MOODY'S
INVESTORS SERVICE

CREDIT OPINION
21 December 2018

Update

Rate this Research

RATINGS

Avista Corp.

Domicile	Spokane, Washington, United States
Long Term Rating	Baa2
Type	LT Issuer Rating
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Nana Hamilton +1.212.553.9440
AVP-Analyst
nana.hamilton@moodys.com

Richa N Patel +1.212.553.9475
Associate Analyst
richa.patel@moodys.com

Michael G. Haggarty +1.212.553.7172
Associate Managing Director
michael.haggarty@moodys.com

Jim Hempstead +1.212.553.4318
MD-Utilities
james.hempstead@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Avista Corp.

Update following downgrade to Baa2, outlook stable

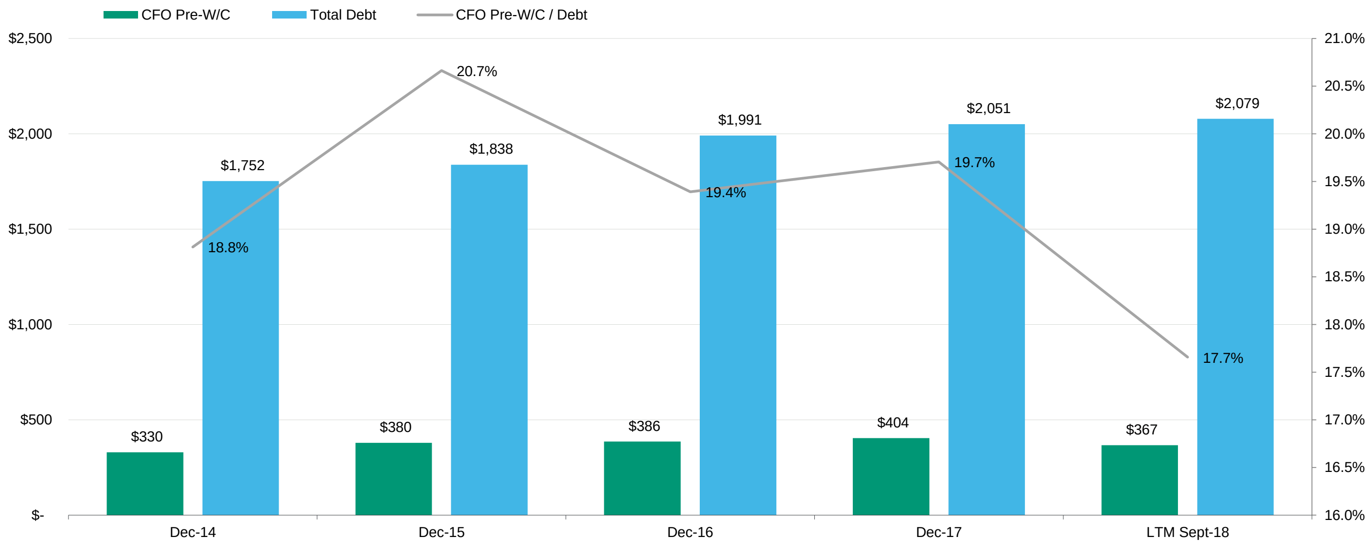
Summary

Avista Corporation's (Avista) credit profile reflects its primary business as a low-risk vertically integrated electric and gas utility with supportive cost recovery mechanisms, such as electric and gas decoupling. The credit also incorporates less predictable regulatory outcomes in Washington, Avista's primary regulatory jurisdiction. In addition Avista is constrained by cash flow loss associated with tax reform, given the historically high contribution of deferred income taxes to operating cash flows.

On 5 December 2018, the Washington Utilities and Transportation Commission (WUTC) rejected Hydro One, Ltd. (HOL unrated) HOL's proposed acquisition of Avista, concluding that the proposed merger agreement is not in the best interest of Avista or its customers from a political and financial risk perspective. On 17 December 2018, the companies submitted a petition to the WUTC seeking a reconsideration of their decision. We do not assume any significant change to Avista's regulated capital structure and dividend policy as a result of the proposed transaction. As a result, the transaction was not a major credit driver for Avista. For reference, HOL announced in July 2017 it had reached an agreement to acquire Avista for $5.3 billion in an all-cash transaction, including the assumption of roughly $1.9 billion of Avista reported debt.

