Fitch Affirms Reedy Creek Improvement District's Utilities Rev Bonds at 'A'; Outlook Stable

Fitch Ratings-New York-13 April 2017: Fitch Ratings has affirmed the 'A' rating on the following Reedy Creek Improvement District (FL) (RCID or the District) bonds:

--$67.025 million electric system revenue bonds series 2013-1 and 2015-2;

The Rating Outlook is Stable.

SECURITY

The bonds are secured by a first lien on net revenues of the combined utility system, after payment of operations and maintenance costs.

KEY RATING DRIVERS

COMBINED UTILITY SYSTEM SERVING WALT DISNEY WORLD: RCID is a combined system providing eight utility services to portions of Osceola and Orange counties in central Florida, which include Walt Disney Company's theme parks and resorts. Electric service accounts for the majority of the revenues, at 53% of 2016 total utility revenues.

SINGLE CUSTOMER RELIANCE: Utility service requirements are dominated by the Florida-based theme parks owned by Walt Disney Company (Disney, Fitch Issuer Default Rating 'A'/Stable Outlook). Disney consistently accounts for more than 80% of the District's total system revenues. As a result, the District's rating is highly correlated with, but not directly linked to Disney. Disney's solid credit quality has been a positive rating factor for the District in recent years.

IMPORTANCE OF THEME PARKS: The theme parks and resorts located within the District's service area are important to Disney's financial performance. As such, Fitch believes that making payments to the District for essential utility services are a high priority for Disney and a credit positive for RCID.

IMPROVEMENT IN FINANCIAL METRICS: The District's historically weak but stable financial metrics improved to levels above medians for the 'A' rating category in 2016. Coverage of full obligations and days cash on hand rose to 1.39x and 57 days, respectively, compared to medians of 1.13x and 75 days. Leverage continued to decline with adjusted debt to funds available for debt service at 4.9x for 2016.

SHORT-TERM POWER PURCHASES: The vast majority of the District's power supply is purchased pursuant to short-term, two- and three-year contracts. Although short-term contracts have resulted in competitive wholesale power costs due to favorable market conditions in recent years, the duration of these agreements exposes the utility to longer-term price uncertainty.

RATING SENSITIVITIES

CHANGE IN DISNEY CREDIT QUALITY: The credit quality of the Walt Disney Company remains a key credit factor in the Reedy Creek Improvement District's rating given the substantial concentration of utility services provided to the Disney theme parks and resorts. Movement in Disney's credit quality could therefore impact the District's rating.

ADEQUATE FINANCIAL METRICS: A failure to increase utility service rates to maintain adequate financial performance could lead to negative rating action, particularly as the District's financial metrics have historically been weak for the 'A' rating category. Conversely, a stronger financial profile and favorable terms for its longer-term power supply could indicate a material improvement in credit quality.

CREDIT PROFILE

RCID was created in 1967 by a special act of the state legislature. The legislation granted the District governmental powers to promote recreation oriented projects, economic development and tourism - objectives the legislature determined served a valid public purpose. The act was passed in anticipation and support of the development of Walt Disney World Resort (Disney World), which opened in 1971. The District continues to provide eight essential utility services (including electric, water, sewer, natural gas and solid waste) primarily to Disney World.

SLIGHTLY IMPROVED FINANCIAL METRICS

Fitch views the District's financial profile as stable and supportive of its current rating category. Although results were stronger in fiscal 2016, cash flow, leverage and liquidity metrics have generally remained in line with Fitch's expectations and weaker than rating category medians. Coverage of full obligations rose above the five year average (1.1x) in 2016, reaching the category median of the prior year of 1.3x. Lower purchased power costs helped widen margins. The District's operating margin rose to 17.2%, from an average of 13.4% in 2011-2015.

Management's comfort in maintaining slim liquidity stems from the inherent flexibility to raise rates in a fairly quick fashion (60 to 90 days), and the supportive working relationship it has with Disney.

Fitch expects margins and leverage to continue improving, as 40% of outstanding debt retires by 2019, and 54% by 2021.

DISTRICT IS EXPOSED TO THE DISNEY OPERATION

The District exhibits high customer concentration with Disney accounting for 86% of utility operating revenues in 2016.

Favorably, Disney World has a long track record as one of the world's top tourist destinations; and Disney continues to make substantial investments in its theme parks and resorts, which accounted for 31% of Disney's 2016 revenues.

During periods of macroeconomic volatility, Fitch expects these cyclical businesses to be under pressure but that the Disney credit and financial profile will likely remain consistent with its current ratings. Utility reliability is an integral part of this operation and it is Fitch's view that Disney places a high priority on making payments to the District for utility services, thereby supporting the District's 'A' 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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