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Summary:

Grays Harbor County Public Utility District No. 1, Washington; Retail Electric

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Table Of Contents

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Credit Profile		
US$49.215 mil elec rev and rfdg bnds ser 2015A due 01/01/2045		
Long Term Rating	A/Stable	New
US$15.075 mil elec rev and rfdg bnds ser 2015B due 01/01/2023		
Long Term Rating	A/Stable	New
Grays Harbor Cnty Pub Util Dist #1 elec		
Unenhanced Rating	A(SPUR)/Stable	Affirmed

Rationale

Standard & Poor's Ratings Services assigned its 'A' long-term rating to Grays Harbor County Public Utility District (PUD) No. 1, Wash.'s series 2015A and 2015B (taxable) electric revenue and refunding bonds. In addition, we affirmed our 'A' long-term rating and underlying rating (SPUR) on the district's previously issued electric revenue bonds.

The rating reflects our view of the district's:

- Rate-setting autonomy and historically demonstrated willingness to implement rate increases, including an 8% increase that went into effect on Jan. 1, 2013, two rate increases combining for a 5.25% rate increase in 2014, and additional 3% annual rate increases expected for July 1, 2015 through 2018 to fund capital needs and higher power costs from Bonneville;
- Low cost, non-carbon power supply, most of which relates to the district's contract with Bonneville for the Slice and Block products through Sept. 30, 2028, with a growing portion of supply from renewable energy resources that currently meet state renewable portfolio standard (RPS) requirements;
- Stable and diverse customer base;
- Good overall debt service coverage (DSC) of 1.63x in audited fiscal 2013 (up from 1.36x in fiscal 2012) and an estimated 1.77x in fiscal 2014, along with good liquidity;
- Projected improvement in DSC to a range of 1.8x to 2.1x during fiscal years 2015 to 2018, with fixed-charge coverage ranging from 1.2x to 1.3x.

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

- Moderate hydro exposure because of its participation in Bonneville's Slice product, which allows the district to pay a percentage of Bonneville's costs in return for a percentage of the annual output, although the district has generally managed its exposure well in recent years, some of which saw a below-average amount of water;
- Only adequate fixed-charge coverage as estimated for unaudited fiscal 2014 at 1.19x; and
- Somewhat stagnant and shallow service area economy, with employment dominated by wood producing industries though diversifying.

The business profile score is '4' on a 10-point scale on which '1' is the strongest. The business profile reflects our view of the district's slightly above-average rates, stable and diverse customer base, somewhat shallow service area economy, low-cost power portfolio mostly from Bonneville, and good management practices and policies and rate-setting autonomy.

The bonds are secured by a first lien on net revenue of the electric system. Bond provisions include a fully funded debt service reserve fund, a 1.25x rate covenant, and a 1.25x additional bonds test. The district also has the ability to issue non-voter-approved limited GO bonds, but no GO bonds are outstanding and the district has no plans to issue such debt. The series 2015A bond proceeds will be used to current refund all of the district's series 2005 bonds, advance refund a portion of its series 2006 bonds, and generate $8 million in proceeds to fund 40% of the next two years of capital needs. The series 2015B bond proceeds will be used to advance refund a portion of the series 2006 bonds.

The district's headquarters are in the City of Aberdeen (population: 16,850), located about 110 miles southwest of Seattle. The district serves a population of about 73,300 residents covering 1,959 square miles, and serves almost all of Grays Harbor County except the City of McCleary. The district's 41,443 customers are mainly (84%) residential, but account growth has been flat since 2007 given the downturn in the economy. However, the district reports that it is beginning to see modest growth in the service territory (residential, commercial, and industrial) to pre-recession levels. Economic activity includes growth in cargo shipments at the port, which is creating new jobs, and an expansion of rail facilities. The leading 10 industrial customers represented 14.4% of energy sales revenue in 2014, up from 13.5% in 2012, with the leading two, Cosmo Specialty Fibers and the Ocean Gold Seafood, representing 6.3% combined. A loss of one of these top customers would not necessarily hurt the district's margins given that the related power could be sold at a higher price in the wholesale market. Retail-only energy sales revenue was 54% residential in 2014, but in terms of total energy sales revenue, wholesale sales accounted for a substantial 24%. Median household effective buying income in the county is 83% of the national average, somewhat limiting the district's rate-making flexibility. Unemployment in the county was moderately high at 10.0% as of 2014, down from 11.8 % in 2013.

The district is load-resource (demand-supply) balanced in most months, but has a surplus in some months on a firm basis. This allows the district to take advantage of the wholesale market for power sales. In fiscal 2014, approximately 84% of the district's energy resources (megawatt-hours) were sourced from Bonneville-supplied low-cost hydropower, including the Slice and Block products. These Bonneville contracts were renewed in 2011 and extend through 2028. The district's Block allocation is about 62 average megawatts (aMW), with Slice at critical water at around 86 aMW. Hydro conditions in fiscal 2014 were about 10% above normal. The district is also a generation-owning utility, with excess capacity and exposure to natural gas and power price volatility. About 8% of its energy resources in fiscal 2014 came from its Frederickson combustion turbine project near Tacoma, Wash. The district purchased this gas-fired generation in 2001 with a contract for 45 MW of capacity. This is a jointly owned project with Franklin PUD and Benton PUD.

