S&P Global Ratings

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Summary:

Seattle; Retail Electric; Wholesale Electric

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Summary:

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Credit Profile		
US$310.74 mil mun lt and pwr imp and rfdg rev bnds ser 2022 due 07/01/2052		
Long Term Rating	AA/Stable	New
Seattle mun lt & pwr rev bnds		
Long Term Rating	AA/Stable	Affirmed

Rating Action

S&P Global Ratings assigned its 'AA' rating to Seattle's $310.74 million municipal light and power improvement and refunding revenue bonds, series 2022. At the same time, S&P Global Ratings affirmed its 'AA' long-term rating and underlying rating (SPUR) on Seattle's electric system revenue bonds outstanding. The utility does business as Seattle City Light (SCL). The outlook is stable.

Seattle pledges the light system's net revenue to the bonds. The city will use approximately $229 million of series 2022 bond proceeds to finance various capital improvements and $103 million to currently refund its 2012A bonds outstanding.

Credit overview

The 'AA' rating reflects SCL's ability to produce stable coverage and liquidity through various hydrological and economic conditions, especially considering recent inflationary pressures. Concentration in hydroelectric generation, from both owned assets and power purchases, exposes the city to some surplus sales risks, although it has built a rate stabilization account (RSA) and accompanying rate adjustment mechanism to offset the potential effects of this variability. The maturity and diversity of the underlying service area and stable customer base contribute to credit stability, in our view.

The stable outlook reflects S&P Global Ratings' expectation that SCL will maintain its current liquidity levels through rate-stabilization policies and continued conservative revenue forecasting. The outlook further reflects our view that average fixed charge coverage (FCC) will remain in line with historical levels despite recessionary pressures thanks to projected rate increases coupled with tighter capital spending.

Environmental, social, and governance

SCL predominantly sources its power through non-carbon-emitting hydroelectric resources, which limits the utility's exposure to the costs and operational challenges of legislative and regulatory initiatives to reduce greenhouse gas emissions. However, SCL's reliance on a network of hydroelectric dams exposes the utility to potentially substantial ongoing remediation costs for fish passage and fish habitats. In addition, we consider environmental risk as slightly elevated, given that the city is adjacent to Puget Sound and is exposed to storm surges and other extreme events related to sea-level rise.

We believe the utility faces social risk related to its relatively high rates compared with those of its peers in the state. In our view, the service area's above-average income levels coupled with the nominally low electric rates partially mitigate this risk.

Finally, we view the system's governance factors as credit supportive, as they include full rate-setting autonomy; strong policies and planning, including robust cybersecurity risk mitigation and proactive management of hydrology risk; and robust interaction between management and the city council.

Stable Outlook

Downside scenario

We could lower the rating if the city's additional leverage, rising power supply costs from Bonneville Power Administration (BPA), or otherwise rising costs due to inflationary pressures result in materially higher retail rates or a weakened competitive position that frustrates SCL's ability to maintain liquidity and achieve FCC commensurate with recent years' levels.

Upside scenario

We do not expect to raise the rating in the next two years, given SCL's large capital improvement plan and additional debt coupled with a financial forecast that indicates largely flat financial metrics against the backdrop of declining retail sales and annual rate increases.

Credit Opinion

With more than 480,000 customers, SCL is the largest municipal utility in the state of Washington. It provides service within Seattle and surrounding areas of King County. The utility's predominantly hydroelectric power supply portfolio is low cost and carbon free. It provides power to a stable customer base with access to a broad and diverse economy with low industrial concentration and stable economic fundamentals. We believe these factors contribute to SCL's economies of scale and provide the utility with revenue stability and operational flexibility.

SCL's operational profile is highlighted by its primarily hydroelectric assets that are high quality and low cost, with assets and purchased power supply through the BPA offering relatively low-cost supply; the concentration in hydroelectric resources exposes the city to above-average price volatility with respect to surplus sales, although SCL has built an RSA and uses a rate stabilization rate adjustment, offsetting this risk somewhat. We also view favorably management's comprehensive risk management practices, which include comprehensive long-term financial and capital planning, and a dynamic power supply management strategy that should position the utility well in the face of evolving state and federal regulations.

