S&P Global
Ratings

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Summary:

Lafayette, Louisiana
Lafayette Public Power Authority, Louisiana; Combined Utility; Retail Electric; Wholesale Electric

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Credit Profile		
US$159.57 mil util rev bnds ser 2024 due 11/01/2049		
Long Term Rating	AA-/Stable	New

Credit Highlights

- S&P Global Ratings assigned its 'AA-' long-term rating to the City of Lafayette, La.'s approximately $160 million series 2024 utilities revenue bonds.
- At the same time, S&P Global Ratings affirmed its 'AA-' rating on the city's senior-lien utilities revenue bonds; and its 'AA-' rating on Lafayette Public Power Authority's (LPPA) electric revenue bonds, issued by LPPA to finance the power plant it co-owns for the benefit of the city. The city's municipal electric, water, and wastewater system does business as Lafayette Utilities System (LUS).
- S&P Global Ratings also affirmed its 'A+' rating on Lafayette's separately pledged and self-supporting communications system debt that has a subordinate-lien backstop from the combined LUS utility systems, if needed.
- The outlook is stable.

Security

Proceeds from the series 2024 bonds will be used to fund the construction of the Bonin 4 plant, a new natural gas-fired generation unit that will help LUS replace the energy from the coal-fired Rodemacher unit 2, which is scheduled to retire in 2027.

LUS consists of electric, water, and wastewater systems. Unlike the existing system revenue bonds, the series 2024 bonds exclude from the revenue pledge the combined system's wastewater net revenues. We believe this exclusion, which is a function of a change in state law, does not change our opinion of the credit quality of the combined utility. The senior-lien utilities revenue bonds outstanding are secured by net revenues from the electric, water, and wastewater systems. The series 2024 bonds share a parity pledge with the utilities revenue bonds outstanding. LUS had about $182 million of senior debt outstanding as of fiscal year-end 2023.

Our credit analysis primarily focuses on the electric system, as it represented 74% of system net revenues in fiscal 2023. However, we also incorporate the credit attributes of the water, wastewater, and communications systems into our analysis and factor in the diversity provided by each of the utility systems.

LPPA is a wholesale utility that sells power generated from Rodemacher unit 2 exclusively to LUS through a full-requirements, take-or-pay power sales contract, whereby LUS pays LPPA before paying its own direct debt service. Accordingly, we rate LPPA's debt based on the strength of the power sales contract and the quality of cash flows to LPPA from LUS. LPPA had about $65 million of debt outstanding as of fiscal year-end 2023. In our fixed cost coverage (FCC) calculation for LUS, we impute LPPA's debt service as debt-like.

The communications system's (LUS Fiber) revenue bonds are secured by Lafayette's separately pledged and self-supporting communications system debt that has a subordinate-lien backstop from the combined LUS utility systems, if needed.. However, if LUS Fiber's net revenues became insufficient, LUS would have to meet communications system obligations by using its capital additions fund. Bond covenants require that LUS carry a minimum in the capital additions fund equal to at least 7.5% of adjusted revenue (total revenue less cost of goods sold). The current minimum requirement in the fund exceeds maximum annual debt service for the communications system bonds. The 'A+' rating reflects the application of our "Assigning Issue Credit Ratings Of Operating Entities" criteria, published May 20, 2015, which results in a one-notch rating differential. We have included the telecommunication bond payments as direct debt service of the combined utility in our analysis. LUS had about $73 million of communications system subordinate debt outstanding as of fiscal year-end 2023.

Credit overview

The rating reflects our expectation that leverage and debt service requirements will increase as a result of LUS' sizable five-year capital improvement plan (CIP), although not to the extent that it would lead to a lower rating.

About two-thirds of the $589 million CIP for 2024-2028 will fund the construction of the Bonin 4 natural gas-fired plant and is expected to be financed by proceeds from the series 2024 and the anticipated series 2026 bonds. The Bonin plant, which will enter service in late 2028 or early 2029, will consist of a simple-cycle combustion turbine with an expected capacity of 250 megawatts (MW), and will complement market purchases and short-term capacity arrangements that LUS will add to its power supply portfolio following the late 2027 retirement of Rodemacher unit 2. Commercial operations for the new plant are expected to begin in late 2028 or early 2029, with engineering design slated to start in fall 2024. In our view, if executed as planned, the project can meaningfully reduce LUS' exposure to outsize environmental compliance costs associated with the existing coal plant. The new plant will also enhance system reliability and provide flexibility to accommodate future technologies.

