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Utilities face debt pileup

Unless Reagan eases credit, electricity production's annual growth will stagnate at 1.5 percent.

In the early 1970s, annual growth rates for electrical consumption in the United States were projected at between 6 and 7 percent. On Jan. 21, 1981, Northeast Utilities, a leading electricity producer, announced that a Connecticut state conservation program would limit annual growth in demand from its customers to 1.5 percent for several years.

A report by the Congressional Research Staff last summer considered a scenario in which electricity demand would grow by only 3.3 percent annually for the entire next decade, based on reserve margins of capacity at 5 percent less than what authorities consider to be safe levels.

The plight of U.S. utility corporations is one of the leading challenges awaiting Reagan administration action to reverse four years of regulatory dictatorship over capital investment.

The most capital-intensive industry in the country, utilities spent $26 billion on over 300 construction projects last year, with most funds going into nuclear- and coal-related capacity.

In 1981, the industry will inject a new $29 billion of capital outlays into the economy.

Preliminary estimates by our staff indicate that if the Carter era's environmentalist assault on power generation were lifted, up to $30 billion in additional capital outlays annually could be injected into U.S. construction, capital goods, and other supplier firms at an early date.

While many industry executives have greeted Mr. Reagan's commitment to review the recent years' regulatory assault on investments, there is little optimism in the industry that its problems can be reversed in the short term.

Although it is clear that nowhere near adequate deliberation on the possible solutions to the industry's problems has yet taken place, the scope of the electricity grid crisis emerging across the country is well documented.

From the credit standpoint, two additional problems currently hamstringing investment are a serious deterioration in industry earnings, and the recent years' pileup of short-term debt.

At this point, even if Reagan implements a 10 percent tax cut at an early date, this will have little effect on utility planning. As one securities analyst put it, "In order to benefit from a tax cut, you have to already be paying taxes. Many utility firms stopped paying taxes long ago, because they're not generating any profit."

Since utilities are highly capital-intensive, firms in this industry cannot delay expenditures.

When a utility firm can't get financing on the long-term market to meet capital needs, it must go to a bank, get those funds, and refinance them at a later time with long-term paper.

In October 1979, when Federal Reserve Chairman Paul Volcker imposed his credit slowdown on the U.S., high-interest debt whacked the industry hard. During 1980, Moody's and Standard and Poor's, the leading investor rating services, downgraded the credit ratings on the debt issues of over 20 firms. In one typical case last year a leading nuclear producer was paying more on its first mortgage bonds than the 13.7 percent return it was getting on its own equity.

In 1980, utility firms projected that they would borrow $17.3 billion on the long-term market. Due to the weakness of the long-term markets last year, however, they never received more than $14 billion.

By the end of 1979, short-term bank debt had shot up to $7.3 billion after just three months of Volcker's credit constraints. Although 1980 short-term debt tallies have not yet been released, analysts predict that another significant increase, possibly hitting $10 billion total, will turn out to have occurred last year.

After 15 months of Volcker's policies, the same utility corporations which had been 60 percent self-financing just two decades ago—that is, were able to finance 60 percent of their capital outlays from earnings, *despite* consumer rate declines—had become 70 percent dependent on external credit sources.

Preliminary analysis thus shows that the nation's power grid will be endangered unless low-interest credit, in addition to lifting of regulatory penalties, is made available at an early date. The cost to the economy as a whole would otherwise be intolerable.

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