SCL's current portfolio of renewable resources complies with Washington's Renewable Portfolio Standard (known as I-937). Management reported that current power contracts will be sufficient to meet the state's renewable mandate under a no-load growth scenario until about 2028. Management also reported that the utility is continuing to plan to ensure it satisfies the Clean Energy Transformation Act requirements of a 100% carbon-neutral electric service to retail load by 2030. The utility expects it will begin seeing load growth after 2028 due to electrification of the service territory; SCL is in the midst of completing its 2022 integrated resource plan, which will address potential future resources to meet this projected growth. The city is proactively working with key stakeholders to advance the electrification and grid modernization of Seattle.

Due to conservative budgeting, management has reduced its reliance on and potential revenue volatility from surplus energy sales. A portion of wholesale net revenue comes from forward sales of typically nine months or less, and SCL maintains strict limits on the portion of its surplus position made available for forward sales to avoid potentially high replacement power costs in low-water years. S&P Global Ratings believes the system's risk management policies are conservative, and adequately reduce the risk related to forward sales. Furthermore, as part of SCL's strategy, beginning in 2010, city council enacted a series of annual base-rate increases. It also established an RSA to further offset potential revenue volatility. In our view, management has established an excellent track record of rate setting, as evidenced by SCL's historically robust and stable financial metrics, further supported by the utility's two automatic pass-through mechanisms.

Seattle's average overall rates are above the state average, suggesting that despite solid demographics, there are some constraints to revenue-raising flexibility. However, we note nominal rates are low compared with those of other major cities. The city automatically passes through cost fluctuations from BPA, and maintains an RSA surcharge that is automatically applied if the balance of its RSA drops below a certain level. Although these mechanisms have supported very stable financial metrics, Seattle's competitive position has eroded somewhat in recent years, and could decline further given projected annual rate increases ranging from 3%-5% through 2028.

SCL has exhibited consistently stable and generally robust financial performance, which supports the 'AA' rating. FCC averaged 1.58x over the past three years. The utility's actual performance consistently outpaces previous projections, highlighting management's conservative budgeting practices. Current projections indicate ongoing maintenance of coverage near historical levels, which we believe is reasonable, especially given the previously mentioned conservative forecasting practices.

The utility's liquidity has been similarly strong. When including the $99.4 million RSA, liquidity totaled $293 million as of Dec. 31, 2021, or more than 140 days' worth of operating expenses.

Finally, SCL has a moderate debt burden, characterized by a strong debt and liabilities profile with a 56% debt-to-capitalization ratio. The utility's five-year capital improvement plan totals $2.37 billion, with about 51% to be funded through operating revenue and the remaining 49% through debt. Leverage is projected to remain largely in line with historical levels.

Related Research

- Through The ESG Lens 3.0: The Intersection Of ESG Credit Factors And U.S. Public Finance Credit Factors, March 2, 2022

Ratings Detail (As Of June 13, 2022)

Ratings Detail (As Of June 13, 2022) (cont.)		
Seattle muni lt & pwr rfdg rev bnds		
Long Term Rating	AA/Stable	Affirmed
Seattle muni lt & pwr rfdg rev bnds		
Long Term Rating	AA/Stable	Affirmed
Seattle mun lt & pwr imp rev bnds ser 2019A dtd 2//20/08/2 due 04/01/2049		
Long Term Rating	AA/Stable	Affirmed
Seattle mun lt & pwr rfdg rev bnds ser 2019B dtd 08/22/2019 due 02/01/2026		
Long Term Rating	AA/Stable	Affirmed
Seattle mun lt & pwr (BHAC) (SEC MKT)		
Unenhanced Rating	AA(SPUR)/Stable	Affirmed
Many issues are enhanced by bond insurance.		

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