MOODY'S
INVESTORS SERVICE

# Rating Action: Moody's assigns Aa1 to Energy Northwest (WA) Columbia Generating Station and Project 3 Revenue Bonds. Outlook stable

**01 May 2018**

**Approximately $637 million of debt affected**

New York, May 01, 2018 -- Moody's Investors Service assigned a Aa1 rating to Energy Northwest's (ENW) (WA) $231 million of Columbia Generating Station (CGS) Electric Revenue Refunding Bonds, Series 2018-C, $3 million of Columbia Generating Station (CGS) Electric Revenue Refunding Bonds, Series 2018-D (Taxable), $401 million of Project 3 (Project 3) Electric Revenue Refunding Bonds, Series 2018-C, and $2.8 million of Project 3 Electric Revenue Refunding Bonds, Series 2018-D (Taxable). These bonds are supported by net billing agreements with Bonneville Power Administration (BPA, Aa1 stable) and thus are rated the same as BPA's other supported obligations. The rating outlook is stable.

RATINGS RATIONALE

The Aa1 rating on ENW's CGS and Project 3 revenue bonds reflects BPA's contractual obligation to pay obligations due under each project's net billing agreements, including debt service, BPA's long history of meeting its contractual obligations, and BPA's Aa1 issuer rating.

BPA's Aa1 issuer rating reflects its credit strengths comprising of US Government (Aaa stable) support features, strong underlying hydro and transmission assets, very competitive power costs, and long-term power supply contracts with customers through 2028. Explicit US Government support features include borrowing authority with the US Treasury ($2.69 billion available as of September 30, 2017) and the legal ability to defer its annual US Treasury debt repayment if necessary. BPA's importance to the US Northwest region and its role as a US government agency represent drivers of implicit support. The US federal government's strong explicit and implicit support features are key credit strengths that support the Aa1 rating even though BPA demonstrates financial metrics that are weak for the rating.

BPA's rating acknowledges long-term credit challenges such as hydrology and wholesale market price risk, a 'regulated utility' like ratemaking process, environmental burdens, and consolidated financial metrics that range in the 'Ba' to 'A' category per Moody's U.S. Public Power Electric Utilities with Generation Ownership Exposure methodology. Hydrology and wholesale market prices are the greatest volatility drivers of BPA's financial performance and have been the main driver of BPA's declining internal liquidity over the last ten years. These factors are likely to persist owing to the volatility associated with hydro resources along with the weak wholesale power market that exists in the Pacific Northwest. Additionally, BPA's accelerated repayment of federal appropriations debt and declining availability under the US Treasury line are factors that could suggest a weakening of the US government's explicit support features over time.

Moody's believes that a combination of policies that have favored customers, such as BPA's regional cooperation debt program, and challenging wholesale power market have led to an erosion of financial strength that weakens BPA's position in its rating. Recently, BPA published a new strategic plan that provides some credit positive objectives like reducing the debt ratio to a 75% to 85% range and maintaining $1.5 billion of US treasury line availability. However, the announced strategic goals could be insufficient to offset BPA's credit deterioration, particularly if the new strategic goals do not translate into robust actions to improve credit quality. Steady and material progress in reversing the trend of weakening financial strength, improving internal reserves for risk, and ensuring strong U.S. Government support elements will be critical considerations in BPA's ability to sustain its credit profile. Ultimately, the extent of any credit benefits of BPA's new strategic goals should become evident by the end of this year when BPA files its initial proposal for the FY2020-2021 rate case.

RATING OUTLOOK

The stable outlook on the CGS and Project 3 revenue bonds reflects BPA's stable outlook. BPA's stable outlook considers BPA's FY 2018-19 final rates and BPA's plan to maintain sufficient availability under the US Treasury line and internal liquidity through FY 2018.

## FACTORS THAT COULD LEAD TO AN UPGRADE

Ratings on the net billed bonds could be upgraded if BPA is upgraded.

BPA's rating could improve over the long term if BPA is able to substantially mitigate hydrology and wholesale price risk and if BPA implements policies to ensure strong internal reserves for risk resulting in at least 250 days cash on hand on a sustainable basis.

## FACTORS THAT COULD LEAD TO A DOWNGRADE

Ratings on the net billed bonds could be downgraded if BPA is downgraded or if the underlying net billing agreements are violated.

BPA's ratings could be lowered if the US government's credit rating is downgraded, if we expect internal liquidity to fall below 60 days or availability under the US Treasury line declines below $1.5 billion on a sustained basis, or BPA experiences regulatory delays in receiving full recovery of costs. Other factors that could lead to a downgrade include any sign of waning federal government support or decline in the proportion of subordinated, deferrable debt owed to the US Treasury beyond actions currently planned.

## LEGAL SECURITY

CGS and Project 3 bonds are separately secured by a pledge of specific project revenues primarily sourced under tri-party net billing agreements with BPA and project participants.  There are no debt service reserves. The net billing agreements obligate 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 2007, ENW and BPA adopted a new direct pay agreement whereby ENW participants directly pay all costs to BPA rather than through ENW. BPA has made a clear and tested commitment to pay under the net billing agreements through more than more than 30 years of stressful circumstances including legal challenges in the early 1980s.

## USE OF PROCEEDS

Bond proceeds will be used to extend CGS and Project 3 debt service as part of BPA's Regional Cooperation Debt 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 federally owned generation and electric transmission assets in the Pacific Northwest spanning all or parts of eight states. The Army Corps of Engineers and the Bureau of Reclamation own and operate the hydro projects. Many of the statutory authorities of BPA are vested with the Secretary of Energy, who appoints and acts through the BPA administrator. 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 published in November 2017. The additional methodology used in these ratings was US Municipal Joint Action Agencies published in October 2016. Please see the Rating Methodologies page on www.moodys.com for a copy of these methodologies.

## REGULATORY DISCLOSURES

For ratings issued on a program, series or category/class of debt, this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series or category/class of debt or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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