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Rating Action: Moody's assigns Aa2 and Aa3 to JEA (FL) sr. and sub. electric system rev. bonds; revises outlook to negative

08 Dec 2017

New York, December 08, 2017 -- Issue: Electric System Revenue Bonds, Series Three 2017B; Rating: Aa2; Rating Type: Underlying LT; Sale Amount: \$185,000,000; Expected Sale Date: 12/29/2017; Rating Description: Revenue: Government Enterprise;

Issue: Electric System Subordinated Revenue Bonds, 2017 Series B; Rating: Aa3; Rating Type: Underlying LT; Sale Amount: \$200,000,000; Expected Sale Date: 12/29/2017; Rating Description: Revenue: Government Enterprise;

Summary Rating Rationale

Moody's Investors Service today assigned an Aa2 rating to the planned issuance by JEA (FL) of approximately \$185 million of senior lien electric system revenue bonds, Series Three 2017B and an Aa3 rating to JEA's planned issuance of approximately \$200 million of electric system subordinated revenue bonds, 2017 Series B.

Concurrently, Moody's revised JEA's rating outlook to negative from stable while affirming the Aa2 rating on about \$1.138 billion of JEA's senior lien electric system revenue bonds, the Aa3 rating on about \$1.063 billion of JEA's subordinate lien electric system revenue bonds, the Aa2 ratings on about \$450.2 million of JEA's St. Johns River Power Park System (SJRPP) revenue bonds and about \$106 million of JEA's Bulk Power Supply System revenue bonds (Plant Scherer revenue bonds) in all instances outstanding at September 30, 2017.

Proceeds from the planned offering of Electric System Revenue Bonds, Series Three 2017B and Electric System Subordinated Revenue Bonds, 2017 Series B will be used to refund certain of JEA's outstanding Electric System Revenue Bonds and Subordinated Revenue Bonds, respectively, and in both instances to also pay for any related costs of issuance.

The change in rating outlook to negative reflects the increasingly pressing credit challenges facing JEA owing to the exposure to new nuclear construction with its 20-year purchased power agreement (PPA) with the Municipal Electric Authority of Georgia (MEAG Power) for 206 megawatts (MWs) of capacity from the much delayed and over-budget Vogtle nuclear project. The change in outlook also recognizes the fact that JEA faces continuing lackluster increase in demand for electricity in its service territory which contributed to a long capacity position. We view the terms of the take-or-pay agreement for the Vogtle PPA as debt which equates to an owner's risk and obligation that will continue to be paid even if the project is terminated. As such, our quantitative analytical focus, which incorporates the debt-like payments associated with the take-or-pay PPA through the fixed obligation charge coverage (FOCC) ratio, is expected to produce metrics that will be weak for the mid-Aa rating category.

JEA's credit still reflects positive qualities, including an unregulated rate setting process and management's good track record of exercising rate autonomy to achieve financial goals and maintain robust liquidity. Even with a series of general rate increases over multiple years, most recently effective December 1, 2016, JEA is maintaining reasonably competitive retail rates for all customer classes. The credit is also supported by strategies focusing on diversifying the generation resource mix and maintaining ownership of good quality transmission assets to reliably serve its customers while maintaining competitive rates. JEA's recently implemented new general funds transfer agreement with the City of Jacksonville and other pension reform steps taken to address the City's underfunded pension plan obligations are credit positive developments that should preclude excessive demands on JEA's strong cash resources and be supportive of credit quality. Although JEA has historically maintained solid adjusted debt service coverage on average in excess of 2.0x and over 250 days of liquidity, in the absence of additional base rate increases or above average service territory growth, we anticipate JEA having considerably less financial flexibility prospectively as the impact of Project J debt results in JEA's FOCC being below 1.80x on a sustained basis in ensuing years.

The Aa2 rating for the SJRPP bonds and the Plant Scherer revenue bonds incorporate the fact that the debt service for these series of bonds are paid as an operating expense of JEA prior to the debt service on the Electric System revenue bonds and the Electric System subordinated bonds. The subordinate lien rating is Aa3, reflecting the weaker security provisions related to the subordinate lien bonds.

Rating Outlook

The negative rating outlook for JEA's electric system, SJRPP and Bulk Power System revenue bonds reflects the increasingly pressing credit challenges JEA faces owing to the exposure to new nuclear construction with its 20-year PPA with MEAG Power. The change in outlook also recognizes the fact that JEA faces continuing lackluster increase in demand for electricity in its service territory which contributed to a long capacity position. We view the terms of the take-or-pay agreement for the Vogtle PPA as debt which equates to an owner's risk and obligation that will continue to be paid even if the project is terminated. As such, when incorporating these obligations into our quantitative approach, we anticipate JEA producing an FOCC that will be weak for the mid-Aa rating category.

