STANDARD & POOR'S RatingsDirect

RESEARCH

Summary:

Guam Power Authority; Retail Electric

Publication date: 12-Apr-2007
Primary Credit Analyst: Theodore Chapman, Dallas (1) 214-871-1401; theodore_chapman@standardandpoors.com
Secondary Credit Analyst: Paul Dyson, San Francisco (1) 415-371-5079; paul_dyson@standardandpoors.com

Credit Profile

Guam Pwr Auth rev bnds		
Long Term Rating	BB+/Stable	Outlook Revised
Guam Pwr Auth (AMBAC)		
Unenhanced Rating	BB+(SPUR)/Stable	Outlook Revised

Many issues are enhanced by bond insurance.

Rationale

Standard & Poor's Ratings Services revised its outlook on the 'BB+' standard long-term rating and Standard & Poor's underlying rating (SPUR) on Guam Power Authority's revenue debt to stable from negative based on the authority's improved operational and fiscal performance over the past two years.

The rating service simultaneously affirmed the ratings on the authority's revenue debt.

The speculative-grade ratings include:

- Guam Power Authority's more-efficient use, and greater availability, of its base-load assets, allowing management to reduce its dependence on the costlier diesel-fired peaking units -- Where historically these fuel-oil burning base-load units had averaged as low as 83% of all energy production, the fiscal 2006 output was in excess of 97%; and these improvements will allow the authority to shift the emphasis on its capital program to continued efforts for undergrounding more of its transmission and distribution system, as well as implementing overall transmission and distribution system stability and reliability improvements to reduce the devastating effect on operations and liquidity that past typhoons have had on the authority.
- Guam Public Utilities Commission's continued support under the Consolidated Commission on Utilities' governance structure that oversees both Guam Power Authority and Guam Waterworks Authority-- The authority remains supported in its biannual levelized-energy-adjustment clause, fuel-adjustment portion of its rates, as well as the authority to be more aggressive toward delinquent customers and illegal connections.
- Guam's (B/Watch Neg) rebounding economy due to increased tourism and tourism-related expansions, as well as the territory's long-term prospects because it stands to gain as many as 8,000 Marines and 9,000 dependents from Okinawa, Japan by 2014 -- The U.S. and Japanese governments have made a $10.3 billion commitment to this end. In fiscal 2005, the U.S. Navy alone accounted for 15.9% of authority revenues.

The rating remains constrained by uncertainty regarding the Guam general government's ability to address a series of long-term liabilities owed to the authority. On March 9, 2007, we placed Guam's 'B' rating on CreditWatch with negative implications following its disclosure that, at that time, it had to borrow $6 million from local banks just to meet payroll for its teachers. Guam accounted for 15.4% of the authority's total fiscal 2005 revenues. While Guam has so far been able to continue to pay its current bills for utility services, uncertainty remains as to whether or not the government will be able to continue to make substantial progress on its accounts payable and promissory notes owed to the authority. The U.S. Supreme Court made this even more uncertain when, on March 28, 2007, it ruled that a proposed Guam deficit bond-financing package -- part of which would have addressed the liabilities owed to the authority -- would have exceeded the territory's debt cap, which was created under the 1950 Organic Act that established Guam's self-rule.

The authority is a statutorily autonomous component unit of the government and, as such, would only transfer or loan money to Guam at the discretion of the Consolidated Commission on Utilities. As of fiscal 2005 audited financial statements, the authority was carrying a $12.4 million accounts receivable from Guam, as well as $24.4 million of combined promissory notes receivable from Guam's public school system and department of public works, compared to roughly $247.0 million of operating revenues. If the territory's situation does not improve, Guam Power Authority's long-term rating could still be pressured. Currently, the governor and legislature are still formulating the details of their fiscal recovery plan.

Fiscal 2006 unaudited results indicate continued improvements to the authority's finances, including about 1.5x annual debt service coverage (DSC). On-balance-sheet cash and cash equivalents of $16.8 million was equivalent to a modest 24 days' cash on hand, but this represents a large underrecovered position on fuel costs. Guam Public Utilities Commission recently approved an 11.87% levelized-energy-adjustment-clause-related increase in January 2007 that should help cash flows improve through the June 30, 2007, effective period. Authority officials had actually requested a deferral from the October 2006 implementation to ensure a full reckoning of fuel supply and delivery contracts were incorporated into the levelized-energy-adjustment clause. Management has not had to adjust base rates in more than a decade. Unaudited fiscal 2006 results follow audited fiscal 2005 results that exhibited very similar figures, including 1.6x annual DSC and similar cash on hand. This is a marked improvement from fiscal 2003, when DSC was below 1x. The Federal Emergency Management Agency (FEMA) has fully reimbursed the authority for approved claims related to past typhoons. The authority also maintains a $20 million CP program (A-1+) that is backed by an irrevocable standby credit agreement with Cathay Bank, as well as a confirming LOC through Nov. 7, 2007, from FHLB of San Francisco (AAA/Stable/A-1+). Management's maintenance of reasonable net margins and liquidity is important given that it has identified more than $650 million of capital projects over the next 10 years, including an estimated $200 million for the continued undergrounding of the system's transmission and distribution lines.

Guam Power Authority is a vertically integrated electric utility that provides service to about 47,000 customers on the island of Guam, the largest and southernmost of the Mariana Archipelago, about 1,500 miles southeast of Tokyo, Japan.

Outlook

The stable outlook reflects the expectation that the authority's financial performance is sustainable, especially given the improvements to its operations and regulatory relationship, as well as Guam's economy. An investment-grade rating is still precluded by the uncertainty over whether Guam will be able to pay the authority all the money it owes and what kind of effect that might have on the authority's ability to address its identified capital requirements. The territory will always face risks associated with severe weather events; its vulnerability to the tourism industry due to factors such as economic cycles, especially in Asia; and pandemic disease outbreaks. Guam, however, remains among the authority's leading customers; therefore, its failure to make realistic progress on the long-term liabilities it owes the authority could remain a challenge for Guam Power Authority. Additional financial challenges will be the funding of identified transmission and distribution system improvements in a prioritized and proactive manner, the establishing and maintaining of emergency liquidity reserves as a hedge against the next severe weather event, and the maintenance of the supportive regulatory relationship the authority has enjoyed since the implementation of its new governance structure in 2003.

Complete ratings information is available to subscribers of RatingsDirect, the real-time Web-based source for Standard & Poor's credit ratings, research, and risk analysis, at www.ratingsdirect.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com; under Credit Ratings in the left navigation bar, select Find a Rating, then Credit Ratings Search.

are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision. Ratings are based on information received by Ratings Services. Other divisions of Standard & Poor's may have information that is not available to Ratings Services. Standard & Poor's has established policies and procedures to maintain the confidentiality of non-public information received during the ratings process.

Ratings Services receives compensation for its ratings. Such compensation is normally paid either by the issuers of such securities or third parties participating in marketing the securities. While Standard & Poor's reserves the right to disseminate the rating, it receives no payment for doing so, except for subscriptions to its publications. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.