However, management said LUS could procure substantial short-term capacity contracts to bridge the gap between the retirement of the coal unit and the new plant coming online. In addition, LUS could rely more heavily on short-term contracts or market purchases in the long term, if management does not secure additional long-term power purchase agreements (PPAs). This could increase LUS' exposure to power price uncertainty, although it can be tempered by the use of a discretionary power cost adjustment. We will monitor LUS' ability to execute on the project and its exposure to power cost volatility, following the shift in power supply.

The rating further reflects our view of LUS' recently robust FCC, which averaged about 1.6x over the past three audited years (inclusive of LUS Fiber's debt service). Liquidity is sound, with $139 million in unrestricted cash, equivalent to 254 days' cash as of Oct. 31, 2023. This financial strength is, in our view, supported by management's proactive cost recovery, demonstrated by the adoption of an annual 8% water, 9.5% wastewater, and 3% electric base rate increase from 2023-2025; and an annual 3.5% electric rate increase from 2026-2028. Despite a sizable debt plan and large capital needs, management's financial projections suggests that FCC will likely remain robust over the next five years, as future rate increases will be implemented in conjunction with rising debt service requirements to ensure financial stability.

The rating further reflects our view of LUS' credit strengths:

- Residential customers represent about 43% of total revenue in 2023 and there is no significant customer concentration, providing revenue stability. Although income levels are 10% below the national average, we believe this was somewhat depressed by the presence of a large higher education institute (the University of Louisiana).
- Competitive rates, reflected by weighted average system rates that were 9% lower than the state average based on the most recent data from the U.S. Energy Information Administration, promote revenue-raising flexibility.

Factors tempering the above credit strengths include our view of:

- Substantial exposure to day-ahead and spot market purchases (45% of energy requirements in 2023), which could worsen and result in unbudgeted costs unless they secure baseload capacity through contracts after retiring Rodemacher Unit 2, although partially offsetting this is LUS' access to diverse power supply from the MISO market that helps enhance reliability;
- Increasing (albeit currently manageable) debt burden, as the 42% debt-to-capitalization ratio could rise to about 58% within the next five years due to planned debt; and
- Although LUS Fiber has been self-supporting with steady customer growth since 2012, we believe there are operational and financial risks associated with its retail broadband services given the competitive nature of the telecommunications industry. LUS Fiber could face aggressive responses from commercial incumbents, including dropping prices or advancing technology, which might pressure LUS' FCC and liquidity.

Environmental, social, and governance

In our view, LUS remains exposed to future state or federal legislation that could further restrict carbon dioxide emissions, as Rodemacher unit 2 contributed 45% of total energy needs in 2023. However, LUS' decision to retire Rodemacher unit 2 will significantly reduce its exposure to substantial environmental regulatory costs, which would otherwise be inevitable to comply with the EPA's coal combustion residuals and effluent limitation guidelines. Despite this, adding Bonin 4 will increase LUS' reliance on natural gas, which we consider moderately negative due to its carbon emissions profile. LUS plans to pursue procurement opportunities for solar PPAs when economically feasible to complement its power generation. In addition, LUS faces heightened physical environmental risks given its location in an area susceptible to extreme tropical weather events. This risk is mitigated by LUS' ongoing investments in system-hardening initiatives, including replacing aging distribution and transmission poles and undergrounding distribution lines.

