

CREDIT OPINION

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Knoxville (City of) TN Electric Enterprise

Update to credit analysis

Summary

Knoxville Electric Enterprise, TN (Aa2 stable revenue rating) benefits from a strong regional economy and stable customer base. In addition, the system is well managed and revenues continue to provide healthy debt service coverage of approximately 4.07 times fiscal 2025 revenues and satisfactory liquidity of 68 days.

The enterprise's debt profile is manageable with a moderately above-average debt ratio and affordable debt to operating revenues ratio. Currently, additional debt plans include an estimated \$37 - \$47 million over the next three years and should not significantly impact the overall debt profile of the electric system. A medium-term challenge will be the successful completion of the electric system's Enhanced Grid Modernization effort and implementation of broadband service to Fiber Division customers. While the majority of the Enhanced Grid Modernization project is related to the implementation of new advanced technologies which will improve the reliability of the electric system, a portion is also related to the ongoing deployment of a high speed fiber network which will allow for the provision of broadband services to local customers.

Credit strengths

- » Large, stable service area with limited customer concentration
- » Healthy debt service coverage

Credit challenges

- » Below average resident income levels
- » Moderately above-average debt profile
- » Ongoing roll out of Enhanced Grid Modernization

Rating outlook

The stable outlook reflects the expectation that the electric system will continue to proactively review and adjust rates to maintain debt service coverage and cash flow to support pay-as-you-go capital investment. The outlook also reflects the system's broad and stable service area.

Factors that could lead to an upgrade

- » Increases in days cash on hand to levels more in line with rating category
- » Increases in service area wealth to around 140% of the national median
- » Increased system demand and customer growth

Factors that could lead to a downgrade

- » Deterioration of debt service coverage to below 2.25 times
- » Declines in days cash on hand to below 50 days
- » Significant increases in debt levels
- » Reliance on electric system by fiber division beyond current expectations

Key indicators

Exhibit 1

Knoxville (City of) TN Electric Enterprise

Sources: Knoxville (City of) TN Electric Enterprise, Moody's Ratings

Profile

The Knoxville Utilities Board (KUB) provides electric transmission and distribution, fiber broadband services, gas distribution, water treatment and distribution, and sewer collection and treatment to a population of 487,401 (2023 American Community Survey) located in the City of Knoxville (Aa1 stable) and County of Knox (Aa1 stable).

Detailed credit considerations

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moodys.com> for the most updated credit rating action information and rating history.

Service Area and Characteristics: Knoxville service area provides continued customer growth

KUB's electric system will continue to experience moderate customer growth over the near-term given the regional significance of the City of Knoxville tax base. KUB is a Tennessee Valley Authority (Aaa stable) electric distributor with approximately 226,224 customers as of fiscal 2024. Electric service is provided not only to the City of Knoxville, but also Knox County and portions of the adjacent counties.

The Knoxville-Knox County area is the regional business, educational and health care service center for eastern Tennessee (Aaa stable). Large, institutional employers, such as the University of Tennessee and the Tennessee Valley Authority (Aaa stable), anchor the local job base and provide stability. In addition, the local economic base also benefits from its proximity to Oak Ridge National Laboratories.

From 2019 through 2024, the system's customer base, which is predominantly residential, has experienced moderate growth, increasing approximately 1.7% annually. Officials expect that growth over the next five years will be similar to current levels.

The electric system's total peak capacity of 3,029 MW is sufficient to meet current and future needs. The system reached a new peak demand of 1,350 MW (64.2% of peak capacity) in 2024 as a result of colder weather conditions and ongoing growth. The system is well diversified, with residential customers comprising 88.7% of the customer base and 48.7% of system revenues in fiscal 2025. The top 10 customers account for a reasonable 14.9% of total system revenues, with Carpenter Creek LLC as the largest source of revenue.

The Electric Division is in the midst of a major ongoing initiative, the Enhanced Grid Modernization effort. This project includes the installation of a high-speed fiber optic network (owned by the Electric Division) which allows KUB to implement new advanced technologies (smart switches, additional substations, etc) that improve the overall reliability and flexibility of the electric system. In addition to improving the reliability of the electric system, the fiber optic network allows KUB to offer broadband services to residents within the service area. A separate Fiber Division was established in 2022 and a plan to offer broadband service was reviewed and approved by the State Comptroller of TN, TVA and Knoxville City Council. The Fiber Division operates completely separately from the Electric Division and the only financial assistance from the Electric Division is \$55 million in start-up loans (monies loaned to the division over five years). This loan amount cannot be increased unless it is again reviewed by TVA and will be fully repaid by the Fiber Division with annual payments through fiscal 2032. The Fiber Division also pays utilization and access fees to the Electric Division for use of the fiber optic network which began in late fiscal 2022 and will continue to ramp up based on fiber customer additions. Roll-out of broadband services to customers through the Fiber Division will be done with a measured approach. Only when customers sign-up for Broadband service, will fiber be run from the street to the residential properties. Management has various roll out plans and target take rates in place which are conservative in nature and will only advance if these targets are achieved.

