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Ratings

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Summary:

Fort Pierce Utilities Authority, Florida; Combined Utility

Primary Credit Analyst:
Timothy P Meernik, Centennial + 1 (303) 721 4786; timothy.meernik@spglobal.com

Secondary Contact:
Nicole Shen, New York (1) 332-323-4605; nicole.shen@spglobal.com

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Summary:

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Credit Profile		
US$145.265 mil util rfdg rev bnds ser 2022 dtd 06/21/2022 due 10/01/2052		
Long Term Rating	A/Stable	New
Fort Pierce Util Auth COMBUTIL (AMBAC)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Fort Pierce Util Auth util (ASSURED GTY)		
Unenhanced Rating	A(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Rating Action

S&P Global Ratings assigned its 'A' long-term rating on the Fort Pierce Utilities Authority (FPUA, or the authority), Fla.'s $145 million series 2022 utilities refunding revenue bonds. At the same time, S&P Global Ratings affirmed its 'A' long-term rating and underlying rating (SPUR) on FPUA's utility bond obligations outstanding. The outlook is stable.

As of Sept. 30, 2021, FPUA had $54 million in debt outstanding. Net revenue of Fort Pierce's water, wastewater, electric, natural gas, and fiber systems secures the bonds.

FPUA will use the series 2022 bonds to finance various capital improvements, including a new wastewater treatment plant, and refund the series 2009 bonds outstanding. About $30 million of the debt issuance is for the refunding.

We consider bond provisions credit neutral. The bonds have a rate covenant requiring net revenue to equal or exceed 1.25x annual debt service coverage (DSC); FPUA can issue additional bonds if certain conditions are met.

Credit overview

The rating reflects our view of FPUA's diverse revenue stream from several utility systems. In addition, the authority's customer base has grown consistently in recent years, which we expect to continue. However, we expect financial metrics will somewhat weaken over the coming years. The series 2022 issuance and other capital needs will result in thinner liquidity and a higher debt burden, although we believe all-in DSC, liquidity, and the debt-to-capitalization ratio will remain at levels that, in our view, support the rating.

The rating further reflects our view of FPUA's:

- Robust economic growth in the service area, while recognizing median household effective buying income (EBI) in Fort Pierce is only 59% of the national level, which could restrain rate-raising flexibility;
- Adequate water supply and treatment capacity for the foreseeable future and participation in the Florida Municipal Power Agency's (FMPA) all-requirements power supply project (ARPSP), which provides the authority with a diverse power supply in terms of shafts; and

- Credit-supportive adjustment mechanisms for the electric and natural gas systems, allowing the authority to pass through wholesale cost changes in a timely manner to its retail customers.

Partly offsetting the above strengths, in our view, are FPUA's:

- Electric rates 12% above the state average on a weighted-average basis, along with significant electric, water, and wastewater rate increases planned for the coming months;
- All-in DSC of 1.21x to 1.32x over the next several years as debt service increases, which is a weakening from the recent levels; and
- Declining liquidity, which we project near 50 days of operations with less than $15 million in available reserves in fiscal 2022, a drop from 90 days and more than $20 million at the end of fiscal 2021.

The stable outlook reflects our forward-looking view that FPUA will gradually improve its all-in DSC and liquidity as the authority implements annual base rate increases over the next several years and continues to use its electric and natural gas adjustment mechanisms. In addition, the revenue stream diversity provided by the combined utility benefits the authority by mitigating major fluctuations within any particular system.

Environmental, social and governance

In our view, FPUA's environmental exposures are elevated relative to those of peers. Fort Pierce is on the Atlantic coast, exposing the authority to hurricanes and sea level rise. The authority is constructing a new wastewater treatment plant partly because the existing plant is located on a barrier island, near sensitive habitat. We note that hurricanes have not materially affected FPUA in recent years and that the authority continues to harden its infrastructure, including buildings' roofs, electric pole replacements, and undergrounding electric lines. On the electric system, the authority obtains electricity largely from fossil fuels. In fiscal 2020, the authority's fuel mix was 80% natural gas, 13% coal, and a small amount of nuclear and solar resources. (Florida does not have a renewable portfolio standard.) While the coal percentage is modest, FPUA could be subject to future environmental regulations on carbon dioxide emissions. In addition, there are negative environmental attributes associated with natural gas extraction and transmission.

We believe the authority's social risk factors are elevated compared with those of other rated utilities because of low median household EBI in the service area coupled with sizable rate increase plans, which results in weaker rate affordability. During the early months of the COVID-19 pandemic, FPUA had a moratorium on customer shutoffs. Customers who were unable to pay their bills were placed on payment plans. The accounts receivable balance gradually declined to $6.6 million at the end of fiscal 2021 from $7.9 million at the end of fiscal 2020.

We believe FPUA's governance factors are credit neutral. The authority annually produces five-year financial forecasts and capital improvement plans. We view these plans favorably because they can provide guidance, help identify problems, and require a forward-looking view. FPUA has implemented cybersecurity processes that we view positively.

Stable Outlook

Downside scenario

We could lower the rating if all-in DSC declines significantly below projected levels, possibly as a result of greater-than-anticipated capital needs, or if unforeseen capital needs result in a significant drawdown in unrestricted cash and investments. Given significantly below-average income levels, the rating could come under pressure in case of cost overruns for capital projects or resistance to rate increases.

