Fitch Rates Utah Municipal Power Agency's Power Supply System Rev Bonds 'A'; Outlook Stable

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SAN FRANCISCO--(BUSINESS WIRE)--Fitch Ratings has assigned an 'A' rating to the following bonds issued by the Utah Municipal Power Agency (UMPA):

--$98,450,000 power supply system revenue bonds, series 2016A;

--$18,125,000 power supply system revenue bonds, series 2016B.

Proceeds from the series 2016A bonds will provide long-term financing for the acquisition and repair and replacement costs for the West Valley Power Plant. Proceeds from the 2016B bonds will finance the construction of the Provo Power Plant and a new administration building. The bonds will be sold via negotiation the week of Oct. 3.

The Rating Outlook is Stable.

SECURITY

The bonds are payable from the net revenues of the system, subordinate to UMPA's outstanding bonds that amount to approximately $8.5 million and reach final maturity on July 1, 2018. UMPA's revenues are provided primarily from the sale of electricity to its six members, all city-owned retail electric utilities.

KEY RATING DRIVERS

WHOLESALE POWER PROVIDER: UMPA is an all-requirements, electric services provider serving the distribution systems of six member cities located in Central Utah. The member cities collectively serve a population of over 170,000.

LEGALLY CONTRACTED SALES: Members are bound under power sales agreements (PSAs) to purchase and receive substantially all retail electric power needs from UMPA. The PSAs extend through 2065, well beyond the life of the debt, and provide UMPA with full authority to recover costs from members, including those related to a member default.

FAVORABLY CONCENTRATED: UMPA's member MWh sales and revenues are highly concentrated in the cities of Provo (65.3%; electric revenue bonds rated 'AA-') and Spanish Fork (21.4%), both of which demonstrate solid credit fundamentals including healthy financial profiles, stable customer bases and MWh sales, and manageable levels of customer concentration.

RATE FLEXIBILITY: UMPA and its members maintain the ability to make timely rate adjustments to fully recover costs. UMPA's rates have risen significantly over the past decade in response to increased costs, declining non-member sales, the need for additional investment, and the recent implementation of a rate stabilization fund charge. However, the continued competitiveness of members' retail rates demonstrates that additional flexibility remains.

SATISFACTORY FINANCIAL METRICS: Financial metrics are satisfactory for the rating with fiscal 2016 (unaudited) debt service coverage estimated at 1.42x and unrestricted cash on hand at approximately $16.8 million or 94 days. Liquidity levels are projected to gradually increase as the agency builds up its rate stabilization fund, amounting to 38 days cash in fiscal 2016, to the policy target of 90 days by 2023.

FUTURE RESOURCE DECISIONS: The recent acquisition of the West Valley Power plant provides UMPA with peaking capacity, although the full plant exceeds member needs at present. Additional changes to the agency's power supply are expected as baseload purchase power contracts expire over the near term and environmental mandates increase the cost of legacy, coal-fired resources.

RATING SENSITIVITIES

IMPROVED LIQUIDITY: Continued improvement in the Utah Municipal Power Agency's liquidity metrics, which is projected through the eight-year funding of the board-approved rate stabilization fund (targeted at 90 days cash), could compensate for historically volatile coverage levels and lead to positive rating action.

CREDIT PROFILE

UMPA is an all-requirements, joint-action agency serving six member cities in central Utah. The six members are: Provo, Spanish Fork, Nephi, Salem, Manti, and Levan. Collectively, the six members serve approximately 53,731 electric customers.

UMPA was created in 1980 through an interlocal agreement between its six member cities for the purpose of developing a reliable and cost-effective power supply. The all-requirements PSAs between UMPA and each city, as well as the interlocal agreements, were renegotiated in 2015. The current PSAs and agreements, which took effect on Jan. 1, 2016, expire at the latter of 2065 or as long as the agency has debt outstanding.

