MOODY'S
INVESTORS SERVICE

New Issue: MOODY'S ASSIGNS Aa1/VMIG 1 RATINGS TO MWD OF SO. CAL.'S 2011 SERIES A WATER REVENUE REFUNDING BONDS; Aa1 RATINGS ON PARITY DEBT AFFIRMED

Global Credit Research - 20 May 2011

APPROXIMATELY $4.7 BILLION OF DEBT AFFECTED, INCLUDING THE CURRENT OFFERING

Metropolitan Water District of So. California
Water/Sewer
CA

Moody's Rating

ISSUE	RATING
Water Revenue Refunding Bonds (SIFMA Index Mode), 2011 Series A	Aa1/VMIG 1

Sale Amount	$230,000,000
Expected Sale Date	05/24/11
Rating Description	Water Revenue

Opinion

NEW YORK, May 20, 2011 -- Moody's Investors Service has assigned Aa1/VMIG 1 ratings to the Metropolitan Water District of Southern California's Water Revenue Refunding Bonds (SIFMA Index Mode), 2011 Series A-1, A-2, A-3, and A-4. At this time we have also affirmed our Aa1 ratings on the District's outstanding water revenue bonds, as well as the VMIG 1 ratings on the District's other "self-liquidity" supported SIFMA Index bonds and weekly variable rate demand bonds. The outlook for the District's long-term ratings is stable.

RATING RATIONALE

The Aa1, long-term portion of the assigned rating primarily reflects the critical importance of the District's water supplies to its exceedingly large Southern California service territory; the District Board's demonstrated willingness and ability to raise water rates as needed to maintain the enterprise's strong financial profile, even during difficult economic times; and District management's above average financial, operational, and long-term capital planning ability. The past year's unusually wet winter, both in California and the Colorado River basin, also factors favorably into the rating assignment, since it is allowing the District to continue to rapidly rebuild its storage supplies. These supplies had been significantly reduced in recent years due both to the drought and to legally imposed cutbacks on the State Water Project. Notwithstanding the recent upswing in water availability, procuring sufficient, reliable long-term water supplies will remain a challenge, and a negative rating factor, but one which we believe the District is well capable of meeting. The current offering also lacks a debt service reserve requirement, while many of the District's prior issues benefited from reserves sized at 50% of the standard three-prong test. In the context of the District's overall financial resources and projected improvement in operating results over the next few years, this relative weakness is not sufficient to warrant a rating distinction. The VMIG 1, short-term portion of the assigned rating reflects our evaluation of the District's ability to pay the purchase price of tendered bonds in Index Mode from its own liquid, financial resources.

CURRENT OFFERING STRUCTURE: Multi-modal variable rate debt with a mandatory tender on a scheduled tender period termination date. The District is irrevocably committed, though not obligated, to purchase tendered bonds on the scheduled tender dates from remarketing proceeds and/or its own funds.

LEGAL SECURITY: Annual principal and interest payments are secured by the District's pledge of and a first lien on net operating revenues of the District's water enterprise, on parity with prior bond issues under the District's 1991 Master Resolution, as amended. The District is "irrevocably committed" to pay the purchase price of the bonds on the scheduled mandatory tender dates from remarketing proceeds or its own funds, though failure to do so would not constitute an Event of Default under the District's Master Resolution. It would, however, be an Event of Default under the applicable paying agent agreement, triggering a special mandatory redemption period (one-third of the outstanding amount at 18, 36, and 54 months from the purchase default). These scheduled special mandatory redemption obligations would be on parity with the District's senior lien bond obligations.

USE OF PROCEEDS: Refund a portion of the District's outstanding debt for debt service savings.

INTEREST RATE DERIVATIVES: The District has a very large, $1.4 billion swap portfolio, consisting of 17 transactions distributed among four counterparties. While these primarily floating-to-fixed rate transactions expose the District to various additional financial risks, Moody's believes these risks remain manageable.

