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Summary:

American Municipal Power Inc., Ohio; Wholesale Electric

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Summary:

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Credit Profile		
US$138.855 mil greenup hydroelec proj rev bnds ser 2016A due 02/15/2051		
Long Term Rating	A/Stable	New

Rationale

Standard & Poor's Ratings Services has assigned its 'A' rating to American Municipal Power (AMP) Inc., Ohio's $144.18 million electric revenue bonds (Greenup Hydroelectric Project), series 2016A. The outlook is stable.

The rating reflects what we view as the following credit strengths:

- A take-or-pay power sales contract with 47 of AMP's 132 members, with a 25% step up for defaulting participants. The contract obligates participants to pay, including provisions for debt service, regardless of whether the project is in commercial operation;
- The medium-investment-grade credit profile of the 14 largest participants, whose electric departments will account for 80% of the Greenup hydroelectric facility (and 100% including the step up);
- The Greenup project's being part AMP's larger power supply strategy, which includes other projects recently completed or under construction. These include the coal-fired Prairie State Generating Station Project, and the Combined Hydroelectric Project and Meldahl Hydroelectric Projects, all of which we rate 'A'. Through these projects, management has reduced its membership's exposure to baseload market purchases and is achieving a more diversified power supply;
- The Greenup project's operational status, which eliminates construction risk. Furthermore, the project has demonstrated capacity factors that are only slightly below AMP's Belleville hydroelectric project; and
- The hydroelectric project's attractiveness as a renewable energy resource in an increasingly carbon-constrained environment. We believe that recent regulations from the Environmental Protection Agency, including its Clean Power Plan to reduce carbon dioxide emissions (despite the recent stay issued by the Supreme Court), further enhances this attractiveness.

We believe credit weaknesses include the following factors:

- Although the credit quality of the leading participating members is medium investment-grade, in our view, we believe that the credit profile of remaining participating members is low investment-grade, constraining further credit improvement.
- The AMP members participating in the Greenup project are also participating in other AMP projects. Although Greenup is separately secured and there are no cross-default provisions per se, a member that defaults on another project could default on the Greenup project (and vice versa).
- Over the past decade, AMP has issued a substantial amount of debt across all projects -- nearly $5 billion -- increasing the joint action agency's overall leverage. However, we expect that debt issuance will moderate, with the utility issuing less than $1 billion over fiscal years 2016-2020.

On a scale of '1' to '10', ('1' being the strongest), Standard & Poor's has assigned a business profile of '4'. The business profile reflects the rate setting autonomy of AMP and its members, the broad footprint of the participating members, the role that the Greenup project plays within the utility's overall power supply strategy, and what we consider to be AMP's strong management team.

In 2009, the utility entered an agreement with the City of Hamilton, Ohio, whereby Hamilton agreed to sell to AMP, for $139 million, a 34.1 MW share (48.6%) of its wholly owned 70.2 MW Greenup facility, upon commercial operation of AMP's 105 MW Meldahl hydroelectric facility (Hamilton is a 51% share participant in the Meldahl project). We expect the Meldahl project to achieve commercial operation in April 2016. We expect the 2016A bond proceeds to finance AMP's purchase of Greenup.

Greenup is a three-turbine facility on the Ohio River, roughly midway between AMP's Meldahl and Belleville Hydro projects. It has been in operation since 1982, so project participants (and bondholders) bear no construction risk. As a run-of-the-river project, generation is subject to Army Corps of Engineers interruption for various reasons, chiefly high and low water derates. Since 2000, Greenup has run at capacity factors ranging from 35% to 50%, which is slightly below levels at AMP's Belleville facility and expected levels at other AMP hydro units under construction on the Ohio River.

The Federal Energy Regulatory Commission operating license expires in February 2026, and we expect that AMP and Hamilton, which will be coholders of the license, will file for a 30-year renewal well before expiration.

