

## **FITCH AFFIRMS ANCHORAGE ML&P'S (AK) ELECTRIC SYSTEM REV BONDS AT 'A+'; OUTLOOK STABLE**

Fitch Ratings-San Francisco-07 October 2016: Fitch Ratings has affirmed its 'A+' rating on the following bonds issued by Anchorage, AK on behalf of Anchorage Municipal Light and Power (ML&P):

--\$338,355,000 senior lien electric revenue bonds, series 2005A, 2009A, 2009B, and 2014A.

The Rating Outlook is Stable.

### **SECURITY**

The bonds are secured by a pledge of net revenues of the electric system.

### **KEY RATING DRIVERS**

**VERTICALLY INTEGRATED RETAIL SYSTEM:** ML&P is an enterprise fund of the Municipality of Anchorage providing generation, transmission, and distribution of electricity to approximately 30,932 customers within the municipality.

**SOLID FINANCIAL PERFORMANCE:** Financial performance remains solid with debt service coverage at 2.26x and a healthy operating margin of 17.8% in 2015. Financial projections show coverage levels remaining at or above 2015 levels through 2020.

**ADEQUATE CASH LEVELS:** The system's unrestricted cash levels improved to \$23.3 million or an adequate 81 days in 2015. Liquidity levels are expected to improve significantly in 2016 with an end of August balance of approximately \$42 million driven by solid operating performance, less capital spending, and regulatory restrictions preventing the utility's relatively high dividend payment to the municipality.

**NEW, EFFICIENT GENERATION ASSETS:** ML&P is replacing older, less efficient generation assets through its ownership in the Southcentral Power Plant (SPP) and construction of Plant 2A. The highly efficient, natural gas-fired combined cycle plants are expected to improve reliability and significantly decrease fuel consumption.

**LONG-TERM GAS SUPPLY SECURED:** ML&P recently increased its ownership interest in the Beluga River Gas Field, a well-maintained, mature, on-shore gas field that has provided the majority of the system's gas needs over the past decade. Fuel supply needs are projected to be largely met through 2033 following the acquisition.

**REGULATED RATE SETTING:** ML&P's rates are regulated by the Regulatory Commission of Alaska (RCA), along with most other Alaskan utility systems, which is uncommon for retail public power entities. ML&P's relationship with the RCA appears constructive and ML&P has historically received favorable rulings on rate requests. Relatively large projected rate increases and some evidence of ratepayer sensitivity to rate changes may reduce ML&P's financial flexibility to some degree.

**HIGH DEBT LEVELS:** ML&P's debt levels are high for the rating, but expected to moderate gradually with no additional new money issuances planned.

### **RATING SENSITIVITIES**

Date: 12/15/17 Exh # 171  
Regulatory Commission of Alaska  
U-18-094 By: BP U-17-000  
Northern Lights Realtime & Reporting, Inc.  
(907) 337-2221

**MLP1468**

RATE INCREASES: Anchorage Municipal Light and Power's ability to implement planned rate increases following the commercial operation of Plant 2A, which is expected before the end of 2016, is important to maintaining the rating at its current level.

## CREDIT PROFILE

ML&P is an enterprise department of the Municipality of Anchorage (rated 'AA+/Stable') that provides electric generation, transmission, and distribution services within a portion of the municipality. ML&P's exclusive, 19.9-contiguous-mile service territory includes a large portion of the municipality's commercial and high-density residential area. ML&P's customer base is largely residential, although energy demand and operating revenues are driven by commercial entities.

## SOLID FINANCIAL PROFILE

The utility's financial performance has improved recently compared to historical trends with moderately higher coverage and liquidity levels. Fitch-calculated debt service coverage was 2.26x in 2015 (unaudited), which was well above the utility's average coverage from 2011-2014 of 1.77x. The improved coverage reflects lower debt service costs of approximately \$27.3 million in 2015 compared to approximately \$33.2 million in 2014. ML&P's projected financial performance maintains debt service coverage at or above 2015 levels.

ML&P's unrestricted cash balance increased in 2014 and 2015 following a larger than expected decline in 2013. The ending 2015 balance (unaudited) was \$23.3 million or 81 days cash on hand compared to an ending 2013 balance of approximately \$7.1 million or just 40 days cash.

Unrestricted cash is up significantly in 2016 with approximately \$42 million on hand at the end of August. The sharp increase is due to reduced costs, lower capital spending as plant 2A nears completion, and the RCA's recent restriction on ML&P's dividend to the municipality. Timing issues are projected to result in a decline in the unrestricted cash balance to around \$18.3 million in 2017, according to management's projections. However, cash balances are projected to gradually increase back to current levels from 2018 - 2020.

The utility's combined transfer payment to the municipality -including dividends and payments in lieu of taxes - is relatively high at 9.5% of operating revenue or \$14.6 million in 2015. The RCA has restricted ML&P's dividend payment, which accounted for approximately \$8.8 million in 2015, due to concerns regarding the utility's equity position. Management is currently updating ML&P's equity management plan, although it is uncertain when the dividend restriction will be lifted.

## NEW GENERATION

ML&P is nearing the end of a significant capital program to modernize its thermal generation capacity as existing assets have grown increasingly older and less efficient. With the exception of a 30-MW gas-fired turbine built in 2007 and the early 2013 completion of SPP, which is co-owned with Chugach Electric Association (Chugach; rated 'A'/Stable), the newest unit owned by ML&P was installed in 1984. Following the completion of Plant 2A, which is expected to be commercially available in the fourth quarter of 2016, ML&P will own some of the most efficient generation resources in the railbelt area.

## FUEL SUPPLY

ML&P's fuel supply is projected to be nearly fully met through 2033 following the utility's purchase in February 2016 of an increased portion of the Beluga River Gas Field. ML&P's ownership interest in the field increased to approximately 56.7% from 33% as a result of the acquisition, which saw ML&P purchase 70% of ConocoPhillip's one-third interest in the field.

ML&P financed the \$103 million purchase with internal funds, the bulk of which were restricted by the RCA towards future fuel supply purchases. Chugach purchased the remainder of ConocoPhillip's ownership share as part of the transaction. The Beluga River Gas Field is currently owned by ML&P (56.67%), HilCorp (33.3%), and Chugach (10.0%).

ML&P has largely relied on gas from the Beluga River Gas Field to meet all of its gas needs since 2005. HilCorp will operate the well-maintained, mature, on-shore gas field.

#### HIGH DEBT LEVELS

ML&P's debt metrics are high for the rating. Debt per electric customer is approximately \$15,313 and debt-to-funds available for debt service (FADS) is at 7.7x. The utility has no new money debt issuance plans over the next five years, which should lead to a gradual moderation in the utility's debt load. Management plans on financing the \$206.2 million, five-year capital plan primarily with unrestricted cash reserves.

#### Contact:

Primary Analyst  
Matthew Reilly, CFA  
+1-415-732-7572  
Director  
Fitch Ratings, Inc.  
650 California St, 4th Floor  
San Francisco, CA 94108

Secondary Analyst  
Lina Santoro  
Analytical Consultant  
+1-212-908-0522

Committee Chairperson  
Dennis Pidherny  
Managing Director  
+1-212-908-0738

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: [elizabeth.fogerty@fitchratings.com](mailto:elizabeth.fogerty@fitchratings.com).

Additional information is available at 'www.fitchratings.com'.

Applicable Criteria  
Revenue-Supported Rating Criteria (pub. 16 Jun 2014)  
<https://www.fitchratings.com/site/re/750012>  
U.S. Public Power Rating Criteria (pub. 18 May 2015)  
<https://www.fitchratings.com/site/re/864007>

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