

Rating Update: Guam Power Authority

MOODY'S AFFIRMS Ba1 RATING ON GUAM POWER AUTHORITY REVENUE BONDS; OUTLOOK POSITIVE

IMPROVED CREDIT OUTLOOK

Electric Utilities
GU

Opinion

NEW YORK, Aug 27, 2007 -- Moody's Investors Service has affirmed the Ba1 credit rating on Guam Power Authority's (GPA) \$408,388,601 outstanding revenue bonds. Moody's has also changed the outlook from stable to positive on the bonds. The improved outlook reflects management's success at meeting several of its financial and operational objectives; the trending downward of the Guam government's receivables and the stable debt service coverage margin despite significant volatility in fuel prices. GPA's financial plan including a rate increase petition is also a positive factor. The rating also considers the existing weak internal liquidity; fuel dominance; and potential future impact of major adverse weather events on GPA's financial strength.

LEGAL SECURITY: First lien and pledge on net revenues of electric system; rate covenant requires net revenues equal 1.30 times debt service; fully-funded at bond issuance a debt service reserve at maximum annual debt service; and additional bonds test which requires 1.30 times debt service coverage as adjusted by estimated new revenue from rates.

INTEREST RATE DERIVATIVES: None.

RECENT DEVELOPMENTS: The most significant recent development is GPA's rate petition which is expected to be presented in late 2007 to the Public Utilities Commission of Guam (PUC). If approved, this would be the first base rate increase in ten years and improve internal financial liquidity. Debt service coverage in 2006 was 2.11 which was calculated based on bond covenant requirements. Moody's calculation of debt service coverage on a cash flow basis showed debt service coverage at 1.31 times. FY 2007 debt service coverage is forecasted to be in same range.

GPA has begun development of an Integrated Resource Plan to evaluate fuel diversity opportunities. Major announcements regarding U.S. military expansion plans have been made with 2010-2014 as the potential date of new investment. No definitive dates or plans have been finalized which creates some uncertainty about when GPA will need to meet the projected new growth in demand.

STRENGTHS:

*Governing board is relatively independent from Guam Government allowing more direct focus on business risks.

*Improved energy production from baseload units and hedging program has moderated high cost of fuel

*Monopoly position as essential service provider on island

*Stabilizing presence of U.S. military

*Transmission and distribution system through key load centers being constructed underground is expected to provide protection from severe weather impacts

CHALLENGES:

*Typhoons in the past significantly impacted reliability of the electric system and resulted in lingering financial effects

*Fuel dominance subjects utility to commodity market volatility

*Unlike other public power utilities, GPA's rates are externally regulated

*High level (but trending downward) of government receivables

*Limited liquidity compared to ongoing potential risks

*Meeting potential new demand from U.S. military expansion on island

MARKET POSITION; COMPETITIVE STRATEGY: Guam Power Authority (GPA) has an essential role in the economy of Guam as the sole provider of electricity to the island's 171,000 population. Guam, as a U.S. territory, is an important strategic U.S. military location which provides a stabilizing presence. As an electric utility that serves the island with no transmission interconnections, it has some unique challenges including the need to ensure it has significant power supply surplus capacity and strong system reliability to manage generation outages or adverse weather events. GPA maintains a 96% reserve margin which is equal to the loss of two of its largest generation units on the island. GPA has shifted a significant amount of its generation to base load units which has helped to moderate fuel costs. GPA has privatized the operations of some of its generating units and set performance standards. But the utility remains subject to the volatility of commodity markets which has resulted in significant annual increases in operating expenses. The fuel component of O&M has more than doubled between 2002-2007 to \$175.7 million. While GPA has a hedging program in place and it has operationally shifted to less expensive fuel, the fuel budget remains a pressure on liquidity. GPA has a weak liquidity position.