Avista has some unregulated exposure in addition to its ownership of regulated utility Alaska Electric Light and Power (AEL&P, Baa3 stable), which provide marginal operational and cash flow diversity, but remain neutral in terms of our view of Avista's credit.

Exhibit 1
Historical CFO Pre-WC, Total Debt and CFO Pre-WC to Debt
$ in millions



Source: Moody's Financial Metrics

Credit Strengths

» Low-risk, approximately $3 billion rate base, utility with generally supportive cost recovery mechanisms

» Track record of stable cash flow generation

Credit Challenges

» Decline in cash flow metrics driven by reduction in contribution of deferred taxes to operating cash flow as a result of tax reform

» Inconsistent track record of regulatory outcomes in Washington

» Moderate carbon transition risk

Rating Outlook

The stable outlook incorporates our view that Avista's financial profile will maintain a ratio of cash flow from operations pre-working capital (CFO pre-WC) to debt in the mid-teens range. In addition, the stable outlook assumes that Avista will receive adequate cost recovery authorizations within its regulatory jurisdictions. The stable outlook also incorporates our view that the proposed acquisition by HOL is unlikely to be completed and that unregulated operations will remain below 15% of consolidated earnings and cash flow.

Factors that Could Lead to an Upgrade

» Demonstrated improvement in regulatory environments and relationships

» CFO pre-WC to debt above 19% on a sustainable basis

» CFO pre-WC less dividends above 13% on a sustained basis

Factors that Could Lead to a Downgrade

» Sustained depredation of regulatory relationships in Washington resulting in inadequate regulatory relief

» CFO pre-WC to debt below 14% on a consistent basis

» Direct financial support of HOL's acquisition debt in the event of a successful completion of the acquisition by HOL

Key Indicators

Exhibit 2

Avista Corp. [1]

	Dec-14	Dec-15	Dec-16	Dec-17	LTM Sept-18
CFO Pre-W/C + Interest / Interest	5.2x	5.7x	5.4x	5.2x	4.7x
CFO Pre-W/C / Debt	18.8%	20.7%	19.4%	19.7%	17.7%
CFO Pre-W/C – Dividends / Debt	14.3%	16.2%	15.0%	15.2%	13.0%
Debt / Capitalization	44.6%	44.8%	44.5%	48.4%	48.3%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Financial Metrics™
Source: Moody's Financial Metrics

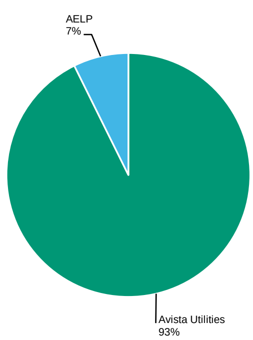
Profile

Avista is primarily an electric and natural gas utility whose Avista Utilities operating division provides electric distribution and transmission, and natural gas distribution services in parts of eastern Washington and northern Idaho. Avista Utilities also provides natural gas distribution service in parts of northeastern and southwestern Oregon. Avista Utilities has electric generating facilities in Washington, Idaho, Oregon and Montana and also supplies electricity to a small number of customers in Montana. At the end of 2017, Avista Utilities had over 380,000 electric and over 340,000 gas customers. Avista also owns Alaska Energy and Resources Company (AERC; not rated), parent of Alaska Electric Light and Power Company (AEL&P; Baa3 stable) which serves around 17,000 electric customers in Juneau, Alaska.

Avista's utility operations are regulated by the Washington Utilities and Transportation Commission (WUTC), the Idaho Public Utilities Commission (IPUC), the Oregon Public Utility Commission (OPUC) and the Montana Public Service Commission (MPSC). AEL&P is under the purview of the Regulatory Commission of Alaska (RCA).

