

FITCH AFFIRMS CONNECTICUT MUNI ELECTRIC ENERGY COOPERATIVE (CT) AT 'A+'; OUTLOOK STABLE

Fitch Ratings-New York-13 March 2017: Fitch Ratings has affirmed the 'A+' rating on Connecticut Municipal Electric Energy Cooperative's (CMEEC) following bonds:

- \$55.9 million power supply system revenue bonds, 2013 series A & B;
- \$23.2 million 2012 transmission services revenue bonds at 'A+'.

In addition, Fitch affirms the following bonds:

- \$20.1 million Connecticut Transmission Municipal Electric Energy Cooperative (TRANSCO) 2012 Series A transmission system revenue bonds at 'A+'.

The Rating Outlook is Stable.

SECURITY

The CMEEC power supply system revenue bonds are secured by a pledge of net revenues of CMEEC, including revenues derived from power sales contracts with its member systems. The TRANSCO bonds are secured by net revenues received by TRANSCO from CMEEC, which are principally derived from separate take-or-pay contracts with the same six member systems.

KEY RATING DRIVERS

NEW ENGLAND JOINT ACTION AGENCY: CMEEC provides wholesale electric power to six member municipal distribution systems, each in highly rated service areas, and two contracted purchasers throughout southern and eastern Connecticut. Participants serve an aggregate retail base of nearly 74,000 customers. CMEEC also provides transmission services via TRANSCO.

SOLID RECOVERY IN FINANCIAL PERFORMANCE: CMEEC's 2015 financial performance and preliminary financial results for 2016 support the current 'A+' rating, and reflect a solid recovery following termination of a power sales contract with the city of Wallingford. Cash flow, leverage and liquidity were all stronger than category medians in 2015, demonstrating results Fitch expects to continue.

INDUSTRIAL CUSTOMER CONCENTRATION: Major retail customers served by CMEEC's largest participants - Groton Utilities (Groton), Bozrah Light & Power (Bozrah), and the Mohegan Tribal Utility Authority (MTUA) - expose CMEEC to a moderate degree of customer concentration risk. However, a flexible power supply portfolio should limit CMEEC's vulnerability to tighter margins due to the loss of a major customer.

POWER SUPPLY RISK: CMEEC is exposed to fluctuating power prices because of its actively managed power supply (mainly short- to intermediate-term contracts). However, its comprehensive risk management policy has kept its costs competitive and margins generally steady. Automatic rate adjustments provide additional protection.

MEMBERSHIP STABILIZES AND DISPUTE APPROACHES RESOLUTION: CMEEC's membership has stabilized favorably, with Bozrah becoming a member in 2016. Although contract

disputes with the city of Wallingford are still in arbitration, CMEEC maintains ample liquidity to absorb the potential obligations. A resolution is expected by the close of 2017.

COST BENEFIT OF TRANSCO: The creation of TRANSCO, a legally separate joint action agency, has allowed CMEEC to maximize the financial return to its ownership of transmission lines, which is ultimately used to reduce net transmission costs.

RATING SENSITIVITIES

CONTINUED MEMBERSHIP SUPPORT FOR METRICS: Member support of both CMEEC and TRANSCO is a key credit strength. The inability of members and purchasers to recoup any potential increased power supply costs, combined with an unwillingness of members to support CMEEC financial metrics, particularly following the loss of a significant retail or wholesaler purchaser, would put downward pressure on the rating.

CREDIT PROFILE

CMEEC is a joint action agency that provides power to six member municipal distribution systems - Groton, Bozrah, Jewett City Department of Public Utilities, Norwich Public Utilities, and the city of Norwalk's Second (South Norwalk) and Third (East Norwalk) Taxing Districts. CMEEC also serves two wholesale purchasers: Wallingford Electric Division and MTUA. Wallingford will continue buying forward energy purchases CMEEC made on its behalf through 2017, and participate in the MicroGen and Pierce Projects through at least 2018 and 2021, respectively.

POWER SUPPLY AND TRANSMISSION

The majority of CMEEC's power supply is purchased through short- and intermediate-term contracts, on average one to three years. CMEEC's power supply strategy has largely been effective, as evidenced by its wholesale cost of power being consistently lower than nearby investor-owned utilities.

Last revised in 2014, the risk management policy requires that any commitment with a term greater than five years - whether a long-term power purchase agreement or a generation asset - must be fully subscribed prior to execution. Fitch views this policy favorably, as it reduces CMEEC's exposure to being long on power.

CMEEC created TRANSCO in September 2009 as a separate, legal joint action agency to acquire transmission services required by CMEEC for its participants. CMEEC is obligated to pay all of TRANSCO's obligations on a take-or-pay basis, including debt service. The transmission-related agreements extend through 2052.

IMPROVED FINANCIAL PERFORMANCE

CMEEC's financial profile remains supportive of the current rating having strongly recovered from the 2014 deterioration following the loss of Wallingford's purchases. Fitch expects CMEEC to maintain its financial profile at this recovered level, as it has historically.

Debt service coverage rebounded to 1.77x, exceeding the rating category median of 1.34x, and liquidity remained robust at 105 days cash on hand in 2015.

CMEEC's members continue to demonstrate strong financial profiles, and support CMEEC's credit quality. Member systems exhibit robust liquidity, and ample margins to cover their fixed obligations. The five largest members maintained an average of 127 days cash on hand in 2015.

Moreover, service areas are highly rated: Fitch rates the general obligations debt of the cities of Groton, Norwich and Norwalk 'AA'/Stable, 'AA'/Stable and 'AAA'/Stable, respectively.

GOVERNANCE CONCERNS

Fitch views CMEEC's recent controversy regarding the funding of costly off-site strategic planning trips for its Board members and their associates as credit neutral. The potential financial impact of reimbursement is manageable. However, management and governance is affected, as time and resources are diverted to address this issue and the proposed state legislation to dissolve CMEEC, which has not garnered material legislative support.

Fitch will be looking for management and the Board to continue to focus on strategic planning, and maintain sound rate and financial performance, which are key to supporting the rating.

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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>

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