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Ratings

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Summary:

Central Iowa Power Cooperative; Rural Electric Coop

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Long Term Rating	A/Stable	Affirmed

Credit Highlights

- S&P Global Ratings affirmed its 'A' issuer credit rating (ICR) on Central Iowa Power Cooperative (CIPCO).
- The outlook is stable.

Security

CIPCO borrows exclusively from the Federal Financing Bank (FFB), CoBank ACB, the U.S. Department of Agriculture's Rural Utilities Service (RUS), and the National Rural Utilities Cooperative Finance Corp. (CFC). CIPCO does not have capital market debt.

The ICR represents our view of CIPCO's overall creditworthiness and its capacity and willingness to meet its financial commitments in full as they come due. It does not apply to any specific financial obligation, as it does not consider the nature and provisions of those obligations, their standing in bankruptcy or liquidation, statutory preferences, or the legality and enforceability of the obligations. Long-term debt is secured by property pledged under the cooperative's mortgage indenture. As of fiscal year-end 2023, CIPCO had about $477 million in debt outstanding, including $449 million in long-term debt.

Credit overview

CIPCO is a generation and transmission (G&T) cooperative that supplies power to 12 rural electric distribution cooperatives plus the South Iowa Municipal Electric Cooperative Assn. (SIMECA), which combines the load of 15 small municipalities.

The rating reflects our view of CIPCO's stable membership base, robust cost recovery, and healthy financial metrics, and is tempered by open positions in its power supply portfolio that could introduce operational and power cost uncertainty. CIPCO's power supply, which primarily consists of long-term power purchase agreements (PPAs, 51.6% of energy supply in 2024) and owned generation assets (27.3% of energy supply), gives it access to a diverse portfolio of generation, but it nonetheless relies on spot market purchases to supply about 16.5% of energy requirements, exposing the cooperative to market price volatility. This risk is mitigated in part by CIPCO's ability to pass through costs effectively, as highlighted by its rate-setting autonomy, annual member rate reviews, and frequent discretionary energy cost adjustments to offset unbudgeted costs, particularly during periods of weather volatility and unplanned operational events. Management has also locked in additional PPAs and completed a repowering project that provides additional peaking capacity and operational flexibility. In addition, management is looking at adding 250MW natural-gas-fired peaking units in an effort to reduce reliance on spot market purchases during price spike events.

The rating also reflects our view of CIPCO's financial stability despite heightened market and fuel prices during winter storms in 2021 and 2022. Furthermore, fixed-charge coverage (FCC) increased modestly to approximately 1.54x in fiscal 2023 from 1.28x in the prior year and is expected to remain stable based on unaudited 2024 financials, but could modestly weaken in coming years as CIPCO progresses through its capital plan. We also view CIPCO as maintaining ample liquidity ($77 million in unrestricted cash and investments and $73 million in undrawn committed lines of credit, as of Dec. 31, 2023). Nonetheless, several members exhibited very weak cash levels at fiscal year-end 2023, which could in turn limit CIPCO's ability to pass through costs.

The rating further reflects our view of CIPCO's strengths, including:

- Member contracts through 2062 for all 13 members, providing long-term revenue predictability, and a stable agricultural service area economy (including ethanol production) with no material concentration in any leading customers.
- Wholesale rates that compare favorably with those of other G&T cooperatives, and member retail rates that were generally close to the state average in 2023.
- Management schedules bilateral baseload purchases and plans to layer in five-year capacity contracts to meet Midcontinent Independent System Operator (MISO) resource adequacy requirements and avoid a capacity shortfall during peak periods. These purchases are budgeted 1.5 years in advance to account for capacity price uncertainty, with energy charges adjusted throughout the year to pass through unbudgeted costs.

Tempering the preceding credit strengths are the following factors:

- The customer base is highly dispersed and rural, as evidenced by about five customers per line mile, which results in relatively high fixed cost allocation per customer, which could in turn constrain distribution members' rate-making flexibility.
- Through 2029, CIPCO projects adding more than $200 million of long-term debt (a 44% increase), which management plans to finance with RUS loans, to support the construction of new 250MW gas peaking units. This would elevate its currently manageable debt burden, with the debt-to-capitalization ratio potentially rising to about 80% from the current 65%. The gas peaker construction project could account for about half of the capital spending through 2029, while the remainder ($232 million) will center on transmission improvements to enhance system reliability and facilitate growth.

