MOODY'S RATINGS

CREDIT OPINION
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Grant County Public Utility District 2, WA

Update to credit analysis following revision of outlook to positive

Summary

Grant PUD's credit profile (Aa3 positive) reflects the district's solid revenue base that includes a mix of retail sales to customers within Grant County, as well as wholesale revenue, including under take-or-pay contracts. Although Grant PUD has fairly meaningful exposure to customer concentration, much of this risk is mitigated by its extremely low cost of power from its ownership of Wanapum hydroelectric plant and the Priest Rapids Plant. The district's approach to risk management, including exposure to hydrology risk and wholesale markets, appears well considered and includes exchange contracts with multiple counterparties through 2026, though longer-term exposure to wholesale power pricing and hydrology risks remain.

The district's credit profile is also supported by historically strong financial metrics that received a boost from a substantial increase of wholesale revenue in 2023. Debt service coverage (DSCR) has increased steadily over the past decade, increasing from 1.34x in 2014 to 2.77x in 2022; in 2023, DSCR jumped to 5.5x after operating revenue increased by more than 50% from $99 million to just under $311 million. Additionally, days cash on hand (DCOH) more than doubled to 619 from 290, with the latter reflecting a relative low point as the district had been spending down cash for capital improvements. The district's five-year capital improvement plan is substantial at more than $1 billion, and could create credit challenges.

On May 21, Moody's affirmed the district's Aa3 rating and assigned a positive outlook.

Credit strengths

» Ownership of low cost, hydroelectric generation plants

» Extensive hedging that limits near-term exposure to hydrological conditions

» Highly competitive retail rates

» Strong debt service coverage and healthy liquidity

Credit challenges

» Below average wealth in service area

» Industrial load concentration

» Long term hydrology and wholesale market risk

» Significant capital spending

Rating outlook

The rating outlook for the district is positive. Financial metrics are expected to remain strong even as the district faces a substantial capital program, though DSCR will likely revert to levels more in-line with the pre-2023 trends, while DCOH will remain solid if somewhat weaker than the highs reached in 2023. The district's extremely competitive rates create a substantial buffer for the district should retail load falter, or room to generate additional revenue to cash fund its capital program.

Factors that could lead to an upgrade

» Consolidated DSCR in excess of 3.0x or liquidity significantly improves on a sustained basis supported by stronger financial policies

» Substantial improvement to service area economic strength

Factors that could lead to a downgrade

» Consolidated DSCR materially drops below 2.0x or unrestricted liquidity materially drops below 250 DCOH on a sustained basis

» Major load loss on a sustained basis

» Weakening of risk management or financial policies

» Significant operating problems at PRP

» Large cost overruns on capital program

Key indicators

Exhibit 1

	2019	2020	2021	2022	2023
Debt Outstanding ($'000)	1,269,395	1,200,725	1,171,430	1,142,316	1,104,542
Total Days Cash on Hand (days)	609	468	324	290	619
Debt Ratio (%)	43.0	41.2	38.3	36.6	30.9
Adjusted Debt Ratio (%)	55.5	54.6	48.3	42.7	35.1
Debt Service Coverage Ratio by Net Revenues (x) (post PILOTs)	2.02	2.15	2.32	2.77	5.50

Source: Moody's Ratings, Audited Financial Statements

Profile

Grant PUD operates a utility system that owns approximately 2.2 GW of hydro power plants located on the Columbia River and primarily generates and delivers electricity to all of Grant County, which is located in central Washington State. The district also provides wholesale fiber-optic services. In 2023, the electric system had more than 55,000 active meters.

Detailed credit considerations

Revenue Generating Base: Ultra-low cost hydroelectric power serves retail and wholesale markets

The district derives much of its credit strength from its ultra-low cost hydroelectric generation facilities. Grant PUD benefits from its ownership of around 2.2 GW of nameplate hydro generation capacity from the 1,222 MW Wanapum hydroelectric plant (Wanapum) and the 950 MW Priest Rapids Plant (together with Wanapum, PRP). PRP's all-in-costs including debt service attributable to PRP are highly competitive at around $19.44/MWh in 2022 and substantially below market prices. Grant PUD's Electric System retains 63.3% of PRP's output and the remaining output is sold to the PPA Purchasers. The district has the ability to effectively benefit from up to 93.3% of PRP's generating capacity through physical and financial settlements to meet the Electric System's load requirements and pay its proportion share of the cost of production. The district also has rights to the output of two very small hydro generation projects in Grant County, a portion of the output from the Nine-Canyon Wind Farm until 2030, and a small contract with Bonneville Power Administration for a small Grand Coulee area load until 2028.

