The Economic Downturn - Impacts & Opportunities Web Seminar

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NYW

Poll Questions

How does your system pay for the majority of its capital projects?

- System revenue bonds
- City/Town general obligation bonds
- State revolving funds
- Cash funded

Do you need to access the market in 2009 to pay for capital projects?

- yes
- no

Long-term debt market
Continued volatility expected

- Recent turmoil in the financial markets has led to constraints in the availability of credit including to governmental entities

- Following the failure of Leman Brothers in mid-September lending froze for two weeks in the municipal market

- NYC, NY MTA and NYW were the first large deals to enter the market following the Lehman bankruptcy

- Access to the market is still limited for many borrowers – growing concern over pent-up demand

Long-term debt market
Continued volatility expected

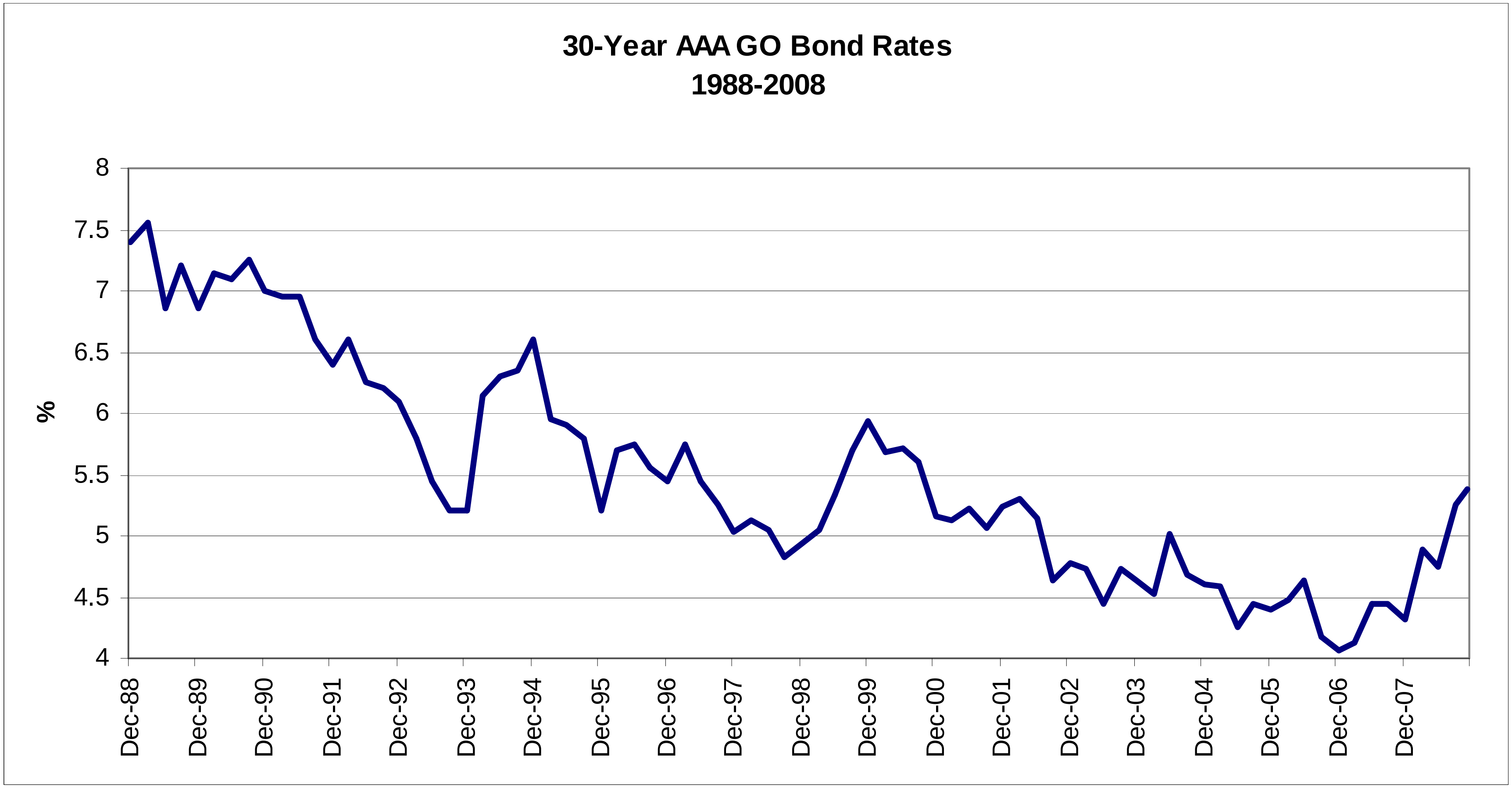
- Market for higher rated (AA-/Aa3 and higher) general obligation and essential service revenue bonds

- Demand from retail buyers is strong while demand from institutional buyers has been weak and uneven

- Rates are relatively attractive to investors, especially given the tax-exemption – in NYC, bond interest is triple tax-exempt from federal, state and city personal income taxes.

