CREDIT OPINION
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Energy NW - Nine Canyon Wind Project

Update to Key Credit Factor

Summary

Energy NW - Nine Canyon Wind Project's (Nine Canyon: A1 stable) credit profile reflects its power purchase contracts (PPAs) with five participants with a weighted average credit quality of A1 and PPA terms that incorporate many features of traditional 'take or pay' PPAs. While the operations and maintenance (O&M) cost cap and vague termination language are atypical and represent weakness in the contractual structure of the project, Nine Canyon's strong liquidity and ability to manage its O&M costs sufficiently mitigates these weaknesses. At the end of FY2023 (June 30), Nine Canyon had 735 days cash on hand in addition to a 12 month debt service reserve. Washington State's stringent decarbonization requirements for electric utilities also provide a regulatory incentive for the off-takers to purchase the power from Nine Canyon. Additionally, the scheduled ramp down in debt service by more than 50% starting in FY2024 increases financial flexibility and is supportive of credit quality.

Credit strengths

- Take-or-pay contracts with participants of A1 weighted average credit quality
- Long operating experience
- Historical operating costs below O&M cap
- Robust liquidity
- State support for renewables

Credit challenges

- Atypical contract features for take-or-pay contracts include an O&M cap and vague termination language
- Costs including debt service are typically above market prices

Rating outlook

The stable outlook considers the project's strong participant credit quality, demonstrated ability to keep costs within its O&M cap under its PPA, robust internal liquidity, and stringent decarbonization mandate for Washington state electric utilities.

Factors that could lead to an upgrade

- The project's rating could improve if the weighted average credit quality of the participants improve to Aa3 while the project maintains robust liquidity and manages its costs well below the O&M cost cap.

Factors that could lead to a downgrade

- The project incurs major and sustained operational problems
- Internal liquidity declines materially
- Weighted average participant credit quality drops below A1
- Inability to recover costs under take-or-pay contracts or contracts are challenged

Key indicators

Exhibit 1

	2019	2020	2021	2022	2023
Total Sales (mWh)	196,620	244,710	236,320	238,620	199,750
Debt Outstanding ($'000)	78,530	70,105	61,270	51,975	42,220
Debt Ratio (%)	105.7	101.3	82.2	87.5	115.3
Adjusted Debt Ratio (%)	112.6	110.1	92.1	100.3	125.7
Total Days Cash on Hand (days)	912	776	821	753	735
Fixed Obligation Charge Coverage (if applicable)(x)	1.11	1.00	1.02	0.94	0.72

Note: Nine Canyon used excess unrestricted funds and excess debt service reserve funds to pay a portion of debt service for FY2022 and FY2023, respectively.
Source: Moody's, Issuer

Profile

The Nine Canyon project is a wind power project that totals 95.9 MW (63 wind turbines) and sells power under take-or-pay contracts to creditworthy public power entities in Washington State. The project was built in three phases (each a Phase) comprising of the 48.1 MW Phase 1, 15.6 MW Phase 2 and 32.2 MW Phase 3 with commercial operations occurring in 2002, 2003, and 2008, respectively. Phase 1 and 2 use Siemens 1.3 MW wind turbines while Phase 3 uses Siemens 2.3 MW turbines.

Detailed credit considerations

Revenue Generating Base

Strong Participants But PPA Contains Weak or Unclear Provisions Compared to a Typical JAA's Take-or-Pay Arrangement

The project benefits from take-or-pay PPAs with highly rated public power participants. Five of these participants with a weighted average credit quality of A1 are responsible for debt service since only the Phase 3 related bonds are outstanding (see Exhibit 2). Since Nine Canyon's Phase 1 and 2 related bonds have been fully repaid, the other five participants who participated only in Phase 1 or Phase 2 are no longer responsible for any debt service costs.

Exhibit 2

NIne Canyon Wind's Bond Participants

Purchaser	Rating	Debt Service, %
Grays Harbor County P.U.D. 1, WA	A1	37.52
Franklin County Public Uitlity Dist 1, WA	A1	25.00
Benton County Public Utility District 1, WA	Aa3	18.63
Lewis County Public Utility District 1, WA	Aa3	15.71
Mason County Public Util Dist 3, WA	Aa3	3.14

Source: Issuer, Moody's

For O&M, all of the project's original ten participants are obligated to pay their share of operating costs (see Exhibit 3).

