile reflects the system's dynamic and stable economy and customer base, anchored by military presence, a strong tourism industry and growing industrial and manufacturing sectors. The system has limited operational risk as it purchases treated water from Norfolk and all wastewater is treated by Hampton Roads Sanitation District. As such, financial trends, including coverage of around 2x and liquidity between 400-500 days cash on hand, are slightly below medians. Additionally, coverage and liquidity have been exceptionally stable, supported by multiyear planning and timely rate increases. Including the 2026 bonds, debt represents a low 1.7x operating revenues.

Credit strengths

- » Dynamic service area stabilized by military presence
- » Stable financial metrics supported by strong management and timely rate increases
- » Very manageable long-term liabilities

Credit challenges

- » Elevated exposure to hurricanes and sea level rise

Rating outlook

The positive outlook reflects the likelihood that the system's coverage and liquidity will remain stable, supported by timely rate increases and multiyear planning. Additionally, debt to operating revenue will remain very manageable.

Factors that could lead to an upgrade

- » Maintenance of coverage above 2.0x and liquidity over 400 days
- » Continued trend of debt to revenues in line with Aaa medians

Factors that could lead to a downgrade

- » Trend of debt service coverage around 1.5x and liquidity around 250 days cash on hand
- » Significant increase in debt approaching 4x operating revenue

Key indicators

Exhibit 1

Virginia Beach (City of) VA Water & Swr Ent					
System Characteristics					
Asset Condition (Net Fixed Assets / Annual Depreciation)	27 years				
System Size - O&M (\$000)	\$113,717				
Service Area Wealth: MFI % of US median	110.60%				
Legal Provisions					
Rate Covenant (x)	1.15x				
Debt Service Reserve Requirement	DSRF funded at MADS (Aaa)				
Management					
Rate Management	Aaa				
Regulatory Compliance and Capital Planning	Aaa				
Financial Strength					
	2021	2022	2023	2024	2025
Operating Revenue (\$000)	\$129,715	\$130,069	\$130,433	\$137,495	\$146,117
System Size - O&M (\$000)	\$89,665	\$88,761	\$95,923	\$112,395	\$113,717
Net Revenues (\$000)	\$41,201	\$42,258	\$37,977	\$33,422	\$43,526
Net Funded Debt (\$000)	\$191,951	\$180,973	\$168,874	\$155,592	\$162,504
Annual Debt Service (\$000)	\$18,005	\$16,800	\$17,514	\$17,992	\$19,005
Annual Debt Service Coverage (x)	2.3x	2.5x	2.2x	1.9x	2.3x
Cash on Hand	471 days	482 days	471 days	420 days	429 days
Debt to Operating Revenues (x)	1.5x	1.4x	1.3x	1.1x	1.1x

Source: Moody's Ratings, city audits

Profile

Virginia Beach's water and sewer system provides treated water distribution and wastewater collection to the City of Virginia Beach (Aaa stable). The system serves about 135,000 water customers and 132,000 wastewater customers.

Detailed credit considerations

Service area and system characteristics

The system's customer base and service area will remain stable, anchored by strong military presence and growing manufacturing and industrial sectors, which benefit from the port in nearby Norfolk. The customer base is diverse and total customer counts have been relatively stable over the last decade, increasing less than 1% annually. Officials expect these trends to continue.

The water and sewer system serves the northern half of the city. The city purchases wholesale water from the City of Norfolk (Aa2 stable) pursuant to a long-term contract. The Hampton Roads Sanitation District (Aa1 stable) provides treatment and bills customers directly. The city collects a flat monthly charge for sewage collection. The limited operations of the system is a notable credit strength, insulating the city from the risks and challenges associated with owning and operating treatment facilities and the large capital investment they require.

Debt service coverage and liquidity

The system's strong operations are a result of conservative management practices, regular rate increases and long-range financial planning. Moody's calculated coverage averaged 2.23x over the last five years. While this is below the median for Aaa rated systems,

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coverage has been very stable. Lower coverage is also somewhat mitigated by the limited operational risk that the system has given it is just distribution and collection.

The city council typically approves rates for a multi-year period and formally adopts increases annually as a part of the budget process. The current five year plan includes 5% increases in water rates in fiscal 2027 and 2028. Management's multiyear projections show coverage hovering at or above 2x through 2031.

Liquidity

The system's unrestricted cash position is strong and has historically exceeded the city's formal target of 80-100% of O&M (292-365 days). The city has historically used restricted cash for capital needs and 2026 bond proceeds will replenish restricted cash for already completed projects. The capital plan includes some cash funded projects, but officials project that unrestricted cash will remain comfortably within policy targets.

Debt and legal covenants

Following the issuance of the 2026 bonds, the system's debt to operating revenues ratio will be around 1.7x, which is very manageable and in line with Aaa peers. The utility's adopted capital improvement plan (CIP) through fiscal 2031 includes \$263 million in projects, just over 60% of which will be funded with debt (including the 2026 bonds). Despite the additional debt plans identified within the CIP, the system's overall leverage will remain manageable due to management's long-range planning, conservative budgeting, and regular rate increases.

Debt structure

Bondholders benefit from a debt service reserve requirement fully funded with cash at maximum annual debt service (MADS) on all outstanding debt. The rate covenant requires 1.15x coverage, which the system has historically well exceeded.