Exhibit 3

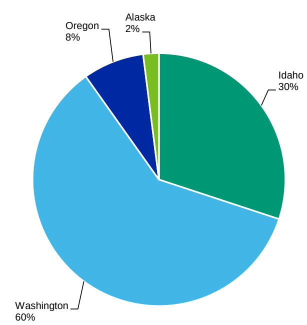
2017 Earnings Contribution



Excludes Other Segment
Source: Avista Corporation

Exhibit 4

Estimated Rate Base by Jurisdiction



Source: Company Documents & Moody's Investors Service

Detailed Credit Considerations

CREDIT SUPPORTIVE COST RECOVERY MECHANISMS, ALTHOUGH RECENT REGULATORY OUTCOMES IN WASHINGTON HAVE BEEN LESS PREDICTABLE

We view Avista's regulatory jurisdictions to be generally credit supportive. The Washington Utilities and Transportation Commission (WUTC), which regulates roughly 60% of the company's rate base and revenue, has electric and gas decoupling mechanisms which allow for timely recovery of fixed costs for the utility and drive stable and predictable gross margin and cash flow in the face of declining use. Even so, the use of historic test years result in the need for Avista to file general rate cases frequently to recover and earn on investments and recent regulatory proceedings for Avista in Washington have been contentious. Rate base attrition adjustments, which we considered credit supportive, were ruled by the Washington Court of Appeals in August 2018 as against the state's used and useful law in an ongoing review of Avista's 2015 Washington rate case currently pending WUTC action.

On 26 April 2018, the WUTC issued a final order in Avista's electric and natural gas general rate cases filed on May 26, 2017. Although Avista had requested three-year electric and gas rate plans in its original filing, the WUTC's order provided only for new rates effective 1 May 2018. In its order, the WUTC approved a net electric revenue increase of $10.8 million consisting of an increase in base revenues of $23.2 million, an increase of $14.5 million in power supply costs and a decrease of $26.9 million for the impacts from the tax cuts and jobs act (TCJA). For natural gas, the WUTC approved a $2.1 million decrease in revenues, made up of a $3.4 million increase in base revenues net of a $5.5 million decrease to reflect TCJA impacts. Both electric and natural gas rate orders were based on a slightly below industry average ROE of 9.5% and equity layer of 48.5%. Furthermore, the WUTC agreed to withhold $10.4 million of the electric excess deferred federal income taxes that resulted from TCJA for the purpose of accelerating the depreciation schedule for Colstrip Units 3 and 4 to reflect a remaining useful life of those units through December 31, 2027.

While we consider the outcome of this rate case as neutral from a credit perspective, the company has had a contentious regulatory relationship with the commission in recent history. Avista's February 2016 rate filing was rejected by the WUTC in December 2016, and the company's request for reconsideration of the decision was rejected by the commission in February 2017. This was a surprising outcome considering our view that a core competency of utility management is managing regulatory relationships, making an outright denial by the regulator unusual and unexpected. Since the WUTC is Avista's most important regulator, overseeing roughly 60% of the company's rate base and revenue generation, a strong regulatory relationship with the WUTC is important for adequate regulatory relief and for Avista's credit.

In Idaho, Avista was authorized electric and gas decoupling mechanisms in December 2015 for a three year period beginning January 1, 2016. In December 2017, the IPUC approved a multi-party two-year rate plan settlement to increase annual electric base revenues by $12.9 million and $4.5 million and gas base revenues by $1.2 million and $1.1 million effective 1 January 2018 and 1 January 2019 respectively. Both electric and gas revenue increases are based on a 9.5% ROE and 50% equity ratio relative to a requested 9.9% ROE and 50% equity ratio. The authorized electric revenue increase was more than half of Avista's filed request for a $28 million increase and the authorized gas rate increase was approximately 40% of Avista's request for a $5.6 million gas revenue increase.

As part of its March 2016 rate case order in Oregon, Avista is now allowed to implement a revenue-per-customer decoupling mechanism. In September 2017, the OPUC approved a settlement to increase natural gas base revenues by $3.5 million based on a 9.4% return on equity (ROE) and a 50% equity ratio, with an increase of $2.6 million effective on 1 October 2017 and an increase of $0.9 million effective on 1 November 2017.

