FitchRatings

Public Finance
Public Power
U.S.A.

Garland, Texas

Ratings

Standalone Credit Profile	aa–

New Issues

$152,915,000 Electric Utility System Revenue Refunding Bonds (taxable), Series 2021B	AA–
$61,320,000 Electric Utility System Revenue Refunding Bonds (tax-exempt), Series 2021A	AA–

Outstanding Debt

(Garland Power & Light) Electric Utility System CP Notes	AA–
(Garland Power & Light) Electric Electric Utility System Revenue Refunding Bonds[a]	AA/AA–

[a]Series 2013 (AA); New Series 2014, 2015, 2016, 2016A, 2016B, 2018, 2019, 2019A, 2020, 2021, 2021A, 2021B (AA–).

Rating Outlook

Negative

Applicable Criteria

U.S. Public Power Rating Criteria (April 2021)

Public Sector, Revenue-Supported Entities Rating Criteria (February 2021)

Related Research

2021 Outlook: U.S. Public Power and Electric Cooperatives (December 2020)

Public Power - Fitch Analytical Comparative Tool (FACT) - 2020 (June 2020)

U.S. Public Power: Peer Review (June 2020)

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New Issue Summary

Sale Date: Sept 1, 2021

Series: Tax-Exempt New Series 2021A and Taxable Series 2021B

Purpose: Refunding Series 2018 CP Program (New Series 2021A); refunding 5-year note (New Series 2021B)

Security: System revenues

Garland Power & Light's (GP&L) 'AA–' debt ratings reflect a very strong revenue framework and strong operating performance, which enabled the utility to maintain leverage consistent with Fitch Ratings' 'aa' financial profile, despite incurring $137 million of debt-funded storm costs related to winter storm Uri in February 2021. The assignment and affirmation of GP&L's ratings further reflect Fitch's expectation that the utility's post-storm leverage, measured as net adjusted debt to adjusted funds available for debt service (FADS), will stabilize below 6.0x and 6.5x in Fitch's base case and stress case scenarios, respectively, reflecting the long-term recovery of debt-funded storm costs.

Fitch's removal of GP&L's Negative Watch reflects the adequacy of the utility's liquidity following the February storm, as well as implementation of a long-term plan for funding and recovering associated storm costs. Fitch expects GP&L's cash on hand to exceed 300 days at fiscal year-end (FYE) 2022 and to grow to prestorm levels in excess of 500 days by FYE 2022. GP&L's strategy to manage liquidity through the event included use of its rate mitigation funds, built up over time, in lieu of raising rates.

The Negative Outlook reflects Fitch's view that state investigations, litigation regarding the storm and the implementation of legislation are likely to continue over the medium term, with unknown credit implications for market participants. In addition, uncertainty remains as to the amount that the Electric Reliability Council of Texas (ERCOT) will recover in relation to the cumulative short-payments that it did not receive from defaulting members and the magnitude of residual short payments, if any, that could be uplifted to ERCOT members.

The 'AA' rating on GP&L's senior lien bonds reflects the small remaining debt, its closed lien and the added cushion against default afforded to the lien relative to subordinate obligations.

Key Rating Drivers

Revenue Defensibility: 'aa'; Competitive Power Provider with Rate Flexibility: GP&L provides competitive electricity and services to a largely residential customer base and to municipal and cooperative power companies under multiyear contracts. The utility has the independent ability to raise retail and wholesale electric rates, and retail rates are highly affordable.

Operating Risk: 'a'; Very Low Operating Costs; Weakened Operating Cost Flexibility: Fitch's 'a' assessment of GP&L's operating risk profile and weaker operating cost flexibility reflect the ERCOT market's inability to provide reliable service during Uri, plus extended price spikes in the storm. GP&L's 'aa' operating cost burden reflects its history of very low operating costs and elimination of Texas Municipal Power Agency (TMPA) capacity payments in fiscal 2019.

