

Bond Case Briefs

Municipal Finance Law Since 1971

Moody's: US Regulated Utilities to Continue Steady M&A.

Mergers and acquisitions in the US utilities industry will keep to a steady pace over the next few years, says Moody's Investors Service, as utilities look to expand and diversify. Moody's says utility deals have been generally neutral to credit quality because they have been financed with a balanced mix of debt and equity.

Slow growth in electricity use is forcing the utilities to look beyond their service territories for growth, says Moody's in the report "US Regulated Utilities: Expansion, Diversification Goals Continue to Support Steady Utility M&A."

"Load growth has been moderating in recent years, the slower pace driven primarily by energy conservation and efficiency, increased distributed generation and the economic downturn," says Jeffrey Cassella, a Moody's Analyst. "The slower growth has pushed some utilities to look beyond their service territories for additional load growth in areas that are growing faster than the national average."

Many utilities are also looking to expand their regulated businesses as a way to increase the stability and predictability of their cash flows, while at the same time they add to their operational efficiency as they spread operating and maintenance costs over a wider customer base.

Declining returns on equity among the utilities will also motivate the utilities to look to mergers as a way to lower costs as they seek to capture synergies and reduce overhead costs.

"The industrial logic behind consolidating a homogenous, fragmented industry sector makes sense," added Cassella, "because spreading fixed costs across a larger asset platform is more efficient and should benefit consumers longer term."

Capital markets are likely to be conducive to deals, says Moody's, access to these markets having improved since the economic downturn. Better access as well as the improved credit quality of the utilities will support more leveraged transactions.

Moody's expects regulators to remain receptive to consolidation in this fragmented industry, although regulatory intervention remains a risk. Higher interest rates may slow down the pace of debt-financed acquisitions, but rates should still remain at levels that will not hinder the financing of future deals.

For more information, Moody's research subscribers can access this report at:

https://www.moodys.com/research/US-Regulated-Utilities-Expansion-Diversification-Goals-Continue-to-Support-Steady-PBC_159270