In Alaska, the RCA approved an all-party settlement in November 2017, authorizing a $1.3 million base rate increase, based on an 11.95% ROE and 58.18% equity ratio, in line with interim rates that went into effect in November 2016. The authorized return is significantly above the average of recently authorized returns for the industry, a credit positive. However, we note that Alaska has a statutory period of 450 days or approximately 15 months to decide on rate cases, the longest in the nation and has not authorized cash flow stabilizing mechanisms such as revenue decoupling.

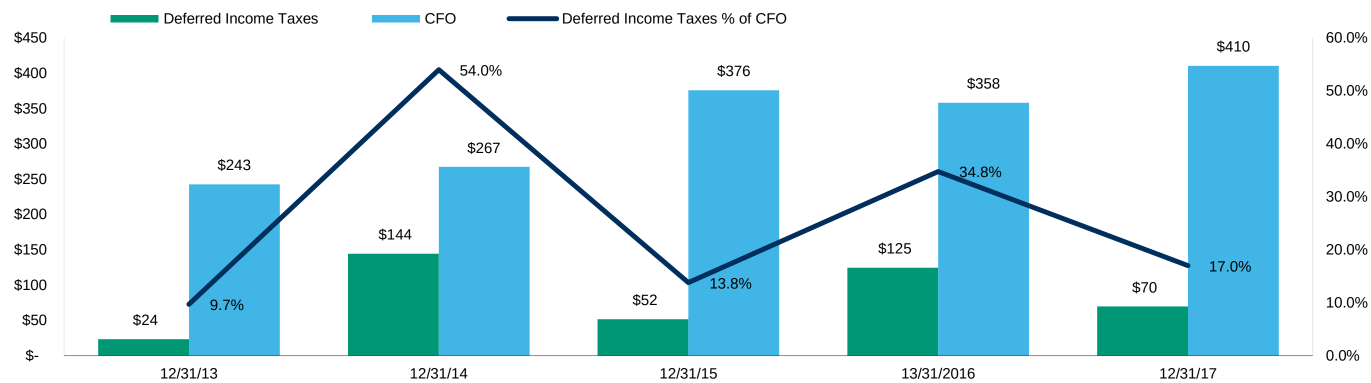
WEAKENING FINANCIAL PROFILE

As of 30 September 2018 (LTM), Avista's key financial metrics illustrate a decline, with cash flow from operations before the changes in working capital (CFO pre-WC) to debt at 17.7%, which is the middle end of the “Baa” scoring range of 13%-22% for this factor in our rating methodology for regulated electric and gas utilities.

Deferred income taxes have historically constituted a significant portion of Avista's operating cash flow, over half of operating cash flow in 2013, a third in 2016, and averaging about 26% over the 2013 to 2017 period. With the lower tax rate and loss of bonus depreciation from tax reform, we project cash flow to debt coverage around 16% over the next two years.

Exhibit 5

Avista Corp. Historical Deferred Income Taxes Contribution to Operating Cash Flow (CFO)
($ in millions)



Source: Moody's Financial Metrics™

RECENT DEVELOPMENTS IN WASHINGTON'S CLEAN AIR RULE ARE POSITIVE FOR AVISTA

In September 2016, the Washington State Department of Ecology adopted the Clean Air Rule (CAR) which establishes emission standards for green house gas (GHG) emissions from certain sources in the state, including power plants and natural gas distributors. The plan called for a reduction of GHG emissions over time, at a pace of 1.7% annually until 2035.

In a positive development for Avista and other affected parties, the Thurston County Superior Court invalidated CAR in an April 2018 order. The State Department of Ecology has filed an appeal, which remains pending, with Washington State Supreme Court. Although the outcome of the appeal remains uncertain, Avista intends to seek recovery through the rate making process for costs related to complying with any requirements.

