

The Virgin Islands Consortium

Moody's Downgrades WAPA Again, Gives Negative Outlook

Business / **Published On January 26, 2017 09:57 PM /**

Staff **January 26, 2017**



Coming on the heels of multiple downgrades of USVI bonds by all three major U.S. ratings firms -- Fitch, Moody's S&P -- Moody's on Wednesday downgraded the Virgin Islands Water and Power Authority's senior electric system revenue bond rating to Caa1 from B1 and the electric system subordinated revenue bond rating to Caa2 from B2.

The ratings outlook, like those of the USVI's bonds, is negative, according to Moody's.

As of January 2017, the authority had approximately \$118.8 million in rated senior electric system revenue bonds outstanding and approximately \$96.8 million in rated subordinated electric system revenue bonds, according to Moody's. The rating action is

prompted by growing pressure on WAPA's financial prospects in light of the authority's direct exposure to increasing economic and financial stresses in the U.S. Virgin Islands and an inability to disconnect itself from local economic conditions, including the continued slow payment pattern and weak financial profile of governmental customers and a very high adjusted net pension liability (around \$220 million). The rating action also considers VI WAPA's weak liquidity profile with currently around 5-7 days cash on hand. VI WAPA's limited financial resources constrain the authority's capacity to mitigate working capital swings as a result of slow payments of government receivables, absorb other unexpected calls on its liquidity profile and finance future capital expenditures to maintain the reliability of its electric system.

The authority's \$20 million working capital credit lines with FirstBank Puerto Rico (long-term bank deposit rating B1 negative) and Banco Popular de Puerto Rico (long-term deposit rating Ba2 negative) are fully drawn and mature on June 25, 2017. A positive for bondholders is the recent interim base rate increase that will be effective February 1, 2017 and that could provide the authority with around \$14.5 million in additional annual revenue. VI WAPA currently expects that the Public Services Commission (PSC) will decide by end of June 2017 whether the interim base rate becomes a permanent base rate increase. This additional revenue should provide VI WAPA with sufficient liquidity resources to address short-term liquidity needs including any beginning amortization of the up to \$160 million LPG projects costs, once the project reaches substantial completion later this year, as well as continued amortization of the \$20 million obligation to its former fuel supplier Traftura.

In addition, according to Moody's, bondholders benefit from a fully funded debt service fund and a fully funded debt service reserve fund which cover debt service by around 1.6 times. VI WAPA's rating recognizes the challenges of operating within an island economy with relatively sluggish growth, high unemployment and a narrow local economy that is dependent on discretionary tourism, and the ongoing struggle of the authority to cover its cost base and operate its facilities efficiently given significant excess capacity, the age of its equipment and high retail rates. We acknowledge the regulatory support the utility has received as it has progressed toward the near completion of a project to convert its base-load generation resources from oil-fueled to tri-fueled (initially propane), thereby lowering the cost of electricity for Virgin Islands ratepayers while reducing its deferred fuel balances. We view the completion of this project as an important milestone towards strengthening VI WAPA's long-term credit quality.

Rating Outlook

The negative outlook reflects the weak liquidity profile of the authority partially caused by high outstanding receivables from governmental customers and VI WAPA's inability to disconnect itself from the financial and economic stress in the U.S. Virgin Islands.

Factors that Could Lead to an Upgrade

Improvement in the authority's liquidity profile

Improvements in the credit quality of the Government of the US Virgin Islands

Rate increases supporting improved cost recovery and translating into improvement of financial metrics with Moody's total fixed charge coverage ratio improving to 1.0x

Factors that Could Lead to a Downgrade

Continued deterioration of VI WAPA's liquidity profile and financial metrics, threatening the long-term sustainability of the authority and making a restructuring of its debt more likely.