



## Fitch Rates Tacoma, WA's Electric System Rev Bonds 'AA-'; Outlook Stable

Fitch Ratings-San Francisco-07 August 2017: Fitch Ratings has assigned a 'AA-' rating to the following bonds, issued by the city of Tacoma, WA (the city) on behalf of Tacoma Power, a department of the city:

--\$69,905,000 electric system revenue bonds, series 2017.

Bond proceeds will reimburse and pay for capital improvements to the electric system and pay the costs of issuance. The bonds will be sold via negotiated sale the week of Aug. 14, 2017.

In addition, Fitch affirms the 'AA-' rating on \$358.3 million outstanding electric system revenue bonds, series 2010A, 2010B, 2010C, and 2013A and 2013B.

The Rating Outlook is Stable.

### SECURITY

The bonds are payable from the net revenues of the electric system.

### KEY RATING DRIVERS

**RETAIL PROVIDER:** Tacoma Power operates a vertically integrated retail electric system and a relatively smaller telecommunications business called Click! Network (Click). The electric system serves a gradually growing, non-concentrated customer base located in and around the city of Tacoma.

**LOW COST POWER SUPPLY:** Power supply needs are met through low cost, carbon-free, and flexible hydroelectric generation resources that are both owned and contracted. The Bonneville Power Administration (BPA) provides approximately half of Tacoma Power's needs under a long-term

contract that expires in 2028.

**SOLID FINANCIAL PROFILE:** Financial metrics remain consistent with the rating. Debt service coverage improved in 2016 due to lower debt service, increased wholesale revenues, and recent retail rate increases. Liquidity levels are sound with 240 days cash on hand at the end of 2016.

**WHOLESALE SALES:** Tacoma Power is a net seller into the wholesale power market in most years. These nonfirm, short-term sales are subject to variability in hydrological conditions and market prices, leading to volatility in wholesale revenues. Favorably, the utility has implemented retail rate increases to reduce its reliance on wholesale revenues to support financial performance.

**TELECOMMUNICATIONS BUSINESS:** Click is not self-supporting and is expected to require approximately \$6 million in financial support in 2017 from the electric system. The competitive nature of the telecommunications industry could continue to erode the Click customer base and provide an additional level of risk. Continued financial support by the electric system, to the detriment of financial metrics, could pressure the rating.

## **RATING SENSITIVITIES**

**MANAGEMENT OF REVENUE STREAMS:** Rating stability for Tacoma Power is dependent upon the utility's ability to manage volatile wholesale sales, uncertain telecommunication revenues, and retail electric revenues in a manner that maintains stable financial performance.

## **CREDIT PROFILE**

Tacoma Power is a division of the city's Department of Public Utilities (the department). The utility operates the city's vertically integrated electrical generation and distribution facilities along with Click, its telecommunications division. Click accounted for approximately 6.4% of operating revenues in 2016.

Tacoma Power is one of the largest publicly owned utilities in the Pacific Northwest, serving approximately 176,784 customers in a modestly growing

service area that is approximately 180 square miles and serves the greater Tacoma area.

### Low Cost Power Supply

Fitch views Tacoma Power's resource mix as a significant credit strength. Consisting largely of owned and contracted hydroelectric resources, Tacoma's power supply is relatively low-cost, carbon free, and flexible in operation. Current resources are projected to be sufficient to meet power supply needs through 2037 under critical water conditions.

Tacoma Power is a net seller into the wholesale electricity market under most water conditions. Wholesale revenues for any year are based on market prices, loads and water availability for generation, which creates volatility in the utility's overall revenues. Tacoma Power has implemented a series of rate increases to make the utility less dependent on its wholesale sales and strengthen its retail revenue base.

### Telecommunications Exposure

Fitch views Click as increasing the business risk profile of Tacoma Power due to the competitive nature of the telecommunications industry. Click is not self-supporting and is expected to require approximately \$6 million in 2016 from the electric system. Competition from larger telecommunication companies could continue to erode the Click customer base and revenues.

### Solid Financial Profile

Financial metrics have been generally strong and stable over the past five years with the exception of 2015 when coverage levels declined as a result of higher debt service costs and lower wholesale revenues. In 2016, Fitch-calculated debt service coverage and coverage of full obligations improved to 2.84x and 1.46x, respectively, which was generally consistent with preceding years except 2015. The return to more baseline financial performance was due to a combination of lower debt service, improved wholesale revenues, and the implementation of retail rate increases.

Liquidity levels are sound with unrestricted funds equal to 240 days cash on hand (DCOH). The utility's rate stabilization fund, which is included in that total, has remained at \$48 million since 2012. These funds are available to offset or minimize the need for large rate increases in any given year.

The utility has used its significant cash balances to pay down debt in recent years and plans to do so again following this transaction. Management plans to utilize up to \$28 million in unrestricted cash to defease a portion of outstanding debt and levelize debt service through 2020. Cash balances are expected to remain at levels commensurate with the rating following the transaction.

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## **Applicable Criteria**

Rating Criteria for Public Sector Revenue-Supported Debt (pub. 05 Jun 2017)  
(<https://www.fitchratings.com/site/re/898969>)

U.S. Public Power Rating Criteria (pub. 18 May 2015)  
(<https://www.fitchratings.com/site/re/864007>)

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