S&P Global Ratings

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Summary:

Grant County Public Utility District No. 2, Washington; Wholesale Electric

Primary Credit Analyst:
Paul J Dyson, San Francisco (1) 415-371-5079; paul.dyson@spglobal.com

Secondary Contact:
Doug Snider, Centennial + 1 (303) 721 4709; doug.snider@spglobal.com

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Credit Profile		
US$220.06 mil priest rapids hydroelec proj rev rfdg bnds taxable ser 2020Z-2 due 01/01/2044		
Long Term Rating	AA/Stable	New

Rationale

S&P Global Ratings assigned its 'AA' long-term rating to Grant County Public Utility District No. 2 (Grant PUD), Wash.'s proposed $220 million series 2020Z-2 (taxable) Priest Rapids Hydroelectric Project revenue refunding bonds. The outlook is stable.

The bonds are being issued to refund various debt outstanding of the PRP.

The ratings reflect our view of the PRP's:

- Unconditional power sales contracts between project owner Grant County PUD and multiple power purchasers for 100% of combined project output;
- Very low production costs at the consolidated PRP of $18.13 per megawatt-hour (MWh) in 2018, although estimated to increase to about $24.60 per MWh in 2019 as a result of below-average hydro run-off, but with the district anticipating an average of a very low $20 per MWh in fiscal years 2020 through 2023;
- Continued successful replacement of fish-friendly turbines and other measures that have resulted in reduced spill, enhanced project economics, and compliance with environmental regulations, with additional improvements ongoing;
- Generally solid operating performance, including a plant availability factor of 86% in 2018; and
- Continued adequate financial performance, with power purchasers, including the district, paying their share of project costs plus 15%, such that debt service coverage (DSC) is consistently about 1.15x.

Partly offsetting the above strengths, in our view, are Grant PUD's:

- High capital requirements associated mostly with turbine and generator restoration and powerhouse improvements, but also with regulatory compliance and license implementation, which could put pressure on the long-term competitiveness of the project's production costs, although management expects per unit costs to remain well below Bonneville's firm priority rate over the next five years; and
- High project debt burden, with debt to capitalization of 80%, although management anticipates a reduction in borrowing costs given that it will fund a sizable portion of the five-year PRP capital improvement plan of $412 million with equity contributions directly from the electric system.

The business profile score is '3' on a 10-point scale, with '1' being the strongest. The business profile reflects our view of the PRP's extremely competitive cost of power, moderate operating risks, good economics of service territories, and strong management practices and policies.

The series 2020Z-2 bonds and bonds previously issued in 2010 or later are secured by a lien on the net revenue of the consolidated PRP project. Bond provisions include a 1.15x rate covenant on both parity and junior-lien debt, a 1.15x additional bonds test, and a debt service reserve fund capitalized at maximum annual interest. Parity bonds issued prior to 2010 for each of the two hydro developments are also payable from net revenue of the combined PRP, pursuant to the resolution and prior resolutions. In 2010, the district consolidated the two developments into one system, PRP. This consolidation had been planned since the late 1990s and simplifies administration and financing, provides cost savings, and signifies that power purchasers consider the combined developments a single project. In addition, the Federal Energy Regulatory Commission provided a single license that covers both projects.

For more information on the district and the PRP, see our report published Dec. 31, 2019 on RatingsDirect.

Outlook

The stable outlook reflects our anticipation that long-term contracts through 2052 will continue to provide a stable revenue stream. Strong project economics provide credit stability and override credit risks regarding regulation, environmental mandates, and member credit quality. We anticipate that the project will remain competitive with other generators or resource options in the region despite the high capital investment required to comply with fish species protection requirements and other improvements.

Upside scenario

Given high project debt and capital needs as well as management's projection of rising per unit power costs, we do not anticipate raising the ratings during the next two years. Also limiting rating upside is our expectation that DSC is unlikely to materially improve.

Downside scenario

We do not anticipate lowering the ratings over the next two years given the competitive cost of power, but could do so in the unlikely event that costs become no longer competitive on a sustained basis, or if other operating risks arise.