DISTRICT PROVIDES CRITICAL WATER SUPPLIES TO EXCEPTIONALLY LARGE SERVICE TERRITORY

The District provides supplemental water supplies to its 26 member agencies located mostly along the urbanized southern California coast, roughly from Los Angeles to San Diego. The District's 5,200 square mile service area includes all or parts of six counties (Ventura, Los Angeles, San Bernardino, Orange, Riverside, and San Diego) and a population of about 19 million, or about half of the state's total population. The District's operations, therefore, not only provide an essential municipal service, but they also have statewide political and economic significance.

While the District's water supplies are not its service territory's only supply source (hence the District's characterization as a "supplemental" water supplier), its supplies are nevertheless critical for its customers. District supplies account for between 40% to 60% of its service territory's total annual water use. Its individual member agencies' average, annual reliance on District supplies ranges from about 30% to 100%, with some members' demands quite variable around their annual averages. This annual variance is driven by local rainfall within each member agency's own service area and watershed. Member agencies do not have an annual contractual obligation to purchase any water from the

District, but their high reliance on District supplies over the long-run generally obviates the need for such commitments.

A few of the District's member agencies are pursuing alternate sources of new water supplies. These efforts, however, are integrated into the District's own long-term resource planning and, given the inherently tight water supply environment in Southern California, do not pose a threat to the District's fundamental water supply relationship with its member agencies or its likely future sales. In some cases, such as seawater desalinization projects, these alternate supply sources are even financed in part with District subsidies.

RECENT BELOW AVERAGE FINANCIAL PERFORMANCE PROJECTED TO CONTINUE FOR AT LEAST AN ADDITIONAL YEAR

The District's financial performance in recent years has been below average for an Aa1-rated water enterprise, but the District has consistently demonstrated a willingness to raise rates to restore its financial health. Over the 2006-2012 period it will have raised rates by an aggregate 76%. And while it has missed its own operating target of 2.0x debt service coverage in five of the last seven years, these were arguably exceptional years in terms of reduced supply availability followed by reduced customer demand. With the lifting in April of drought related sales restrictions and 7.5% rate increases effective 1/1/11 and 1/1/12, the District will likely return to meeting its coverage target in fiscal 2013, as well as replenish its financial reserves.

As anticipated, the District's GAAP-basis financial performance in fiscal 2010 was below average for a water enterprise with Aa1-rated revenue bonds. It was, though, modestly improved from fiscal 2009. Fiscal 2011 will be another relatively weak year, owing to well below average sales volume, currently projected at 1.63 million acre-feet (maf) compared to a budgeted amount of 1.93 maf. Prior years (FYs 2006-08) had seen sales averaging about 2.24 maf per year, though with the current regulatory and economic environment, a return to sales at these levels is not likely any time soon.

The District now projects cash-basis debt service coverage of just 1.44x for senior lien bonds, compared to a 1.63x level projected in December, 2010. FY 2011 accrual-basis coverage should be moderately stronger, given a resumption of sales to agricultural users and for groundwater replenishment. While sales volume will likely remain below average in the near-term owing to the weak economy and the lingering effect of prior years' conservation efforts, rate increases already in place should improve the District's operating results in fiscal 2012. In that year, the District anticipates 1.84x cash-basis coverage, just below its 2.0x target.

The current decline in local water demand has had an upside for the District's near-term financial and credit profile: increased storage supplies and potentially reduced operating expenditures. After three years of statewide drought, the District's storage supplies had been significantly depleted. Reduced demand and increased deliveries from both the SWP and Colorado River are permitting increased storage replenishment--up to 800,000 acre-feet in the current year. As of January 1, 2010, total District supplies in storage were 1.6 maf, compared to 2.4 maf two years ago. As of January 1, 2011, storage supplies had been replenished to 2.3 maf, and by the end of 2011 the District anticipates being at its highest storage level in history (3.1 maf). With this level of supplies the pressure on the District to procure relatively expensive alternate water sources/transfers has been eliminated, eliminating this cost and thereby lowering total operating cost going forward.

