MOODY'S
INVESTORS SERVICE

Rating Action: Moody's affirms Santee Cooper's (SC) outstanding senior debt at A2; Assigns A2 rating to 2021 Tax-Exempt Refunding Series A and 2021 Tax-Exempt Improvement Series B; Outlook remains stable

11 Aug 2021

Approximately $6.8 billion of debt affected

New York, August 11, 2021 -- Moody's Investors Service ("Moody's") has affirmed South Carolina Public Service Authority's (Santee Cooper or the Authority) A2 rating on its existing revenue obligation bonds and has assigned an A2 rating to Santee Cooper's $138 million of Revenue Obligations, 2021 Tax-Exempt Refunding Series A and $289 million of Revenue Obligations, 2021 Tax-Exempt Improvement Series B. Santee Cooper's rating outlook remains stable.

RATINGS RATIONALE

Today's rating action reflects Santee Cooper's continued efforts in improving its financial flexibility by taking advantage of debt service savings through planned refundings, as well as providing greater visibility into the authority's governance structure owing to the confirmation of the Chairman until December 2025 and affirmation by the Board of the current President & CEO until January 2022, leaving room for a suitable replacement to be identified. All major pieces of litigation involving the issuer were settled in the prior year, providing greater certainty with respect to its future financial obligations.

The rating action also reflects the signing of Act 90 of 2021 by the Governor in July, which provides further clarity concerning changes to Santee Cooper's governance, retail rate setting and due process for challenges, debt approval requirements and certain limitations on new construction and acquisition and purchase of major utility facilities, among other items. Specifically, Act 90 provides guidance on the qualification and composition of the board, reduces the terms to four years from seven years and added two non-voting ex-officio members from Central Electric Power Cooperative, Inc. (Central), the authority's largest customer. Act 90 also codified the process by which the Authority's Board of Directors adjust retail electric rates, effective January 1, 2022. The process as codified is substantially similar to the Authority's historical process but now establishes the exclusive process for challenging rate adjustments approved by the Board.

The codification of the process provides greater certainty to Santee Cooper in the face of potential future rate challenges if it is able to demonstrate that it has followed the requirements such as adequate notice, public meetings and the sharing of information. Santee Cooper maintains sole rate making authority, but will need to submit proposed rate adjustments for review and comment to the Office of Regulatory Staff (ORS). Moody's considers these collective considerations as governance factors under its ESG framework.

With the House and Senate having rejected prior proposals to manage, purchase or reform Santee Cooper back in 2020, and NextEra Energy, Inc. formally removing its bid in April of this year to purchase Santee Cooper, Santee Cooper's ownership structure is expected to remain unchanged for the time being, which provides greater level of stability to operations. While a sale could be pursued at some point in the future, new legislation would have to be passed for that avenue to be pursued.

Combining the large refunding that occurred in FY 2020, and the current planned refunding transaction, the net present value of interest savings represents around $190 million, that when coupled with fuel cost savings should provide Santee Cooper sufficient headroom to enable it to maintain a fixed charge coverage ratio (FCCR) of around 1.40x and above during the four-year rate freeze period that is a component in the Cook Settlement. Days cash are expected to decline to around 130 days by 2024 with some strengthening anticipated after 2025, when the base rate freeze period is over. A second payment of $65 million associated with the Cook Settlement will occur this year, with a final payment of $70 million set to occur in FY 2022. In that regard, the authority has already set aside $85 million in cash to help cover the bump in debt service scheduled for FY 2023.

Santee Cooper's FCCR for FY 2020 was 1.47x, an increase from the 1.32x in FY 2019 (excluding the non-cash financial impact of the $200 million legal settlement liability). The improvement in FCCR was primarily due to lower operating expenses during the year as well as slightly lower debt service costs from the prior year refunding. The debt ratio and adjusted debt ratio in FY 2020 were 118.5% and 132.6% respectively, but are expected to begin a gradual decline over the next few years, owing principally to planned amortization and modest future borrowing requirements. As a result, the authority should be able to comfortably absorb the currently planned $289 million in new money issuance.

Although the authority experienced an increase in accounts receivable days during 2020 as a result of covid-19, the daily delinquency and balances have returned to pre-covid levels. Further, load demand through the second quarter of 2021 have been higher than forecasts revised by the authority last year, and as a result, the authority assumes that the impact from covid-19 have mostly abated.

Per management, Santee Cooper's $2.3 billion capital expenditure program from 2022-2028 will be 45% funded through internally generated funds, with some modest additional borrowing anticipated of around $1.2 billion over the next few years relative to over $1.6 billion in par net of new issuances through 2030. Further, per Act 90 of 2021, the State's Joint Bond Review Committee must approve proposed debt issuances, including refundings that do not generate savings in total debt service. Despite interest cost savings through the current and prior year's refundings, high leverage following the termination of the Summer project will persist for many years which is likely to chronically pressure the Authority's ability to recover costs while maintaining its cost competitiveness.

