

# RatingsDirect®

---

## Summary:

# PacifiCorp

### Primary Credit Analyst:

Gerrit W Jepsen, CFA, New York (1) 212-438-2529; gerrit.jepsen@standardandpoors.com

### Secondary Contact:

Matthew L O'Neill, New York (1) 212-438-4295; matthew.oneill@standardandpoors.com

## Table Of Contents

---

Rationale

Outlook

Standard & Poor's Base-Case Scenario

Business Risk

Financial Risk

Liquidity

Other Credit Considerations

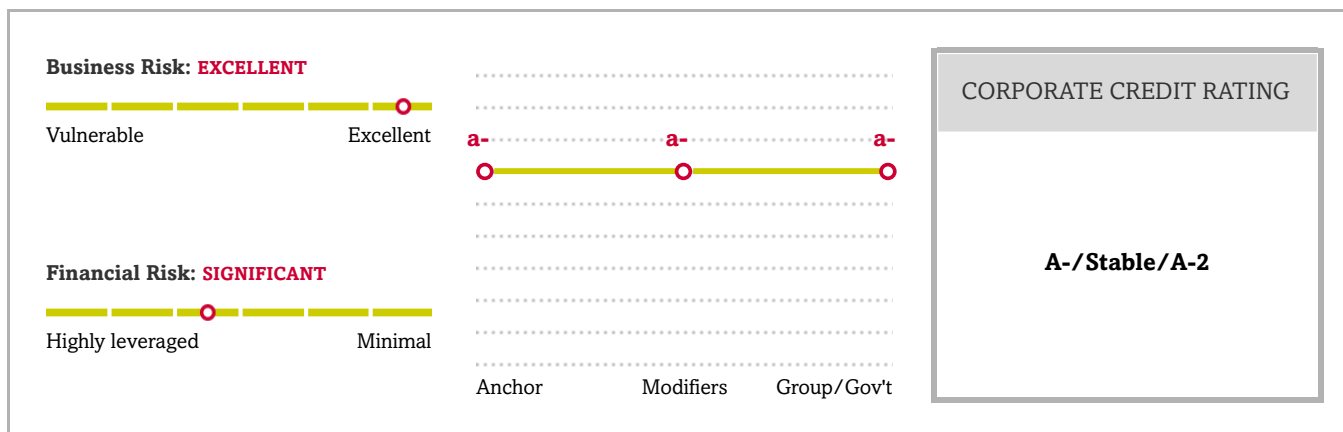
Group Influence

Ratings Score Snapshot

Recovery Analysis

Related Criteria And Research

# Summary: PacifiCorp



## Rationale

Business Risk: Excellent	Financial Risk: Significant
<ul style="list-style-type: none"> <li>• Stable operating cash flow from the regulated utility operations that supports the credit profile</li> <li>• Lack of competition in regulated service territories</li> <li>• About 70% of retail revenue derived from residential and commercial customers, which provides cash flow diversity and at least a base level of usage</li> <li>• Prudent management of coal-fired generating units to comply with environmental requirements</li> <li>• Cost recovery through base rates and rate surcharges for expenses such as fuel and capital investments</li> </ul>	<ul style="list-style-type: none"> <li>• Discretionary cash flow to remain negative during heavy capital spending period</li> <li>• EBITDA growth consisting of revenue increases and customer growth to remain approximately the same as that in recent years</li> <li>• Ability to consistently access capital markets to fund capital investments</li> <li>• Sizable parent-level debt</li> </ul>

## Outlook

The stable rating outlook reflects our expectation that management will continue to focus on utility operations and reach constructive regulatory outcomes to avoid any meaningful increase in business risk. The outlook also reflects our projection that cash flow measures will decrease as construction projects move forward and bonus depreciation benefits drop. Our base-case forecast calls for adjusted funds from operations (FFO) to adjusted debt and adjusted operating cash flow to adjusted debt both averaging between 18% and 23%. These measures are consistent with our expectations for the rating.

### Downside scenario

We could lower the rating if PacifiCorp's business risk increases materially through ongoing under-recovery of operating costs or capital improvements, or if financial measures consistently underperform our base-case forecast and remain at less credit-supportive levels, including adjusted FFO to total debt dropping below 13%.

