RATING ACTION COMMENTARY

Fitch Rates Tacoma, WA's Electric System Revenues 'AA-'; Outlook Stable

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Fitch Ratings - Austin - 22 May 2025: Fitch Ratings has assigned a 'AA-' rating to the following bonds issued by Tacoma, WA's electric system (Tacoma Power):

--Approximately $135.0 million electric system revenue bonds, series 2025A;

--Up to approximately $90.0 million electric system revenue refunding bonds, series 2025B

Series 2025A bond proceeds will fund a portion of Tacoma Power's capital needs in 2025 and 2026, reimburse certain previous capital expenditures, and fund costs of issuance. Proceeds of the series 2025B bonds, along with cash reserves, will be used to refund outstanding bonds and pay costs of issuance. Sale of the 2025B bonds will depend on market conditions. Both bond series are expected to price on June 3.

Fitch has also affirmed the 'AA-' ratings on the approximately $547.2 million of parity revenue bonds and revenue refunding bonds outstanding.

The Rating Outlook is Stable.

Additionally, Fitch has assessed Tacoma Power's Standalone Credit Profile (SCP) at 'aa-'. The SCP represents the credit profile of the utility on a standalone basis irrespective of its relationship with, and the credit quality of, the city of Tacoma (Issuer Default Rating AA+/Stable).

Tacoma (WA) [Electric]

Tacoma (WA) /Electric System Revenues/1 LT	LT	AA- Rating Outlook Stable	Affirmed	AA- Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

The 'AA-' rating reflects Tacoma Power's very strong, but historically variable financial performance in the context of its strong revenue defensibility characteristics and very low operating risk. The electric utility relies on hydroelectric power resources for nearly all its power supply. Financial performance can fluctuate depending on hydrology conditions and market energy prices due to both the variable cost of supply and excess energy sales into the wholesale market.

Tacoma Power maintained its very low leverage ratio, measured as net adjusted debt to adjusted funds available for debt service (FADS), through fiscal 2023 at 3.8x. This was driven by a robust operating margin of 14%, a five-year high. Increased operating revenues were driven by a 3.5% retail rate increase that went into effect on April 1, 2023. The system also benefitted from high wholesale market power prices, which persisted into fiscal 2024.

Unaudited financial results in 2024 indicate similar results with leverage of 3.9x. Operating income was reduced in 2024, primary due to a change in accounting treatment regarding the city's general fund transfer, which was reclassified to an operating expenditure as compared to prior years when it was considered a non-operating expenditure.

Over half of the system's power supply is procured through Tacoma Power's Block and Slice wholesale power contract (WPC) with the Bonneville Power Administration (Bonneville; IDR AA/Stable), which expires in September 2028. Bonneville is working with its 100+ preference customers in the region, including Tacoma Power, to establish the next set of WPCs scheduled to begin on Oct. 1, 2028, through Sept. 30, 2044. Tacoma Power management expects to execute its next WPC with Bonneville by the end of 2025 with similar terms to its current contract. Our rating analysis assumes there are no material changes to the overall power supply contract terms with Bonneville in the next WPC.

Revenue Defensibility - 'a'

Variable Wholesale Sales and Strong Service Area Characteristics

The utility derives most of its revenues from retail electric sales within the city of Tacoma, which Fitch considers monopolistic. However, revenues derived from competitive wholesale market sales limit Fitch's revenue defensibility assessment to 'a'. Wholesale revenues have varied between 8% and 31% of total revenues in the last five years but have recently represented a manageable 16% of operating revenues in 2023 and 2024. Market energy prices have declined from very high levels experienced in 2022, which resulted in exceptionally strong above budget performance that year.

The revenue defensibility assessment also incorporates a strengthening in service area characteristics, including an uptick in customer growth in recent years, growing 2.1% over the past five years, income levels gradually increasing in relation to the national average and unemployment in the city that remains somewhat elevated to the national average.

Tacoma Power establishes its own electric rates through its local five-member Public Utility Board, with approval by City Council. Rates are typically adjusted annually to recover costs and remain very affordable with average energy costs equal to only 1.4% of the city's MHI. Rates remain below the state average at 94%. More recent rate increases of 5.3% in 2025 and 2026 (already approved) are higher than historical increases and reflect inflationary cost pressures impacting much of the sector. Management projects potential annual rate increases to continue beyond 2026, but Tacoma Power's rate flexibility should remain very strong.

