Moody's
INVESTORS SERVICE

New Issue: Moody's assigns Baa2 to City of Burlington's (VT) Electric Revenue Bonds; outlook changed to positive from stable

Global Credit Research - 22 Jul 2014

Approximately $33 million of debt securities affected

BURLINGTON (CITY OF) VT ELECTRIC ENTERPRISE
Electric Distribution and Generation
VT

Moody's Rating

ISSUE		RATING
Electric System Revenue Bonds, 2014 Series A		Baa2
Sale Amount	$12,000,000	
Expected Sale Date	07/29/14	
Rating Description	Revenue: Other	
Electric System Revenue Refunding Bonds, 2014 Series B		Baa2
Sale Amount	$6,010,000	
Expected Sale Date	07/29/14	
Rating Description	Revenue: Other	

Moody's Outlook POS

Opinion

NEW YORK, July 22, 2014 --Moody's Investors Service has assigned a Baa2 rating to the City of Burlington's (VT) Electric System Revenue Bonds, 2014 Series A and Series B. Moody's has also affirmed the Baa2 on outstanding debt and changed the outlook to positive from stable, affecting $33 million of debt. The Burlington Electric Department (BED) also has $45 million of outstanding general obligation bonds secured by the City of Burlington's (VT) general obligation pledge (GO rated Baa3, stable).

RATING RATIONALE

The Baa2 rating reflects the department's strength as the exclusive provider of electric service to the city as well as its stable customer base which includes the University of Vermont. The Baa2 also reflects rates which are regulated by the state public service board (PSB), exposing the department to regulatory lag risk, which is unusual for public power utilities that generally benefit from local rate setting authority. The PSB has approved all department rate requests for the last two decades, evidencing a supportive regulatory regime. The rating also reflects the department's improved power supply diversity and debt service coverage ratios (DSCR) in recent years. The department's liquidity, while improving, is still weak with approximately 50 days cash on hand.

Outlook

The outlook change to positive from stable reflects our belief that the department will continue to reduce its exposure to the power supply market through long term contracts and diversify the power supply portfolio through the acquisition of the Winooski hydro facility. The outlook change also reflects our expectation of stable or improving debt service coverage ratios and other financial metrics.

What Could Change the Rating - UP

The rating could face upward pressure if the department improves its liquidity position, maintains or improves its coverage ratios, and successfully manages its power supply contract risk.

What Could Change the Rating - DOWN

In light of the positive outlook, limited near term prospects exists for the rating to be lowered. The rating could face downward pressure if the debt service coverage ratio falls below the 1.25x rate covenant, if the department has difficulty managing the newly acquired hydro facility, or if liquidity weakens.

Strengths:

- Improving financials including net revenues, debt ratio, and stabilized DSCR

- Reduced exposure to wholesale power market through long term contracts

- History of full rate increase request approvals from state oversight

- Budgeting no short term market contracts for purchased power by 2016

Challenges:

- Weak liquidity compared to similarly rated peers

- Local economy has weak medium term economic forecast

- BED's short term contracts for power supply expire in the near term, exposing the utility to very modest market risk

DETAILED CREDIT DISCUSSION

LEGAL SECURITY: The bonds are secured by the net revenues of the electric system. There is a 1.25 times rate covenant and the debt service reserve requirement is equal to maximum annual debt service on the senior revenue bonds.

The department also has approximately $43 million of general obligation (GO) bonds that are expected to be repaid from electric department operating revenues. The rate covenant on the consolidated debt outstanding is 1.00 times. Per the General Bond Resolution, the claim on the revenues of the department by the revenue bondholders is prior to any claim of the GO bondholders.

INTEREST RATE DERIVATIVES AND VARIABLE RATE DEBT: None

2014A BONDS FINANCE THE WINOOSKI ONE HYDRO PLANT

The Series 2014A bonds are being issued to finance $12 million of the total $16 million project cost of acquiring the Winooski One hydro plant, which is located on the Winooski River between the Cities of Burlington and Winooski, Vermont. The hydro plant first opened in 1993 and the development plans offered BED the option to acquire the project after 20 years of operation, which is being exercised. The plant will bolster management's efforts to secure stable and predictable long term supply and diversify their power sources. The 7.4 MW facility will provide 8-9% of annual system load and will be qualified to sell Renewable Energy Credits in New England.

