Research Update:

Valley Clean Energy, CA Assigned 'A-' Issuer Credit Rating; Outlook Stable

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Overview

- S&P Global Ratings assigned its 'A-' issuer credit rating (ICR) to Valley Clean Energy (VCE), Calif.
- The outlook is stable.

Rationale

Security

The ICR represents our view of VCE's capacity and willingness to meet its financial commitments as they come due and does not apply to any specific financial obligation. VCE has no debt outstanding, nor does it plan to issue any debt in the near term.

Credit highlights

VCE is a community choice aggregator (CCA) that began operations in 2018, providing service to roughly 64,000 customers in the cities of Davis, Woodland, Winters, as well as unincorporated Yolo County. The CCA directly competes with the service area's incumbent investor-owned utility, Pacific Gas and Electric Co. (PG&E; BB-/Positive), to provide customers the energy portion of their electric service. (PG&E's transmission and distribution assets deliver the electricity.)

The rating reflects VCE’s stable customer base, highlighted by a continuous participation rate of 90%+ since inception, coupled with the CCAs customer diversity and participation in the broad and diverse Sacramento-Roseville-Arden-Arcade metropolitan statistical area. These factors together provide VCE with a degree of revenue certainty, in our view. However, we note that the CCA derives approximately one-fifth of its revenues from agricultural customers in a given year. We believe these customers are generally more sensitive to rate increases, while also producing somewhat uneven energy sales from year to year, which tempers the preceding strength somewhat.

The rating is also supported by VCE’s healthy liquidity position, with unrestricted reserves and committed credit facilities totaling $59 million, or nearly 300 days’ worth of operating expenses, as of Dec. 31, 2024, which we believe provides a sound financial cushion. Despite limited direct capital overhead, in our opinion, VCE's operational profile (specifically, the need to procure long-term resources for a noncaptive customer base) coupled with its ongoing need to manage the power charge indifference adjustment mechanism (PCIA) necessitates enhanced liquidity.

The rating further reflects our view of the following factors:

- VCE implemented a protective joint powers authority agreement that requires that members provide six months' notice prior to their exit, subject to an affirmative vote from their respective governing boards. Additionally, departing members must make VCE whole for any costs and obligations incurred in serving them prior to their departure. We believe this arrangement provides a safety net that mitigates financial losses and provides a temporal buffer to adjust operations accordingly. However, this provision does not insulate VCE from the risk of individual customers opting out of service.
- VCE's historical fixed-cost coverage (FCC) averaged a very strong 1.44x over the past three years. However, our calculations based on management's projections indicate a decline to about 1.1x moving forward in the face of rising energy costs and lower relative revenue collections. Nonetheless, we believe forecast levels remain supportive of the current rating.
- VCE is well positioned to meet California's stringent renewable portfolio standard (RPS), as well as evolving federal requirements, given its predominantly renewable power portfolio, which should help the CCA avoid rapidly rising energy costs that many others in the state are facing.
- VCE sets rates based on its cost of service, which helps ensure sufficient recovery of variable costs.
- VCE maintains industry standard policies, highlighted by its regularly updated, exceptionally detailed financial forecast, which we believe are especially important considering the complex nature of the CCA.
- Exposure to wildfires through California's strict liability standard and inverse condemnation is limited, given the absence of ownership of transmission and distribution assets. However, the CCA has indirect exposure to wildfires, and the associated costs, that affect Pacific Gas and Electric (PG&E) transmission and distribution assets needed to serve VCE's customers.

Partially offsetting these strengths, in our view, are the following factors:

- Like other CCAs, direct retail competition with the incumbent investor-owned utility, PG&E, limits VCE's rate-setting flexibility.
- VCE must balance its obligation to enter long-term contracts, the passthrough of ever-rising energy costs, and a noncaptive customer base given the potential for customer opt-out. In addition, the CCA must balance its ambitious renewable targets with the need for reliable baseload energy. The significant demand for new renewable projects throughout the state, coupled with the lengthy process for renewable project planning and construction, compounds these challenges.
- While the CCA's energy portfolio is composed of predominately long-term power purchase agreements (PPAs; 73% in 2025, increasing to 90% by 2028), we note VCE faces potential exposure to individual counterparties. The CCA currently has 12 long-term contracts (four of which are not yet online) signed across 11 counterparties, most of which are not rated by S&P Global Ratings. The concentration among a relatively small number of counterparties for its power supply means that a potential counterparty default would necessitate that the CCA make short-term, potentially high-priced, energy purchases. Mitigating this risk somewhat is

VCE's counterparty credit policies and procedures, developed in tandem with TEA, including ongoing credit reviews and (if necessary) credit posting requirements by energy suppliers.

