

U.S. Municipal Bond Market

Texas' ERCOT-Area Public Power Utilities on 'Rating Watch Negative,' Per Today's Fitch Rating Action

- Fitch Ratings placed all public power and electric utilities and electric cooperatives within the ERCOT's footprint on **Rating Watch Negative** today. The rating agency said it will take no longer than six months to review the impact of the event.
- Areas of focus, according to the rating agency, will zero in on near-term liquidity requirements and additional leverage that might result as part of any financial solutions. Fitch also pointed out the possibility of multi-notch downgrades exists but are unlikely given the historical levels of liquidity and strong market access.

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Fitch Places All ERCOT-Area Public Power Utilities on Rating Watch Negative

We wrote in our Monday commentary we expected potential rating agency action connected with the local government, water, and electric (public power) sectors as a result of last week's Big Freeze, or Texas Freeze extreme weather event. Those rating actions have started, and this initial batch is from Fitch Ratings.

Summary of Utility Issuers Impacted by Feb. 24, 2021 Fitch Ratings Action

Entity	Description	Fitch Rating	Feb 24, 2021 Recent Action
Austin (TX)	Elect system revs, Combined revs sub	AA	Rating Watch Negative
Brazos Electric Power Cooperative, Inc. (TX)	Util sys revs	A+	Rating Watch Negative
Brownsville (TX)	Elect sys revs	A+	Rating Watch Negative
Bryan (TX)	Elect sys revs, Rural elec sys revs	AA-	Rating Watch Negative
Denton (TX)	Util sys revs	A+	Rating Watch Negative
Denton County Electric Coop. (TX)	dba CoServ Electric	AA-	Rating Watch Negative
Floresville (TX)	Elect sys revs	A	Rating Watch Negative
Garland (TX)	Elect sys revs	AA, AA-	Rating Watch Negative
Guadalupe Valley Electric Coop (TX)	Elect sys revs	AA-	Rating Watch Negative
Lower Colorado River Authority (TX)	Elect sys revs	AA-	Rating Watch Negative
New Braunfels (TX)	Comb util revs	AA	Rating Watch Negative
Pedernales Electric Cooperative, Inc. (TX)	First mort	AA-	Rating Watch Negative
San Antonio (TX)	Comb util revs	AA+	Rating Watch Negative
Miguel Elect. Coop- Atascosa Cnty Ind Dev Corp. (TX)	Pol cont	A+	Rating Watch Negative
Schertz-Seguin Local Government Corp. (TX)	Con revs	A+	Rating Watch Negative
Seguin (TX)	Wat & sew revs	A+	Rating Watch Negative
South Texas Electric Cooperative (TX)	Elec coop	A+	Rating Watch Negative
Southmost Regional Water Authority (TX)	Sup con revs	A+	Rating Watch Negative

Fitch's areas of focus will zero in on near-term liquidity requirements and additional leverage that might result as part of any financial solutions.

Source: Fitch Ratings and HilltopSecurities.

Fitch Ratings placed all public power and electric utilities and electric cooperatives within the footprint of the Electric Reliability Council of Texas (ERCOT) on Rating Watch Negative today. The rating agency highlighted the severity of the weather event within the release, but also singled out the uncertain financial impact to the entities as a key reason for the action. In other words, it seems there needs to be some time to allow the utilities themselves, and perhaps then also Fitch, to understand the entire financial impact that last week's storms could have on the bottom line. Fitch explained that they will review the impact of the events as soon as practical, but no later than six months from now.

Fitch's areas of focus will zero in on near-term liquidity requirements and additional leverage that might result as part of any financial solutions.

Potential Factors that Could Impact Credit Quality

A supply and demand imbalance for energy was highlighted by a supply constraint which saw electricity costs soar from the typical cost of \$20/MWh to the price cap of \$9,000/MWh. It is possible this supply breakdown could lead to unexpected exponential costs for the utilities. Fitch is reporting this scenario drove energy costs into the hundreds of millions of dollars for some utilities. Therefore, the rating agency notes: "These higher costs have triggered Fitch's concerns regarding funding requirements and liquidity in the near term, and cost recovery and the potential for increased financial leverage over the medium term for its rated issuers." The areas of focus, according to the rater, will zero in on near-term liquidity requirements and additional leverage that might result as part of financial solutions. Fitch Ratings pointed out that the possibility of a multi-notch downgrade exists even though liquidity and market access is strong. Fitch further explains:

Risk Exists Despite Strong Liquidity: Municipal utilities carry strong liquidity, generally in the form of unrestricted cash reserves, while cooperatives typically maintain adequate liquidity in the form of lines of credit. The issuers placed on RWN (Rating Watch Negative) averaged over 250 days liquidity on hand (based on cash reserves and lines of credit) as of their last audit. While this robust liquidity positions the utilities to absorb above-budget costs, Fitch believes the magnitude of last week's expenditures could exceed the liquidity immediately available to these issuers and prompt the need for additional short-term sources. Although unlikely given the sector's historical access to liquidity and capital, failure of an issuer to secure sufficient liquidity could prompt a multiple notch downgrade.

Fitch is reporting last week's events drove energy costs into the hundreds of millions of dollars for some utilities.

We will continue to monitor releases related to these and other entities that could potentially be impacted by last week's extreme weather event.

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- [Higher than Typical Gas Costs for Oklahoma Municipal Power Authority](#), February 22, 2021
- [The Financial Impact from The Big Freeze is Just Heating Up](#), February 22, 2021
- [Texas Freeze](#), February 18, 2021
- [Some Preliminary Details Released of Proposed \\$1.9 Trillion American Rescue Plan](#), February 10, 2021
- [Deep Cuts Remain; State and Local Govt. Jobs Down Over 1.3 Million](#), February 8, 2021
- [State Outlook Remains Negative; Direct Fiscal Relief Still Needed](#), February 5, 2021
- [U.S. COVID-19 "Spikes Like We Have Not Yet Seen" Could Be Coming; Sixth Phase Relief Status](#), February 1, 2021
- [Yellen Hearing: Supports Defeat of Pandemic, Loss of Govt. Jobs "Economic Malpractice"](#), January 19, 2021

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