- Spreads relative to US treasuries has widened substantially

Long-term interest rates have risen…



Source: Thomson Financial, Municipal Market Data

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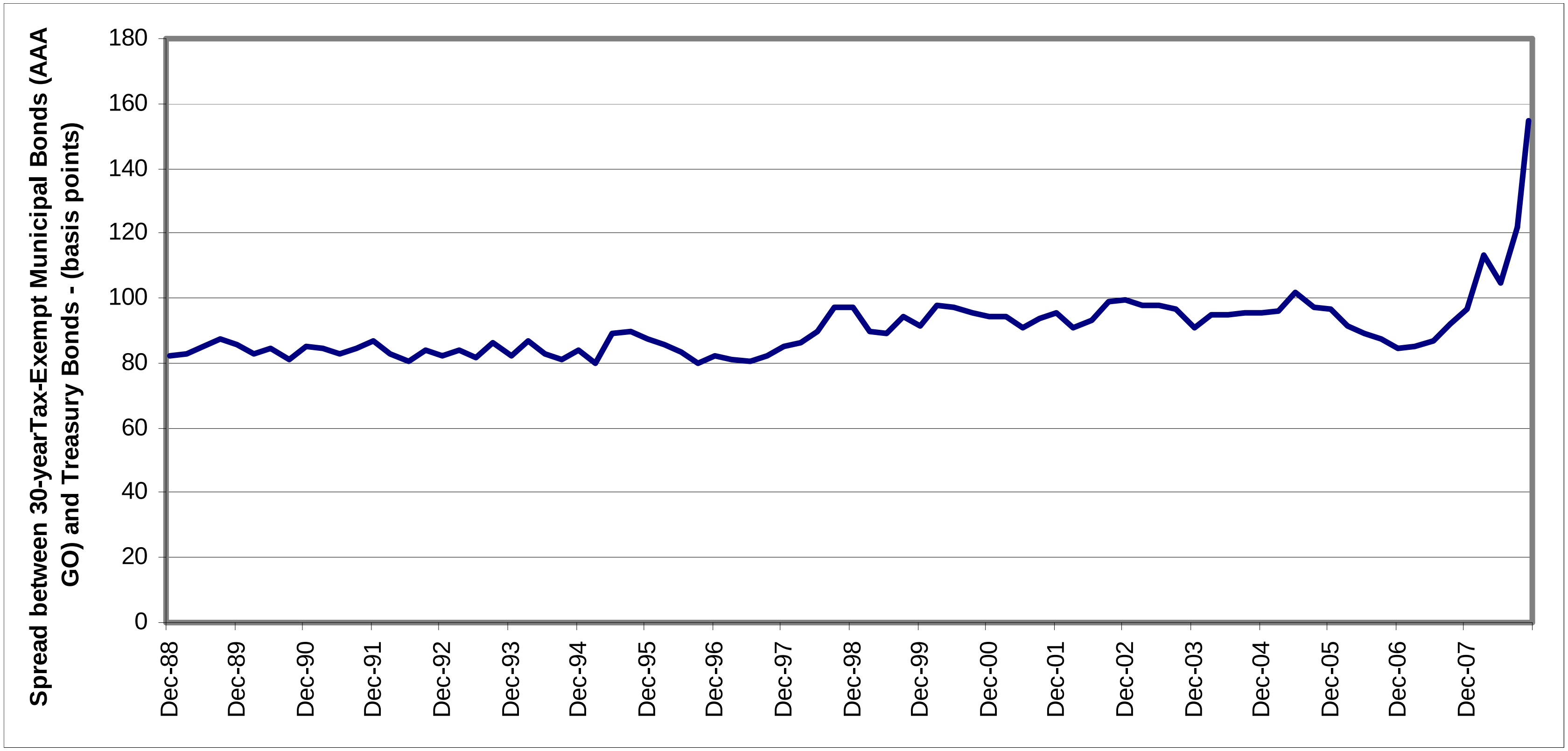
…and credit spreads between municipals and treasuries may attract new buyers

Spread between 30-year Tax-Exempt Municipal Bonds (AAA GO) and Treasury Bonds
1988 – 2008



Source: Thomson Financial, Municipal Market Data

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Short-term debt market offers attractive cost of funds but *continued volatility expected*

- Disruption in the auction rate securities market beginning in August 2007 – broker-dealers no longer the buyer of last resort (investors have no right to tender)