Operating Risk - 'aa'

Very Low-Cost Hydroelectric Power Supply

Tacoma Power's very strong operating risk profile reflects its consistently very low operating cost burden. Tacoma Power's operating cost burden averaged 7.5 cents/kWh over the past five years. This is attributed to its owned and contracted hydroelectric power supply, which provides approximately 85% of total generation.

Operating cost flexibility is weaker due to concentration in a single fuel type, hydroelectric generation. However, this weakness does not outweigh the benefits of the very low-cost seven hydroelectric facilities across western Washington, with the balance provided by two smaller hydroelectric contracts and market purchases.

Given its long-term power supply is carbon free, Tacoma Power is well positioned to comply with Washington's renewable portfolio standards (RPS) and future mandates as part of the Clean Energy Transformation Act (CETA), which begins in 2030. Tacoma Power projects it will meet all renewable energy requirements through a combination of incremental hydro and purchased renewable energy credits (RECs).

Capital planning and management is midrange given an age of plant of 25 years, indicating potentially high lifecycle investment needs. However, Tacoma Power has been investing in capital at a higher rate than depreciation over the past five years. The capital plan totals approximately $512.6 million between 2024 and 2028, approximately 40% of which will be debt-funded. Large capital projects include FERC relicensing expenses, dam maintenance and modernization, and advanced metering infrastructure and technology upgrades.

Financial Profile - 'aa'

Variable Financial Performance Offset by Very Low Leverage Profile

Tacoma Power's financial profile is very strong and incorporates the expectation that annual financial performance can fluctuate based on hydrology. Tacoma Power's leverage ratio has ranged between 3.8x and 8.6x from 2019 to 2023. Very low leverage of 3.8x in 2023 and 3.9x in 2024 (unaudited) resulted from strong operating cash flows due to retail rate increases and strong wholesale revenue collections, despite higher purchased power costs in those years.

Fitch's leverage metric also incorporates very strong cash reserves, over $400 million in 2023 and 2024, as an offset to outstanding debt. Tacoma Power intends to spend down up to $75 million of its cash towards the planned debt restructuring with the series 2025B bonds. If the restructuring is not completed due to market conditions, the cash will still be used to finance the larger structured principal payments due in upcoming years in the current debt service structure. Liquidity is quite strong with days cash on hand above 350 days cash on hand in recent years and Fitch calculated coverage of full obligations (COFO) above 2.0x in 2023 and 2024.

increases. Leverage may periodically spike due to variable water conditions, but volatility in financial performance is captured in Fitch's assessment, and supportive of the rating.

Asymmetric Additional Risk Considerations

There are no asymmetric additional risk considerations that affected this rating.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

-- Rate actions that do not support stability in the financial profile or the utility's own financial policies;

-- Sustained leverage approximating 8.0x in Fitch's rating case.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

-- Stronger than expected growth in cash flow from operations that drives the financial leverage ratio below 5.0x on a sustained basis in Fitch's rating case.

PROFILE

Tacoma Power is a division of Tacoma's Department of Public Utilities. The division provides vertically integrated electric services to over 195,000 customers. The electric utility serves approximately 180 sq miles in the city and surrounding area of Pierce County, WA, with electricity primarily supplied from a long-term contract with BPA and seven owned hydro resources across four rivers in the region.

Tacoma Power is governed by a Public Utility Board appointed by the mayor and confirmed by the city council. The board has approval authority for most department business, but the biennial budget, rates and bond issues must also be approved by city council. Fitch considers Tacoma Power a related entity to the city for rating purposes given the city's oversight of the system, including the authority to establish rates and operations. The city's credit quality does not constrain the bond rating. However, as a related entity, the issue ratings could become constrained by a material decline in the city's general credit quality.

Sources of Information

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Tacoma Power's ESG Relevance Score of '2' for GHG Emissions & Air Quality varies from the public power sector guidance score of '3' since carbon-free systems (hydro, wind, nuclear, biomass and biowaste, geothermal) are not significantly exposed to the generation of GHG emissions from operations.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visithttps://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

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APPLICABLE CRITERIA

U.S. Public Sector, Revenue-Supported Entities Rating Criteria (pub. 10 Jan 2025) (including rating assumption sensitivity)

U.S. Public Power Rating Criteria (pub. 24 Feb 2025) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

FAST Econometric API - Fitch Analytical Stress Test Model, v3.1.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Tacoma (WA)	EU Endorsed, UK Endorsed

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