Debt Service Coverage and Liquidity: Continued healthy debt service coverage in fiscal 2025

KUB's electric system will maintain a strong overall financial position given prudent fiscal management and conservative budgeting practices. While debt service coverage declined in fiscal 2019 and 2020, the system maintains solid levels with fiscal 2024 coverage of 4.07 times. The system does make payments in lieu of taxes on an annual basis to the city, however these payments are subordinate to debt service.

Maximum annual debt service (MADS) coverage over the next five years (inclusive of current and future debt issuances as well as annual rate increases and the loan to the Fiber Division) is projected to be between 4.34 and 4.78 times. The fiscal 2025 operating ratio of 79.8% is modestly higher than the median but reflects the fact that the system passes through energy charges from TVA directly to its customers.

KUB has full rate setting authority and passed on TVA's wholesale rate increase of 5.25% in October 2024 to customers. In addition to the TVA rate increases, KUB instituted a 3% increase in 2024 (effective April 1, 2024) and a 4% rate increase in 2025 (effective April 1, 2025). KUB has approved a 3% rate increase effective April 1, 2026 and 2% increase effective April 1, 2027. KUB has also instituted an automatic purchase power adjustment so that any future TVA increases are passed on to customers without the need for KUB Board approval.

Liquidity

The system's liquidity is expected to remain satisfactory given prudent management, supported by established fiscal policies. The system has a minimum cash balance policy of no less than \$50 million. Since 2010, unrestricted cash has been well above the policy.

In fiscal 2025 cash was \$108 million or 68 days and net working capital was approximately \$49 million. The enterprise also has an additional \$25 million in long-term contingency fund investments.

Debt and Legal Covenants: Legal provisions provide adequate protections for bondholders

The system's debt ratio (44.2% in fiscal 2025) and debt to operating revenue ratio (0.66 times fiscal 2025 revenues) will remain manageable despite future debt plans, given average amortization of principal and timely rate increases. In an effort to keep pace with growth as well as maintaining the system, officials continue to undertake a ten-year \$1.2 billion Capital Improvement Plan (CIP), 24% of which is funded with additional debt. The CIP primarily addresses the Century II initiative, which focuses on construction and refurbishment of substations, as well as replacing 2,600 distribution poles and 14 miles of underground cable per year. Management's 10 year financial plan includes various rate increases which will offset the projected annual debt issuances and maintain strong debt service coverage.

The legal provisions under the current resolution are expected to ensure adequate protection for bondholders. While the resolution includes a 1.20 times rate covenant and does not require a debt service reserve fund, we believe that the system's current debt service coverage adequately mitigates these features. All outstanding debt is secured by the net revenues on a parity basis and additional parity bonds may be issued if net revenues during twelve of the preceding twenty-four months are equal to 120% of aggregate maximum annual debt service (MADS), including the new parity bonds.

Legal security

All of the enterprise's debt is backed by a net revenue pledge of the electric system.

Debt structure

The enterprise's debt profile is made up of 100% fixed rate securities.

Debt-related derivatives

The enterprise is not currently party to any derivative agreements.

Pensions and OPEB

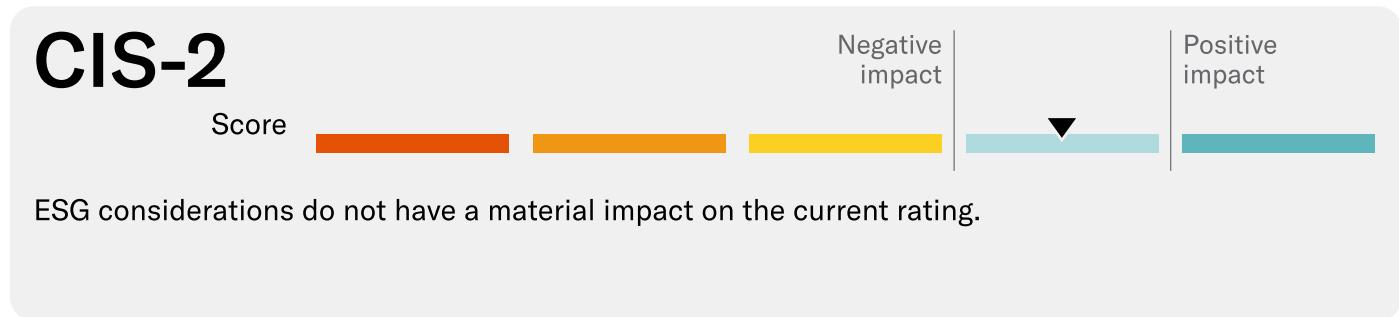
Employees participate in the Knoxville Utilities Board Pension Plan which is a single employer defined benefit plan administered through an Administrative Committee consisting of seven KUB employees that are appointed by KUB's President and CEO. As of December 31, 2024, the plan had 359 active members, 589 retirees and beneficiaries and 10 terminated vested participants. Based on the January 1, 2023 actuarial report, KUB contributed \$2.2 million for fiscal 2025 which constitutes 100% of the actuarial required contribution.