### Upside scenario

Although we do not expect an upgrade because of near-term capital needs, we could raise the ratings if we raised the ratings on parent MEHC and if PacifiCorp's credit quality strengthened through both reduced business risk and stronger financial measures that consistently exceeded our base-case forecast, including FFO to total debt greater than 23%.

## Standard & Poor's Base-Case Scenario

Assumptions	Key Metrics			
<ul style="list-style-type: none"> <li>• Low-single-digit EBITDA growth from retail sales growth and incremental cost recovery through various rate mechanisms, including base-rate increases and rate surcharges</li> <li>• Capital spending of about \$1.1 billion in 2015, \$900 million in 2016, and \$775 million in 2017</li> <li>• Annual owner distributions of roughly \$500 million in 2015, 2016, and 2017</li> <li>• Capital spending and dividend payouts that result in discretionary cash flow that is positive once capital spending declines, indicating limited, if any, external funding needs</li> </ul>		<b>2014*</b>	<b>2015E</b>	<b>2016E</b>
	FFO/total debt (%)	21.4	18-20	19-21
	Debt/EBITDA (x)	3.6	3.2-3.7	3-3.5
	CFO/debt (%)	21.6	19-21	20-22
<p>Note: Standard &amp; Poor's adjusted figures. *Last 12 months ended Sept. 30, 2014. E--Estimate. CFO—Cash flow from operations.</p>				

## Business Risk: Excellent

We base our assessment of PacifiCorp's business risk profile as "excellent," as defined in our criteria, on the company's "strong" competitive profile, "very low" industry risk derived from the regulated utility industry, and the "very low" country risk of the U.S., where the utility operates.

PacifiCorp's competitive position reflects the stable regulatory framework of the low-risk regulated utility. We consider the utility's geographical, market, and regulatory diversity over its six-state service territory strengths because these factors provide extensive market diversity. About 70% of retail revenue is derived from residential and commercial customers, providing cash flow diversity and at least a base level of usage. PacifiCorp also has a high level of cash flow diversity since it serves a total of about 1.7 million retail customers, in Utah, Wyoming, and Idaho through its Rocky Mountain Power operating unit; and in Oregon, Washington, and California through its Pacific Power unit.

Utah and Oregon are the most important markets for the company, providing about 45% and 25% of annual retail sales, respectively. As the two largest markets for PacifiCorp, constructive regulatory dialogue is required to maintain timely recovery of fuel costs and capital investments, along with other costs. Rocky Mountain Power has had good sales growth, especially in Utah. Salt Lake County accounts for slightly more than 20% of PacifiCorp's customer base.

The utility has a well-diversified power supply portfolio that consists of coal (approximately 60%), gas (about 10%), purchased power (20%), and other sources (about 10%). We expect PacifiCorp's coal fleet to comply with existing environmental rules. However, regarding the proposed Clean Power Plan, we will monitor the utility's progress to comply with the rule, once final.

## Financial Risk: Significant

Based on the medial volatility financial ratio benchmarks, our assessment of PacifiCorp's financial risk profile is "significant," reflecting the repetitive cash flows of a utility providing regulated electric service. Our assessment also takes into consideration the company's ongoing capital spending and mostly steady recovery of costs through various rate mechanisms. Capital spending and dividend payments will lead to a drop in discretionary cash flow over the forecast period, indicating the need for external funding and vigilant cost recovery to maintain cash flow measures. Although we expect equity to grow, we also expect the utility to continue using debt financing.

For the 12 months ended Sept. 30, 2014, FFO to debt and operating cash flow to debt were both about 21%. For the same period, debt to EBITDA was about 3.6x. Our baseline forecast includes financial measures about the same as to slightly better than existing levels for FFO to debt and operating cash flow to debt and slightly stronger forecast debt to EBITDA than current levels.

## Liquidity: Adequate

PacifiCorp has "adequate" liquidity, as our criteria define the term. We believe the company's liquidity sources are likely to cover its uses by more than 1.1x over the next 12 months and to meet cash outflows even with a 10% decline

in EBITDA.

