

DISPATCH

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Munis' Credit Outlook Stable

Moody's Analysts Discuss Industry Credit Outlook

Munis Must Watch Liquidity, Keep Strong Balance Sheet



The credit rating outlook for municipal utilities is stable, but changing risks to liquidity, rate pressure and changes in the way utilities generate power are issues public power utilities must manage effectively, according to representatives from Moody's Investors Service. Moody's Senior Vice President Dan Aschenbach and Analyst Andrew Cleary were guests at FMPA's Audit and Risk Oversight Committee (AROC) meeting in April where they provided an update on the industry and its credit outlook.

Managing Risks to Liquidity

A utility's risk management approach is an important credit consideration in these times. Evaluation of risk exposures should include how those risks could affect the utility and its liquidity. Citing examples such as the impact of Hurricane Katrina on natural gas supply or the recent credit market failures, Aschenbach explained that risks are ever-changing, so utilities should have a process or a forum, like FMPA's AROC, to stay abreast of the issues. Aschenbach said, "The message is know your risk to liquidity."

Rating agencies also expect a utility to maintain a strong balance sheet. Aschenbach

reviewed a list of financial metrics on which municipal electric utilities are compared, including debt service coverage ratio, debt service safety margin, net worth and capital. "[FMPA is] fitting in with many of these ratios. The one that is much lower is the days of cash on hand," said Aschenbach.

Beyond looking at industry medians, a rating agency must also look at the individual utility's circumstances. "If you are a utility that has a large amount of gas-fired generation and you have to manage fuel supply, your need for more liquidity is greater than maybe a utility that has a larger percentage of coal resources," explained Aschenbach.

In fact, Moody's watches how utilities industry-wide manage their fuel expenses and balance risks with liquidity. Utilities have options for managing the risk of volatile

fuel prices, including hedging, rate stabilization or a combination of both. When asked which approach is most desirable, Aschenbach responded, "Certainly a combination of both. The problem with being unhedged is you don't know what your exposure is going to be ... so you don't know if that rate stabilization position is large enough or small enough. So to

the extent that you are more hedged, you are better able to assess the possible risk and ... understand whether that liquidity position is sufficient."

Summing up the subject, Aschenbach explained, "Each utility is different and medians are useful as benchmarks, but threats or

"Municipal credit typically has a very low default rate, very low probability of loss. The ratings are moving up a little bit to reflect that."

Dan Aschenbach
Senior Vice President
Moody's Investors Service
on Moody's transition of municipal credit ratings to a global scale

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The Business Model Working Group

by Larry Mattern

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The Business Model Working Group

By Larry Mattern
Vice President of Power Supply,
Kissimmee Utility Authority



Larry Mattern

The Business Model Working Group (BMWG) was created by the FMPA All-Requirements Project (ARP) Executive Committee in May 2009 by a successful motion that stated “create an ARP business model working group, composed of the representatives of ARP cities, with the purpose of learning and fully understanding the current ARP business model and to have an eye towards suggesting any changes to achieve greater efficiency that can be introduced in any part of the operation of this agency to be brought back to the Executive Committee.”

The committee has taken on the tasks of education and understanding. Having held 15 meetings since its inception just over a year ago, a multitude of topics have been addressed. The topics for the meetings included:

- Review of the All-Requirements Power Supply Contract and Amendment 1, the Capacity and Energy Sales Contract, the True All-Requirements Project, and Consolidated Operating and Joint Ownership Contract for the Cane Island and Hansel Facilities, and the Florida Municipal Power Pool Contract.

- The BMWG toured the Orlando Utilities Commission energy control center and received an overview of the workings of the Florida Municipal Power Pool. The group also visited the Cane Island Unit 4 construction site to view the project’s progress.

- A review of the FMPA hedging program resulted in a recommendation to the Executive Committee of a new hedging policy known as FST. The FST is still under consideration.
- FMPA’s Integrated Resource Planning (IRP) process was reviewed by staff including timelines and requests for direction on the upcoming IRP.

- A cost analysis for the delay or cancellation of Cane Island Unit 4 was presented. The BMWG recommended completing Unit 4 without delay based on the results of the analysis.
- Larger but mostly similar joint action agencies, American Municipal Power and Municipal Electric Authority of Georgia, presented highlights of their business models. The FMPA staff also provided details on a multitude of other joint action agencies for comparison. Options are still under consideration.
- Demand Side Management, wholesale power rates and wholesale power cost comparisons continue to be the center of discussion, at present.

As you see, the committee has been busy with the review process as tasked. However, the most important outcome from the BMWG is that a forum was created for the members to take as much time as necessary to understand and discuss each topic.

BMWG meetings provide a unique opportunity for representatives from various positions in the ARP member cities to interact with the FMPA staff and the other ARP members to clearly understand each piece of the All-Requirements Project business plan. Through comprehensive presentations, the staff clearly presents how we, as an Agency, operate. Presentations often spark discussions that spawn requests for more information and more options.