Financial Profile: 'aa'; Financial Profile Stable Through Stress Scenario: GP&L's fiscal 2020 leverage ratio of 4.9x is very low and reflects elimination of TMPA demand charges in fiscal 2019. Although leverage is expected to rise over the near term, ratios remain consistent with the current assessment through Fitch's base and stress scenario analysis. Liquidity is neutral to the rating at 511 days cash on hand at FYE 2020.

ESG – Environment: GP&L has an ESG score of '4' due to the effects of recent severe winter weather, which could have a negative impact on credit quality and is relevant to the rating in conjunction with other factors.

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to a Positive Rating Action/Upgrade

- Sustained leverage ratios below 5.0x in Fitch's base and stress cases;
- Maintenance of current liquidity ratios;
- Reduced exposure to more volatile wholesale energy sales and related counterparty risk.

Factors that Could, Individually or Collectively, Lead to a Negative Rating Action/Downgrade

- Significant growth in wholesale sales that is not offset by strong liquidity levels and sufficient controls to reduce related market and credit risks;
- Sustained liquidity significantly below historical levels;
- Sustained leverage in the base and stress scenarios above 8.0x;
- Legislative or regulatory changes that impose material new costs for utilities.

Credit Profile

GP&L is a municipally owned electric services provider serving a retail customer base of approximately 72,300 customers as of fiscal 2020. The City of Garland (AAA/Stable) is in Dallas, Collin, and Rockwall counties, approximately 14 miles northeast of downtown Dallas. In addition to its retail customer base, the electric system provides wholesale services to a small portfolio of municipalities and electric cooperative utilities, and coordinates the provision of ERCOT ancillary services. GP&L is an integrated utility with generation, distribution and transmission assets, and is a qualified scheduling entity in ERCOT.

Fitch considers GP&L a related entity of the City of Garland, given the dependent relationship of the electric system as an enterprise unit of the city. The rating on the electric utility revenue bonds is not constrained by the credit quality of the city.

Winter Storm Uri

Fitch placed a Rating Watch Negative on ERCOT municipal and electric cooperative issuers on Feb. 24, 2021. The Watch recognized the potential for negative financial outcomes among ERCOT members given the severity of market disruption and degree of commodity price volatility during the storm, the week of Feb. 14, 2021. (See "Fitch Places Texas Public Power Utilities and Electric Cooperatives on Rating Watch Negative" at www.fitchratings.com.)

Revenue Defensibility

All of GP&L's business lines and revenue sources exhibit very strong, monopolistic characteristics. GP&L derives its revenues from the sale of electricity and related services to retail and wholesale customers, and from provision of transmission services. The utility provides retail electric service in a noncompetitive territory that includes approximately 80% of all electric customers within the city of Garland. The remaining 20% of the city's electric customers are served by other retail providers.

GP&L's wholesale sales are made pursuant to multiyear contracts. These include full load requirement services to the city of Farmersville and partial load requirement services to South Texas Electric Cooperative, the city of College Station, Fayette Electric Cooperative, the city of Weatherford, and Central Texas Electric Cooperative. Contract terms are staggered between 2021 and 2027.

GP&L also sells renewable resources under long-term purchase power agreements (PPAs) extending to 2036 to several utilities under terms and conditions mirroring those between

Rating History (IDR)

Rating	Action	Outlook/ Watch	Date
AA–	Affirmed	Negative	7/30/21
AA–	Affirmed	Negative[a]	2/24/21
AA–	Assigned	Stable	12/14/12

[a]Rating Watch.

GP&L and the renewable project provider. Although GP&L retains payment risk, the off-takers generally consist of stable municipal and cooperative retail systems with full rate-setting authority. GP&L structures wholesale transactions to be consistent with International Swaps and Derivatives Association and Edison Electric Institute standards, and contracts provide make-whole provisions to protect the utility in early termination.

GP&L's wholesale sales exceed those of a typical retail public power utility. Fitch believes this does not detract from GP&L's very strong revenue defensibility due to the extent of its retail operations, the limited contribution from wholesale sales to margins, the multiyear term of wholesale contracts, high wholesale customer credit quality and risk mitigation provisions.