- There is uncertainty about the future rate impacts of the PCIA. VCE must charge its customers the PCIA that reflects the costs that PG&E incurred to procure power for these customers when they were still served by PG&E. The PCIA amount varies year to year, partially depending on market prices, and could pressure the CCA's financial metrics and/or rate affordability. Over the longer term, the magnitude of the PCIA on customer bills will become less pronounced as power supply contracts signed by PG&E for its former customers expire.

Environmental, social, and governance

VCE's energy transition risk is low, based on its predominantly carbon-free resource portfolio. However, as a practical matter, the intermittency of renewable resources might frustrate the CCA from achieving California's ambitious greenhouse gas emission goals in the absence of advances in long-duration storage technology. VCE's physical environmental risk is slightly elevated, as the sparsely populated western part of Yolo County is located in an area designated by the California Public Utilities Commission as having elevated wildfire risk. VCE does not own any transmission or distribution assets, so its risk of directly sparking a wildfire is remote. However, VCE could face indirect exposure to wildfires from events caused by PG&E's transmission and distribution assets.

We believe VCE’s exposure to social capital factors is slightly elevated. While VCE's residential customers currently pay rates that are slightly lower than PG&E's, PG&E's rates are dramatically elevated (140% of California's average retail system rate in 2023), which could weigh on financial flexibility and customer rate affordability.

Finally, we view the utility's governance factors as generally credit supportive, highlighted by the CCA's robust long-term financial and energy forecasting, coupled with solid cohesion among the board and management. However, the potential for retail customer opt-out is beyond management's control and tempers our view of the CCA's governance factors somewhat.

Outlook

The stable outlook reflects our expectation that VCE will continue to pass through rising power costs to its customers, allowing it to maintain financial metrics at least in line with forecast levels. The outlook further reflects our expectation that said pass-through will not meaningfully worsen VCE's rate affordability and/or customer participation.

Downside scenario

We could lower the rating if the cost of future power, storage, delivery, and/or capacity constrains VCE's ability to achieve projected financial results, especially FCC. We could also lower the rating if VCE experiences customer opt-outs that leave it with meaningful surplus energy purchase commitments whose cost must be recovered through either resale into competitive wholesale markets or rate increases.

Upside scenario

We could raise the rating in the next two years if, contrary to management's financial forecast, VCE achieves FCC materially better than projected, and at levels we believe are sustainable, while maintaining or improving liquidity and a stable opt-out rate.

Credit Opinion

VCE Overview

VCE was originally formed in 2017 (with electric service broadly starting in 2018) to procure retail electric power on behalf of unincorporated Yolo County and the cities of Davis and Woodland. VCE began service to the city of Winters in 2021, and expects it could expand into the city of West Sacramento in the future.

VCE’s customers benefit from participation in the broad and diverse Sacramento-Roseville-Arden-Arcade metropolitan statistical area, resulting in incomes that are slightly higher than national average. VCE's residential customers account for 42% of revenues while its top 10 customers account for just 10%, indicating a generally stable customer base. However, VCE’s reliance on agricultural customers for about 20% of its revenue does expose the CCA to potential revenue variability, as well as a more rate-sensitive customer class.

PG&E, on behalf of VCE, performs monthly retail electric meter readings, bills VCE's customers, collects customer payments, and conveys over its transmission and distribution systems for the electricity VCE procures. VCE segregates and remits to VCE the revenues it collects for VCE; we understand these revenues are insulated from an investor-owned utility (IOU) bankruptcy.

Retail electricity customers who migrated to VCE at the introduction of service in their area may return to their respective incumbent IOU upon 30 days' notice. VCE does not impose fees on departing customers.

VCE has partnered with The Energy Authority (TEA), in consultation with VCE's board, to manage its wholesale energy marketing and trading function. We believe this agreement is prudent given TEA's expertise in the sector.

While the ultimate authority for rate-setting is vested in the board, the CCA reports there has been solid cohesiveness between the board and management. Additionally, VCE has established a discretionary cost adjustment mechanism that management can use inter-year without board approval, if necessary, which we view favorably.

VCE Operations

The CCA's current resources will be sufficient to source 82% of its energy from eligible renewable resources in 2025--well ahead of California's 60% target by 2030. Management anticipates monetizing a portion of its renewable energy credits (RECs), translating to a 75% net RPS in 2025. We view the CCA's ability and willingness to monetize RECs as providing additional flexibility.

VCE has novated some of its existing PPAs into prepay transactions, providing the CCA with annual energy savings. We do not view these debt instruments as a direct risk to VCE, as the debt is nonrecourse, and if the transaction were to unwind, the PPA would revert back to VCE (though without the prior energy savings).