We view the power sales contract that AMP has entered with each of its participating members as a key credit factor. Under the contract, each participant has entered a take-or-pay obligation to make payments which include operating costs and debt service. These payments occur whether or not the units are operating; they are not subject to any reduction, nor are they conditioned upon AMP's performance. Payments are due whether or not (for any reason whatsoever) the project is operating. For the majority of participants, these obligations constitute electric system operating expenses.

The power sales contract contains a provision requiring participants to step-up and purchase up to 25% of their original share from any defaulting participants. The Greenup project is expected to account for 1% of the project participants' energy needs. As such, should the step-up be triggered, we believe that the nondefaulting participants would be able to shoulder the burden. Finally, AMP is not required to provide replacement power in the event of outage.

The top 14 participants account for an 80% share of the project, and these 14 members could cover 100% of project costs if the all other participants defaulted, a prospect that we consider extremely unlikely. The leading members, which enjoy proximity to economic centers, include:

- Cleveland (Ohio) Public Power (18%)
- Danville, Va. (10%)
- Paducah, Ky. (9%)
- Wadsworth, Ohio (8%)
- Orrville, Ohio (7%)
- Bowling Green, Ohio (6%)

Standard & Poor's has assessed the credit profile of these 14 participants, which we believe to be solidly medium investment grade, and in our opinion, the large number of the entire 47-member participant base enables Standard & Poor's to decouple the rating from a weak-link analysis. We believe that the likelihood the step-up provision will be fully tested is minimal, so the rating reflects our view of the overall credit quality of the leading members.

In general, and with a couple of exceptions, these 14 leading members demonstrate the following credit characteristics:

- Customer bases, which range from 5,000 to 72,000, are primarily residential and commercial, although five of the members have industrial concentration greater than 50%. Six also have customer concentration, with the top five retail customers accounting for more than 30% of revenue. As such, these participants are exposed to a heightened potential for load loss.
- Retail rates are generally below average. However, demographics are weak, with median household effective buying incomes that are generally under the U.S. average, and unemployment rates that are generally above that of the nation. This suggests only moderate rate-raising flexibility.
- Leading participants have exhibited generally adequate-to-solid coverage of total fixed costs (which include an imputed share of debt service related to all AMP projects, as well as direct debt), and generally robust liquidity, which are, with a couple of exceptions, over 100 days of annual operating expenses.
- Debt levels are generally moderate at roughly $6,500 per retail customer (including direct debt and shares of AMP project obligations).

AMP is nearing the end of capital-intensive period. In the past 10 years, the utility has debt-financed about $5 billion in generation projects, but expects to issue just $1 billion of additional debt over the next five years. While Standard & Poor's views the agency's overall leverage that AMP has added as a risk, we believe the cooperative's sophisticated management team and the efforts it has taken to assist and monitor the financial operations of its members mitigates this. Moreover, we note the benefits of management's strategy to diversify power supply, meet member load growth, displace inefficient generation, manage carbon intensity, and reduce exposure to market priced energy. Just a decade ago, the utility met the vast majority of member energy needs via power purchases. Management estimates that by 2017, purchased power will account for just 38%, while owned and member-owned coal fired generation will account for 24%, gas fired generation 16%, and hydropower and other renewable resources 19%. In our opinion, this represents a well-diversified power supply portfolio.

Outlook

The stable outlook reflects our view of the strength of the take-or-pay contracts coupled with participating members' rate-setting autonomy. Absent a significant change in the credit profile of the largest participants in the project, we do not expect to raise or lower rating over the next two years.

Upside scenario

We could raise the rating if coverage metrics meaningfully exceed covenanted levels.

Downside scenario

We could lower the rating if coverage metrics meaningfully fall short of covenanted levels.

Related Criteria And Research

Related Criteria

- USPF Criteria: Electric And Gas Utility Ratings, Dec. 16, 2014
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011
- USPF Criteria: Assigning Issue Credit Ratings Of Operating Entities, May 20, 2015
- Criteria: Use of CreditWatch And Outlooks, Sept. 14, 2009

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.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.