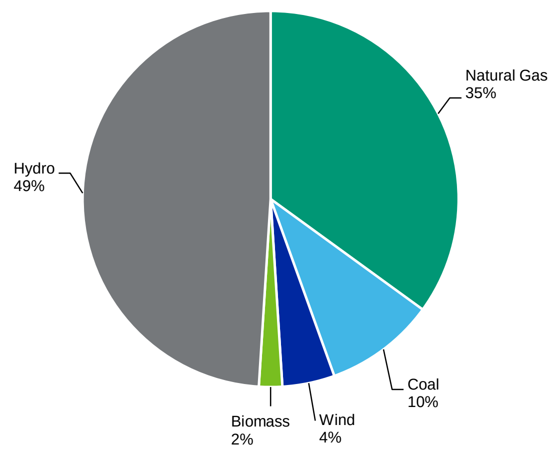
Avista projects approximately 2.4 million metric tons of GHG emissions in 2018 from owned and controlled resources. This includes emissions from approximately 550 MW net capacity Avista-owned gas power plants (excludes Kettle Falls plant) and Avista's 222 MW net capacity share (15% ownership) of units 3 and 4 of the Colstrip coal power plant. It also includes emissions from the 270 MW Lancaster gas plant whose output is contracted to Avista through 2026 under a power purchase agreement.

We view the ability to reduce emissions from owned generation as more feasible than from natural gas deliveries - which are primarily based on customer needs and generally outside the control of the company - since the company only acts as a conduit for natural gas deliveries. Therefore, it would be a credit negative if Avista was held financially accountable for the emissions of roughly 117 Bcf of gas deliveries per year, resulting in increased rates and customer bills with no added benefit of service.

MODERATE CARBON TRANSITION RISK

With an electric generation resource mix consisting of about 10% coal and 45% fossil fuels, Avista has moderate carbon transition risk within the regulated electric and gas utility sector. The Washington and Idaho commissions have agreed to set aside $10.4 million and $12 million respectively of TCJA related electric tax benefits to offset costs associated with accelerating the depreciation of Avista's only coal facilities, Colstrip Units 3 & 4, to reflect a remaining useful life through 31 December 2027. No official date has been set for the closure of the plant. Moody's framework for assessing carbon transition risk in this industry is set out in "Prudent regulation key to mitigating risk, capturing opportunities of decarbonization" (2 Nov 2017).

Exhibit 6
Avista Utilities Electric Generation Resource Mix
As of 31 December 2017



Based on maximum capacity
Excludes AEL&P
Source: Company Presentation

Liquidity Analysis

We expect Avista to maintain adequate liquidity over the next 12-18 months.

Avista's external liquidity sources consist of a $400 million senior secured revolving credit facility, which expires in April 2021. At the end of September 2018, there was $343.8 million available under the line of credit. Since Avista currently has unsecured investment grade ratings from two nationally recognized rating agencies, the company has the option to request the banks to relinquish the existing First Mortgage Bond collateral position. Avista has not asked for the release, keeping the company as one of the few US regulated utilities to maintain a secured bank credit facility.

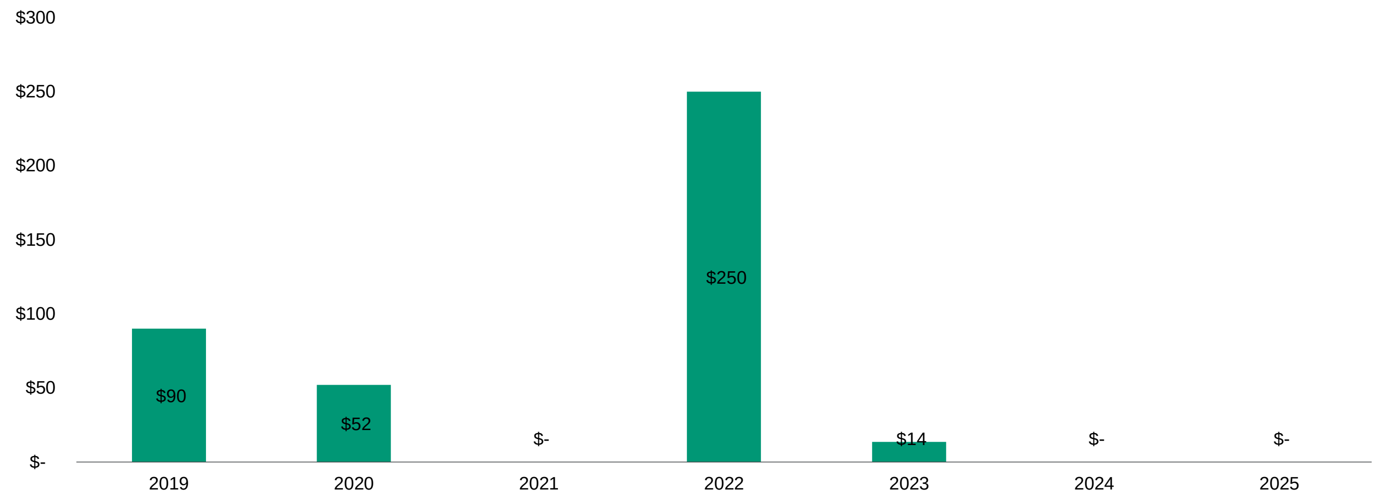
The secured nature of the credit facilities constrains Avista's liquidity flexibility, in our opinion, since the typical investment grade issuer (having an unsecured facility) can use collateral as an option to improve bank credit access during periods of unforeseen liquidity stress.