Santee Cooper's credit profile reflects its monopoly position in serving a large customer base either through wholesale power sales to Central and its 20 distribution cooperatives through 2058, retail sales or direct sales to some of the largest industrial firms in the state and to military installations.

Separately, the contract with Century Aluminum was extended through 2023. Although Century Aluminum does not represent a material share of the Authority's revenue base, we view last year's ruling that Santee Cooper had the exclusive right to provide electrical service to Century Aluminum as credit positive since it is one of Santee Cooper's legacy customers and helps to fortify its monopoly position within its service territory.

RATING OUTLOOK

The stable outlook captures improved visibility regarding Santee Cooper's financial profile over the next few years thanks to the settlement of a major lawsuit in August 2020, and anticipated interest cost savings from future, current and prior year's refundings. The stable outlook also reflects increased operating stability given no change in ownership structure in the foreseeable future and increased guidelines for the governance structure, while management maintains some flexibility with respect to operations in order to deliver on its strategy of maintaining targeted debt service coverage ratios, rate competitiveness, and stable levels of liquidity.

FACTORS THAT COULD LEAD TO AN UPGRADE OF THE RATINGS

- Further mitigation steps are executed to reduce leverage caused by the Summer project through a combination of expenditure reductions, new revenues, refinancing opportunities, and customer growth

-Clarity about the Authority's resource plan and approach to replace the Winyah Generating Station as part of a carbon transition plan

FACTORS THAT COULD LEAD TO A DOWNGRADE OF THE RATINGS

- Three year average fixed charge coverage falls below 1.30x and liquidity is consistently below 110 days;

- Further political influence weights on Santee Cooper's operations

LEGAL SECURITY

The bond resolution includes a sum-sufficient rate covenant and no debt service reserve account or additional bonds test but Santee Cooper must deposit annually into the Capital Improvement Fund an amount which, together with amounts deposited during the prior two years, equals to a minimum of 8% of required revenues in the preceding three fiscal years. As of December 31th, 2020, the capital improvement fund balance was $123.8 million. These funds are typically used for debt service or for capital but could be used for any corporate purpose. The amount Santee Cooper is required to transfer to the state is restricted to a maximum of 1% of Santee Cooper's projected operating revenues. There is no external rate regulation except for federal regulation on transmission rates.

Per Act 90 of 2021, signed by the Governor in June, the State's Joint Bond Review Committee must approve proposed debt issuances, including refundings that do not generate savings in total debt service.

USE OF PROCEEDS

Proceeds from the 2021 Series A&B bonds are being used to fund a portion of the issuer's on-going capital improvement program, refund a portion of outstanding senior debt and pay costs of issuance. The $138 million from Series 2021A bonds are being issued to refund the 2011 Series C and 2012 Series A bonds along with associated redemption costs. The 2021 Series B Bonds are being issued to pay down approximately $200 million of outstanding Commercial Paper Notes and Revolving Credit Notes as well as future capital project needs. Santee Cooper is still evaluating their new money needs and market conditions, consequently the amount of 2021 Series B Bonds issued may be reduced from the indicated maximum issuance of $350 million.

PROFILE

South Carolina Public Service Authority (Santee Cooper) is a component unit of the State of South Carolina (GO bonds rated Aaa) and was created by the State Legislature in 1934. It is governed by a 12 member board of directors, 4 year staggered terms, with a 3 term limit, appointed by the Governor with the advice and consent of the Senate. One board member has to come from each congressional district in the state and each of the Authority's direct-serve counties and a chairperson appointed at large. The board will also include two non-voting representatives from Central, Robert C. Hochstetler and Robert G. Ardis, III. Board members serving prior to January 1, 2018 may not be reappointed.

The Authority provides electric service, retail and wholesale, and wholesale water supply in several regions of the state. It also serves in other capacities including flood control; real estate management; park management and economic development assistance for local communities.

The Authority's assets include wholly owned and ownership interests in a variety of coal, natural gas, nuclear, hydro, biomass, landfill and solar generating units totaling 4,830 megawatts (MW) of summer power supply peak capability. This consists of 3,215 MW of coalfired capacity, 1,117 MW of natural gas and oil capacity, 322 MW of nuclear capacity, 142 MW of hydro capacity, 29 MW of landfill methane gas capacity and 5 MW of solar capacity.

The Authority also operates an integrated transmission system which includes lines owned by the Authority as well as those owned by Central, the Authority's largest wholesale customer.

METHODOLOGY

The principal methodology used in these ratings was US Public Power Electric Utilities with Generation Ownership Exposure Methodology published in August 2019 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1170209 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1288435 .

At least one ESG consideration was material to the credit rating action(s) announced and described above.

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