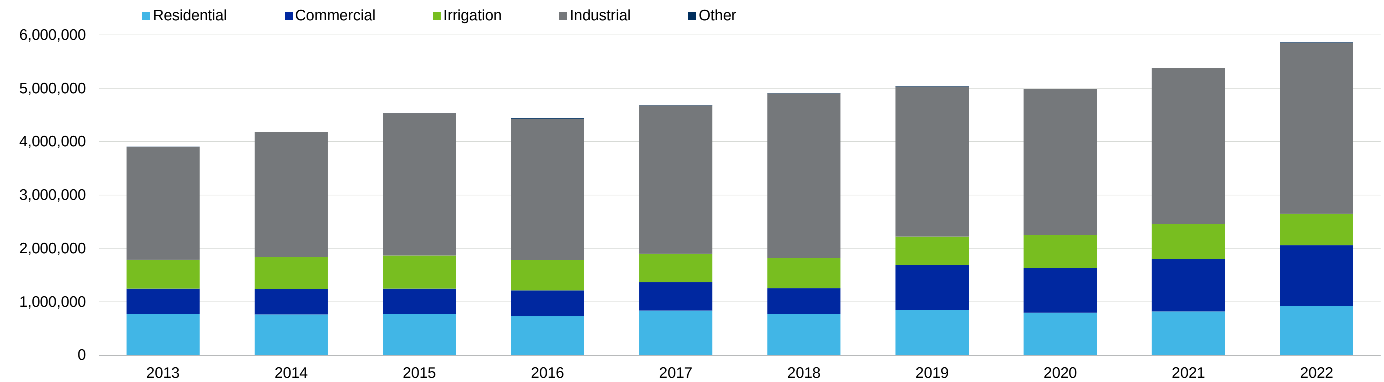
A weakness to the district's reliance on hydro is the concentration in two large plants. This risk was highlighted in February 2014, when the district discovered a fracture at the Wanapum dam that resulted in reduced power generation and repair work. Wanapum reached normal operations in March 2015 and the direct and indirect cost of the fracture totaled approximately $78 million before insurance.

Towards the mid to late 2020's, the district's long power position could change and lead to the need for new long term power supplies depending primarily on the growth of industrial and large commercial customers. According to the district's integrated resource plan, Grant PUD is considering contracts with renewables and gas fired power providers to meet its growing load requirements. The district has also entered into a memorandum of understanding with NuScale Power to study small modular nuclear reactor technology.

Retail electric sales typically represent Grant PUD's largest revenue stream, though unusually high wholesale prices in 2023 resulted in wholesale revenue outpacing retail revenue for the year. In 2022, retail energy sales were 65% of operating revenue while net wholesale revenue was 24%, which was roughly in-line with recent historical trends; in 2023, retail energy sales revenue increased by 1.4%, but fell to just 43% of operating revenue, while net wholesale revenue jumped to 50%. Given the auction price for PRP slice covering 2024 and the estimated unmet district load (EUDL) used by the electric system, 2024 is expected to be another strong wholesale year, though the district's five-year forecast includes a reversion to more typical historical patterns.

Residential retail accounts are 79% of total accounts, followed by commercial/industrial at 14%, with irrigation and other customers representing the remainder. Although residential customers are the dominant customer type by account numbers, they contribute just 19% of retail revenue, while commercial and industrial customers contribute 70% and irrigation and other customers at about 11%. With a predominantly rural service territory, median income levels in Grant County, WA (unrated) are below both the state and national levels, with higher than average poverty levels and unemployment rates. However, given the relatively smaller contribution to revenue from residential retail and with the growth of data centers and manufacturing, weaker socioeconomic measures are a less meaningful risk than in more typical public power utilities. Since 2013, industrial and commercial customers have been the largest contributors to retail sales growth (exhibit 1); power intensive businesses like data centers are attracted to the region owing to the district's low retail rates that are around 50% below the state average.

