FITCH RATES ENERGY NORTHWEST (WA) ELEC REV RFDG BONDS 'AA'; OUTLOOK STABLE

Fitch Ratings-Austin-22 July 2014: Fitch Ratings assigns 'AA' ratings to the following bonds issued by Energy Northwest (ENW), WA and secured by payments from the Bonneville Power Administration (Bonneville):

--Approximately $200 million Project 1 electric revenue refunding bonds, series 2014C;
--Approximately $72.4 million Project 3 electric revenue refunding bonds, series 2014C.

The bonds are scheduled to price on Aug. 4, 2014, via negotiation. Bond proceeds will repay a short-term note borrowing that was drawn to refund the 2014 maturities of Project 1 and Project 3 bonds. The refunding will extend the bond maturities to 2025-2028. The debt extension is part of Bonneville's debt portfolio management strategy, which will allow for the accelerated repayment of more expensive federal appropriation debt.

Fitch also affirms the following outstanding ratings on parity debt issued by ENW, Cowlitz Falls and the Port of Morrow, OR, and secured by payments from Bonneville:

--$715.9 million ENW Project 1 revenue bonds at 'AA';
--$3.3 billion ENW Columbia Generating Station revenue bonds at 'AA';
--$1.07 million ENW Project 3 revenue bonds at 'AA';
--$84.7 million Port of Morrow transmission facilities revenue bonds), series 2012 (taxable) at 'AA';
--$88.0 million Lewis County Public Utility District No. 1 Cowlitz Falls hydroelectric project revenue refunding bonds, series 2013 at 'AA'.

Fitch also affirms Bonneville's implied non-federal revenue obligations at 'AA'.

The Rating Outlook for all bonds is Stable.

SECURITY

The bonds are on parity with ENW's outstanding $5.1 billion in electric revenue bonds, as well as the outstanding Port of Morrow transmission revenue bonds and Lewis Public Utility District No. 1 Cowlitz Falls hydro bonds.

Bonneville's payments are made as an operating expense from the Bonneville Fund. These payments are paid prior to Bonneville's payments on borrowings from the U.S. Treasury ($3.9 billion) and federal appropriations debt ($4.3 billion).

KEY RATING DRIVERS

BONNEVILLE'S OBLIGATION SECURES BONDS: The ratings on the ENW, Cowlitz Falls, and Port of Morrow bonds reflect the credit quality of Bonneville and its absolute and unconditional obligation to make payments for debt service.

COMPETITIVE REGIONAL SUPPLIER: Bonneville provides wholesale electricity to a population of more than 12 million in the Pacific Northwest region through a competitive resource portfolio consisting primarily of low-cost hydropower. .

LOW-RISK POWER SALES CONTRACTS: Bonneville sells power through long-term, take-or-pay contracts through 2028 that recover cost of service from 125 preference customers. New contracts went into effect in fiscal 2012 that limit Bonneville's financial exposure to member load increases and lower-than-expected output from the federal system.

TWO-YEAR RATE SETTING: Bonneville sets rates based on a two-year rate cycle, with mid-period cost adjustments allowed if certain financial thresholds are triggered. Increases in Bonneville's tier 1 power rate (9%) and transmission rate (11%) in fiscal 2014 are expected to stabilize financial performance.

RELIANCE ON NET SECONDARY REVENUES: Bonneville's financial performance relies on net secondary revenues from wholesale market power sales. Lower than expected net secondary revenues have pressured financial margins and reserves in recent years.

DECLINING CASH RESERVES: Declining cash reserves remains a concern but is somewhat mitigated by interim rate-setting options available to Bonneville and a $750 million federal line of credit with the U.S. Treasury Department.

LIMITED CAPITAL ACCESS: Bonneville's access to capital is limited as it cannot issue debt on its own and has a $7.7 billion ceiling on borrowing from the U.S. Treasury. However, Fitch expects that access to alternative forms of financing will be sufficient to meet Bonneville's significant capital needs.

RATING SENSITIVITIES

FURTHER REVENUE AND RESERVE DECLINES: A continuing trend of net secondary revenues lower than expected and declining cash reserves could pressure the ratings.

CREDIT PROFILE

ENERGY NORTHWEST

ENW, formerly known as the Washington Public Power Supply System, was created in 1957. ENW has 27 members, consisting of 22 public utility districts and the cities of Centralia, Port Angeles, Richland, Seattle, and Tacoma, WA. ENW owns and operates the Columbia Generating Station (CGS), the Packwood Lake Hydroelectric Project, and the Nine Canyon Wind Project. ENW also has financial responsibility for Projects 1&3, nuclear projects that were terminated.