We believe social risks, including rate affordability, are credit neutral in the near term, given below-rate weighted average electric rates, insignificant customer payment delinquencies, and modest base-rate increases in the near term across three systems, although Lafayette's poverty rate, which is above the national average, tempers these factors. We continue to monitor the strength and stability of electric utilities' revenue streams for evidence of delinquent payments or other revenue erosion. Although the rate of inflation as measured by the Consumer Price Index (CPI) has softened, Bureau of Labor Statistics data shows that electricity price inflation continued to outpace the broader CPI by 100 basis points to more than 200 basis points during March-August 2024. The amalgam of increases in delinquent credit card, consumer, and auto loans, along with financial pressures associated with the resumption of student loan payments and weaker than historical household savings rates, will likely compound the financial pressures electricity consumers face. Potentially exacerbating issues of energy affordability are weak economic indicators, such as S&P Global Economics' forecast of a 25% recession risk within the next 12 months, which is elevated relative to the historical baseline. A cooling labor market, geopolitical risks, and a potentially disruptive election, might add to recessionary pressures. (See "Economic Outlook U.S. Q4 2024: Growth And Rates Start Shifting To Neutral," published Sept. 24, 2024, on RatingsDirect.)

We believe the utility's governance factors are also credit neutral, as LUS has full rate-setting autonomy and maintains comprehensive long-term forecasts and capital plans, which in our view enhances financial and operational stability.

For more information on LUS, see our analysis, published Sept. 29, 2023.

Outlook

The stable outlook reflects our view that LUS' financial profile has sufficient cushion, supported by adopted multiyear rate increases, a stable customer base, and affordable rates; and we believe LUS' coverage and liquidity will remain sustainably robust in the face of a large CIP and increasing debt service requirements. We also expect LUS Fiber to remain financially self-supporting without any immediate requirements for a large cash infusion from LUS.

Downside scenario

We could lower the rating over the next two years if the service territory economic attributes, including income levels and poverty rate, significantly worsen, limiting LUS' rate-raising flexibility; or if the cost for the new generation plant turns out to be substantially higher than the current estimate, which could meaningfully impair financial performance either due to additional debt issues or an outsize cash drawdown.

Upside scenario

In our view, the possibility of a positive rating action is constrained by the rising debt burden, uncertainties associated with LUS' future power supply portfolio, and exposure to extreme weather.

Lafayette, Louisiana--key credit metrics			
	--Fiscal year ended Oct. 31--		
	2023	**2022**	**2021**
Operational metrics			
Electric customer accounts	71,521	77,308	70,096
% of electric retail revenues from residential customers	46	46	45
Top 10 electric customers' revenues as % of total electric operating revenue	7	13	13
Service area median household effective buying income as % of U.S.	90	89	87
Weighted average retail electric rate as % of state	91	91	85

Lafayette, Louisiana--key credit metrics (cont.)			
	--Fiscal year ended Oct. 31--		
	2023	2022	2021
Financial metrics			
Gross revenues ($000s)	270,255	281,947	233,667
Total operating expenses less depreciation and amortization ($000s)	199,631	227,981	187,132
Debt service ($000s)	33,517	33,281	34,527
Debt service coverage (x)	2.1	1.6	1.3
Fixed-charge coverage (x)	1.9	1.5	1.3
Total available liquidity ($000s)*	138,780	120,408	122,766
Days' liquidity	254	193	239
Total on-balance-sheet debt ($000s)	181,885	200,555	224,055
Debt-to-capitalization (%)	22	25	28

*Total available liquidity includes available committed credit line balances, where applicable. Debt service coverage--Revenues minus expenses divided by debt service. Fixed-charge coverage--Sum of revenues minus expenses minus total net transfers out plus capacity payments (or their proxy), divided by the sum of debt service plus capacity payments (or their proxy). N.A.--Not available.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of October 3, 2024)		
Lafayette comb util (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Lafayette communications sys (AGM)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Lafayette communications sys (BAM)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Lafayette communications sys (BAM)		
Unenhanced Rating	A+(SPUR)/Stable	Affirmed
Lafayette taxable retail elec (BAM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Lafayette util (AGM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Lafayette util (BAM)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed
Lafayette Public Power Authority, Louisiana		
Lafayette, Louisiana		
Lafayette Pub Pwr Auth (Lafayette) elec rev rfdg bnds		
Long Term Rating	AA-/Stable	Affirmed
Lafayette Pub Pwr Auth (Lafayette) taxable retail elec (BAM)		

Ratings Detail (As Of October 3, 2024) (cont.)		
Unenhanced Rating	AA-(SPUR)/Stable	Affirmed

Many issues are enhanced by bond insurance.

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.