Exhibit 2
Industrial and large commercial customers have driven retail sales growth
Retail sales (MWh)



Source: Moody's Ratings, Grant County PUD 2

A notable credit risk is the concentration of the district's top customers. In 2022, the district's top ten industrial/commercial customers used 48.5% of total retail energy sold and contributed 46.4% of retail revenue. These large customers primarily consist of manufacturing, data centers and food processing, with varying degrees of credit quality. Grant PUD's high customer concentration exposes the district to sudden load declines if a customer leaves or shuts down although this is partially mitigated by the district's low cost power, ability to sell into the wholesale market, and relatively strong liquidity. Additionally, the district takes active measures to mitigate its exposure by requiring large new customers (like data centers) to pay all up-front capital costs incurred by the district to serve their loads. Looking forward, Grant PUD forecasts continued strong growth in industrial and large commercial customers, with electric system load growth expected to grow by 5.9% annually over the next five years and 4% over the next decade.

As noted above, net wholesale power revenue on a consolidated basis was unusually high in 2023. The district manages some of the downside risk of its exposure to Columbia River hydrology and market pricing through a combination of slice and pooling agreements that shifts hydrology and wholesale price risk to its counterparties. The electric system currently has a power sale agreement with Avangrid Renewables, Inc. for a 10% slice of PRP through December 31, 2024, and a 20% slice of PRP with Portland General Electric through December 31, 2026, shifting the associated water and wholesale price risks for that portion of PRP output. Under the current pooling agreement (through September 29, 2025), the counterparty (Morgan Stanley Capital Group) receives rights to the actual output of 33.3% of the PRP, which will vary with water conditions. In return, the counterparty provides firm power to meet Grant PUD's load, regardless of the actual output of PRP, and certain scheduling services. The district continues to largely retain operating risk. These agreements, up to five years in length, have been renewed or replaced over time, a pattern that is expected to continue into the future.

Additionally, Grant PUD sells up to 30% of PRP's original nameplate output (Reasonable Portion Contract) to a collection of seventeen load serving utilities and public power entities (PPA Purchasers) under cost based, take-or-pay power purchase agreements (PPAs) maturing in April 1, 2052, though the district has the first right to use the proceeds of the sale of this power to satisfy load unmet by the district's 70% share of PRP (Estimated Unmet District Load, EUDL). Pricing and revenue generated under the Reasonable Portion Contract is determined by auction, which rose substantially for 2023 and 2024, with revenue from the Reasonable Portion sales used to purchase power on the market to meet the EUDL. As the district's retail load has grown, the PPA Purchasers' effective share of PRP have declined given the EUDL feature under the contracts. The district is expecting the cost of unmet load requirements may exceed funds generated by the EUDL mechanism as soon as 2025.

Finally, about 6.7% of output from PRP contractually goes to long-term purchasers, including 2.5% to exchangers and 4.2% to conversion contracts.

Financial Operations and Position: Unusually strong 2023 better positions the district for large capital program

The district's financial position is strong given an unusually robust performance in 2023, when operating revenue increased by nearly 52%, driven by a substantial growth in wholesale revenue. Audited financials for 2023 show consolidated debt service coverage of

5.5x, up from 2.77x in 2022. The district also benefitted from a 3% increase in retail rates in 2023, with another 3% increase already adopted for 2024. Strong wholesale power pricing in 2024 should also result in a financial boost for the district, though the district's 2024 budget as well as five-year operating budget includes more conservative revenue projections. Those projections include a 2.5% revenue increase in 2024 and 2% annual increases thereafter, a more conservative view than the 6.9% compound annual growth rate in revenue from 2018-2022. On a Moody's adjusted basis, DSCR has grown steadily over the past decade, even when excluding the unusual 2023 results; in 2014, coverage was just 1.34x, exceeding 2.0x in 2019. The district's budget forecast shows consolidated DSCR declining to 2.18x by 2029 as net wholesale revenue shifts to retail energy sales and operating expenses grow. Moody's expects the district to maintain coverage above its 1.80x target and will likely maintain coverage of at least 2.0x going forward on a consolidated basis.