Approved in 2006, the state's Energy Independence Act (I-937) requires 3% of the district's load to be sourced from renewable energy resources by 2012, then 9% by 2016 and 15% by 2020. The district has 20 MW of capacity from the Nine Canyon Wind Project, which represented 3% of total energy sales (eligible renewable) in 2014. The district also has two relatively new resources to meet the state's renewable requirements, including a 20-year power purchase agreement for 6 MW of wind capacity in the Coastal Wind Project (1% of energy). The other project, a 15 MW biomass project (4% of energy), is located in the Sierra Pacific mill located just outside Aberdeen. Both of these resources qualify under I-937 and, with the addition of Nine Canyon, the district reports that it is fully covered for renewable resources through 2020.

A leading credit strength of most public power providers, the district included, is the ability to adjust rates without regulatory approval. The district has demonstrated an ability and willingness to make rate adjustments, both up and down, during the past several years. The district increased rates 8% in February 2010, 7% in February 2011, and 8% in January 2013. It followed these rate increases with two additional rate increases in 2014 totaling 5.25%. The district's rates are closely tied to Bonneville's rate actions given that Bonneville accounts for 89% of the district's power supply. The current rate structure reflects three sizable increases in 2001 and 2002 (of 20.5%, 26.0%, and 11.0%) resulting from increased power costs and cost recovery adjustment clauses implemented by Bonneville. The district's forecast through 2017 indicates annual rate increases of 3% during fiscal years 2015 to 2018 to fund various capital projects and meet higher power costs from Bonneville and other projects.

The district's financial performance has generally been good and consistent during the past several years. DSC was around 1.5x to 1.6x in fiscal years 2009 to 2011, but declined to 1.4x in fiscal 2012 given reduced retail and wholesale sales. Management reports that fiscal 2012 was also a transitional year for the district, as a new general manager was hired and decided to delay capital projects and cut operating costs to avoid raising rates. Retail sales were also lower given economic conditions, and wholesale sales declined given that wholesale prices were lower than in previous years. Fixed-charge coverage ended at 1.09x in fiscal 2012, down from 1.17x in 2011. However, given an 8% rate increase that went into effect in January 2013 and two additional rate increases combining for 5% in 2014, margins and coverage have improved. DSC was 1.63x in fiscal 2013 and is estimated at 1.77x for unaudited fiscal 2014. Fixed-charge coverage improved to 1.17x in fiscal 2013 and is estimated at 1.19x for fiscal 2014.

The district projects DSC to improve to 1.8x in 2015, with fixed-charge coverage increasing to 1.2x. The district projects DSC during fiscal years 2016 to 2018 at 1.8x to 2.1x, with fixed-charge coverage at 1.2x to 1.3x, which we view as good and consistent with the rating. The district's forecast remains reasonably conservative, with wholesale sales assuming a pessimistic 85% exceedance scenario for its hydroelectric generation (driest 15th percentile year) and just 1% annual load growth. Cash reserves for audited fiscal 2013 totaled $22.3 million, equal to 83 days of operating expenses, with unaudited fiscal 2014 cash of $20.4 million, or 72 days of operations. The district also maintains a $10 million line of credit with a bank that adds 35 days of cash. The district projects cash balances to remain near $23 million, or about 80 days' cash, during fiscal years 2015 to 2019, not including its bank line.

The district has an internal DSC target of 1.75x and a goal to fund 60% of capital from rates (and the rest from debt). Management projects capital spending during the next four years at approximately $40 million. No additional bond issuance is planned.

Outlook

The stable outlook reflects our anticipation that liquidity and coverage will remain good during the next two years given the district's lack of plans to issue debt, manageable capital spending plans, and planned rate increases. Upside potential is unlikely given our view of the district's relatively shallow economic base, limited rate flexibility, and exposure to cost increases from Bonneville. However, neither do we anticipate lowering the rating during the next two years given the district's solid financial metrics and prudent financial management and budgeting practices.

Related Criteria And Research

Related Criteria

- USPF Criteria: Electric And Gas Utility Ratings, Dec. 16, 2014
- USPF Criteria: Methodology: Definitions And Related Analytic Practices For Covenant And Payment Provisions In U.S. Public Finance Revenue Obligations, Nov. 29, 2011

Related Research

- U.S. State And Local Government Credit Conditions Forecast, April 2, 2015
- U.S. Public Power 2015 Outlook: Despite Several Looming Issues, Credit Quality Should Remain Stable, Jan. 9, 2015

Ratings Detail (As Of May 1, 2015)		
Grays Harbor Cnty Pub Util Dist #1 elec rev bnds		
Long Term Rating	A/Stable	Affirmed
Grays Harbor Cnty Pub Util Dist #1 elec		
Unenhanced Rating	A(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		

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