Exhibit 3

NIne Canyon Wind's O&M Participants

Purchaser	Rating	Annual O&M Budget and Project Output, %
Grays Harbor County P.U.D. 1, WA	A1	20.89
Okanogan County Public Utility District 1, WA	A1	16.61
Grant County Public Utility District 2, WA	Aa3	12.54
Franklin County Public Uitlity Dist 1, WA	A1	10.49
Douglas County Public Utility District 1, WA	Aa2	10.23
Benton County Public Utility District 1, WA	Aa3	9.39
Chelan County Public Util. Dist 1, WA	Aa2	8.30
Lewis County Public Utility District 1, WA	Aa3	6.32
Mason County Public Util Dist 3, WA	Aa3	3.14
Cowlitz County Public Utility District 1, WA	A1	2.09

Source: Issuer, Moody's

Nine Canyon's PPAs contains many features found in a traditional take-or-pay arrangement whereby the participants have to pay for their respective share of debt service and operating costs, with a 25% step up feature for each phase in case of a participant default and generally does not contain specific project performance requirements.

The PPA also contains terms atypical in a JAA 'take or pay' arrangement, such as an annual payment limit and unclear termination provisions. The payment cap consists of the project's scheduled debt service, annual O&M cap of $7 million (2006) adjusted by an inflation index, and any credits or debits of any Renewable Energy Production Incentive (REPI) credits. We understand that the annual payment limit caps a participant's payment requirements for any given fiscal year, which could delay the step up requirement under the PPA until the next fiscal year. While the cost cap is a weakness relative to other take or pay projects, Moody's also recognizes that Nine Canyon's historical O&M costs have been below the cap that has risen over time. The Project's O&M costs have averaged around $7 million per year over the last two years, which we estimate is well below the inflation adjusted cap.

Furthermore, Moody's understands that if a specific phase has not been in operations for 12 months and is not capable of returning to operations without capital improvements that make it uneconomic, the off-takers (with 60% approval) could ultimately seek to terminate the nonperforming phase. In such a scenario, Energy Northwest would have to sell all of the applicable assets and use the proceeds to pay down debt and expenses for that specific phase with any remainder given to the applicable participants. In Moody's view, the off-take contractual terms are ambiguous as to whether the participants would be required to pay for any debt that remains outstanding for the applicable phase assuming the PPA is terminated. We understand that Energy Northwest and their legal counsel believe the participants will continue to be responsible for their respective share of any outstanding debt in the scenario described above. In Moody's view, the Project's strong liquidity and demonstrated operating performance serve as important mitigants that help address this contract uncertainty and the O&M cost cap.

Since all three phases are in commercial operation, the only other possible termination events are at stated maturity or for a participant default. Under a participant default, the PPA explicitly states that the defaulting participant remains obligated to pay for its share of the debt service even after PPA termination.

Financial Operations and Position

Long Operating History

The project has a long operating history with the earliest phase reaching commercial operations in 2002 and the last phase having reached commercial operations in 2008. For Phase 1 and 2, Nine Canyon experienced numerous gearbox and main bearing failures in the past that Siemens addressed under warranty, which expired in August 2012. A separate settlement was reached regarding the main bearings in 2010. The project continues to replace the older gearboxes when necessary and given the expiration of the warranty for Phase 1 and 2, Nine Canyon typically maintains spare gearboxes on site and performs gear oil sampling on a six-month basis. For Phase 3, Nine Canyon has an extended warranty that expires in August 2028 and covers major components although it excludes the cost of crane support.

Ultimately, the project's operating performance is a key credit consideration given the unclear termination provision and O&M cost cap. An inability to maintain a sound operational performance leading to costs that are high relative to the O&M cost cap would be credit negative. For energy production, the Nine Canyon project generated about 199.8 GWh of power in FY2023, which is well below the annual average of 234 GWh from FY2009 through FY2022, due to lower wind speeds.

Support for Renewable Energy But Expensive Power

Nine Canyon benefits from Washington State's clean energy mandate for electric utilities passed in May 2019 that requires all utilities provide its customers with 80% non-greenhouse gas emitting power by January 2030 and 100% by January 2045. This requirement is in addition to the renewable portfolio standard requirement that utilities source 15% of its power from renewable power. Moody's views Washington State's renewable portfolio requirement and non-GHG power supply requirements as important regulatory incentives for the participants to purchase Nine Canyon's power given the project's historically more expensive all-in costs. For FY2023, Nine Canyon's reported cost at approximately 7.51 cents/kWh and had 5-year average cost of 6.74 cents/kWh.

Low Debt Service Coverage

Nine Canyon's debt service coverage ratios (DSCRs) have averaged around 0.89 times and the DSCRs in both FY2022 and FY2023 were below 1.0x at 0.94x and 0.72x, respectively. The below 1.0x DSCRs reflects Nine Canyon's usage of unrestricted cash reserves in FY2022 and the usage of excess debt service reserves for FY2023. On the latter, the excess debt service reserve was due to debt service decreasing by more than 50% from around $12 million in FY2023 to around $5.4 million in FY2024. We understand Nine Canyon will slowly utilize more of its unrestricted cash reserves over time as it nears final bond maturity in 2030. That said, the participants remain fully obligated to pay their pro-rata share of debt service to the extent such excess reserves are unavailable.

