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$274.98 mil mun light and pwr imp and rfdg rev bnds ser 2023A due 02/01/2053		
Long Term Rating	AA/Stable	New
Seattle mun lt & pwr rev bnds		
Long Term Rating	AA/Stable	Affirmed

Credit Highlights

- S&P Global Ratings assigned its 'AA' rating to Seattle's $274.98 million municipal light and power improvement and refunding revenue bonds, series 2023A.
- 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.

Security

Seattle pledges the light system's net revenue to the bonds. The city will use approximately $249 million of series 2023A bond proceeds to finance capital improvements and $55 million to currently refund various bonds outstanding.

Credit overview

The 'AA' rating reflects SCL's ability to sustain robust coverage and liquidity through various hydrological and economic conditions. Concentration in hydroelectric generation, from both owned assets and power purchases, exposes the utility to uneven surplus sales given fluctuations in hydrology. However, SCL has built a rate stabilization account (RSA) and accompanying rate adjustment mechanism to offset some of 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. SCL's large capital plan (largely spurred by distribution investments) and rising energy costs pose additional challenges, although we believe the utility is well positioned to continue to pass through costs and maintain robust cost recovery.

Environmental, social, and governance

SCL predominantly sources its power through non-carbon-emitting hydroelectric resources, which limits the utility's exposure to many challenges of legislative and regulatory initiatives to reduce greenhouse gas emissions. The utility is compliant with Washington's renewable portfolio standard (I-937) and well positioned to comply with its decarbonization bill, the Clean Energy Transition Act, through its existing low-carbon portfolio (well north of 80% of identified carbon-free resources in 2022), eligible energy purchases, demand management and efficiency programs, and the acquisition of renewable energy credits as needed. We believe the continued costs of complying with mandates will be manageable, given management's proactive approach and the existing portfolio of assets.

However, SCL's reliance on a network of hydroelectric dams exposes the utility to potentially substantial ongoing remediation costs for fish passage and habitats. In addition, we consider physical climate 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.

SCL's weighted-average rate is above the state average, somewhat reducing rate-raising flexibility. However, the service area's above-average incomes and the nominally low electric rates mitigate this risk. In total, we consider SCL's social factors credit neutral. However, S&P Global Ratings believes that unsustainably strong business and consumer economic activity that are driving inflation will likely lead to further interest rate increases and will ultimately produce an economic slowdown. Yet, although S&P Global Ratings sees an economic weakening on the horizon, it no longer foresees imminent recession risk. (See "Economic Outlook U.S. Q3 2023: A Sticky Slowdown Means Higher For Longer," published June 26, 2023, on RatingsDirect.) Consequently, we continue to monitor the strength and stability of public power and cooperative electric utilities' revenue streams for evidence of delinquent payments or other revenue erosion because elevated consumer prices and interest rates will likely continue whittling discretionary incomes.

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.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that SCL will maintain solid liquidity levels through rate-stabilization policies and continued conservative revenue forecasting. The outlook further reflects our view that average fixed charge coverage (FCC) will at least approximate projected levels due to forecast rate increases.

Downside scenario

We could lower the rating if rising debt service requirements, increasing power supply costs from Bonneville Power Administration (BPA), and/or increased spending on regulatory compliance result in materially higher retail rates or a weakened competitive position that frustrates SCL's ability to maintain liquidity and achieve FCC commensurate with forecast 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. A higher rating would be predicated upon a financial profile that materially outpaced financial projections as SCL progresses through its capital program.

Credit Opinion

With more than 490,000 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 virtually 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. However, the concentration in hydroelectric resources exposes the utility to above-average price volatility with respect to surplus sales, although SCL's RSA and cost adjustment offset this risk somewhat. The utility's most recent integrated resource plan explores the addition of a modest amount of relatively higher-priced wind and solar assets starting in 2026 to maintain compliance with state renewable and decarbonization mandates.

We view favorably management's comprehensive risk management practices, which include long-term financial planning, capital planning, and a dynamic power supply management strategy that should position the utility well in the face of evolving state and federal regulations.

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 reduce the risk related to forward sales.

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. However, according to information from the Energy Information Administration, Seattle's average overall rates exceed the state average by about 18%, suggesting that despite solid demographics, there are some constraints to revenue-raising flexibility. Seattle's competitive position could erode, given projected annual rate increases ranging from 3%-4.5% through 2028. This risk is tempered, in our view, because SCL's nominal rates are low compared with those of other major cities.

SCL has exhibited consistently stable and generally robust financial performance, which supports the 'AA' rating. Although FCC averaged more than 1.6x over the past three years, our calculations based on management's projections suggest a decline to 1.4x-1.5x through 2028, which remains commensurate with the rating. We note that the utility's actual performance consistently outpaces previous projections, highlighting management's conservative budgeting practices.

The utility's liquidity has been similarly strong. When including the $75 million RSA, liquidity totaled more than $420 million as of Dec. 31, 2022, or more than 200 days' operating expenses. Following a discretionary defeasance and planned capital spending, liquidity is projected to decline somewhat, although still remain between 130-170 days through 2028.

Finally, SCL has a moderate debt burden, characterized by a 53% debt-to-capitalization ratio in fiscal 2022. The utility's five-year capital improvement plan totals $2.7 billion, with about 54% to be funded through operating revenue and the remaining 46% through debt. Leverage is projected to remain largely in line with historical levels.

Seattle, Washington--key credit metrics

	--Fiscal year ended Dec. 31--		
	2022	**2021**	**2020**
Operational metrics			
Electric customer accounts	493,663	485,155	477,577
% of electric retail revenues from residential customers	40	41	41
Top 10 electric customers' revenues as % of total electric operating revenue	16	16	21
Service area median household effective buying income as % of U.S.	N.A.	146	145
Weighted average retail electric rate as % of state	N.A.	118	121
Financial metrics			
Gross revenues ($000s)	1,289,300	1,170,400	1,079,100
Total operating expenses less depreciation and amortization ($000s)	767,200	741,600	705,878
Debt service ($000s)	230,241	222,781	228,480
Debt service coverage (x)	2.3	1.9	1.6
Fixed-charge coverage (x)	2.0	1.6	1.5
Total available liquidity ($000s)*	423,600	292,500	199,200
Days' liquidity	202	144	103
Total on-balance-sheet debt ($000s)	2,643,500	2,587,300	2,553,500
Debt-to-capitalization (%)	54	56	58

*Total available liquidity includes available committed credit line balances, where applicable. Debt service coverage--Revenues minus expenses divided by debt service. Fixed-charge coverage--Sum of revenues minus expenses minus total net transfers out plus capacity payments (or their proxy), divided by the sum of debt service plus capacity payments (or their proxy). N.A.--Not available.

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 28, 2023)

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 and pwr imp and rfdg rev bnds ser 2022 due 07/01/2052		
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.