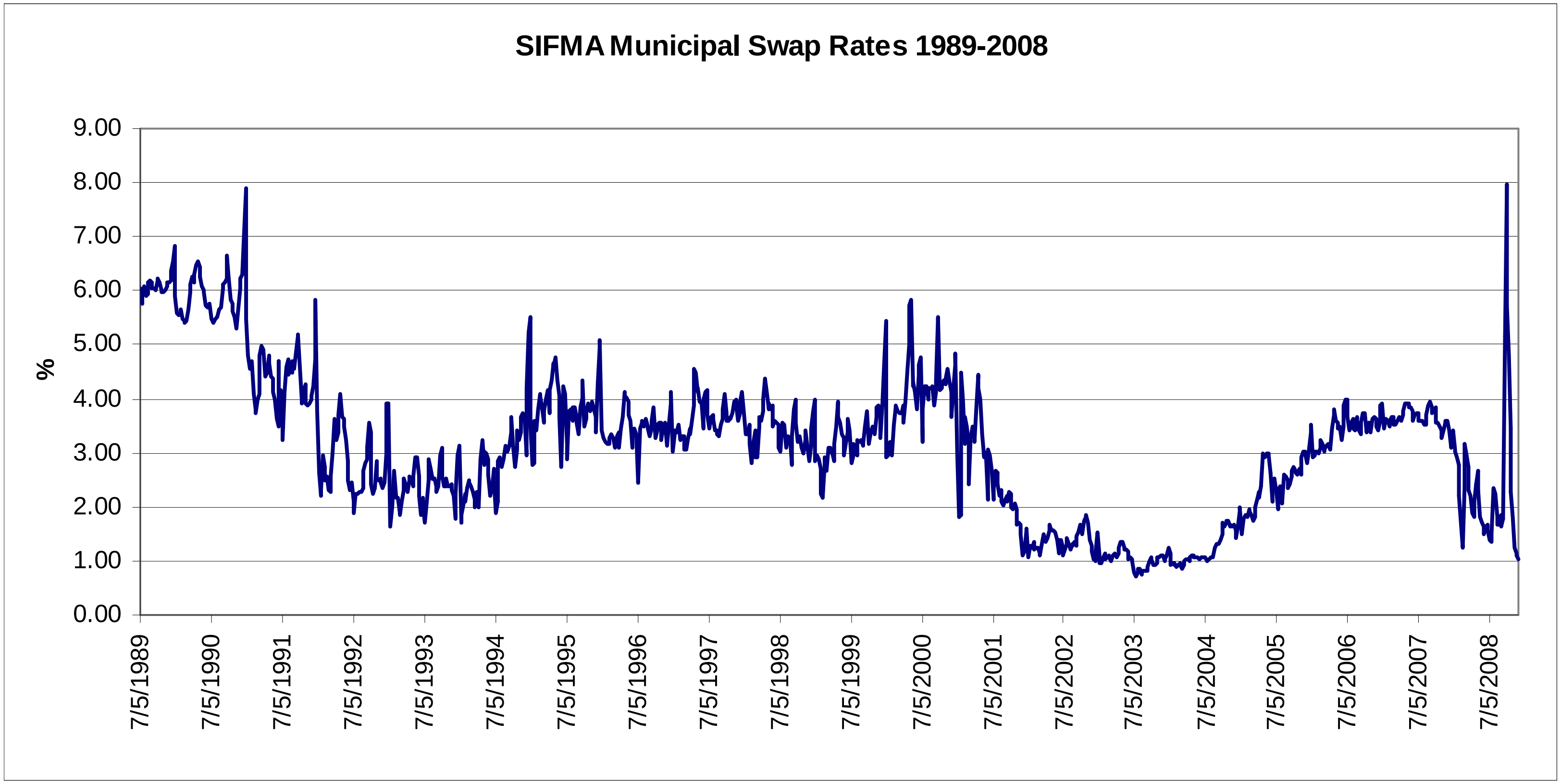
- Credit downgrades by financial guarantors beginning in December 2007

- Weakening financial strength and credit downgrades of banks providing liquidity for short-term debt instruments – such as variable rate debt and commercial paper – resulted in a spike in interest rates in mid-September

- Currently (and historically) variable rate debt offers a relatively favorable cost of funds – but liquidity capacity is limited and is expected to be further constrained going forward

- *Risks must be managed* – bank downgrades, failed remarketings, and "headline" risk

Short-term debt market offers attractive cost of funds but *continued volatility expected*



7-day high-grade market index comprised of tax-exempt Variable Rate Demand Obligations
Source: Securities Industry and Financial Markets Association