The storage purchases have not been a pure positive however, since they have reduced the District's financial reserves. As of fiscal 2010 year end, the District's two key reserve funds (its rate stabilization and "revenue remainder" funds) totaled $297 million. The District anticipates these will be drawn down by an additional $83 million in fiscal 2011. It is worth noting that the supplies the District has added to storage over the last two years is roughly equivalent to $920 million (based on the District's untreated, Tier 1 rate of $560 per acre foot on January 1, 2011). As demand increases in the near future, the District reasonably anticipates that recent rate increases and reduced costs will improve its financial reserves. This improvement should occur even if sales volume settles at 1.8 maf rather than the 2.2 maf of a few years ago. The District anticipates approaching $300 million in reserves at the end of 2013 and reaching $400 million in 2015. This would be about halfway between its minimum and maximum reserve thresholds and represent about 37.5% of it projected, cash operating expenditures in that year (2015).

SIGNIFICANT BUT MANAGEABLE VARIABLE RATE DEBT EXPOSURE

With recent years' increased focus on fixed-rate debt issuance, the District's total outstanding variable rate debt exposure has been reduced but still remains significant at about 37% of its total, outstanding water revenue debt (as of May 1, 2011). About two-thirds of these variable rate obligations are swapped to fixed, giving the District a correspondingly large interest rate swap portfolio, but relatively predictable annual interest rate costs. The District's net variable rate exposure is just 12.2% of its total revenue bond debt. With the District's sound cash flow and reserves, managing fluctuating interest costs remains easily within its means. The more significant risk, though one which the District is also capably managing, is the replacement of expiring liquidity facilities. To date, the District has not experienced any significant difficulty in either finding replacement providers or in extending existing facilities, and we do not expect this trend to change, absent a fundamental change in the market. This expectation incorporates the projected market-wide flood of liquidity facility renewals in 2011, and the relatively constrained supply compared to prior years.

CHALLENGING LONG-RUN WATER SUPPLY ENVIRONMENT LARGELY MITIGATED BY THE DISTRICT'S STORAGE SUPPLIES AND SHORT-TERM PURCHASES

Rainfall variations and increasingly stringent regulatory constraints imposed on the District's two main water supply sources--the federal Colorado River System and the California State Water Project (SWP)--result in highly variable annual deliveries to the District. The past year's well above normal precipitation will increase near-term deliveries, but it will not significantly change the long-run constraints on these systems. The Colorado River watershed has experienced below normal rainfall for almost the entire last decade, and what actually constitutes "normal" rainfall for this watershed is subject to considerable debate. Depending on the historic timeframe evaluated, normal could be substantially lower than the level currently assumed. The District's SWP supplies will likely remain subject to significant regulatory constraints for the foreseeable future, notwithstanding a recent, modest easing of some constraints related both to legal decisions and increased rainfall. SWP supplies are channeled through the Sacramento-San Joaquin Bay Delta, an environmentally sensitive estuary. Issues related to the long-term environmental health and competing uses of the Bay Delta remain contentious, and potentially very expensive to solve. As the largest contractor for SWP supplies, the District will likely be a major contributor to any reengineering of the Delta to improve its environmental health and supply reliability. The District has to date very capably addressed these challenges, primarily by improving its own storage capacity and delivery system integration. The District's demonstrated willingness and continued ability to raise rate as necessary to support its infrastructure expansion is a key strength in addressing the likely continued supply challenge.

Outlook

Moody's outlook on the District's long-term ratings is stable. While the District's near-term operating results will be below average for its Aa1 revenue bond rating level, the District continues to demonstrate a willingness and ability to raise rates as necessary to return it to more solid

financial footing. The recent sharp downturn in water demand relative to projections is likely a temporary phenomenon, and one which has the upside of helping to replenish what were severely depleted storage supplies.

What Would Change the Rating - UP

Given the District's already very high rating and the likely continued, challenging water supply environment in California, upward rating movement is unlikely. However, significantly improved water supply reliability and a reduction in the variability in the District's annual financial performance could provide upward rating pressure.

What Would Change the Rating - DOWN

* Consistently weak financial performance relative to the District's Aa1 rated peers, whether from reduced sales/supplies or unwillingness to raise rates on a timely basis.

* Sufficiently reduced supply reliability such that the District's storage supplies could not be reasonably expected to be replenished on a timely basis.

