MOODY'S RATINGS

Rating Action: Moody's Ratings upgrades Alabama Municipal Electric Authority to Aa3 from A1; outlook stable

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New York, January 17, 2025 -- Moody's Ratings (Moody's) has upgraded Alabama Municipal Electric Authority's (AMEA) outstanding Taxable Power Supply System Revenue Refunding Bonds, 2020 Series A to Aa3 from A1. AMEA has about $22.0 million of revenue bonds outstanding. The rating outlook is stable.

RATINGS RATIONALE

The upgrade of AMEA's rating to Aa3 reflects the improvement in credit fundamentals, including sound liquidity, strong fixed obligation charge coverage (FOCC), and low leverage. The Aa3 rating also reflects the authority's effective management of resource risk and continued decline in carbon transition risk. The rating also incorporates the A1 weighted average credit quality of the participants.

In the last few years, AMEA has improved its resource visibility by executing several power supply contracts including the requirements service agreement (RSA) with Southern Power Company (Baa1 stable) which will be the authority's main power provider upon the expiration of the authority's power supply contract with Alabama Power Company (A1 stable) at the end of 2025. The authority expects a reduction of around 25% in its power supply cost starting January 2026 under the RSA with Southern Power Company. The authority will also benefit from the cost savings achieved from the prepaid power contracts executed in the last two years. These improvements should eventually benefit the participants by decreases in rates and thus should improve the competitiveness of the authority.

The Aa3 rating also reflects solid financial performance with FOCC above 3.0x for the past four years and maintenance of low leverage levels with an adjusted debt ratio of around 30% in fiscal 2023. We expect the leverage to continue declining due to the manageable capital expenditure requirements that do not require additional debt issuance. Liquidity is sound, with 118 days cash on hand as of fiscal year end 2023.

The Aa3 rating is further supported by the continued decline in the carbon transition risk. Historically, AMEA had a material exposure to carbon transition risk with 43% of the fuel coming from coal in fiscal 2022. This ratio declined to 28% in fiscal 2024. We expect the coal exposure to be completely eliminated from the authority's fuel mix by fiscal 2027 upon the expiration of the power supply contract with Alabama Power Company.

RATING OUTLOOK

The stable outlook reflects our expectation that participant members' average weighted credit quality will remain sound. In addition, the authority's financial performance will remain robust with at least 2.0x FOCC.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATING

- Material improvement in the weighted average participant credit quality

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATING

- Material decline in the weighted average participant credit quality

- Challenges by any member participant's take-and-pay or other contract obligations

- Cost recovery challenges or significant unexpected borrowing resulting in declines in key financial metrics, including a decline in the FOCC below 2.0x

LEGAL SECURITY

AMEA's 2020 Series A Taxable Power Supply Revenue Refunding Bonds are secured by the revenue AMEA receives under its take-and-pay, all-requirements power sales contracts with its 11 participant members. Payments under these agreements are established at a level sufficient to cover expenses and debt service; these contracts expire in 2045, five years after the bond maturity.

The rate covenant on the bonds is sum-sufficient, and the debt service reserve requirement sized at maximum annual debt service (MADS) of around $1.7 million is surety-funded. Each member has agreed, pursuant to its contract, to pay deficiencies on a pro rata basis if net revenue is insufficient to meet debt service. The security package also includes an interest in all funds established by the authority including construction funds, operating and maintenance funds, general reserve funds and debt service reserve funds.

PROFILE

AMEA is a joint action agency that provides electricity to its 11 participant members that are mostly located in southeastern and southern Alabama, under a full-requirements, take-and-pay power sales contract that expires in 2045. The top participant, that generated 41% of the authority's revenue in fiscal 2023, is the Utilities Board of the City of Foley, AL (Aa2). AMEA's members serve around 136,000 retail electric customers within a service territory with a population of 199,000.

AMEA owns a 95 MW GE LM6000 peaking facility, which has generally performed in line with peaking facilities with availability factors above 95% since commercial operations began in May 2004. There is no long term services agreement but all internal work related to the combustion turbines is done by either General Electric or TransCanada (certified OEM service providers). The remainder of the plant servicing is done mostly through local contractors, and AMEA performs its own O&M.

AMEA purchases firm network integration transmission services under the Southern Company Open Access Transmission Tariff to deliver electric power to serve the AMEA members' loads.

METHODOLOGY

The principal methodology used in this rating was US Municipal Joint Action Agencies published in December 2022 and available at https://ratings.moodys.com/rmc-documents/396803. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

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For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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