GP&L's service area exhibits strong demographic and demand characteristics, reflecting the city's inclusion in the Dallas-Fort Worth metroplex. The utility's total retail customer base realized a five-year CAGR of 0.8% through 2020. Median household income and unemployment approximate 97% and 90% of the U.S. averages, respectively.

Garland, with a population of approximately 240,000 in 2020, is the second-largest city in Dallas County, with access to a sizable regional labor force and multimodal transportation network, capable of supporting its long-standing manufacturing base. Top employers in Garland include Kraft Foods, Sherwin-Williams, US Food Services, Hatco (Resistol), Andersen Windows, Arrow Fabricated Tubing and General Dynamics. More broadly, the metropolitan area continues to see growth in its diverse commercial and industrial bases, as well as an increasing number of data center and financial service businesses.

Notwithstanding Garland's presence in the regional economy, its largely residential customer base provides GP&L with further demand stability. The utility's residential customers accounted for 39% of 2020 electric revenue. The top 10 customers accounted for only 6.6% of GP&L's fiscal 2020 revenue.

GP&L has the independent ability to increase its distribution retail and its wholesale power supply contract rates without external approval. Its retail rate structure includes a base rate and a recovery adjustment factor. Changes to the base rate require approval from the city council. However, the utility director can change the recovery adjustment factor on a monthly basis to support financial operations. The utility's retail rates approximate the state average and electric costs are highly affordable at 2.4% of Garland's median household income.

Garland has received timely and sufficient recovery of its transmission costs of service from the Texas Public Utility Commission. Newly activated transmission assets are included in rate base through ongoing interim capital filings.

Operating Risk

GP&L exhibited a very low operating cost burden of 6.7 cents per kilowatt-hour (kWh) in fiscal 2020, reflecting economic fuel and energy purchases and elimination of TMPA contract obligations. Garland and the cities of Denton, Bryan and Greenville created the TMPA in 1975, which developed the Gibbons Creek Steam Electric Station coal-fired plant in Grimes County, TX. Effective Oct. 1, 2018, GP&L and the other TMPA member cities elected not to extend their power supply contracts with TMPA, ending the required demand charge, which contributed close to 15% of GP&L's cost burden in fiscal 2018.

After an operating cycle of seasonal use, the plant was retired in October 2018 and sold on Feb. 10, 2021. Although no cash was received from the sale, the new owners are reportedly obligated for decommissioning and other plant closure costs. TMPA continues to operate owned transmission assets on behalf of its four members.

Fitch has assessed GP&L's operating cost flexibility as weaker, consistent with all public power utilities operating within the ERCOT organized power market and reflecting exposure to ongoing risks associated with the ERCOT market operating structure and volatile commodity prices, which were evident during the February weather event. The financial impact to GP&L of these weaknesses included higher than anticipated natural gas and purchased power costs to serve load during the storm, which amounted to a net storm cost of $134 million.

GP&L's Olinger Units 3 and 4 were available for the storm and performed throughout. Olinger Units 1 and 2 were on extended outages unrelated to the extreme weather; Spencer Units 4 and 5 were on planned seasonal maintenance outages, and also were not available during the storm.

GP&L's diverse power supply reflects a transition over the past five years from reliance on coal to a power supply incorporating competitively priced market purchases and renewable PPAs. The utility's fiscal 2020 retail power supply is well diversified and flexible, consisting of owned (natural gas-fired) capacity of 521MW, bilateral PPA (75MW), renewable (wind/solar) PPAs (213MW), and hydro (1.8 MW). GP&L's natural gas-fired units continue to represent valuable capacity in the tightening ERCOT market, serve as a physical hedge against high market prices and provide GP&L with a degree of operational flexibility. GP&L's resource portfolio exceeds its 2020 peak load of 473MW.

GP&L's lifecycle investment needs are moderate, based on Fitch's estimated 12-year average age of plant and planned capital spending well in excess of depreciation over the next five years. Capital projects total $291 million in fiscal 2021–2025, the majority of which represents transmission lines and substation upgrades, as well as distribution system projects. Transmission projects are driven primarily by ERCOT planning to address transmission system requirements in the Garland area and by proposed renewable projects connecting to the GP&L transmission system.