BONNEVILLE POWER ADMINISTRATION

Bonneville is the largest of the regional federal power marketing agencies within the Department of Energy. Bonneville was created by Congress in 1937 to market electric power from the Bonneville Dam in the Pacific Northwest region. Bonneville accounts for approximately 33% of the electricity consumed and 75% of the transmission infrastructure in the region.

Bonneville utilizes the energy from the Columbia Generating Station (CGS), a 1,157 MW nuclear plant, as part of its power supply portfolio (approximately 10% of total power supply). Remaining power supply is provided by 31 federally-owned hydroelectric plants. Bonneville is obligated to pay debt service on the ENW bonds related to CGS and Projects 1&3.

BONNEVILLE RATING NOT BASED ON DIRECT FEDERAL SUPPORT
Fitch's ratings on Bonneville's implied revenue obligations and the related ENW, Port Morrow, and Lewis County Public Utility District (PUD) No. 1 bonds reflect the credit quality of the administration as a self-supporting entity. Bonneville's subordinate obligations to the U.S. Treasury offer a layer of

structural support, in that Bonneville may defer payment to the Treasury, if necessary, which provides flexibility to the payment obligations ahead of Treasury. A linkage with the federal government exists in the form of governance by the DOE (including the DOE's current assumption of all hiring decisions at Bonneville), appointment of the administrator, congressional approval on Bonneville's budget, and the banking and lending relationship with Treasury, with all revenues and expenditures required to move through the Bonneville Fund held at Treasury.

RELIANCE ON NET SECONDARY REVENUES

Bonneville has faced financial pressure for the past five years resulting from low power-market prices for its secondary sales. Bonneville's net secondary sales result from the portion of the federal system that is excess to the load demand allocated under preference contracts. Cost-based rates for preference customers are established using extensive modeling of potential hydrological conditions but assume some level of net secondary revenues based on average water conditions and forecast market prices. These revenues have been lower than projected due to below-average water conditions and low market prices, requiring the use of cash reserves in fiscals 2009 - 2013 to replace lower revenues. Fitch views the use of average water conditions for financial planning as an optimistic assumption given below-average water conditions in nine of the past 10 years.

Rate setting in fiscal 2014 assumed reduced net secondary sales of approximately $300 million. Initial indications as of the end of the first quarter in fiscal 2014 were lower than this amount. As the water year has improved to slightly above average, second quarter estimates of net secondary revenues were in the range of the 2014 original forecast of $300 million. Performance that exceeds the forecast will have a direct positive impact on reserve levels.

FINANCIAL FLEXIBILITY REMAINS

Bonneville's cash reserves have declined in recent years. However, Bonneville's risk profile has also lessened over this time period with the new power contracts, flexibility to adjust rates through cost adjusters, and reduced reliance on net secondary revenues in its rate setting. Bonneville's reserves for risk, or unencumbered reserves, declined to $641 million at the end of fiscal 2013 with $182 million in the power business line and the remaining reserves allocated to transmission. This represents 96 days of operations but when the $750 million line of credit with the U.S. Treasury is included, the liquidity metric is more robust at 209 days.

Bonneville's forecast in its July 2013 rate case estimate was that reserves for risk could decline further to total $496 million by the end of fiscal 2015. However, there is a high degree of variability in this estimate and actual reserve performance will depend on hydrological flows in the region, timing of those flows and market prices. Fitch believes that the reduced reliance on net secondary revenues in rate setting should provide greater stability to Bonneville's reserves.

For more information, see the Fitch report, 'Energy Northwest, WA, and Bonneville Power Administration, OR' dated April 7, 2014, at www.fitchratings.com.

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In addition to the sources of information identified in Fitch's Revenue-Supported Rating Criteria and U.S. Public Power Rating Criteria, this action was informed by information from CreditScope.

Applicable Criteria and Related Research:
--'U.S. Public Power Rating Criteria' (March 18, 2014);
--'2014 Outlook: U.S. Public Power and Electric Cooperative Sector' (Dec. 12, 2013);
--'U.S. Public Power Peer Study' (June 12, 2014).

Applicable Criteria and Related Research:
U.S. Public Power Peer Study -- June 2014
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=749789
2014 Outlook: U.S. Public Power and Electric Cooperative Sector (Calm Under Pressure)
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=725447
U.S. Public Power Rating Criteria
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=740841