Avista was in compliance with the facility's sole covenant of less than 65% capitalization, with a ratio of 52.7% as of 30 September 2018. We note that the company has no material adverse change language beyond the close of the facility - a credit positive.

AEL&P has a $25 million line of credit which expires in November 2019 and requires a consolidated debt to capitalization covenant of 67.5%. As of 30 September 2018, there were no borrowings or letters of credit outstanding under the facility and AEL&P was in compliance with its covenant, with a ratio of 52.1%. We note that AEL&P's credit facility is now current, which is uncharacteristic of investment grade companies.

Avista's next material debt maturities occur in December 2019 and 2020, when $90 million and $52 million of senior debt is due, respectively.

Exhibit 7
Avista Corp. Debt Maturities
($ in millions)



* Excludes debt maturities of $15 million at Alaska Energy and Resources Company in 2019
Source: Avista Corporation

Methodology and Scorecard

Exhibit 8
Rating Factors
Avista Corp.

Regulated Electric and Gas Utilities Industry Grid [1][2]	Current LTM 9/30/2018		Moody's 12-18 Month Forward View As of Date Published [3]	
Factor 1 : Regulatory Framework (25%)	**Measure**	**Score**	**Measure**	**Score**
a) Legislative and Judicial Underpinnings of the Regulatory Framework	A	A	A	A
b) Consistency and Predictability of Regulation	Baa	Baa	Baa	Baa
Factor 2 : Ability to Recover Costs and Earn Returns (25%)				
a) Timeliness of Recovery of Operating and Capital Costs	Baa	Baa	Baa	Baa
b) Sufficiency of Rates and Returns	Baa	Baa	Baa	Baa
Factor 3 : Diversification (10%)				
a) Market Position	A	A	A	A
b) Generation and Fuel Diversity	A	A	A	A
Factor 4 : Financial Strength (40%)				
a) CFO pre-WC + Interest / Interest (3 Year Avg)	5.2x	A	4x - 5x	A
b) CFO pre-WC / Debt (3 Year Avg)	19.5%	Baa	14% - 16%	Baa
c) CFO pre-WC – Dividends / Debt (3 Year Avg)	15.0%	Baa	10% - 12%	Baa
d) Debt / Capitalization (3 Year Avg)	45.7%	Baa	47% - 49%	Baa
Rating:				
Grid-Indicated Rating Before Notching Adjustment		Baa1		Baa1
HoldCo Structural Subordination Notching	0	0	0	0
a) Indicated Rating from Grid		Baa1		Baa1
b) Actual Rating Assigned		Baa2		Baa2

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
[2] As of 9/30/2018 (LTM)
[3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.
Source: Moody's Financial Metrics™

Appendix

Exhibit 9

Peer Comparison Table [1]