The principal methodology used in this rating was Analytical Framework For Water And Sewer System Ratings published in August 1999.

REGULATORY DISCLOSURES

Information sources used to prepare the credit rating are the following: parties involved in the ratings and public information.

Moody's Investors Service considers the quality of information available on the credit satisfactory for the purposes of assigning a credit rating.

Moody's adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources Moody's considers to be reliable including, when appropriate, independent third-party sources. However, Moody's is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

Please see ratings tab on the issuer/entity page on Moodys.com for the last rating action and the rating history.

The date on which some Credit Ratings were first released goes back to a time before Moody's Investors Service's Credit Ratings were fully digitized and accurate data may not be available. Consequently, Moody's Investors Service provides a date that it believes is the most reliable and accurate based on the information that is available to it. Please see the ratings disclosure page on our website www.moodys.com for further information.

Please see the Credit Policy page on Moodys.com for the methodologies used in determining ratings, further information on the meaning of each rating category and the definition of default and recovery.

Analysts

Eric Hoffmann
Analyst
Public Finance Group
Moody's Investors Service

Dari Barzel
Backup Analyst
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

Moody's Investors Service
250 Greenwich Street
New York, NY 10007
USA

© 2011 Moody's Investors Service, Inc. and/or its licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ARE MOODY'S INVESTORS SERVICE, INC.'S ("MIS") CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MIS DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. CREDIT RATINGS DO NOT CONSTITUTE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS ARE NOT RECOMMENDATIONS TO

PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. CREDIT RATINGS DO NOT COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MIS ISSUES ITS CREDIT RATINGS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources Moody's considers to be reliable, including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The ratings, financial reporting analysis, projections, and other observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. Each user of the information contained herein must make its own study and evaluation of each security it may consider purchasing, holding or selling. NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

MIS, a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MIS have, prior to assignment of any rating, agreed to pay to MIS for appraisal and rating services rendered by it fees ranging from $1,500 to approximately $2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moodys.com under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Any publication into Australia of this document is by MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657, which holds Australian Financial Services License no. 336969. This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001.

Notwithstanding the foregoing, credit ratings assigned on and after October 1, 2010 by Moody's Japan K.K. (“MJKK”) are MJKK's current opinions of the relative future credit risk of entities, credit commitments, or debt or debt-like securities. In such a case, “MIS” in the foregoing statements shall be deemed to be replaced with “MJKK”. MJKK is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly owned by Moody’s Overseas Holdings Inc., a wholly-owned subsidiary of MCO.

This credit rating is an opinion as to the creditworthiness or a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail investors. It would be dangerous for retail investors to make any investment decision based on this credit rating. If in doubt you should contact your financial or other professional adviser.

MOODY'S
INVESTORS SERVICE

New Issue: MOODY'S ASSIGNS Aa1 RATING TO MWD OF SO. CAL.'S 2011 SERIES B WATER REVENUE REFUNDING BONDS; Aa1 RATINGS ON PARITY DEBT AFFIRMED

Global Credit Research - 23 May 2011

APPROXIMATELY $4.7 BILLION OF DEBT AFFECTED, INCLUDING THE CURRENT OFFERING

Water/Sewer
CA

Moody's Rating

ISSUE	RATING
Water Revenue Refunding Bonds, 2011 Series B	Aa1

Sale Amount	$150,000,000
Expected Sale Date	06/08/11
Rating Description	Revenue

Opinion

NEW YORK, May 23, 2011 -- Moody's Investors Service has assigned an Aa1 rating to the Metropolitan Water District of Southern California's Water Revenue Refunding Bonds 2011 Series B. At this time we have also affirmed our Aa1 ratings on the District's outstanding, parity water revenue bonds. The outlook for the District's rating is stable.

