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Rating Action: Moody's assigns Aa2 to Energy Northwest, WA's Project 1, Columbia Generating Station, and Project 3 electric revenue refunding bonds; Outlook is positive

03 May 2022

Approximately $513 million of debt affected

New York, May 03, 2022 -- Moody's Investors Service has assigned a Aa2 rating to Energy Northwest, WA's $92.6 million Project 1 Electric Revenue Refunding Bonds, Series 2022-A, $400.9 million Columbia Generating Station (CGS) Electric Revenue and Refunding Bonds, Series 2022-A, $16.6 million Project 3 Electric Revenue Refunding Bonds, Series 2022-A, $0.5 million Project 1 Electric Revenue Refunding Bonds, Series 2022-B (Taxable) and $1.8 million Columbia Generating Station Electric Revenue Refunding Bonds, Series 2022-B (Taxable). The rating outlook for Energy Northwest Project 1, CGS, and Project 3 is positive.

RATINGS RATIONALE

The Aa2 rating assignment on Energy Northwest, WA's (ENW's) Project 1, CGS, and Project 3's revenue refunding bonds considers Bonneville Power Administration's (BPA) contractual obligation to pay including debt service under each project's net billing agreement, BPA's long history of meeting its contractual obligations, and BPA's Aa2 issuer rating.

The BPA's Aa2 rating considers its strongly positioned and expansive network of hydro and transmission assets, access to competitive power, long-term power supply contracts with customers through 2028 and credit supportive attributes as a line agency of the Government of the United States of America (Aaa stable). Borrowing ability under the US Treasury line and the ability to defer debt service payments to the US Treasury are two of the most critical support features from the US government. The credit profile also acknowledges credit challenges including hydrology and wholesale market price risk, a 'regulated utility' like ratemaking process, environmental burdens, and historically low consolidated financial metrics for the rating. Hydrology and wholesale market prices remain the greatest volatility drivers to BPA's financial performance.

On April 1, the rating for BPA, Project 1, CGS, and Project 3 were affirmed and their outlooks revised to positive from stable given the substantial increase to the borrowing line between BPA and the US Treasury to $17.7 billion ($5.63 billion outstanding as of FY21) after FY2027 (Sept 30) from $7.7 billion previously. Effectively, the $10 billion increase is allocated over time with the first $6 billion available through FY2027 and the full $10 billion thereafter. To a lesser extent, the positive outlook also acknowledges BPA's improved financial performance over the last two years with rising reserves for risk. Since reaching a low of $484 million in FY2019, BPA's reserves for risk have improved to $825 million as of FY2021. Given robust wholesale power prices relative to prices assumed in BPA's rate case and near average hydro conditions, BPA expects strong financial performance in FY2022 with reserves for risk increasing to $1.1 billion according to its Q1 2022 quarterly report, which would be at its highest level in the last 13 years.

By the end of FY2022, BPA is required to submit an updated financial plan under the law that authorized the borrowing line increase and we will assess how the increased borrowing authority will affect BPA's strategic goals, capital spending plans, and financial policies. Since 2018, BPA has implemented policies that sought to improve or stabilize BPA's standalone credit strength. Such policies and goals include but are not limited to the establishment of a financial reserve policy, a long-term goal to reduce BPA's debt to asset ratio to around the 60% to 70% range, and partial rate funding of capital expenditures. We see these goals and policies as an important foundation to the turnaround of BPA's financial performance since 2019 and a material weakening of these credit support features could offset the benefits of the borrowing line increase.

RATING OUTLOOK

BPA's positive outlook considers BPA's increased borrowing authority under the US treasury and expectations for better than expected financial performance in FY2022. The outlook on Project 1, CGS, and Project 3 reflects the positive outlook on BPA.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- BPA's rating is likely to be upgraded if BPA maintains or expands its credit supportive goals and policies under its new financial plan, while having access to the larger borrowing line.

- The rating on BPA supported bonds could be upgraded if BPA is upgraded.

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Given the positive outlook, a downgrade is not likely. However, BPA's outlook could be revised to stable if BPA materially diminishes its credit supportive policies and goals.

- The outlook associated with BPA's supported bonds could be revised to stable if BPA's outlook is revised to stable. The ratings on BPA supported bonds could be downgraded if BPA is downgraded or if the underlying contractual arrangement is violated.

LEGAL SECURITY

Project 1, CGS, and Project 3 revenue bonds are secured by a pledge of specific project revenues primarily sourced under tri-party net billing agreements with BPA and project participants. The net billing agreement obligates the project participants, consisting of numerous municipal and cooperative electric utilities, to pay ENW their proportionate share of the project's annual costs, including debt service, irrespective of whether the project is operable or terminated. BPA, in turn, is obligated to pay (or credit) the participants identical amounts by reducing the amounts the participants owe for power and service purchased from BPA under their power-sales agreements. BPA has also agreed, in the event of any insufficient payment by a participant, to pay the amount due in cash directly to the project. In 2006, ENW and BPA adopted a voluntary, direct pay agreement whereby BPA directly pays ENW for amounts due under the net billing agreements. There are no debt service reserves.

USE OF PROCEEDS

Proceeds from Project 1 and Project 3 revenue bonds will be used to refund bonds to extend maturities, refinance a short term note, and pay a portion of interest due. CGS will use approximately $339 million to extend debt maturities and pay interest with the remainder of its net proceeds used for capital spending. The debt maturity extensions are according to BPA's Regional Cooperation Debt 2 program.

PROFILE

BPA was created in 1937 by an act of the US Congress and is one of four regional power marketing agencies within the US Department of Energy. BPA is primarily responsible for 22 GW of federally owned hydro generation and 15,000 miles of electric transmission assets in the US Pacific Northwest spanning all or parts of eight states. The US Army Corps of Engineers and the Bureau of Reclamation own and operate the hydro projects. BPA's obligations are not backed by the full faith and credit of the US government and its cash payments are limited to funds available in the Bonneville Fund.

METHODOLOGY

The principal methodology used in these ratings was US Public Power Electric Utilities with Generation Ownership Exposure Methodology published in August 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1170209 . An additional methodology used in these ratings was US Municipal Joint Action Agencies Methodology published in August 2020 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1207102 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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