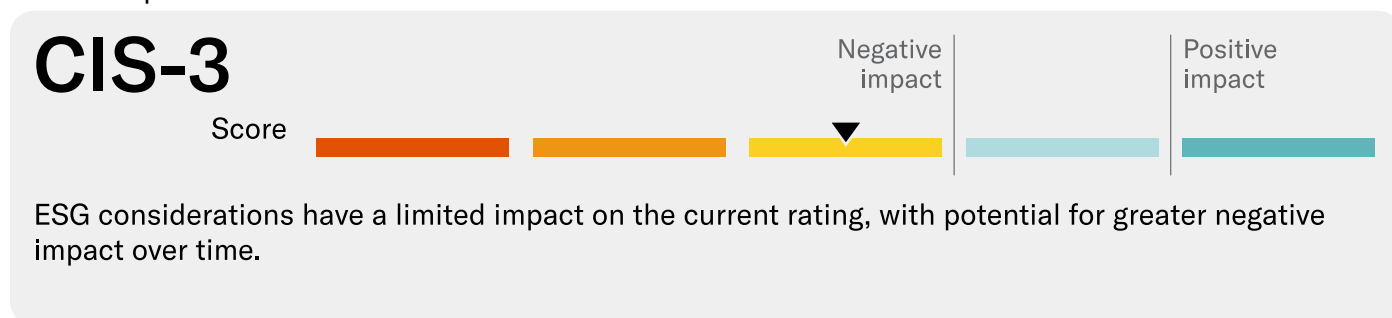
Pensions and OPEB

Pension and OPEB liabilities do not present material credit pressure for the system. The city, which includes system employees, and the city school board participate in the Virginia Retirement System (VRS), a multi-employer defined benefit pension plan administered by the Commonwealth of Virginia. Virginia Beach also provides city and school board employees with other post-employment benefits (OPEB).

ESG considerations

Virginia Beach (City of) VA Water & Swr Ent's ESG credit impact score is CIS-3

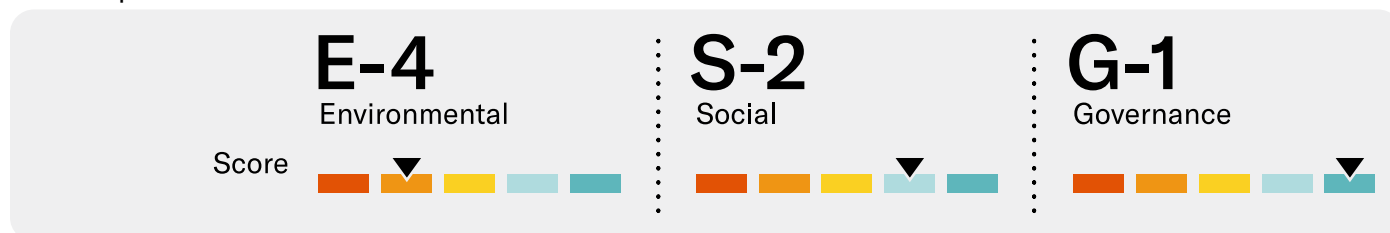
Exhibit 3
ESG credit impact score



Source: Moody's Ratings

Virginia Beach (City of) VA Water and Sewer Enterprise's ESG credit impact score of **CIS-3** indicates that ESG considerations have a limited impact on its credit rating.

Exhibit 4
ESG issuer profile scores



Source: Moody's Ratings

Environmental

The enterprise has elevated credit exposure to environmental risks due to the position of its service area along the coast and related hurricane risk and sea level rise. Exposure to other environmental risks, including carbon transition, natural capital and waste and pollution is low.

Social

The enterprise has limited credit exposure to social risks. The city purchases treated water and transmits it to city customers. Therefore, it is largely insulated from responsible production risk. The enterprise has low exposure to customer relations, demographic and social trends, health and safety, and human capital considerations.

Governance

The enterprise's governance considerations are favorable. The system benefits from strong financial strategy and risk management, as well as management credibility and track record considerations. Exposure to organizational structure and compliance and reporting considerations are neutral-to-low. The system has slightly negative exposure to board structure and policies risk resulting from concentrated control by the city government. Notwithstanding their monopoly service provision, the system faces the risk of public opposition to required rate increases or capital investment.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The US Municipal Utility Revenue Debt methodology includes a scorecard that summarizes the factors that are generally most important to utilities' credit profiles. Because the scorecard is a summary and may not include every consideration in the credit analysis for a specific issuer, a scorecard-indicated outcome may or may not match an assigned rating.

Exhibit 5

Virginia Beach, VA Water and Sewer Enterprise

Rating Factors	Input	Weight	Score
System Characteristics (30%)			
Asset Condition (Years of Annual Depreciation)	27.20399812	10%	Aa
System Size (O&M in Thousands of Dollars)	\$113,717	7.5%	Aaa
Service Area Wealth (Median Family Income as % of US)	111%	12.5%	Aa
Financial Strength (40%)			
Annual Debt Service Coverage (x)	2.29	15%	Aaa
Days Cash on Hand	428.875	15%	Aaa
Debt to Operating Revenue (x)	1.680263077	10%	Aaa
Management (20%)			
Rate Management	Aaa	10%	Aaa
Regulatory Compliance and Capital Planning	Aaa	10%	Aaa
Legal Provisions (10%)			
Rate Covenant (x)	1.15	5%	A
Debt Service Reserve Requirement	Aaa	5%	Aaa
Notching Factors			Up/Down
No Notching Factors Applied			N/A
Scorecard-Indicated Outcome			Aaa
Assigned Rating			Aa1

Data is based on most recent fiscal year available. Debt may include pro forma data for new debt issued or proposed to be issued after the close of the fiscal year.

Source: Moody's Ratings, city audits

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