RATING RATIONALE

The assigned rating primarily reflects the critical importance of the District's water supplies to its exceedingly large Southern California service territory; the District Board's demonstrated willingness and ability to raise water rates as needed to maintain the enterprise's strong financial profile, even during difficult economic times; and District management's above average financial, operational, and long-term capital planning ability. The past year's unusually wet winter, both in California and the Colorado River basin, also factors favorably into the rating assignment, since it is allowing the District to continue to rapidly rebuild its storage supplies. These supplies had been significantly reduced in recent years due both to the drought and to legally imposed cutbacks on the State Water Project. Notwithstanding the recent upswing in water availability, procuring sufficient, reliable long-term water supplies will remain a challenge, and a negative rating factor, but one which we believe the District is well capable of meeting. The current offering also lacks a debt service reserve requirement, while many of the District's prior issues benefited from reserves sized at 50% of the standard three-prong test. In the context of the District's overall financial resources and projected improvement in operating results over the next few years, this relative weakness is not sufficient to warrant a rating distinction.

USE OF PROCEEDS: Refund a portion of the District's outstanding debt for debt service savings.

SECURITY FOR THE BONDS: Pledge of and first lien on net operating revenues of the District's water enterprise, on parity with prior issues under the District's 1991 Master Resolution, as amended.

INTEREST RATE DERIVATIVES: The District has a very large, $1.4 billion swap portfolio, consisting of 17 transactions distributed among four counterparties. While these primarily floating-to-fixed rate transactions expose the District to various additional financial risks, Moody's believes these risks remain manageable.

DISTRICT PROVIDES CRITICAL WATER SUPPLIES TO EXCEPTIONALLY LARGE SERVICE TERRITORY

The District provides supplemental water supplies to its 26 member agencies located mostly along the urbanized southern California coast, roughly from Los Angeles to San Diego. The District's 5,200 square mile service area includes all or parts of six counties (Ventura, Los Angeles, San Bernardino, Orange, Riverside, and San Diego) and a population of about 19 million, or about half of the state's total population. The District's operations, therefore, not only provide an essential municipal service, but they also have statewide political and economic significance.

While the District's water supplies are not its service territory's only supply source (hence the District's characterization as a "supplemental" water supplier), its supplies are nevertheless critical for its customers. District supplies account for between 40% to 60% of its service territory's total annual water use. Its individual member agencies' average, annual reliance on District supplies ranges from about 30% to 100%, with some members' demands quite variable around their annual averages. This annual variance is driven by local rainfall within each member agency's own service area and watershed. Member agencies do not have an annual contractual obligation to purchase any water from the District, but their high reliance on District supplies over the long-run generally obviates the need for such commitments.

A few of the District's member agencies are pursuing alternate sources of new water supplies. These efforts, however, are integrated into the District's own long-term resource planning and, given the inherently tight water supply environment in Southern California, do not pose a threat to the District's fundamental water supply relationship with its member agencies or its likely future sales. In some cases, such as seawater desalinization projects, these alternate supply sources are even financed in part with District subsidies.

RECENT BELOW AVERAGE FINANCIAL PERFORMANCE PROJECTED TO CONTINUE FOR AT LEAST AN ADDITIONAL YEAR

The District's financial performance in recent years has been below average for an Aa1-rated water enterprise, but the District has consistently demonstrated a willingness to raise rates to restore its financial health. Over the 2006-2012 period it will have raised rates by an aggregate 76%. And while it has missed its own operating target of 2.0x debt service coverage in five of the last seven years, these were arguably exceptional years in terms of reduced supply availability followed by reduced customer demand. With the lifting in April of drought related sales

restrictions and 7.5% rate increases effective 1/1/11 and 1/1/12, the District will likely return to meeting its coverage target in fiscal 2013, as well as replenish its financial reserves.

As anticipated, the District's GAAP-basis financial performance in fiscal 2010 was below average for a water enterprise with Aa1-rated revenue bonds. It was, though, modestly improved from fiscal 2009. Fiscal 2011 will be another relatively weak year, owing to well below average sales volume, currently projected at 1.63 million acre-feet (maf) compared to a budgeted amount of 1.93 maf. Prior years (FYs 2006-08) had seen sales averaging about 2.24 maf per year, though with the current regulatory and economic environment, a return to sales at these levels is not likely any time soon.