RECENT DEVELOPMENTS

The department's financial position and its power supply management stabilized in 2013 with the addition of several long term power supply contracts that diversify the fuel mix while also increasing cost predictability. While the department's 50% ownership of the McNeil wood-fired plant provides 39% of its load capacity, the rest of the department's energy requirements are satisfied through the New England power market. In order to mitigate the exposure to increases in ISO NE costs for transmitting purchased power, management has fixed price contracts in place for nearly 100% of its capacity needs through 2017. The department is also replacing its short term bilateral contracts with long term contracts. In 2015, the department's short term purchases through bilateral contracts are expected to be 4%, notably down from a high of 44% in 2010. The department's new medium to long-term contracts are with Vermont Wind for 16MW of capacity until 2021; Georgia Mountain Wind for 10MW of supply until 2037; Nextera Hydro for 5MW of capacity until 2017; and New York Power Authority for 2.6 MW until 2017.

The department's revenue derived from the sale of Class I Renewable Energy Credits (REC) in Connecticut and

Massachusetts has also increased to an expected $8.8 million in 2014. REC sales are contracted at fixed prices for more than 50% of production through 2016. In order to minimize the exposure in the renewable energy credit market, BED's budget assumptions for open positions are conservatively half of the present market prices. For the next three years, the department's cost variance will be related to the operation of its McNeil plant and the plant's production levels, REC sales, and variable demand under its power supply contracts.

Given the stability of the department's power supply, the DSCR in 2013 on a net revenue post city transfer basis was a strong 2.21 times for senior revenue bonds and 1.61 times for consolidated bonds (includes subordinate general obligation bonds). This was a notable improvement from a consolidated DSCR of 1.26 times in 2012. Based on the power supply forecast until 2017, we expect the department to maintain financial metrics on par with 2013 results in the medium term. The department also continues to increase its liquidity position, which is relatively weak compared to its peer group and suppressed by its rate regulatory body. The department's days cash on hand in 2013 was approximately 50 days. To help their liquidity, the department has a $5 million bank line of credit with a local Vermont bank that has no outstanding draws.

Budgeted fiscal 2014 net income of $0.39m was substantially lower than in the previous year, $7.3m, but year to date performance has been over budget at $3.4m as of May. BED is budgeting a net income of $3.5m in fiscal 2015 and a slight increase in liquidity to 55 days cash on hand, excluding the LOC.

The largest of BEDs capital plans is the purchase and integration of the Winooski One hydro facility. Other major projects include a solar installation at a Burlington Airport parking garage, gas turbine control systems, undergrounding of power lines on the downtown waterfront, and other capital projects such as continuation of the smart meter deployment and smart grid infrastructure. These projects will be cash funded or funded through General Obligation bond proceeds and are expected to cost $7.6 million.

KEY STATISTICS:

Type of System: Electric generation and distribution

Total Debt Service Coverage Ratio, net revenue basis post city transfer, FY 2013 (3-YR AVG): 1.61x (1.45x)

Days Cash on hand, FY 2013 (3-YR AVG): 50 days (43 days)

Debt Ratio, FY 2013 (3-YR AVG): 50% (61%)

METHODOLOGY SCORECARD FACTORS:

Factor 1 - Cost Recovery Framework Within Service Territory (25% weight): A

Factor 2 - Willingness to Recover Costs and Maintain Sound Financial Metrics (25% weight): Baa

Factor 3 - Management of Generation Risk (10% weight): A

Factor 4 - Rate Competitiveness (10% weight): A

Factor 5 - Financial Strength (3 year historical averages) - (a) Liquidity (10% weight): 50 days (Baa)

Factor 5 - Financial Strength (3 year historical averages) - (b) Debt Ratio (10% weight): 60% (A)

Factor 5 - Financial Strength (3 year historical averages) - (c) Coverage (10% weight): 1.45 times (Baa)

Scorecard Indicated Rating: A3

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The principal methodology used in this rating was U.S. Public Power Electric Utilities with Generation Ownership Exposure published in November 2011. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

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