ESG considerations

Knoxville (City of) TN Electric Enterprise's ESG credit impact score is CIS-2

Exhibit 2

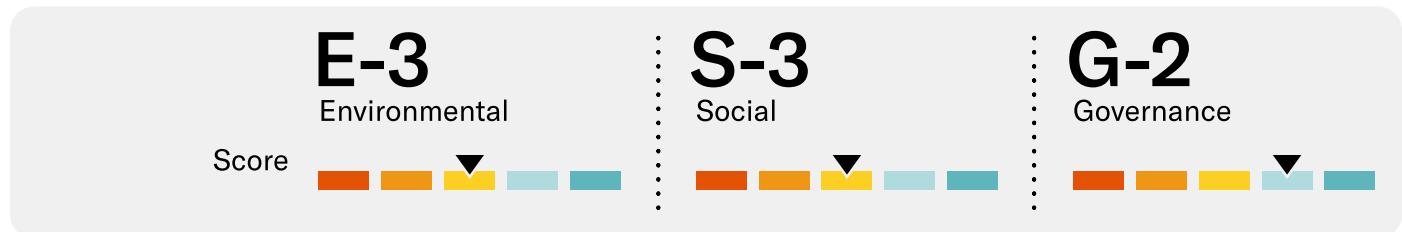
ESG credit impact score



Source: Moody's Ratings

Knoxville Electric Enterprise, TN's ESG credit impact score of **CIS-2** indicates that ESG considerations have a low impact on the enterprise's ratings.

Exhibit 3
ESG issuer profile scores



Source: Moody's Ratings

Environmental

The electric enterprise's moderate exposure to environmental risks considers the utility's geographical concentration in and around the City of Knoxville and its exposure to weather events. Like many local electric utilities, Knoxville Electric Enterprise is a Tennessee Valley Authority (TVA) power distributor. While Knoxville Electric Enterprise does have higher exposure to heat stress and extreme rainfall and moderate exposure to wildfires, which could damage poles and wires, these specific exposures are not currently so significant as to add sizeable risk.

Social

Exposure to social considerations is moderate, reflective of broadly shared public concerns about environmental, social and affordability issues that could lead to adverse regulatory or political intervention. These risks are balanced by lower exposure to health and safety, human capital and responsible production considerations.

Governance

Governance risk is low. The utility can recover service costs through a rate-setting mechanism that is not subject to state regulatory board approval, though intervention by local political leaders is a potential risk. Based on our assessment of past performance, risks associated with financial strategy, management credibility, organizational structure and compliance and reporting are low.

ESG Issuer Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The US Municipal Utility Revenue Debt methodology includes a scorecard that summarizes the factors that are generally most important to utilities' credit profiles. Because the scorecard is a summary and may not include every consideration in the credit analysis for a specific issuer, a scorecard-indicated outcome may or may not match an assigned rating.

Exhibit 4

Knoxville (City of) TN Electric Enterprise Scorecard

Knoxville (City of) TN Electric Enterprise (820354927)

| Rating Factors | Input | Weight | Score |
|--|---------------|--------|-------|
| System Characteristics (30%) | | | |
| Asset Condition (Years of Annual Depreciation) | 20.1969 | 10% | A |
| System Size (O&M in Thousands of Dollars) | \$586,076 | 7.5% | Aaa |
| Service Area Wealth (Median Family Income as % of US) | 74% | 12.5% | Baa |
| Financial Strength (40%) | | | |
| Annual Debt Service Coverage (x) | 4.07 | 15% | Aaa |
| Days Cash on Hand | 68 | 15% | A |
| Debt to Operating Revenue (x) | 0.6573 | 10% | Aaa |
| Management (20%) | | | |
| Rate Management | Aaa | 10% | Aaa |
| Regulatory Compliance and Capital Planning | Aa | 10% | Aa |
| Legal Provisions (10%) | | | |
| Rate Covenant (x) | 1.2 | 5% | A |
| Debt Service Reserve Requirement | Baa and Below | 5% | Baa |
| Notching Factors | | | |
| Additional service area economic strength or diversity | | | Up |
| Unusually strong or weak capital planning | | | Up |
| Credit event/trend not yet reflected in existing data sets | | | Down |
| Scorecard-Indicated Outcome | | | |
| Assigned Rating | | | Aa2 |

Data is based on most recent fiscal year available. Debt may include pro forma data for new debt issued or proposed to be issued after the close of the fiscal year.

Sources: Knoxville (City of) TN Electric Enterprise, Moody's Ratings

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