	Avista Corp.			Puget Sound Energy, Inc.			Idaho Power Company			Portland General Electric Company		
	Baa2 Stable			Baa1 Stable			A3 Stable			A3 Stable		
	FYE	FYE	LTM	FYE	FYE	LTM	FYE	FYE	LTM	FYE	FYE	LTM
(in US millions)	Dec-16	Dec-17	Sept-18	Dec-16	Dec-17	Sept-18	Dec-16	Dec-17	Sept-18	Dec-16	Dec-17	Sept-18
Revenue	1,442	1,446	1,423	3,165	3,460	3,364	1,259	1,345	1,360	1,923	2,009	1,982
EBITDA	473	488	459	1,368	1,396	1,403	477	527	522	693	751	774
CFO Pre-W/C / Debt	19.4%	19.7%	17.7%	21.6%	24.0%	23.2%	14.9%	17.4%	17.0%	19.3%	21.8%	23.6%
CFO Pre-W/C – Dividends / Debt	15.0%	15.2%	13.0%	15.3%	18.5%	16.6%	10.1%	12.3%	11.8%	15.3%	17.5%	19.2%
Debt / EBITDA	4.2x	4.2x	4.5x	3.1x	3.0x	3.1x	4.6x	4.2x	4.4x	3.9x	3.7x	3.6x
Debt / Capitalization	44.5%	48.4%	48.3%	44.4%	48.5%	48.9%	39.8%	44.4%	44.1%	47.4%	49.9%	49.3%
EBITDA / Interest Expense	5.4x	5.0x	4.6x	5.8x	6.0x	6.2x	4.5x	4.9x	4.7x	5.2x	5.7x	5.7x

[1] All figures & ratios calculated using Moody's estimates & standard adjustments. FYE=Financial Year=End. LTM=Last Twelve Months.
Source: Moody's Financial Metrics

Exhibit 10

Cash Flow and Credit Metrics [1]
($ in millions)

CF Metrics	Dec-14	Dec-15	Dec-16	Dec-17	LTM Sept-18
As Adjusted					
EBITDA	**401**	**418**	**473**	**488**	**459**
FFO	**330**	**386**	**442**	**389**	**333**
- Div	78	82	87	92	97
RCF	**251**	**304**	**355**	**297**	**236**
FFO	330	386	442	389	333
+/- ΔWC	(50)	(4)	(28)	8	103
+/- Other	-	(6)	(56)	15	34
CFO	**280**	**376**	**358**	**412**	**470**
- Div	78	82	87	92	97
- Capex	328	394	407	412	421
FCF	**(127)**	**(101)**	**(136)**	**(93)**	**(47)**
Debt / EBITDA	4.4x	4.4x	4.2x	4.2x	4.5x
EBITDA / Interest	5.2x	5.2x	5.4x	5.0x	4.6x
FFO / Debt	18.8%	21.0%	22.2%	19.0%	16.0%
RCF / Debt	14.3%	16.5%	17.8%	14.5%	11.4%
Revenue	1,473	1,485	1,442	1,446	1,423
Cost of Good Sold	679	653	547	521	507
Interest Expense	78	80	88	97	100
Net Income	188	108	141	126	122
Total Assets	4,697	4,907	5,310	5,518	5,560
Total Liabilities	3,227	3,390	3,672	3,799	3,825
Total Equity	1,470	1,517	1,637	1,719	1,735

[1] All figures & ratios calculated using Moody's estimates & standard adjustments. Periods are Financial Year-End unless indicated. LTM = Last Twelve Months.
Source: Moody's Financial Metrics™

Ratings

Exhibit 11

Category	Moody's Rating
AVISTA CORP.	
Outlook	Stable
Issuer Rating	Baa2
First Mortgage Bonds	A3
Senior Secured	A3
Senior Unsecured MTN	(P)Baa2
ALASKA ELECTRIC LIGHT AND POWER COMPANY(AELP)	
Outlook	Stable
Issuer Rating	Baa3
AVISTA CORP. CAPITAL II	
Outlook	Stable
BACKED Pref. Stock	Baa3

Source: Moody's Investors Service

REPORT NUMBER 1154532

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S
INVESTORS SERVICE