GPA is owned by the Government of Guam, and is governed by the Consolidated Commission on Utilities (CCU), which is an elected five-member board. GPA is regulated by the Guam PUC. This is a relatively new governance arrangement which seems to have allowed management to better focus on business risks with the enterprise. An important test of the relationship with the regulatory board is the upcoming rate petition that GPA is putting forward. A constructive relationship has thus far been in place including GPA getting sound support for the levelized energy adjustment charge (LEAC). The LEAC is reviewed and adjusted by the PUC on a bi-annual basis. The PUC has to consider the rate covenant in any new rate decision.

While the U.S. military has a stabilizing presence, there remains uncertainty regarding timing and degree of the impact of an announced expansion of the U.S. Navy and Marine activities on Guam. Should the expansion be as announced, increased economic activity and electrical demand are expected to be a positive development. Tourism and private and public investment also show positive trends in the past year.

Since 1962, the U.S. Federal Government has made 12 Federal Disaster Declarations for Guam, from typhoons to earthquakes. GPA has been implementing a plan to mitigate the impacts of severe weather events including undergrounding lines in the major load centers. GPA has also been building a self-insurance fund and continues to work with the Federal Emergency Management Agency (FEMA) response to such events.

FINANCIAL PERFORMANCE/FINANCIAL POSITION: GPA has been significantly pressured by fuel prices and the lingering slowness of the Guam government to pay its electric bills. GPA's working capital fund has been at its lowest levels due to the fuel price pressure. While substantial progress has been made in improving the receivable situation, it remains a potential pressure on cash flow. Debt service coverage has averaged 1.31 times between 2001-2006. The debt service coverage ratio is below the median debt service coverage ratio of the largest 20 U.S. public power utilities. FY 2007 debt service coverage is forecasted to be in the same range as the prior six-year period.

The proposed base rate increase has the objective of maintaining sound debt service coverage; improving financial liquidity; and to continue to make improvements to the system's reliability.

GPA's debt ratio has ranged in the high 80% range between 2001-2006. The debt ratio is above average for an integrated public power utility.

CAPITAL PROGRAM: GPA's five-year capital improvement plan amounts to \$477 million, with the bulk of the cost, over \$400 million, related to possible new generation projects that might be considered should there be a major expansion by the military. While GPA believes it can serve projected new load from its existing generation units, studies on how to achieve more fuel diversity and reliability are part of GPA's IRP evaluation. Otherwise, GPA's major capital spending is to continue to underground its transmission and distribution system.

Outlook

The positive outlook reflects GPA's management meeting several key financial and operational objectives and its current plan to improve financial flexibility and to further mitigate several operational risks.

What Could Change the Rating UP: The rating could be upgraded should GPA be successful at getting its base rate increase approved in the next six-month period by the regulatory board and demonstrating

improved financial liquidity. Continued progress towards improvements to system reliability from under grounding transmission and distribution lines and fuel diversity plans are also key factors.

What Could Change the Rating DOWN: The rating could be lowered should fuel price volatility cause further erosion of liquidity; that FEMA fails to be in position to assist in future weather-related events or should the Government of Guam accounts payable to GPA increase.

KEY FACTS:

Peak Demand, 2006: 275 MW

Installed Capacity, 2006: 552.2 MW

Department of Defense as %GPA Revenues, 2006: 17%

Fuel Expense, 2002: \$74,820,000

2007: \$175,752,000

Debt Service Coverage, 2006: 1.31X (Moody's Calculation)

Debt Service Coverage, 2007 Forecasted According to Bond Covenant): 2.31

Debt Ratio, 2006: 88.3%

DEBT STATEMENT as of 6/30/07 (\$000)

Series 1999 \$325,824

Series 1993 \$76,085

KEY CONTACT: Randall Wiegand, Chief Financial Officer, Guam Power Authority (671) 648-3066

Analysts

Dan Aschenbach
Analyst
Public Finance Group
Moody's Investors Service

Joshua Schaff
Backup Analyst
Public Finance Group
Moody's Investors Service

Mark Tenenhaus
Senior Credit Officer
Public Finance Group
Moody's Investors Service

Contacts

Journalists: (212) 553-0376
Research Clients: (212) 553-1653

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