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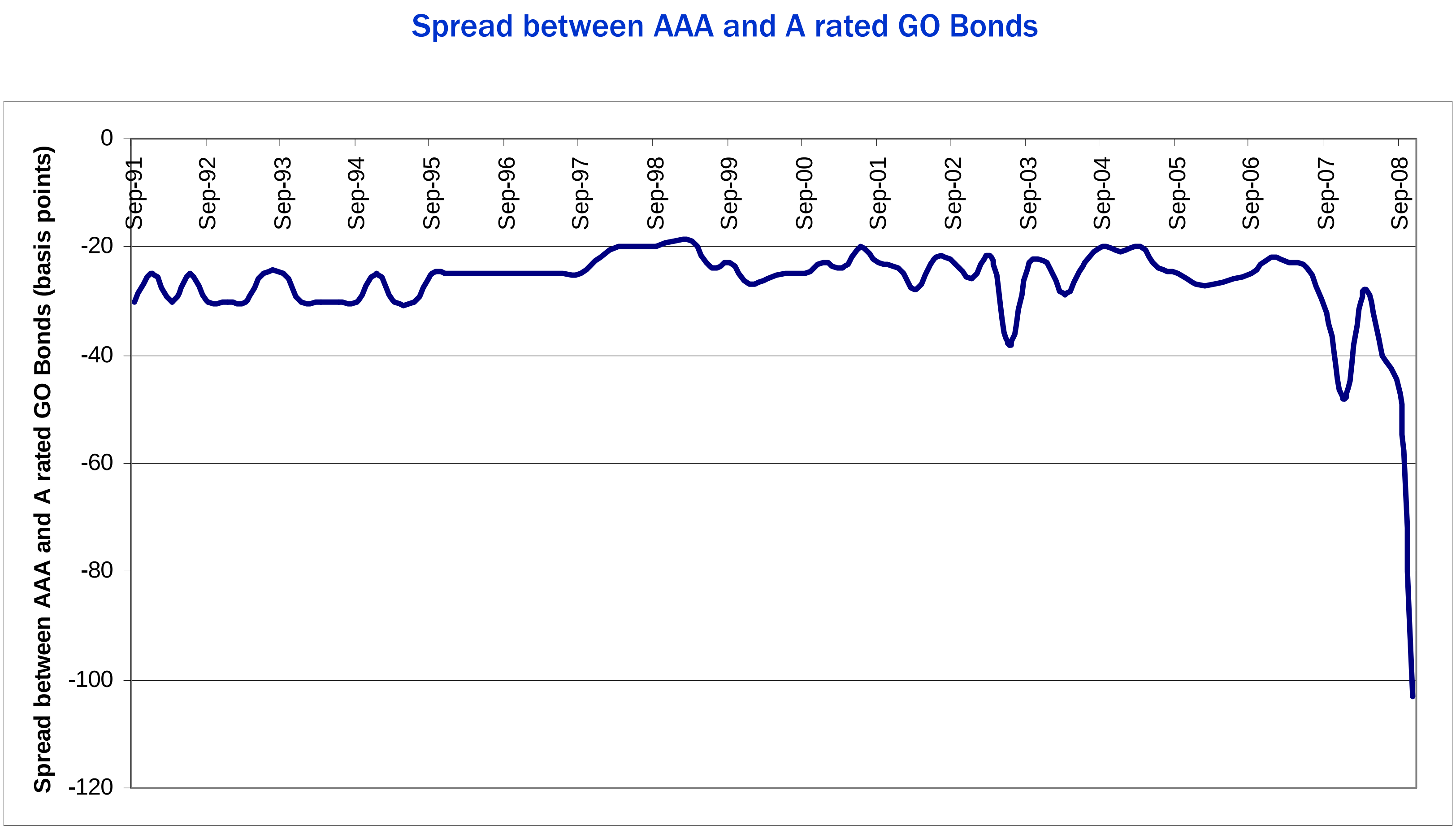
Economic Considerations

- Weakening economy may increase delinquencies in payment of water and sewer bills
- NYC customer base expected to remain relatively stable, given mostly residential customer base – but may be a concern for some systems
- Construction cost stabilization or even deflation may slow down the growth in costs on some construction projects (redeployment of labor from housing sector, reduction in energy and commodity costs)
- Federal economic stimulus package may provide additional funds for water and sewer projects through the State Revolving Funds

The value of strong credit can not be overstated

- Annual rate adjustments must keep pace with cost increases
- Well established rate setting mechanism must be in place
- Financial projections must anticipate risks and include adequate reserves
- Asset maintenance/long term capital planning is critical to long-term system stability and strong credit

Municipal credit spreads have widened significantly



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Questions & Answers

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