Every piece of the business plan is openly discussed for as long as it takes and to the smallest detail. All opinions are welcome and surely given, which often leads to spirited discussion. The debate, the details, various choices, and varying opinions may sound inefficient, but it is really the essence of what makes the BMWG work.

The members of this committee won’t take the short or ambiguous answer. A close examination of the business plan is necessary, when making recommendations that can affect the project well into the future. Progress is being made. Though there may be differences at times, the one common thread that runs through the BMWG is that all of its participants care deeply about the future of the All-Requirements Project. At the end of the day, we will have the right business plan to take the ARP successfully forward. ♦

Meet the Business Model Working Group

Eleven out of 14 cities that purchase wholesale electricity from ARP volunteered to participate on the BMWG.

These volunteers include:

- Larry Mattern, Kissimmee (Chair)
- Matt Brower, Ocala
- Bill Conrad, Newberry
- Gregg Griffin, Green Cove Springs
- Fred Hilliard, Fort Meade
- Rebecca Matthey, Lake Worth
- Don Ouchley, Jacksonville Beach
- Tom Richards, Fort Pierce
- Vince Ruano, Bushnell
- Lynne Tejada, Key West
- Ricky Thompson, Starke

Sharing Knowledge, Building Foundations

By Nicholas P. Guarriello
General Manager & CEO, FMPA



Nicholas P. Guarriello

The recession has made its mark on Florida. Families, businesses and local governments in our communities are learning to do more with less. FMPA's members recognize that competitive rates and an effective business model have never been more important. That's why in May 2009 our All-Requirements Project members kicked off an initiative to thoroughly examine the project's business model and seek opportunities for greater efficiency and effectiveness.

The wholesale power business is complex, so analyzing all components of the All-Requirements Project business model is a bold goal and a significant commitment of time and energy. Our members recognize that the Business Model Working Group (BMWG) is an opportunity to create something of lasting value, the foundation of our future.

The BMWG's dedication is evident. Each of its members have dedicated countless hours to the process of developing a deeper understanding among All-Requirements' member cities about the most complex elements of our business. This shared knowl-

edge will provide a valuable foundation for future decision making.

The BMWG's efforts have also been an investment in the relationships that tie a joint action agency, like FMPA, together. The workshop format of the BMWG meetings has fostered a positive environment for asking questions, exchanging thoughts and developing stronger bonds among members. This working together for the good of the Agency and the spirit it nurtures are the foundation of collaboration and long-term partnership.

In fact, the BMWG's work has proven so valuable that some members have suggested that the process live on after the group's original mission is fulfilled. For example, members have discussed meeting, perhaps on a quarterly basis, to stay abreast of issues and have joint discussions about key aspects of our business. This initiative may be the foundation of a new, more robust model of member involvement and collaboration.

I commend the 11 members of the BMWG for the tremendous investment they're making in the future of FMPA and their local utilities. The shared vision generated by this group of leaders is sure to provide a strong foundation for the Agency's future. ♦

Moody's Analysts Visit FMPA Credit Outlook *continued from page 1*

access to liquidity will differ." Therefore, it is important for each utility to know its risks, identify mitigation actions and maintain liquidity to weather the risks.

Threats to Credit Outlook

Preparing for potential carbon regulation and renewable electricity standards are notable challenges for utilities and a threat to credit outlook.

Replacing coal-fired generation with natural gas and renewable generation will be a challenging transition, and there is a lot of uncertainty surrounding fuel choices for new generation. Aschenbach noted that FMPA still has time before it must add new base load generation to its system,

but explains that industry-wide this issue is one of Moody's top concerns.

Aschenbach also addressed the issue of rates, which he said is probably the biggest impact on investor-owned, as well as public power credit quality.

Rate pressures have increased in recent years due to high, volatile natural gas prices. Going forward, carbon regulation and replacing coal in the power mix may continue to keep costs high. While Moody's expects timely rate setting, political risk due to lower customer tolerance for rate increases could adversely impact utilities' financial metrics, leading to downgrades.

Moody's also anticipates that new nuclear plants could increase credit pressure, as few utilities have strength-



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ened their balance sheets enough to position themselves for the high capital cost of a nuclear construction project. Aschenbach noted that the Municipal Electric Authority of Georgia, a joint action agency like FMPA, has structured a positive approach to its nuclear ownership by amassing almost a billion dollars of liquidity.

Finally, Aschenbach described Moody's recalibration of public power ratings to transition them from a municipal scale to a global scale. The move to a global scale is occurring so that investors can compare all types of investments on equal terms. "Municipal credit typically has a very low default rate, very low probability of loss. The ratings are moving up a little bit to reflect that," said Aschenbach.

FMPA members may request a complete transcript of the presentation and conversation by contacting FMPA's Sue Utley at sue.utley@fmpa.com. ♦



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