

Rating Action: Moody's assigns Aa3 rating to GRU's (FL) Utilities System Revenue Bonds, 2021 Series A

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Approximately \$1.7 billion of debt securities outstanding

New York, July 08, 2021 -- Moody's Investors Service has assigned an Aa3 rating to Gainesville (City of) FL Combined Utility Enterprise's (Gainesville Regional Utilities (GRU)) \$96.64 million Utilities System Revenue Bonds, 2021 Series A.

At the same time Moody's has affirmed the following ratings on GRU's outstanding debt:

- Utilities System Revenue Bonds, rated Aa3
- Variable Rate Utilities System Revenue Bonds, rated Aa3/VMIG 1
- Utilities System Commercial Paper Notes, Series C and Series D (Bank Bonds), A1
- Utility System Commercial Paper Notes, Series C and Series D, Prime-1 (P-1)

The rating outlook is stable.

RATINGS RATIONALE

GRU's Aa3 utility system revenue bonds rating benefits from its resilient and stable service territory, diversified operations as a combined utility enterprise and a track record of raising rates when necessary. GRU continues to diversify its fuel sources by planning to convert its coal-fired Deerhaven Generation Station into a dual-fuel natural gas facility by the end of 2021 and has signed a power purchase agreement with Origis Energy for 50MW of solar power.

GRU's rating is constrained by a very high leverage (88.5% adjusted debt ratio), lack of a debt service reserve requirement, high electric rates, the age of some of its coal and natural-gas fired generation assets and high annual transfers to the city's general fund which reduces the utility's ability to apply free cash flow generation towards rate reductions or investments into the system.

The key challenges for GRU in the next few years will be to manage the annual high transfers to the city (\$38 million in fiscal 2021), renew its fleet in order to reach the city's goal of net zero carbon emissions by 2045 which will likely require additional debt leading to higher debt service costs. GRU's biomass plant remains an uncompetitive renewable energy resources compared to the cost of natural gas but adds to the diversity and reliability of GRU's generation resources.

Given these cost pressures, Moody's continues to expect that GRU will generate consistent but moderately low fixed charge coverage ratios of 1.4-1.5x per year after transfers to the city. Efforts to mitigate future cost pressure, all of which we view as credit supportive actions, include a 7% rate increase for the electric system and 5% for the waste water system in fiscal 2022, the intention to develop a rate ordinance as well as a resolution to reduce the transfers to the city by \$2 million per year until September 30, 2027 beginning in fiscal 2022.

The city of Gainesville, FL (Gainesville (City of), FL, issuer rating Aa2) has only a 40% share of properties within city limits that are taxable, which has resulted in a high reliance on transfers from GRU.

GRU's debt ratio remains high at around 75.1% on an unadjusted basis and 88.5% on an adjusted basis including Moody's adjusted net pension liability in fiscal 2020. Moody's expects debt to gradually decline over time as debt amortizes. GRU also seeks to implement a debt defeasance plan as approved by the City Commission. However, future investments to achieve the city's net zero emission target by 2045 will very likely require additional investments and debt to renew its fleet.

Liquidity is strong particularly when considering the utility's headroom under its commercial paper program with

around \$106 million of unrestricted and discretionary reserves as of September 30, 2020. Days cash on hand was 178 days and days liquidity on hand was 429 days including headroom under the commercial paper program.

The A1 rating on the second lien Utility System Commercial Paper Notes, Series C (Bank Bonds) and Utilities System Commercial Paper Notes, Series D (Bank Bonds) reflects the subordinate pledge of the net system revenues to the utility's outstanding long-term revenue bonds rated Aa3.

The P-1 rating on the Utility System Commercial Paper Notes, Series C and D are based on the short-term Counterparty Risk (CR) Assessment of the bank providing the liquidity support and Moody's assessment of the limited likelihood of an early termination of the liquidity facility without payment at maturity of the notes. The short-term CR Assessment of Bank of America, N.A. is P-1(cr) (for Series C) and the short-term CR Assessment of State Street Bank & Trust Company is P-1(cr) (for Series D). Events that would result in termination of the liquidity facility without payment of the Notes at maturity by the Bank are directly related to the credit quality of GRU.

The VMIG 1 ratings assigned to the Variable Utilities System Revenue Bonds 2005 Series C, 2006 Series A, 2008 Series B, and 2012 Series B are derived from the credit quality of the Bank (Barclays Bank, Plc) as provider of the SBPAs and Moody's assessment of the likelihood of an early termination or suspension of the SBPAs without a final mandatory tender. Events that would cause termination or suspension of the Bank's commitment under the SBPAs without a mandatory purchase funded by a draw on the SBPAs are directly related to the credit quality of GRU. Moody's current short-term CR Assessment of Barclays Bank, PLC is P-1(cr).

RATING OUTLOOK

The stable rating outlook reflects our expectation that GRU will maintain consistent fixed charge coverage ratios in the 1.4-1.5x range and will maintain a good liquidity profile.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- A fixed charge coverage ratio maintained at around 1.6x on a sustained basis
- Maintaining adjusted days cash on hand above 250 days
- Material and sustained reduction in leverage

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Cost pressures preventing timely future rate adjustments and fixed charge coverage ratios declining below 1.4x on a sustained basis and inability to reduce leverage
- Deteriorating liquidity profile with adjusted days cash on hand materially below 175 days cash on hand
- More aggressive demands for transfers to the city's general funds
- Short-term: The short-term P-1 rating on the commercial paper note and the VMIG 1 ratings could be downgraded if Moody's were to downgrade the short-term rating of the banks providing liquidity support to the commercial paper notes or providing standby purchase agreements to the variable rate debt

STRUCTURAL CONSIDERATIONS

GRU had around \$1.6 billion of debt outstanding, consisting in utility system revenue bonds. The subordinated commercial paper program has currently no debt outstanding. Including the 2021 Series A Moody's expects debt to increase to around \$1.7 billion.

The Aa3-rated utility system revenue bonds are secured by a senior lien pledge of net revenues of the combined utilities system of the City of Gainesville.

The rate covenant and additional bonds test requires that net revenues equal at least 1.25x aggregate annual debt service. The utility is required to fund monthly deposits to the debt service account, so funds are available in advance of the principal and interest dates.

There has been no debt service reserve requirement since 2003, which is a credit weakness in GRU's bond

resolution.

The utility system commercial paper notes are rated A1/Prime-1 (P-1) and secured by a second lien pledge of net revenues of the combined utilities system of the City of Gainesville.

USE OF PROCEEDS

Proceeds of the 2021 Series A will be used to fund capital expenditures and the cost of issuance related to the transaction.

PROFILE

Gainesville Regional Utilities (GRU) is a municipally-owned utility system in Gainesville, FL with electric generation and transmission, natural gas, water, wastewater and telecommunication services. In fiscal 2020, GRU reported total revenues of around \$395 million and had 99,200 electric customers. The electric facilities of the System currently serve approximately 124.5 square miles of the County, and approximately 37% of the population of the County, including the entire City, with the exception of the University of Florida campus, which is served principally by Duke Energy Florida.

METHODOLOGY

The principal methodology used in the long-term ratings was US Public Power Electric Utilities with Generation Ownership Exposure Methodology published in August 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1170209 . The principal methodology used in the short-term ratings was Variable Rate Instruments Supported by Conditional Liquidity Facilities published in March 2017 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1057134 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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