Financial Profile

GP&L's leverage ratio improved to 4.9x at FYE 2020 from 6.7x in 2016, reflecting continued strong operating performance, the elimination of TMPA demand charges and system growth.

Liquidity is neutral to the rating, as cash on hand remains robust, with 511 days on hand at FYE 2020. These funds include GP&L's rate mitigation fund equal to $192.2 million as of Sept. 30, 2020. GP&L has historically managed rate mitigation fund monies for strategic and competitive purposes. Coverage of full obligations at 1.4x in fiscal 2020 dipped below 1.0x in several of the last five years, but Fitch does not consider it weak or risk additive based on the utility's robust unrestricted cash position in excess of 120 days.

Fitch Analytical Stress Test (FAST)

Fitch expects the utility's operations to support a financial profile consistent with the current assessment through Fitch's base case and stress case scenarios. Fitch's analysis is further informed by GP&L's financial forecast and reflects modest load growth, corresponding estimates for the cost of purchased power and the lack of base rate changes. The utility's capital forecast reflects transmission system growth that Fitch considers reasonable. The base case scenario indicates that GP&L's leverage ratio will peak at 7.8x in fiscal 2021, reflecting a year of heavy debt-funded capital investments, before declining to under 6.0x by year five of the analysis. The analysis reflects the utility's plans to establish a regulatory asset in the amount of its $134 million in fiscal 2021 storm costs.

The stress case incorporates reduced sales for years one and two, followed by recovery in years three through five. GP&L's leverage ratio rises higher to 8.5x in the first year of stress but moderates to 7.0x by year three and 5.9x by year five.

GP&L's debt profile is neutral to the rating. Following these transactions, GP&L will have approximately $5.0 million in senior (closed lien) debt outstanding and approximately $722 million in second lien debt. GP&L's series 2018 CP note program will be refunded with new series 2021A and replaced with a private placement note program.

ESG Considerations

Garland, TX, (Electric has an ESG Relevance Score of '4' for Exposure to Environmental Impacts due to the extreme winter weather event in February 2021, which has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Financial Summary

