

FITCH AFFIRMS GAINESVILLE REGIONAL UTILITIES BONDS (FL) AT 'AA-' & TAX-EXEMPT CP AT 'F1+'

Fitch Ratings-New York-22 November 2016: Fitch Ratings has affirmed the ratings on the following bonds for the city of Gainesville, Florida:

--Approximately \$900 million in outstanding utility system revenue bonds, multiple series at 'AA-';

--\$85 million utilities system tax-exempt commercial paper (CP) notes program series 2010C at 'F1+'.

The Rating Outlook is Stable.

SECURITY

The revenue bonds are secured by a first lien on the net revenues of Gainesville Regional Utilities (GRU), which is the combined electric, gas, water, wastewater and telecom systems (collectively, the system) supporting the city of Gainesville, FL. The CP notes are secured by an interest in GRU's net revenues that is subordinate to senior-lien indebtedness.

KEY RATING DRIVERS

COMBINED UTILITY SYSTEM: GRU is a combined utility system providing retail electric, gas, water, wastewater, and telecom services to the city of Gainesville, FL and surrounding areas. The electric utility is the largest system, accounting for 56% of combined revenue. Electric rates rank among the highest in the state, while other utility rates are generally more competitive. Each individual utility is self-supporting and financially stable.

HEALTHY SERVICE AREA DEMOGRAPHICS: Service is provided to and around the city and certain locations of the University of Florida, which helps anchor the service area. Steady population growth and new development continue to be viewed favorably and no customer concentration exists.

COSTLY BIOMASS PROJECT: GRU's long-term contractual commitment to purchase capacity and output of a costly, privately-owned biomass facility (Gainesville Renewable Energy Center [GREC]), remains a significant cost driver for the electric system. However, GRU has dispatch responsibilities for GREC, which has been kept idle since mid-August of 2015. Energy has been replaced by lower-cost market purchases, but fairly sizable fixed capacity payments associated with GREC continue.

ELEVATED DEBT: Leverage ratios, including debt to funds available for service (FADS) and equity to capitalization of 8.6x and 19.5%, respectively, are weak for the rating category but should improve over GRU's forecast period ending in fiscal 2021. Scheduled principal amortization should more than offset modest additional borrowing plans.

STABLE FINANCIAL RESULTS: Despite higher fixed costs related to GREC, GRU's financial results on a combined basis have been stable due to cost reduction efforts, manageable general fund transfers and the city commission's willingness to raise rates. Fitch-adjusted debt service coverage (DSC) has declined from stronger levels prior to 2013 but was still solid at roughly 1.90x

over the past two years. Liquidity, including ample cash reserves and credit facilities, is sound and underpins the 'F1+' rating on the tax-exempt CP note program.

RATING SENSITIVITIES

CHANGE IN FINANCIAL PROFILE: Insufficient rate relief by the city commission and/or greater than forecast increases in transfer payments to the city that cause margins and cash flows needed for capital spending to significantly decline would be viewed negatively.

LONG-TERM RATING AND LIQUIDITY: GRU's Short-term 'F1+' rating could be downgraded if GRU is unable to maintain a long-term rating of at least 'A+'.

CREDIT PROFILE

The city of Gainesville is located in north-central Florida and is the home of the University of Florida (UF). Including the large student population, the city has an estimated population of about 128,000, making it the largest city in Alachua County. UF's fall 2016 enrollment exceeded 54,000 and the university remains the largest employer in the county with more than 27,500 employees. Overall, the city's employment base is well diversified among the healthcare, higher education, and light industrial and commercial sectors.

STABLE FINANCIAL PERFORMANCE AND METRICS

GRU's financial performance has been solid historically, although a decline in metrics over the past few years has resulted from a combination of larger annual debt service payments and higher operating costs related to energy and capacity purchases from GREC. GRU began making payments on GREC, a privately owned biomass facility, once commercially available in late 2013. Despite expectations for lower financial metrics/margins and DSC beginning in fiscal 2014, GRU management and the city commission have taken several positive steps to stabilize financial performance, including the implementation of a system-wide cost reduction program, debt refinancing and support for larger, near-term electric rate adjustments.

Financial metrics, while weaker than historical levels, stabilized at fairly sound levels as evidenced by Fitch-calculated DSC of 1.90x in fiscals 2014 and 2015. Including transfers to the city's GF, coverage is lower but still solid for the rating at 1.55x and 1.62x in 2014 and 2015, respectively. Including rate stabilization funds, liquidity remained healthy with 218 days cash on hand in fiscal 2015.

While GREC provides a hedge against future potential carbon emission and renewable portfolio standards, management has decided not to dispatch GREC, which has been idle since mid-2015. GREC's high total costs and the low gas prices over the past two years have compelled management to keep GREC offline and purchase more affordable replacement energy through market purchases. Management believes the cost savings total approximately \$10 million annually.

AMPLE LIQUIDITY SUPPORTS SHORT-TERM REQUIREMENTS

GRU incorporates a risk management study for each of its utilities and sizes the cash reserves needed to support the levels of risk identified by the risk indicators. The utility has identified a cash reserve target of \$59 million for fiscal 2017. GRU also maintains two commercial paper programs totaling \$110 million which provide additional liquidity; \$85 million of authorized tax-exempt commercial paper (\$45.9 million outstanding) and \$25 million of authorized taxable commercial paper (\$8 million outstanding; not rated by Fitch).

The 'F1+' rating reflects GRU's long-term rating and ample internal liquidity, including monies in a rate stabilization fund, totaling approximately \$194 million, in addition to supporting credit agreements with Bank of America and State Street Bank as of Aug. 31, 2016. Credit facilities totaling \$85 million with Bank of America (rated 'A'/F1') provide support for the tax-exempt CP and a \$25 million letter of credit with State Street Bank (rated 'AA'/F1+') provides support for the taxable CP. The credit facilities for the tax-exempt and taxable CP extend through October 1 and Aug. 28, 2017, respectively.

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Applicable Criteria

Fitch Internal Liquidity Worksheet (pub. 13 Jun 2013)
<https://www.fitchratings.com/site/re/710906>
Rating U.S. Public Finance Short-Term Debt (pub. 17 Nov 2015)
<https://www.fitchratings.com/site/re/873508>
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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