MEMBER CONCENTRATION

UMPA made approximately 90% of its fiscal 2016 MWh sales to member systems. The cities of Provo and Spanish Fork are the largest of the members, accounting for 65.3% and 21.4%, respectively, of UMPA's member MWh sales in fiscal 2016. Fitch's analysis of UMPA's members focuses on Provo and Spanish Fork given their relative size and importance to the agency and the PSA provisions that allow UMPA to reallocate costs to remaining members in the event of a member default.

Both Provo and Spanish Fork exhibit solid credit characteristics, including relatively low direct debt levels, solid debt service coverage levels, and ample liquidity. Provo's customer base is concentrated with its largest customer, Brigham Young University (BYU) accounting for 17.8% of MWh sales and 12.3% of operating revenues in fiscal 2015. A recent proposal by the university to develop a self-generation project that would supply approximately 80% of its needs could reduce the system's MWh sales. However, Fitch views Provo's financial profile and rate flexibility as sufficient to offset the potential load loss.

POWER SUPPLY

UMPA's total summertime capacity of 499.4 MW is more than sufficient to serve member cities' peak demand, which reached a recent high of 280 MW in 2015. Power supply resources consist of owned and contracted capacity, including resources that are directly owned by members but dedicated to the agency under capacity purchase agreements that extend through 2065.

UMPA's recent purchase of the West Valley Power Plant (West Valley) in August 2016 secured a needed peaking resource for members. Consisting of five GE LM6000 simple-cycle gas turbine generating units with a total net capacity of 200 MW (winter) and 185 (summer), West Valley provides UMPA and its members with valuable, quick starting peaking capacity.

UMPA is not projected to require the plant's full capacity for member needs until 2024 as member sales grow over time. However, the resource was viewed as more economical than self-building a smaller sized plant and provides the agency with flexibility as other resource decisions are expected to be made over the near term to replace expiring contracts. North American Energy Services (NAES) is contracted to operate the plant through 2018. Capacity in excess of member needs is expected to be sold into wholesale markets, although UMPA management has conservatively assumed no wholesale revenues in its revenue requirement calculation used to set rates for members.

VOLATILE COVERAGE; IMPROVING LIQUIDITY

The agency's financial performance has been somewhat volatile historically, with Fitch-calculated debt service coverage falling modestly below 1.0x twice in the previous five audited years (2011 and 2014) and reaching a recent high of 2.60x in fiscal 2015.

While the narrow coverage levels reflect the agency's budgeted target, the fiscal 2015 results were stronger due to revenues collected to meet the July 1 (fiscal 2016) debt payment, revenue from the rate stabilization fund charge, and a one-time refund from a purchase power contract that was applied as member contributions. Fiscal 2015 coverage was approximately 1.06x after adjusting for the three items mentioned above. In fiscal 2016, Fitch-calculated coverage is estimated at 1.42x based on unaudited actuals.

The agency's historically modest liquidity levels are expected to be bolstered as the rate stabilization fund is increased to meet the policy level of 90 days cash on hand. In fiscal 2015, the unrestricted cash balance was approximately $13.7 million or an adequate 79 days. The fiscal 2015 balance includes approximately $4.6 million in designated rate stabilization funds. Unaudited figures for fiscal 2016 reflect an increased total unrestricted cash balance of $16.8 million, equal to 94 days cash on hand. Approximately $6.9 million of the ending fiscal 2016 balance was designated rate stabilization funds. Management intends to fully fund the 90 day rate stabilization fund over an eight-year timeframe with a dedicated rate surcharge.

Additional information is available at 'www.fitchratings.com'.

Applicable Criteria

Revenue-Supported Rating Criteria (pub. 16 Jun 2014)
https://www.fitchratings.com/site/re/750012

U.S. Public Power Rating Criteria (pub. 18 May 2015)
https://www.fitchratings.com/site/re/864007

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
https://www.fitchratings.com/creditdesk/press_releases/content/ridf_frame.cfm?pr_id=1012319

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