Given its direct competition with PG&E, we believe that if the CCA's all-in energy bills were to become materially more expensive than PG&E's, many customers would opt out of VCE--especially more price sensitive customers, such as agricultural customers. However, VCE has maintained a stable opt-out rate, between 9%-10% since its inception in 2018, indicating a degree of elasticity among the CCA's customers. Moreover, management has reported its customer opt-outs have not meaningfully shifted following past rate actions. Nevertheless, according to U.S. Energy Information Administration data, PG&E's weighted-average rate was approximately 140%

of the California average in 2023; with VCE's rates currently 5% below PG&E's, we believe overall rates are elevated and view the CCA's ratemaking flexibility as constrained.

We are monitoring the strength and stability of electric utilities' revenue streams given inflationary pressures on electricity prices (which have outpaced the broader Consumer Price Index inflation rate), reflecting higher operating and debt costs due to investments in emissions reductions, load growth, and climate resilience. We anticipate that substantial and sweeping tariffs could also pressure electricity prices as utilities source costlier materials and components critical to the sector's build cycle. Coupled with the high degree of unpredictability around federal policy, the economy's stressors and the associated financial pressures consumers are facing, including diminished consumer confidence and expectations of rising inflation and unemployment, might make it more difficult for rate-setting bodies to harmonize the interests of utilities, their customers, and their investors, which could negatively affect utilities' financial metrics. (See “Economic Outlook U.S. Q3 2025: Policy Uncertainty Limits Growth,” June 24, 2025.)

VCE Finances

VCE's liquidity has improved over the past two fiscal years and is robust, with unrestricted reserves of $51.9 million as of Dec. 31, 2024. The CCA also maintains a $7 million line of credit that can be used for any purpose. Together, these resources were equivalent to almost 300 days' operating expenses, which we believe provides a solid financial cushion.

VCE's historical fixed-cost coverage (FCC) averaged a very strong 1.44x over the past three years. However, our calculations based on management's projections indicate a decline to about 1.1x moving forward in the face of rising energy costs and lower relative revenue collections. Forecast 2026 FCC is below 1.0x, but management anticipates using its previously deferred reserves accumulated in its rate stabilization reserve and customer dividends account in lieu of rate increases. When accounting for these transfers, 2026 coverage is forecast to be 1.0x, rebounding to an average of 1.17x thereafter. We believe forecast coverage levels are generally supportive of the 'A-' ICR, but we would revisit this assessment should VCE continue to use cash infusions to achieve sufficient coverage.

Valley Clean Energy, California -- key credit metrics

	--Fiscal year ended Dec. 31--		
	2024	**2023**	**2022**
Operational metrics			
Electric customer accounts	63,629	59,740	61,985
% of electric retail revenues from residential customers	42	42	42
Top 10 electric customers' revenues as % of total electric operating revenue	9	N.A.	N.A.
Service area median household effective buying income as % of U.S.	109	110	111
Weighted average retail electric rate as % of state	140	140	138
Financial metrics			
Gross revenues ($000s)	98,929	95,756	86,709
Total operating expenses less depreciation and amortization ($000s)	71,947	74,869	80,897
Debt service ($000s)	0	729	528
Debt service coverage (x)	N.M.	28.7	11.0
Fixed-charge coverage (x)	1.7	1.5	1.1
Total available liquidity ($000s)*	58,943	34,480	10,139
Days' liquidity	299	168	46

Valley Clean Energy, California -- key credit metrics

	--Fiscal year ended Dec. 31--		
	2024	2023	2022
Total on-balance-sheet debt ($000s)	0	0	712
Debt-to-capitalization (%)	0	0	4

*Total available liquidity includes available committed credit line balances, where applicable. Debt service coverage--Revenues minus expenses divided by debt service. Fixed-charge coverage--Sum of revenues minus expenses minus total net transfers out plus capacity payments (or their proxy), divided by the sum of debt service plus capacity payments (or their proxy). N.A.--Not available. N.M.—Not meaningful.

Ratings List	
New Issue Ratings	
ICR	
Long Term Rating	A-/Stable
New Rating	
Public Power	
Valley Clean Energy, CA Electric System Revenues	A-/Stable

The ratings appearing below the new issues represent an aggregation of debt issues (ASID) associated with related maturities. The maturities similarly reflect our opinion about the creditworthiness of the U.S. Public Finance obligor's legal pledge for payment of the financial obligation. Nevertheless, these maturities may have different credit ratings than the rating presented next to the ASID depending on whether or not additional legal pledge(s) support the specific maturity's payment obligation, such as credit enhancement, as a result of defeasance, or other factors.