The District now projects cash-basis debt service coverage of just 1.44x for senior lien bonds, compared to a 1.63x level projected in December, 2010. FY 2011 accrual-basis coverage should be moderately stronger, given a resumption of sales to agricultural users and for groundwater replenishment. While sales volume will likely remain below average in the near-term owing to the weak economy and the lingering effect of prior years' conservation efforts, rate increases already in place should improve the District's operating results in fiscal 2012. In that year, the District anticipates 1.84x cash-basis coverage, just below its 2.0x target.

The current decline in local water demand has had an upside for the District's near-term financial and credit profile: increased storage supplies and potentially reduced operating expenditures. After three years of statewide drought, the District's storage supplies had been significantly depleted. Reduced demand and increased deliveries from both the SWP and Colorado River are permitting increased storage replenishment--up to 800,000 acre-feet in the current year. As of January 1, 2010, total District supplies in storage were 1.6 maf, compared to 2.4 maf two years ago. As of January 1, 2011, storage supplies had been replenished to 2.3 maf, and by the end of 2011 the District anticipates being at its highest storage level in history (3.1 maf). With this level of supplies the pressure on the District to procure relatively expensive alternate water sources/transfers has been eliminated, eliminating this cost and thereby lowering total operating cost going forward.

The storage purchases have not been a pure positive however, since they have reduced the District's financial reserves. As of fiscal 2010 year end, the District's two key reserve funds (its rate stabilization and "revenue remainder" funds) totaled $297 million. The District anticipates these will be drawn down by an additional $83 million in fiscal 2011. It is worth noting that the supplies the District has added to storage over the last two years is roughly equivalent to $920 million (based on the District's untreated, Tier 1 rate of $560 per acre foot on January 1, 2011). As demand increases in the near future, the District reasonably anticipates that recent rate increases and reduced costs will improve its financial reserves. This improvement should occur even if sales volume settles at 1.8 maf rather than the 2.2 maf of a few years ago. The District anticipates approaching $300 million in reserves at the end of 2013 and reaching $400 million in 2015. This would be about halfway between its minimum and maximum reserve thresholds and represent about 37.5% of it projected, cash operating expenditures in that year (2015).

SIGNIFICANT BUT MANAGEABLE VARIABLE RATE DEBT EXPOSURE

With recent years' increased focus on fixed-rate debt issuance, the District's total outstanding variable rate debt exposure has been reduced but still remains significant at about 37% of its total, outstanding water revenue debt (as of May 1, 2011). About two-thirds of these variable rate obligations are swapped to fixed, giving the District a correspondingly large interest rate swap portfolio, but relatively predictable annual interest rate costs. The District's net variable rate exposure is just 12.2% of its total revenue bond debt. With the District's sound cash flow and reserves, managing fluctuating interest costs remains easily within its means. The more significant risk, though one which the District is also capably managing, is the replacement of expiring liquidity facilities. To date, the District has not experienced any significant difficulty in either finding replacement providers or in extending existing facilities, and we do not expect this trend to change, absent a fundamental change in the market. This expectation incorporates the projected market-wide flood of liquidity facility renewals in 2011, and the relatively constrained supply compared to prior years.

CHALLENGING LONG-RUN WATER SUPPLY ENVIRONMENT LARGELY MITIGATED BY THE DISTRICT'S STORAGE SUPPLIES AND SHORT-TERM PURCHASES

Rainfall variations and increasingly stringent regulatory constraints imposed on the District's two main water supply sources--the federal Colorado River System and the California State Water Project (SWP)--result in highly variable annual deliveries to the District. The past year's well above normal precipitation will increase near-term deliveries, but it will not significantly change the long-run constraints on these systems. The Colorado River watershed has experienced below normal rainfall for almost the entire last decade, and what actually constitutes "normal" rainfall for this watershed is subject to considerable debate. Depending on the historic timeframe evaluated, normal could be substantially lower than the level currently assumed. The District's SWP supplies will likely remain subject to significant regulatory constraints for the foreseeable future, notwithstanding a recent, modest easing of some constraints related both to legal decisions and increased rainfall. SWP supplies are channeled through the Sacramento-San Joaquin Bay Delta, an environmentally sensitive estuary. Issues related to the long-term environmental health and competing uses of the Bay Delta remain contentious, and potentially very expensive to solve. As the largest contractor for SWP supplies, the District will likely be a major contributor to any reengineering of the Delta to improve its environmental health and supply reliability. The District has to date very capably addressed these challenges, primarily by improving its own storage capacity and delivery system integration. The District's demonstrated willingness and continued ability to raise rate as necessary to support its infrastructure expansion is a key strength in addressing the likely continued supply challenge.

