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Fitch Upgrades Cowlitz County Public Utility District No. 1, Washington to 'A'

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NEW YORK--(BUSINESS WIRE)--Fitch Ratings upgrades the rating on \$134 million of Cowlitz County Public Utility District (district), WA electric system revenue bonds to 'A' from 'A-' as a part its surveillance review. The Rating Outlook is Stable.

RATING RATIONALE:

--The upgrade reflects the district's very competitive electric rates, relatively low debt burden and sound financial performance, illustrating solid management of a diverse, unique power resource mix and strategy.

--The district's power resource base is low cost, anchored by its purchase power agreement (PPA) with Bonneville Power Administration (BPA; rated 'AA' with a Positive Outlook by Fitch), accounting for the majority of power requirements for its native load.

--The stable BPA load-following contract also helps balance the district's aggressive acquisition of renewable resources. The new BPA contract beginning October 2011 will consist of 'slice' and 'block' power products. 'Slice' of the federal hydroelectric system products will increase the district's exposure to hydrological conditions and wholesale power market prices.

--The district has engaged The Energy Authority (TEA), a power marketing company, to manage its new BPA contract as well as its renewable resource portfolio.

--The district's renewable resources exhibit speculative characteristics, as the resources exceed the state's 2020 renewable portfolio standard (RPS) requirement, and are currently not being used to serve the district's own load.

--However, over the past two years, the strong returns associated with the off system sale of these resources has offset the district's weaker retail margins.

--Residential rates are very competitive compared with neighboring systems. While moderate rate increases are projected going forward related to increased BPA charges, additional rate increases could be necessary should renewable wholesale sales not materialize as expected.

--Industrial customer concentration is sizable: the top two customers account for 41% of revenues. While the loss of these substantial loads is a concern, the risk is mitigated by: (a) the district's ability to put the power back to BPA, and (b) relatively modest net margins generated by these two customers.

KEY RATING DRIVER(S):

--Following a period of above-average investment in and acquisition of renewable resources, Cowlitz's plans for additional renewable resources and future debt plans are limited.

--Following the new BPA contract in 2011, Fitch will monitor the district's ability to manage its new 'slice' contract and maintain financial metrics in line with rating medians.

--The district's financial performance over the first five months of the year is below budget due to weather-related retail sales decline and a delay in the approval of wind PPA by the California state regulatory commission. The current rating reflects Fitch's assumption that the PPA will be approved.

SECURITY:

The electric distribution system revenue bonds are secured by gross revenues of the distribution system. The bonds are payable following the payment of costs associated with operating and maintenance of the distribution system and payments associated with its resource obligations (including the existing and future production system revenue bonds).

CREDIT SUMMARY:

Cowlitz County PUD's electric distribution system provides electric service throughout the county to 47,844 customers in an area encompassing 1,144 square miles. The district has benefited from the stability of BPA's 'Actual Partial Service-Complex' (APSC) agreement, whereby BPA meets their demand curve after the application of energy they receive from certain other resources.

The stability of the APSC contract enabled the system to be more aggressive with other aspects of its power supply. Over the past three years, the district has added 41 average mega-watts (aMW) of wind-based resources to its portfolio, including White Creek Wind Project (31 aMW), Harvest Wind Project (nine aMW) and Energy Northwest's Nine Canyon (one aMW). While the wind resources will help the district meet the state's escalating renewable portfolio standards (RPS) presently peaking at 15% in 2020, the resources in excess of the RPS target are sold off-system. The margins from these sales are used to help moderate retail rates. While additional renewable investments are expected to be limited, this strategy will continued to be employed for the existing renewable portfolio. Lower than projected wholesale sales revenues (primarily renewable related) could require the district to raise rates. However, Fitch believes that the district has rate flexibility and notes that the district has historically shown a willingness to raise rates to recover costs in a timely fashion. In addition, Fitch notes that positively, the wind resources have been added without a significant increase in the district's debt levels.

Applicable criteria available on Fitch's web site at 'www.fitchratings.com' include:

--'Revenue-Supported Rating Criteria', (Dec. 29, 2009);

--'Public Power Rating Guidelines', (June 11, 2009).