

The Virgin Islands Consortium

Moody's Downgrades WAPA Bonds Further Into Junk Status, Citing Default Risk, High Debt Load And Other Factors

Business / **Published On October 02, 2019 11:18 AM /**

Staff **October 02, 2019**



Moody's Investors Service on Sept. 23 downgraded Virgin Islands Water and Power Authority's senior electric system revenue bond rating to Caa2 from Caa1 and the electric system subordinated revenue bond rating to Caa3 from Caa2. The outlook remains negative. Moody's downgrades followed Fitch's [negative watch on WAPA bonds on Sept. 20](#).

Moody's said the downgrade of the senior electric system revenue bond rating to Caa2 reflects Moody's view that the default risk of the Virgin Islands Water and Power Authority

has increased given an unsustainable capital structure with very tight liquidity, high debt load including a substantial unfunded pension liability, the increased frequency of power outages, reducing the reliability of the electric system, high electric rates, and chronic challenges facing the economy. The Caa3 subordinate lien electric system revenue bond rating reflects the junior position of these securities relative to the senior lien electric system revenue bonds, Moody's said.

In Moody's view, WAPA's capital structure is unsustainable without improvements in WAPA's operating cash flow generation, given the weak liquidity profile with no unrestricted cash on balance sheet and use of overdrafts to manage liquidity, and a history of difficulties to pay fuel suppliers on time. A temporary surcharge for additional leased generating units was approved earlier this year but the authority's retail rates are the highest among US states and territories, and resistance against future rate increases could increase if WAPA is unable to restore the reliability of the electric system in the near term, particularly given the chronic economic challenges, Moody's said.

The ratings agency said WAPA's ratings continue to be constrained by a challenged local economy and service territory (already before hurricanes Irma and Maria in 2017) and vulnerability to weather-related events such as hurricanes.

"We also note that VI WAPA has a very large unfunded pension liability, has higher annual debt service requirements owing to the Vitol capital lease, and faces increased refinancing risk over the next several years as nearly 40 percent of its senior and subordinated debt matures through 2022, some of which includes bullet or balloon obligations needing to be refinanced," said the ratings firm.

Nevertheless, the ratings recognize recent positive developments. These include for instance that the government has paid down overdue receivables at the end of July 2019 and FEMA and HUD grants have provided funds to invest in the hardening of the transmission & distribution system against future hurricanes and the acquisition of new, efficient generating units and increased renewable energy projects, Moody's said.

Financial reporting has improved with the new management providing regular updates on the use of FEMA grants, operations and unaudited financials on EMMA on a monthly basis, according to Moody's.

Nevertheless, the FY 2018 (ending June 30, 2018) audit has not been published yet. Overall management and governance practices remain weak. Moody's confirmed the issuer rating assigned to the Government of the US Virgin Islands at Caa3 with a stable outlook on September 19, 2019.

Rating outlook

The negative outlook considers WAPA's very weak liquidity, very high retail electric rates, growth challenges within the economy and the recent high frequency of power outages, reducing the reliability of the electric system, Moody's said.

Factors that could lead to an upgrade

- Improvement in the authority's liquidity profile

- Improved reliability of the electric system
- 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.
- Improvement in the credit quality of the Government of the US Virgin Islands

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
- Deterioration in the credit quality of the Government of the US Virgin Islands
- Debt restructuring and/or prospects for recovery rate worsen