Outlook

Moody's outlook on the District's long-term ratings is stable. While the District's near-term operating results will be below average for its Aa1 revenue bond rating level, the District continues to demonstrate a willingness and ability to raise rates as necessary to return it to more solid financial footing. The recent sharp downturn in water demand relative to projections is likely a temporary phenomenon, and one which has the upside of helping to replenish what were severely depleted storage supplies.

What Would Change the Rating - UP

Given the District's already very high rating and the likely continued, challenging water supply environment in California, upward rating movement is unlikely. However, significantly improved water supply reliability and a reduction in the variability in the District's annual financial performance could provide upward rating pressure.

What Would Change the Rating - DOWN

* Consistently weak financial performance relative to the District's Aa1 rated peers, whether from reduced sales/supplies or unwillingness to raise rates on a timely basis.

* Sufficiently reduced supply reliability such that the District's storage supplies could not be reasonably expected to be replenished on a timely basis.

The principal methodology used in this rating was Analytical Framework For Water And Sewer System Ratings published in August 1999.

REGULATORY DISCLOSURES

Information sources used to prepare the credit rating are the following: parties involved in the ratings and public information.

Moody's Investors Service considers the quality of information available on the credit satisfactory for the purposes of assigning a credit rating.

Moody's adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources Moody's considers to be reliable including, when appropriate, independent third-party sources. However, Moody's is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

Moody's adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources Moody's considers to be reliable including, when appropriate, independent third-party sources. However, Moody's is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

Please see ratings tab on the issuer/entity page on Moodys.com for the last rating action and the rating history.

The date on which some Credit Ratings were first released goes back to a time before Moody's Investors Service's Credit Ratings were fully digitized and accurate data may not be available. Consequently, Moody's Investors Service provides a date that it believes is the most reliable and accurate based on the information that is available to it. Please see the ratings disclosure page on our website www.moodys.com for further information.

Please see the Credit Policy page on Moodys.com for the methodologies used in determining ratings, further information on the meaning of each rating category and the definition of default and recovery.

Analysts

Eric Hoffmann
Analyst
Public Finance Group
Moody's Investors Service

Dari Barzel
Backup Analyst
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

Moody's Investors Service
250 Greenwich Street
New York, NY 10007
USA

© 2011 Moody's Investors Service, Inc. and/or its licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ARE MOODY'S INVESTORS SERVICE, INC.'S ("MIS") CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MIS DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. CREDIT RATINGS DO NOT CONSTITUTE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS ARE NOT RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. CREDIT RATINGS DO NOT COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MIS ISSUES ITS CREDIT RATINGS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO,

COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources Moody's considers to be reliable, including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The ratings, financial reporting analysis, projections, and other observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. Each user of the information contained herein must make its own study and evaluation of each security it may consider purchasing, holding or selling. NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

MIS, a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MIS have, prior to assignment of any rating, agreed to pay to MIS for appraisal and rating services rendered by it fees ranging from $1,500 to approximately $2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moodys.com under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Any publication into Australia of this document is by MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657, which holds Australian Financial Services License no. 336969. This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001.

Notwithstanding the foregoing, credit ratings assigned on and after October 1, 2010 by Moody's Japan K.K. (“MJKK”) are MJKK's current opinions of the relative future credit risk of entities, credit commitments, or debt or debt-like securities. In such a case, “MIS” in the foregoing statements shall be deemed to be replaced with “MJKK”. MJKK is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly owned by Moody’s Overseas Holdings Inc., a wholly-owned subsidiary of MCO.

This credit rating is an opinion as to the creditworthiness or a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail investors. It would be dangerous for retail investors to make any investment decision based on this credit rating. If in doubt you should contact your financial or other professional adviser.