LIQUIDITY

An important historical mitigant to Grant PUD's exposure to key risks like industrial load concentration and wholesale market risk has been its strong liquidity. The district's strong liquidity served to cushion Grant PUD during the 2008 recession and the Wanapum dam fracture event in 2014. At year end 2023, the district had a Moody's adjusted liquidity of $357.7 million (619 days cash on hand, DCOH), a massive increase of $198.1 million from 2022, reflective of strong wholesale performance. Prior to 2023, however, liquidity on both a nominal basis and as measured by DCOH had been falling for a number of years beginning in 2017 as the district began using its internal liquidity to fund a portion of capital spending.

Grant PUD's current five-year CIP is over $1 billion, including $173 million in 2024 and $254 million in 2025. Grant PUD has multiple ongoing capital projects at the electric system including fiber build-out, electrical system upgrades, transformer purchases, power cable purchases, and substation and distribution line construction projects. Improvements at the PRP system include restoration or replacement of generators, turbine upgrades, unit controls, the station service and substation circuit breakers, bearings, and coating systems for spillway gates. Capital spending with ongoing dam safety initiatives also include Priest Rapids Dam’s right embankment upgrade, assessment of Wanapum Dam’s left embankment, and seismic evaluation of concrete structures at both dams.

The district's five-year budget and capital improvement plan (CIP) shows internal liquidity being the primary source of funding for its CIP, which will begin to weaken its DCOH as operating expenses grow. However, assuming no expansion or acceleration of the CIP, the strong performance in 2023 should continue to provide a boost to DCOH in out years relative to budget.

Debt and Other Liabilities

DEBT STRUCTURE

Debt levels are low, reflective of the district's strategy to use cash to fund capital. Most of the district's $1.1 billion of debt (end of year 2023) consists of traditional fixed rate, amortizing bonds (including those with sinking funds) as the district refunded its outstanding variable rate debt in 2023. The district has $47 million in outstanding mandatory put bonds which it intends to refund in 2025. Outstanding electric system bonds mature in full in 2047 while the PRP bonds mature in 2044. PRP subordinate lien bonds were purchased by the electric system as an investment; those bonds mature in 2053.

LEGAL SECURITY

Electric System's bonds have a pledge of net electric system revenues and a rate covenant of 1.25x DSCR for senior debt and 1.10x for junior lien debt. Draws and deposits from the R&C fund can be used to smooth the DSCR rate covenant. The additional bonds test is 1.25x DSCR. There is no debt service reserve on the outstanding electric system bonds.

PRP bondholders benefit from a pledge of net revenues of the combined Wanapum and Priest Rapids hydro projects and a 1.15x rate covenant. The Electric System has also covenanted to pay for all of PRP's costs including debt service whether or not PRP produced or is capable of producing power and energy. The Electric System's payment obligation to PRP is senior to the Electric System's debt service if PRP produces power and on parity if PRP no longer produces power. The PRP bonds do not have a debt service reserve. Separately, PRP must also maintain a minimum $12 million in the Renewal, Replacement, and Contingency fund.

DEBT-RELATED DERIVATIVES

The district does not have debt-related derivative exposure.