($000; Audited fiscal years ended Sept. 30)	2016	2017	2018	2019	2020
Net Adjusted Debt to Adjusted FADS (x)	**6.68**	**7.13**	**8.12**	**4.72**	**4.87**
Net Adjusted Debt Calculation					
Total Current Maturities of Long-Term Debt	26,605	28,880	30,305	34,335	23,420
Total Long-Term Debt	409,141	469,035	499,838	527,862	576,267
Total Debt	**435,746**	**497,915**	**530,143**	**562,197**	**599,687**
+ Capitalized Fixed Charge – Purchased Power and Gas	447,883	450,140	402,536	299,022	303,850
+ Total Pension Obligation (GASB Fitch-Adjusted NPL + FASB PBO)	21,742	22,357	0	28,478	17,427
– Total Unrestricted Cash	231,281	222,563	195,857	225,861	264,354
Net Adjusted Debt	**674,090**	**747,849**	**736,823**	**663,836**	**656,610**
Adjusted FADS for Leverage Calculation					
Total Operating Revenue	278,970	280,453	288,523	301,684	298,420
Total Operating Expenses	267,791	268,063	246,326	210,581	223,358
Operating Income	**11,180**	**12,390**	**42,197**	**91,103**	**75,062**
+ Depreciation and Amortization	14,273	15,067	16,620	18,719	19,805
+ Interest Income	1,405	1,679	2,559	6,691	5,774
+ Other Non-Cash Charges	36,548	36,192	6,913	6,943	14,878
Funds Available for Debt Service	**63,405**	**65,328**	**68,289**	**123,456**	**115,518**
+ Adjustment for Purchased Power	55,985	56,267	50,317	37,378	37,981
– Total Transfers/Distributions	22,544	21,602	27,884	25,587	22,454
+ Pension Expense	4,028	4,847	0	5,462	3,866
Adjusted FADS for Leverage	**100,874**	**104,840**	**90,722**	**140,709**	**134,912**
Coverage of Full Obligations (x)	**0.98**	**0.98**	**0.91**	**1.50**	**1.38**
Funds Available for Debt Service	63,405	65,328	68,289	123,456	115,518
+ Adjustment for Purchased Power	55,985	56,267	50,317	37,378	37,981
– Total Transfers/Distributions	22,544	21,602	27,884	25,587	22,454
Adjusted FADS for Coverage	**96,846**	**99,993**	**90,722**	**135,247**	**131,046**
Full Obligations Calculation					
Cash Interest Paid	17,656	19,131	19,964	22,544	22,765
Prior Year Current Maturities	25,505	26,605	28,880	30,305	34,335
Total Annual Debt Service	**43,161**	**45,736**	**48,844**	**52,849**	**57,100**
+ Adjustment for Purchased Power	55,985	56,267	50,317	37,378	37,981
Total Fixed Obligations	**99,147**	**102,003**	**99,161**	**90,226**	**95,081**
Liquidity Cushion (Days)	**607**	**402**	**321**	**470**	**511**
Unrestricted Cash (Days)	**389**	**375**	**321**	**446**	**511**
Liquidity Calculation					
+ Total Unrestricted Cash	231,281	222,563	195,857	225,861	264,354
+ Total Borrowing Capacity	199,245	139,245	159,440	80,000	67,735
– Amounts Unavailable	69,910	123,280	159,440	68,000	67,735
Total Liquidity	**360,616**	**238,528**	**195,857**	**237,861**	**264,354**
Cash Operating Expense Calculation					
Total Operating Expense	267,791	268,063	246,326	210,581	223,358
– Depreciation and Amortization	14,273	15,067	16,620	18,719	19,805
– Other Non-Cash Charges	36,548	36,192	6,913	6,943	14,878
Cash Operating Expenses	**253,518**	**252,995**	**229,706**	**191,861**	**203,553**

FADS – Funds available for debt service. GASB – Government Accounting Standard Board. NPL – Non-pension liability. FASB – Financial Accounting Standard Board. PBO – Pension benefit obligation.
Source: Fitch Ratings, Fitch Solutions, Lumesis, Energy Information Administration, Garland, Texas.

Key Definitions

Terms	Definition	Significance
Issuer Default Rating (IDR)	An expression of overall enterprise risk and relative vulnerability to default.	Provides an opinion of the relative ability of an entity to meet financial commitments, expressed as an ordinal measure of credit risk.
Standalone Credit Profile (SCP)	An expression of overall enterprise risk.	Provides an opinion of the credit quality of an entity on a standalone basis, irrespective of its relationship with, or the credit quality of, its related municipality.
Net Adjusted Debt	Adjusted debt – unrestricted cash – funds restricted for debt service	Provides an inclusive evaluation of long-term liabilities offset by funds available for debt service.
Adjusted FADS	EBITDA + interest income + 30% of purchase power expense + operating lease expense – transfers/distributions + pension expense	Provides an indication of cash flow available for the payment of debt service, adjusting for purchased power, operating lease and pension obligations.
Net Adjusted Debt to FADS	Net adjusted debt/adjusted FADS	Provides an indication of net total leverage position against available operating cash flow.
Full Obligations	Cash interest paid + scheduled long-term principal payments + 30% of purchase power expense	Provides an indication of inclusive fixed and debt service obligations.
Coverage of Full Obligations	(EBITDA + interest income + 30% of purchase power expense + operating lease expense – transfers/distributions)/full obligations	Provides an indication of the relative cushion of operating cash flow to fixed charges.
Base Case	The expected forward-looking case in the current macroeconomic environment.	Provides the analytical starting point in the forward-looking analysis, and also informs the stress case.
Stress Case	The potential performance under a common set of assumptions.	Illustrates how cycles affect individual issuers differently, and informs the level of rating stability and credit resiliency.

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.