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Research Update:

Berkshire Hathaway Energy Co. Outlook Revised To Negative On Announced Acquisition; 'A' Ratings Affirmed

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Research Update:

Berkshire Hathaway Energy Co. Outlook Revised To Negative On Announced Acquisition; 'A' Ratings Affirmed

Overview

- Berkshire Hathaway Energy Co. (BHE) announced it has reached a definitive agreement with Energy Future Holdings Corp. (EFH) to acquire the reorganized EFH, including Oncor Electric Delivery Co. LLC, for about $11.2 billion, plus the assumption of Oncor's debt (estimated to be roughly $6.8 billion at year-end 2017). The parties expect the transaction to close by year-end 2017.
- We are affirming our 'A' issuer credit ratings on BHE and on all of BHE's U.S.-based regulated utility subsidiaries. We are also affirming our 'A-1' short-term ratings on BHE and its U.S.-based utility subsidiaries with short-term ratings. We are revising the outlook to negative from stable on BHE and its U.S.-based utility subsidiaries.
- The negative outlook reflects the potential for lower ratings if BHE's financial risk profile, which will deteriorate due to the expected financing used in the acquisition, does not improve after the transaction closes such that adjusted funds from operations (FFO) to total debt remains consistently above 13% after 2017. This level of FFO to total debt leaves little room for underperformance relative to our forecast.

Rating Action

On July 7, 2017, S&P Global Ratings affirmed its 'A' issuer credit ratings on Berkshire Hathaway Energy Co. (BHE) and all of BHE's U.S.-based regulated utility subsidiaries. We are revising the outlook to negative from stable on BHE and its U.S.-based utility subsidiaries.

Rationale

Berkshire Hathaway announced it has reached a definitive agreement with Energy Future Holdings Corp. (EFH) to acquire the reorganized EFH, including Oncor Electric Delivery Co. LLC (Oncor) for a total cash purchase price of roughly $11.2 billion ($9 billion for 80% ownership plus $2.2 billion for the remaining 20%), in addition to assuming Oncor debt of about $6.8 billion at closing.

The ratings affirmation on BHE and its U.S.-based subsidiaries reflects our view that the Oncor acquisition will enhance BHE's business risk profile, which we assess as excellent. Oncor's low-risk, well-managed regulated transmission and distribution assets will lead to an improved business risk for BHE and also complement BHE's growth strategy of acquiring utility assets. Post-acquisition, Oncor will contribute roughly 20% to BHE's consolidated EBITDA. Even though BHE has proposed to acquire 100% ownership of Oncor, we do not believe that BHE's business risk will benefit fully from Oncor's addition because of the proposed structural and legal regulatory commitments that, in our view, would provide a level of insulation between BHE and Oncor. Such regulatory commitments would limit BHE from realizing the full benefits of Oncor to its business risk profile and the insulation would also limit full and unfettered access to Oncor's cash flows.

The negative outlook reflects our view that BHE's financial risk profile will likely weaken after the acquisition. In the absence of a definitive financing plan for the transaction, we assume that the acquisition will be mostly debt financed, similar to previous acquisition transactions BHE has pursued. In our base-case scenario, a mostly debt-financed transaction, including the assumption of existing Oncor's debt, and the addition of Oncor's cash flows to BHE, pressures BHE's financial measures and overall credit profile.

The financial measures, including our core ratio of FFO to debt, remains at the very low end of our financial profile benchmark range, slightly above 13%, with very limited cushion for underperformance. We expect modest improvement in financial measures in the outer years, based on management's financial policy. Parent Berkshire Hathaway Inc. does not rely on BHE to make distributions, bolstering BHE's equity capital through retained earnings and helping to support its balance sheet, even as BHE makes acquisitions and capital investments. Discretionary cash flow, which is strengthened due to limited dividends, will remain positive after factoring in the acquisition financing. Our financial risk assessment is based on our medial volatility financial ratio benchmarks. We will continue to monitor the company's disclosures about the financing plan for the acquisition and re-evaluate our forecasts, if it is materially different from our assumptions.

