FitchRatings

FITCH RATES LONG ISLAND POWER AUTHORITY SERIES 2016A/B ELECTRIC SYSTEM GEN REVS 'A-'; OUTLOOK STABLE

Fitch Ratings-New York-24 August 2016: Fitch Ratings has assigned an 'A-' rating to the Long Island Power Authority's (LIPA) issuance of the following electric system general revenue bonds:

--$175 million, series 2016A (MMD FRN Rate);
--$414 million, series 2016B, fixed rate.

The series 2016A bonds are expected to be privately placed the week of Aug. 29, and proceeds will be used to repay the authority's outstanding series 2012C variable rate bonds. The series 2016B bonds are expected to be sold in September, and proceeds will be used primarily to fund capital improvements and refund certain fixed rate bonds.

Fitch has also affirmed the 'A-' ratings on the following LIPA debt and commercial paper bank notes:

--$4 billion, senior lien electric system revenue and refunding bonds;
--implied electric system revenue subordinate obligations;
--$200 million series 2014 CP-1A (federally taxable) and 1B;
--$100 million series 2014 CP-2A (federally taxable) and 2B.

The Rating Outlook is Stable.

SECURITY

The electric system general revenue bonds are senior lien obligations of LIPA secured by the net revenues of the electric system, after payment of operating and maintenance expenses. LIPA's subordinate lien general revenue obligations are also secured by the net revenues of the electric system, but are subordinate to payments on LIPA's outstanding senior lien electric revenue bonds and floating rate notes.

KEY RATING DRIVERS

SOLID UTILITY FUNDAMENTALS: LIPA is one of the nation's largest municipal electric distribution systems, serving 1.1 million retail customers. The authority benefits from sound utility fundamentals, including a flexible power supply mix, an affluent and well-diversified customer base and cost recovery mechanisms that stabilize cash flow. A series of comprehensive operating agreements with capable external service providers further support operations.

BUSINESS MODEL TRANSITION: The 2013 LIPA Reform Act, enacted in response to operating challenges following Superstorm Sandy, broadened the responsibilities of the utility's system
operator (PSEGLI) and expanded the state's (Department of Public Service [DPS]) regulatory oversight of LIPA. Fitch views many of the legislated provisions as supportive of credit quality. However, added regulatory oversight could affect LIPA's financial and rate flexibility over time.

CONSTRUCTIVE REGULATORY RECOMMENDATIONS: The constructive recommendations submitted by the DPS following its initial review of LIPA's three-year rate plan, and adopted by the LIPA board, support LIPA's Stable Outlook. The authority implemented the first phase of a three-year rate increase on Jan. 1, 2016.

RATE PRESSURES PERSIST: Despite electric rates that have become more competitive regionally, political and consumer rate pressures persist as LIPA's average residential revenue per kilowatt hour (kwh) remains among the highest in the nation at approximately 19.4 cents/kwh.

HIGH DEBT LEVELS: LIPA's debt levels remain high, totaling $10.2 billion at Dec. 31, 2015 including capital lease and securitization obligations, or $9,337 per retail customer, well above the peer utility median of $3,318. Although Fitch recognizes the benefits of the separately secured $4.1 billion in securitized debt, the repayment profile remains an obligation and burden of current ratepayers. Positively, LIPA's three-year rate plan aims to reduce debt financing of future capex to less than 64%, which should moderate future borrowings

SOUND LIQUIDITY: LIPA's liquidity was solid at 103 days of operating cash, and 202 days including available short-term notes and external bank facility at Dec. 31, 2015. Weaker metrics reported in recent years were affected by significant storm costs, but federal reimbursement of roughly 90% of the costs incurred is now complete.

RATING SENSITIVITIES

IMPROVED OPERATING STABILITY: Evidence of improved operating stability and financial performance at the Long Island Power Authority sufficient to offset persistent political and consumer-driven rate pressures could result in consideration of a positive rating action.

CREDIT PROFILE

LIPA owns one of the largest municipal electric distribution systems in the U.S., serving a population of about 3 million people located throughout Nassau and Suffolk counties, and the Rockaways section of New York City. The service area economy continues to exhibit well above average wealth and income levels. Unemployment in Nassau and Suffolk Counties (general obligations debt rated 'A'/Outlook Stable and 'A-'/Outlook Stable, respectively) is below that of the state and nation.

Operations and management services related to the LIPA transmission and distribution system, which had been provided by a subsidiary of National Grid plc, shifted to PSEG-LI, a subsidiary of Public Service Enterprise Group ([PSEG] Issuer Default Rating 'BBB+'/Stable) as of Jan. 1, 2014, for a 12-year term, pursuant to the operating services agreement (OSA). PSEG is paid a management fee and can earn performance incentives.

Effective Jan. 1, 2015, fuel management services shifted to an affiliate of PSEG - PSEG Energy Resources and Trade, LLC. The power supply and fuel management services are also provided pursuant to the OSA, which expires Dec. 31, 2025.

The power supply agreement remains with National Grid, plc, to provide capacity and energy from its oil and gas-fired generating units on Long Island. This agreement is in place through May 2028.

NEW ISSUE DETAILS

The series 2016A proceeds will be used to refinance LIPA's outstanding series 2012C variable rate demand bonds and should not expose LIPA or its bondholders to any meaningful new risks. The series 2016A bonds will initially bear interest at a variable rate based on prevailing AAA

Municipal Market Data General Obligation Yield Curve plus an applicable spread and will have a final maturity of May 1, 2033

In addition to the bond issuance, LIPA is also expected to enter into a five year basis swap that will effectively convert the cost of the series 2016A bonds to 69.4% of one-month LIBOR plus an applicable spread. There is an additional requirement at the end of the basis swap agreement for LIPA to pay the counterparty 100% of any decrease in the market value of the series 2016A bond. However LIPA reserves the right to call or remarket the bond after five years, in which case the value of the basis swap would be $0.

The authority will continue to bear the interest rate risk associated with the series 2016A debt, but LIPA's overall variable rate exposure remained reasonable at 3.7% of total debt at year end 2015.

The series 2016 B bonds will bear interest at a fixed rate and have an expected final maturity of May 1, 2046.

For additional information on LIPA's long term ratings see the recent full rating report dated Feb. 18, 2016. The report and press release are available at 'www.fitchratings.com'.

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Applicable Criteria
Revenue-Supported Rating Criteria (pub. 16 Jun 2014)
https://www.fitchratings.com/site/re/750012
U.S. Public Power Rating Criteria (pub. 18 May 2015)
https://www.fitchratings.com/site/re/864007