Upside scenario

Given customers' weak median household EBI and the authority's planned rate increases, as well as projections of weaker financial metrics, we do not expect to raise the rating over the next two years.

Credit Opinion

In fiscal 2021, FPUA's water and wastewater systems accounted for 57% of net operating revenue and the electric and natural gas systems provided 44%. (The fiber system's net revenue contribution was negative 1%.) Because the water and wastewater systems account for more than half of net operating revenue, we have applied our criteria "U.S. Municipal Water, Sewer, And Solid Waste Utilities: Methodology And Assumptions," published April 14, 2022, on RatingsDirect. We note, however, that the analysis incorporates the operational and financial characteristics of the electric, natural gas, and fiber systems.

FPUA's service area economy has positive and negative credit attributes. Residential customers provide almost half of the authority's operating revenue, and we view these customers as having more stable demand profiles than commercial and industrial customers have. Also, customer concentration in the service area is insignificant. St. Lucie County, where Fort Pierce is located, has had strong economic growth and the unemployment rate in Fort Pierce was 3.8% in March 2021, below the national average of 4.3%. Median household EBI is weak in Fort Pierce, although we note it is much better in St. Lucie County. (About 22% of FPUA's revenue comes from outside the City of Fort Pierce.) In our view, the income levels constrain revenue-raising flexibility.

The authority's water and wastewater rates are affordable, in our view. The average residential customer's combined water and wastewater bill was about $90 in fiscal 2021, or 3% of median household EBI. However, electric rates were 112% of the state average in 2020, according to data from the U.S. Energy Information Administration. In the coming months, FPUA plans to raise water and wastewater rates by 20% and electric rates by 10%, subject to approval from the city commission. We view the rate increases as significant, particularly considering the income levels. These rate increases are needed to meet growing operating and capital expenses.

FPUA's water system has adequate supply and treatment capacity for the foreseeable future. The authority obtains water from 36 surficial aquifer wells and 11 Floridan aquifer wells. FPUA has a 20 million gallon per day (mgd) conventional plant and a 10.3 mgd reverse osmosis plant; average daily treatment was about 10 mgd in fiscal 2021. Unaccounted-for water was 6.3% in fiscal 2021, which we view as low. On the wastewater system, the authority will construct the Mainland Water Reclamation Facility in the coming years. The facility will be less exposed to extreme

weather and sea level rise because it will be located inland and will also enable FPUA to avoid costly environmental upgrades needed at the existing Island Water Reclamation Facility. The Island Water Reclamation Facility has sufficient capacity to meet the authority's needs for the next few years.

We believe the electric system's participation in FMPA's ARPSP provides FPUA with a diverse power supply. FMPA participates in several electricity generation stations: the St. Lucie Power Plant, Stanton Energy Center, Indian River Generating Station, Cane Island Power Park, Treasure Coast Energy Center, the Stock Island Generating Facility, and a solar project. FPUA's contract with FMPA is a 30-year evergreen, automatically renewing each year unless notice given. In addition, we understand that Stanton Unit 1 will retire by 2025 and Stanton Unit 2 will transition to natural gas-fired generation. With the retirement of Stanton Unit 1 in a few years, FMPA is examining whether it needs to procure additional resources. In our view, FPUA is somewhat protected from electricity supply planning because of participation in the ARPSP.

FPUA's cost recovery has been healthy over fiscal years 2019 to 2021, with all-in DSC averaging 1.47x. All-in DSC is S&P Global Ratings' internally adjusted coverage metric that treats 50% of FPUA's purchased power costs as debtlike and transfers out of the utility as an operating expense. Based on our analysis of management provided financial projections, we expect that all-in DSC will decline to 1.21x to 1.32x over the next three years as debt service increases before reaching 1.4x in fiscal 2026. We view FPUA's projections as generally conservative, while also noting the authority projects flat purchased power costs for the electric system. If power costs increase significantly in future years, all-in DSC may be lower than projected.

In our view, FPUA's liquidity position will weaken in the coming years, providing the authority with a modest financial cushion. At the end of fiscal 2021, FPUA had $20.8 million in unrestricted cash and investments, representing 90 days of liquidity. Financial projections suggest a drawdown of unrestricted reserves to $14.7 million, or 53 days, in fiscal 2022. Liquidity will not material improve until the out-years of the forecast as FPUA uses some reserves for capital needs.

At the end of fiscal 2021, FPUA had a small amount of debt, in our view, with a debt-to-capitalization ratio of 21%. As a combined utility, FPUA has a more capital-intensive profile than a single-system, distribution-only utility. With the series 2022 issuance, we expect the debt-to-capitalization ratio to increase to near 45%, which we view as still manageable for the authority.

Including the projects funded by the series 2022 issuance, FPUA's five-year capital improvement plan totals about $240 million. The authority plans to largely fund the remainder of the plan with various internal funding sources. Some additional debt may be needed depending on the ultimate cost of the new wastewater plant and the availability of grant funding. The utility's defined benefit pension plan is well funded (99.8%) and other postemployment benefit obligations are minimal.

Related Research

Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

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