Environmental, social, and governance

In our opinion, CIPCO faces moderate climate transition risk exposure due to the presence of coal-fired generation in its power supply portfolio; coal provided 25% of energy requirements in 2024. While CIPCO's coal presence is relatively low compared to many Midwest peers, and has declined by more than 30% over the past decade, we believe the cooperative remains exposed to potential future greenhouse gas emission regulations. We also note that CIPCO faces physical environmental risks, as evidenced by major derecho storms and extreme winter weather over the past few years, although management's planning, policies, and procedures limited the financial and operational impacts to the cooperative.

In our opinion, social risks are credit neutral given that CIPCO's member rates were near the state average in 2023 and its wholesale rates remain competitive with those of other G&T cooperatives in the region. We are monitoring the strength and stability of utilities' revenue streams for evidence of delinquent payments or other revenue erosion. Along with a rate of inflation, as measured by the Consumer Price Index (CPI), that has persisted above 2% for longer than anticipated, Bureau of Labor Statistics data shows that the trailing-12-months' electricity price inflation continued to outpace the broader CPI by an average of 140 basis points during January-December 2024. The increases in delinquency rates and debt balances among household, credit card, and auto loan debt, along with household savings rates that are tracking below pre-pandemic levels, compound the financial pressures consumers face as utilities invest in the hardening of existing assets to withstand more frequent and severe climate events while also investing in emissions reductions. Potentially exacerbating issues of energy affordability are S&P Global Economics' forecast of weakening GDP, and the uncertainty surrounding whether and when the president will implement economic initiatives proposed as a candidate, including imposing tariffs. The potential for the president's proposals to add to inflation and weaken GDP growth might add to the economic headwinds facing utility customers, which can negatively influence capacity to make timely utility bill payments. (See "Economic Outlook U.S. Q1 2025: Steady Growth, Significant Policy Uncertainty," published Nov. 26, 2024, on RatingsDirect).

Governance factors are credit neutral, in our opinion, as demonstrated by management's sound financial and operational policies, including a well-maintained target of at least 1.2x debt service coverage, leverage ratios (an equity-to-asset ratio that has exceeded the targeted 20%), level principal amortization that results in a declining trend of annual debt service requirements, and long-term financial and power supply planning. We understand that management currently maintains no financial hedges due to the reduced natural gas cost volatility over the past two years, and has the ability to hedge with a short turnaround if necessary. However, this could lead to greater price uncertainty in the future if market conditions evolve.

Outlook

The stable outlook reflects our expectation that the cooperative will continue to ensure operational reliability and mitigate market exposure through a multi-pronged approach (including procuring long-term PPAs, purchases of short-term baseload contracts, and constructing a peaking unit by 2029) and will produce sound coverage metrics through dynamic rate adjustments and cost management. The outlook further reflects our view that CIPCO's robust liquidity will provide financial flexibility to meet its obligations and other contingencies.

Downside scenario

We could lower the rating within the next two years if the cooperative's coverage and liquidity decline significantly, whether due to materially higher debt service payments associated with unplanned additional loans, inadequate rate adjustments to pass through unexpected costs to distribution members, or market disruptions (which could occur during extreme weather) causing material financial damages beyond normal capacity.

Upside scenario

We are unlikely to raise the rating over the next two years given CIPCO's projected financial metrics showing potentially moderating FCC; sizeable market exposure in the near term; low customer density; and diverse incomes throughout the service area.

Credit Opinion

CIPCO members and SIMECA serve more than 133,000 electric accounts and a population of about 300,000 across much of southern and eastern Iowa. CIPCO's service area economy focuses heavily on agriculture. The cooperative's members serve an exceptionally rural and dispersed population, with the 12 member cooperatives averaging five customers per line mile, and only two members serving more than five per line mile. No individual customer represents more than 2.5% of total energy sales. All but five members charge overall rates that are above the state average, according to the most recent available data from the Energy Information Administration. However, the sparse service territories and the 54% load factor contribute to reduced efficiency in recovery of fixed costs for the member cooperatives, leading to higher rates.

The cooperative maintains a diverse fuel mix that consists of wind (41.1%), coal (25.2%), solar (7.3%), natural gas (2.1%), spot market purchases from the MISO (16.5%), short-term bilateral energy purchases (4.6%), and other resources (2.9%). The utility's generation portfolio provides about 1,017MW of total generation resources, consisting of minority interests in coal plants; one wholly owned peaking facility (Summit Lake repowering project); and contractual resources from a mix of hydro, wind, solar, landfill gas, and diesel gas units. The arrangement has diversification benefits, with no reliance on a single plant or fuel, as well as economies of scale in operations. Operating availability of CIPCO's major resources is above industry averages in most years.