Liquidity

The project's minimum liquidity consists of a cash funded debt service reserve sized according to the traditional three prong test, a minimum $750K operating reserve, and a reserve and contingency account. Nine Canyon also has a decommissioning trust that had $3.2 million at the end of FY2023. Including the operating and contingency reserves, the project's unrestricted liquidity totaled a robust 735 days cash on hand at FY2023. Nine Canyon's overall strong liquidity position materially reduces concerns regarding the PPA's contractual weaknesses including the O&M cost cap. That said, we understand Nine Canyon will continue to use excess reserves to pay a portion of debt service as it nears final bond maturity in 2030.

Debt and Other Liabilities

Legal security

Nine Canyon's bonds are secured by a pledge of the net revenues of the project's three Phases, whose revenue are derived from take-or-pay contracts. Nine Canyon can issue additional debt with 100% participant approval for each project phase and the inclusion of the new debt under the respective PPAs.

Debt structure
The project's debt consists of traditional fixed rate, amortizing debt with a final maturity in 2030. Debt totaled around $42 million at fiscal year end 2023 (June 30th).

Debt-related derivatives
None.

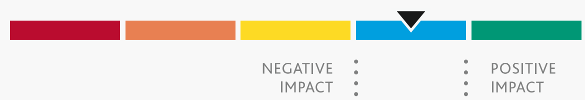
Pensions and OPEB
The project participates in Washington State's statewide, multiple employer Public Employees Retirement System (PERS) pension plan. Moody's calculates the district's adjusted net pension liability (ANPL) for FY2023 relating to its proportionate share of PERS to be around $2.8 million, compared to the issuer's reported proportionate share of the net pension liability of around $228K. Moody's adjusts the reported pension liabilities of entities that report under governmental accounting standards, to enhance comparability across rated issuers. Under governmental pension accounting, liabilities are discounted using an assumed rate of investment return on plan assets. Under our adjustments, we value liabilities using a market based discount rate for high quality taxable bonds, a proxy for the risk of pension benefits. Separately, Nine Canyon has a reported OPEB liability of $211K.

ESG considerations

Energy NW - Nine Canyon Wind Project's ESG credit impact score is CIS-2

Exhibit 4
ESG credit impact score

CIS-2



ESG considerations do not have a material impact on the current rating.

Source: Moody's Investors Service

Energy Northwest-Nine Canyon Wind Project (ENW Nine Canyon) **CIS-2** credit impact score reflects positive carbon transition exposure since the company's generation assets consist solely of carbon emissions free, wind power plants and Washington state has stringent decarbonization mandates for in-state electric utilities but also social and governance risks broadly in line with peers.

Exhibit 5
ESG issuer profile scores

ENVIRONMENTAL
E-1

SOCIAL
S-2

GOVERNANCE
G-2

Source: Moody's Investors Service

Environmental

ENW Nine Canyon's **E-1** issuer profile score (IPS) largely reflects positive carbon transition exposure since the company's generation assets consist solely of carbon emissions free, wind power plants and Washington state has stringent decarbonization mandates for in state electric utilities.

Social

ENW Nine Canyon's **S-2** issuer profile score (IPS) considers social risks that is broadly in line with peers and does not pose a particular risk.

Governance

ENW-Nine Canyon's (**G-2**) issuer profile score (IPS) considers governance risks that is broadly in line with peers and does not pose a particular risk.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.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

Moody's evaluates Nine Canyon under the US Municipal Joint Action Agencies methodology, and, as depicted below, the scorecard indicated outcome is A2, which is one notch lower versus the A1 assigned rating. The higher A1 assigned rating reflects the project's long demonstrated history of maintaining costs below the O&M cap, robust unrestricted liquidity, and declining debt service.

Exhibit 6

ENW Nine Canyon's Scorecard

Factor	Subfactor/Description	Score	Metric
1. Participant Credit Quality and Cost Recovery Framework	Participant credit quality. Cost recovery structure and governance	A1	
2. Asset Quality & Exposure to Environmental Regulation	Asset diversity, complexity, history, and exposure to environmental regulation	Baa	
3. Liquidity	Adjusted days liquidity on hand (3-year avg) (days)	Aaa	770
4. Leverage and Coverage	a) Adjusted debt ratio (3-year avg) (%)	Baa	105%
	b) Fixed obligation charge coverage ratio (3-year avg) (x)	Ba	0.9x
Notching Factors		**Notch**	
	1. Competitiveness	0	
	2 - Contractual Structure and Legal Environment	-1	
	3- Participant Diversity and Concentration	0	
	4 - Construction Risk	0	
	5 - Financing Structure	0	
	6 - Unmitigated Exposure to Wholesale Power Markets	0	
Scorecard Indicated Outcome:		**A2**	

Source: Moody's

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