Factors that Could Lead to an Upgrade

The rating is not likely to be upgraded in the near to intermediate term owing to the negative outlook and ongoing nuclear construction risk

The outlook could stabilize if JEA introduces additional strategies to avoid the anticipated decline in its financial flexibility as the Vogtle project moves forward and payments to MEAG Power increase under the PPA and pressure the adjusted FOCC ratio

Factors that Could Lead to a Downgrade

In terms of metrics, sustained erosion of adjusted days liquidity below 250 days and/or prospects for sustained weakening of the FOCC ratio below 1.8x for the electric system could result in a lower rating

Further construction delays and cost overruns at the Vogtle project materially beyond the latest revised schedule and cost to complete

Legal Security

JEA's senior lien bonds have a rate covenant that requires net revenues to cover debt service by 120% and an additional bonds test that requires net revenues to cover maximum annual debt service by 120%. A renewal and replacement account is required to be funded at least equal to 5% of gross revenues of the preceding year or 10% of net revenues of the preceding year. Senior lien bonds are also secured by a debt service reserve sized at maximum annual interest, which we consider to be a weak protection measure for bondholders.

JEA's subordinate lien bonds are payable from a subordinate lien on the net revenues of JEA's electric system. Subordinate lien bonds have a sum-sufficient rate requirement and adjusted net revenues must also be at least equal to 115% of debt service on the senior and subordinate lien bonds. There is a sum-sufficient additional bonds test. Subordinate lien bonds do not require a debt service reserve, which we consider to be a weak protection measure for bondholders.

As of FYE 2017, JEA had approximately \$167.9 million aggregate principal amount of SJRPP Revenue Bonds outstanding under its First Power Park Resolution (the First Resolution), which are referred to as "Issue Two Bonds" and approximately \$282.3 million aggregate principal amount of SJRPP Revenue Bonds outstanding under its Second Power Park Resolution (the Second Resolution), which are referred to as "Issue Three Bonds".

Issue Two Bonds under the First Resolution are payable solely from and secured by a pledge of and lien on revenues of JEA's 80% ownership interest in the SJRPP, along with other available pledged funds, including contract debts that are payable as an O&M cost of the JEA Electric System and FPL under a joint ownership agreement between JEA and FPL. The respective payments of JEA and FPL with respect to the SJRPP are several and not joint.

Related Issuers
JEA, FL
JEA, FL - Electric Enterprise

Related Research
Credit Opinion: JEA, FL - ELECTRIC ENTERPRISE: Update to analysis following downgrade
Announcement of Periodic Review: Moody's announces completion of a periodic review of ratings of JEA, FL - Electric Enterprise
Announcement of Periodic Review: Moody's announces completion of a periodic review of ratings of JEA, FL - Electric Enterprise
Rating Action: Moody's downgrades to Aa2 JEA, FL Variable Rate Water and Sewer System Revenue Bonds LOC-backed 2008 Series A-2
Rating Action: Moody's downgrades JEA (FL) Electric Enterprise ratings to A2 for senior lien revenue bonds; outlook negative



Debt service requirements for Issue Three Bonds governed by the Second Resolution are the sole responsibility of JEA. The Second Resolution permits the use of a surety bond to satisfy the debt service reserve requirement and allows for issuance of variable rate debt with payment terms other than April 1 and October 1. Under the Second Resolution, the debt service reserve is a weak level of protection for bondholders in our view since it is established at maximum annual interest. The debt service reserve under the First Resolution governing Issue Two Bonds is more protective of bondholder interests since it is based upon average annual debt service.

JEA's Bulk Power Supply System Scherer 4 Project issue is secured by a pledge of and a lien on the proceeds of the bonds; the revenues as defined in the Bulk Power Supply System resolution are all revenues derived from ownership and operation of the project. JEA is required to make payments from the electric system as an O&M expense into the Plant Scherer Project Revenue Fund for any output, capacity, use and service of the project at least equal to 115% of the aggregate debt service. The debt service reserve account is required to be at maximum annual interest, which we view as a weak protection measure for bondholders.

Use of Proceeds

The proceeds from the planned offering of Electric System Revenue Bonds, Series Three 2017B and Electric System Subordinated Revenue Bonds, 2017 Series B will be used to refund certain of JEA's outstanding Electric System Revenue Bonds and Subordinated Revenue Bonds, respectively, and in both instances to also pay for any related costs of issuance.

Obligor Profile

JEA is a municipal utility whose service territory covers Jacksonville, Florida (Duval County), and parts of three adjacent counties. It is split into three enterprise funds, including the Electric Enterprise; the Water and Sewer Enterprise Fund; and the District Energy System. The Electric Enterprise is comprised of the JEA Electric System, the Bulk Power Supply System, and St. Johns River Power Park System. Jacksonville is a major ground transportation center and is also considered a significant rail hub and has one of the largest ports on the South Atlantic Seaboard. The local economy is diversified among defense, transportation and distribution, financial services, consumer goods, information services, manufacturing and insurance sectors. Statistics from Moody's economy.com indicate that Jacksonville fares well versus the U.S., as it has been doing since the recession's end and slow gradual recovery.

Methodology

The principal methodology used in these ratings was US Public Power Electric Utilities With Generation Ownership Exposure published in November 2017. Please see the Rating Methodologies page on www.moody's.com for a copy of this methodology.

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