

The Virgin Islands Consortium

Ratings Firm Downgrades WAPA Bonds To Junk Status

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ST. CROIX -- Moody's Investors Service on Thursday downgraded the Virgin Islands Water and Power Authority's senior electric system revenue bond rating to Ba2 from Baa3 and the electric system subordinated revenue bond rating to Ba3 from Ba1, a move that sent W.A.P.A.'s bonds into [junk status](#).

The ratings, which were placed on review for downgrade on March 31, 2016, remain on review for possible further downgrade, according to Moody's.

The downgrade comes on the heels of a recent decision by the Public Services Commission to [deny](#) W.A.P.A. a [requested electric rate increase](#) and instead placed the

petition under a 60-day review. The semiautonomous entity said it needed the increase to help stabilize its finances, and to have, at minimum, 45 days cash on hand, which equates to roughly \$34 million. W.A.P.A. also said the rate increase would bolster the market's confidence in the authority's bonds.

According to Moody's, W.A.P.A. has approximately \$127 million in electric system revenue bonds outstanding and approximately \$100 million in subordinated electric system revenue bonds.

In a press release issued this afternoon, W.A.P.A. Interim C.E.O., Julio Rhymer Jr., said the downgrade was expected in wake of the P.S.C.'s decision, along with W.A.P.A.'s deteriorating financial condition.

"In light of last week's decision by the Public Services Commission to delay action on a requested emergency rate increase, resulting in W.A.P.A.'s inability to amass sufficient days of cash on hand, the rating downgrade, originally scheduled for June 6 but acted on Thursday, was largely anticipated," Mr. Rhymer said. "The downgrade of senior bonds from Baa3 to Ba2 and subordinate bonds from Ba3 to Ba1, follows previous pronouncements by not only Moody's but by Fitch, another rating agency, which contends that W.A.P.A. is in a precarious financial position based largely on outstanding receivables, the lack of liquidity and a [multi-million dollar lawsuit](#) recently brought by a former fuel supplier."

Moody's said the rating action was prompted by the authority's weak liquidity profile, the potential need to refinance around \$23 million in outstanding credit lines that mature by end of June 2016, and the potential for additional liquidity requirements in the form of a \$25 million payment to former fuel supplier Trafigura Trading LLC, which might materialize over the next 12 months. Despite expected modestly improving operating cash flow generation owing to recent customer gains and access to a \$13 million term loan from the Rural Utility Service (RUS), W.A.P.A.'s financial flexibility will remain tight over the next 12 months if maturing credit lines cannot be extended. Bond debt service over the next 12 months is secured by a debt service and fully cash funded debt service reserve fund. The authority's unrestricted cash position of around \$13.7 million has been [bolstered by the Virgin Islands government's efforts](#) since the beginning of this year to reduce outstanding electric receivables to an estimated \$22 million as of today from a peak of around \$41 million at June 30, 2015. Moody's said while progress has been made on this front, the Ba2 rating on the senior electric system revenue bonds is, however, more consistent with the authority's weak management and governance practices evidenced by a short-term approach towards liquidity and financial management as well as frequent late filing of audited financial statements.

Mr. Rhymer said the two-notch drop in the authority's credit rating does not bode well for W.A.P.A. on the bond market. He said the territory's hospitals, along with some of the semi-autonomous agencies of the government, continue to owe the authority millions of dollars for past electrical and potable water service. These agencies, Mr. Rhymer said, are not current and have sizeable outstanding balances. "WAPA is literally subsidizing their operations while our finances deteriorate."

Moody's noted Mr. Mapp's proposal to incorporate a [permanent charge that recovers street lightning costs](#) to help bolster W.A.P.A., and it also mentioned the P.S.C.'s

reviewing of W.A.P.A.'s request, which could go either way following a 60-day review, as encouraging signs. However, while these efforts could positively impact W.A.P.A.'s financial performance in the medium term, their successful implementation is uncertain and unlikely to restore W.A.P.A.'s weak financial profile to levels commensurate with a higher rating in the short term, Moody's said.

Rating Outlook

The ratings remain on review for possible further downgrade.

Moody's review will focus on: (1) W.A.P.A.'s ability to restore financial flexibility by refinancing outstanding credit lines of around \$23 million before their maturity at the end of June 2016 and maintaining sufficient cash on hand to finance its operations and service its debt; (2) the pending lawsuit with former fuel supplier Trafigura Trading LLC, which alleges that the authority failed to pay overdue trade payables for fuel deliveries of around \$25 million; (3) the review of W.A.P.A.'s emergency base request which was denied for the time being but will be reviewed by an authorized hearing examiner over the next 60 days; and (4) the sustainability of the government's efforts to reduce outstanding government receivables as well as (5) the sustainability of the authority's efforts to strengthen its financial management.

Factors that Could Lead to an Upgrade

- A rating upgrade is currently unlikely; however the outlook could be stabilized in the event of:
- Successful refinancing of outstanding credit lines
- Improvement of liquidity sources to a level more in line with the Ba2 rating category (around 30 days cash on hand)
- Sustainable reduction of overdue government receivables

Factors that Could Lead to a Downgrade

- Inability to refinance outstanding credit lines
- Inability to improve cash on hand to a level that supports financing of ongoing operating expenses and debt service as well as expected additional calls on liquidity that would weaken its current liquidity

Despite Thursday's downgrade, which W.A.P.A. had been attempting to stave off through the implementation a multi-pronged action plan, Mr. Rhymer said efforts will continue to solidify the authority's financial condition.

"The action plan includes a commitment by the administration to continue addressing the outstanding streetlight obligation which has been significantly reduced and the obligations of the territorial hospitals; a strategy to right-size the Authority and the building of operational reserve—setting aside funds of about \$34 million dollars over two years---funds that can be used in the event existing lines of credit are called for immediate repayment," he said.

Mr. Rhymer cautioned that continued negative ratings can lead to firms currently on contract with W.A.P.A. requiring the authority to secure lines of credit to safeguard the financial commitments of those existing contracts.

“With low credit ratings, the cost of such credit lines could become very expensive...these are all costs that will ultimately be passed on to our customers, resulting in increased rates for the services provided by the Authority,” he said.

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