PENSIONS AND OPEB

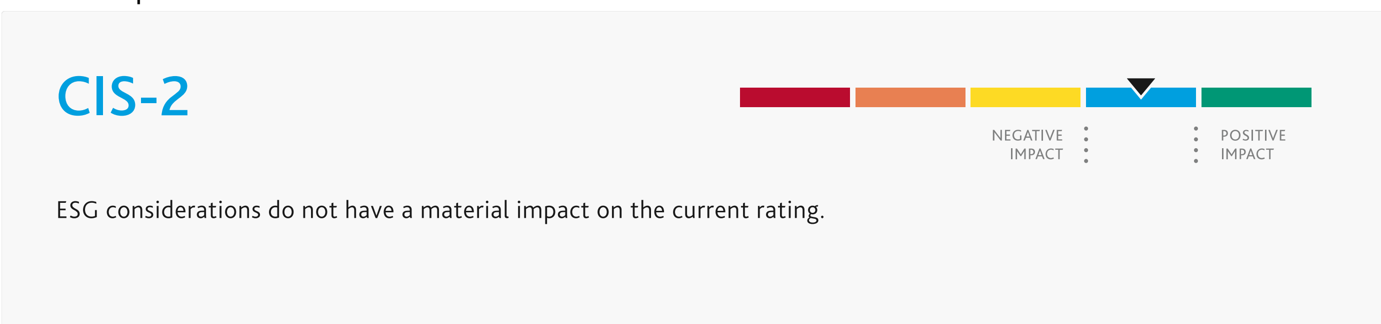
Pensions and OPEB are not a material driver of the district's credit profile. The district participates in Washington State's statewide, multiple employer Public Employees Retirement System (PERS) pension plan. Moody's calculates the district's adjusted net pension liability (ANPL) for 2023 relating to its proportionate share of PERS to be around $118.8 million, compared to the utility's reported proportionate share of the net pension asset of around $14.7 million for the electric and generation systems. Moody's adjusts the reported pension liabilities of entities that report under governmental accounting standards, to enhance comparability across all 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. The district also reported OPEB liability of $9.6 million as of year end 2023.

ESG considerations

Grant County Public Utility District 2, WA's ESG credit impact score is CIS-2

Exhibit 3

ESG credit impact score



Source: Moody's Ratings

Grant County Public Utility District 2, WA Electric Enterprise's (Grant PUD) ESG Credit Impact Score is neutral-to-low (**CIS-2**). Its ESG attributes are considered to have a neutral-to-low impact on the current rating. Grant PUD's **CIS-2** reflects moderate environmental risks, neutral-to-low social risks, and neutral-to-low exposure to governance risks.

Exhibit 4

ESG issuer profile scores

Source: Moody's Ratings

Environmental

E-3. The district has exposure to physical climate risks mostly in the form of volatile weather patterns and the inherent risks in operating around 2.2 GW of hydroelectric power plants whose power output is subject to regional hydrology conditions. Concurrently, the district benefits from its ownership of carbon-free power resources.

Social

S-2. Grant PUD has limited exposure to social risks given the carbon-free nature of its hydroelectric facilities and very low cost power.

Governance

G-2. As an independent utility district with a monopoly on its service territory with no direct state or federal restrictions on its rate setting, governance risks for the district are limited. The district's governing body is comprised of a five-member board of commissioners. Two commissioners-at-large each serve four-year terms and the remaining three commissioners serve six-year terms. The terms are staggered so that two members of the board are elected every two years.

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 Grant PUD under the US Public Power Electric Utilities with Generation Ownership Exposure methodology, and, as depicted below, the grid indicated outcome is Aa3, which is the same as the Aa3 assigned rating. The -0.5 notch reflects the absence of debt service reserves on the district's debt.

The grid is a reference tool that can be used to approximate credit profiles in the public power sector in most cases. However, the grid is a summary that does not include every rating consideration. Please see the methodology on US Public Power Electric Utilities with Generation Ownership Exposure published in January 2023 for more information about the limitations inherent to grids.

Exhibit 5

US Public Power Electric Utilities with Generation Ownership Exposure Methodology Scorecard

Grant County Public Utility District 2, WA

Factor	Subfactor	Score	Metric
1. Cost Recovery Framework Within Service Territory		A	
2. Wllingness and Ability to Recover Costs with Sound Financial Metrics		Aa	
3. Generation and Power Procurement Risk Exposure		A	
4. Competitiveness	Rate Competitiveness	Aaa	
5. Financial Strength and Liquidity	a) Adjusted days liquidity on hand (3-year avg) (days)	Aaa	411
	b) Adjusted Debt ratio (3-year avg) (%)	Aa	42.1%
	c) Adjusted Debt Service Coverage or Fixed Obligation Charge Coverage (3-year avg) (x)	Aa	3.53
Preliminary Grid Indicated rating from Grid factors 1-5		Aa2	
		Notch	
6. Operational Considerations		0.0	
7. Debt Structure and Reserves		-0.5	
8. Revenue Stability and Diversity		0.0	
Grid Indicated Rating:		Aa3	

Source: Moody's Ratings

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