Principal Liquidity Sources	Principal Liquidity Uses
<ul style="list-style-type: none"> <li>We estimate FFO of about \$1.6 billion</li> <li>Credit facility availability of approximately \$1.2 billion</li> </ul>	<ul style="list-style-type: none"> <li>Capital spending of roughly \$1.1 billion</li> <li>Debt maturities of about \$120 million</li> <li>Dividends of approximately \$500 million</li> </ul>

## Other Credit Considerations

Other modifiers have no impact on the rating outcome.

## Group Influence

Under our group rating methodology, we designate PacifiCorp as a core entity to BHE since it is unlikely to be sold in the near term; it operates in lines of business or functions integral to the overall group strategy; it has strong, long-term commitments of support from senior group management in good times and under stressful conditions; it constitutes a significant proportion of BHE's longstanding utility operations; it is closely linked to BHE's reputation because of its regulated nature; it has been operating many years; and it is likely to receive support from the group should it fall into financial difficulty. In addition, PacifiCorp's business is similar to those of BHE's principal utility operations, which will continue to be a large portion of the consolidated group.

In addition, BHE meets the provisions and conditions in our group rating methodology to be considered an insulated subsidiary, including the requirement that PacifiCorp's SACP exceed BHE's group credit profile (GCP). Insulation measures in place that inhibit the utility from fully supporting the parent and justify a one-notch rating differential between PacifiCorp and BHE include:

- PacifiCorp is prohibited from acquiring obligations or securities of BHE or affiliates,
- To pay dividends, PacifiCorp must maintain investment grade credit ratings,
- Separate books and records must be maintained,
- Affiliate transactions must be at arm's length,
- PacifiCorp has a regulatory commitment not to pay dividends if its common equity ratio drops below 46.25%, and
- To pay dividends, interest coverage should be at least 2.5x and debt leverage cannot exceed 65%.

## Ratings Score Snapshot

### Corporate Credit Rating

A-/Stable/A-2

### Business risk: Excellent

- Country risk:** Very low
- Industry risk:** Very low

- **Competitive position:** Strong

**Financial risk: Significant**

- **Cash flow/Leverage:** Significant

**Anchor:** a-

**Modifiers**

- **Diversification/Portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Neutral (no impact)

**Stand-alone credit profile :** a-

- **Group credit profile:** bbb+
- Entity status within group: Insulated (+1 notch above group credit profile)

## Recovery Analysis

We assign recovery ratings to first mortgage bonds (FMBs) issued by U.S. utilities, which can result in issue ratings being notched above an ICR on a utility depending on the rating category and the extent of the collateral coverage. The FMBs issued by U.S. utilities are a form of "secured utility bond" (SUB) that qualifies for a recovery rating as defined in our criteria.

The recovery methodology is supported by the ample historical record of 100% recovery for secured bondholders in utility bankruptcies in the U.S. and our view that the factors that enhanced those recoveries will persist in the future (the limited size of the creditor class and the durable value of utility rate-based assets during and after a reorganization, given the essential service provided and the high replacement cost).

Under our SUB criteria, we calculate a ratio of our estimate of the value of the collateral pledged to bondholders relative to the amount of FMBs outstanding. FMB ratings can exceed an ICR on a utility by up to one notch in the 'A' category, two notches in the 'BBB' category, and three notches in speculative-grade categories depending on the calculated ratio.

PacifiCorp's FMBs benefit from a first-priority lien on substantially all of the utility's real property owned or subsequently acquired. Collateral coverage of more than 1.5x supports a recovery rating of '1+' and an issue rating one notch above the ICR.

## Related Criteria And Research

### Related Criteria

- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria - Corporates - Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- General Criteria: Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013
- Collateral Coverage and Issue Notching Rules for '1+' and '1' Recovery Ratings on Senior Bonds Secured by Utility Real Property, Feb. 14, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

### Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	Intermediate	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Copyright © 2015 Standard & Poor's Financial Services LLC, a part of McGraw Hill Financial. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, [www.standardandpoors.com](http://www.standardandpoors.com) (free of charge), and [www.ratingsdirect.com](http://www.ratingsdirect.com) and [www.globalcreditportal.com](http://www.globalcreditportal.com) (subscription) and [www.spcapitaliq.com](http://www.spcapitaliq.com) (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at [www.standardandpoors.com/usratingsfees](http://www.standardandpoors.com/usratingsfees).