Liquidity

We assess BHE's liquidity as adequate because its liquidity sources are likely to cover uses by more than 1.1x over the next 12 months and will be sufficient to meet cash outflows even with a 10% decline in EBITDA. The assessment also reflects the company's generally prudent risk management, sound relationships with banks, and a generally satisfactory standing in credit markets.

Principal liquidity sources:

- We estimate FFO of about $6 billion;
- Average expected credit facility availability of roughly $6.35 billion annually; and
- Financing support from parent Berkshire Hathaway Inc. to maintain liquidity to the level of at least adequate through the Oncor acquisition.

Principal liquidity uses:

- Debt maturities, including outstanding commercial paper, of about $2.2

billion;
- Maintenance capital spending of about $2.25 billion; and
- Acquisition of Oncor for about $9 billion plus $2.2 billion.

Other credit considerations

The ratings on BHE include a one-notch negative adjustment for comparable rating analysis to account for the impact of higher-risk nonutility businesses, which are captured neither in the industry risk analysis nor the competitive position analysis. Non-utility businesses, including non-utility renewable generation, pipelines, and real-estate-related operations, currently account for roughly 20% of consolidated EBIDTA. Moreover, the core financial ratio indicates a financial risk profile that is at the weaker end of the significant range and falling even further due to the debt leverage used to fund the Oncor acquisition.

In addition, the ratings include a one-notch negative adjustment resulting from our assessment of BHE's financial policy to reflect our view of event risk related to unexpected acquisitions and investments, such as the Oncor acquisition, that may result in more volatile cash flow measures and incremental debt leverage.

Group rating methodology

Under our group rating methodology, we would consider Oncor to be a core subsidiary of BHE, reflecting our view that Oncor is unlikely to be sold, has strong long-term commitment from senior management, is successful at what it does, and contributes meaningfully to the group.

Issue rating

We rate the senior unsecured debt at BHE one notch lower than the issuer credit rating because priority liabilities, including operating subsidiary utility debt, exceeds 20% of total consolidated assets. The short-term rating is 'A-1' based on our issuer credit rating on the company.

Outlook

The negative outlook on BHE and its U.S. utility subsidiaries reflects the potential for lower ratings if BHE's financial risk profile, which will deteriorate due to the financing used in the Oncor acquisition, does not improve after the transaction closes such that adjusted FFO to total debt remains consistently above 13% after 2017. This level of FFO to total debt leaves little room for underperformance relative to our forecast.

Downside scenario

We could lower ratings on BHE and its U.S. utility subsidiaries if BHE's financial risk profile remains weak after the merger such that FFO to total debt is consistently below 13%. This could occur if the transaction is funded primarily with debt or if capital spending increases materially while investment recovery lags. A one-notch downgrade would be warranted if the adjusted FFO to total debt ratio failed to achieve expectations for modest improvement following the acquisition, and remained below 13% on a sustained basis.

Upside scenario

We could affirm the ratings on BHE and revise the outlook to stable after the merger closes if the combined company demonstrates that it can consistently achieve FFO to total debt of at least 13% after 2017 with further strengthening following the closing.

Ratings Score Snapshot

Corporate Credit Rating: A/Negative/A-1

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)
- Liquidity: Adequate (no impact)
- Financial policy: Negative (-1 notch)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Negative (-1 notch)

Stand-alone credit profile: bbb

- Group credit profile: aa
- Entity status within group: Strategically important (+3 notches from SACP)

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013

- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- Criteria - Corporates - Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria - Corporates - Utilities: 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: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Corporates - Utilities: Notching Of U.S. Investment-Grade Investor-Owned Utility Unsecured Debt Now Better Reflects Anticipated Absolute Recovery, Nov. 10, 2008
- Criteria - Insurance - General: Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Berkshire Hathaway Energy Company		
Sierra Pacific Power Co.		
PacifiCorp		
MidAmerican Energy Co.		
Corporate Credit Rating	A/Negative/A-1	A/Stable/A-1
MidAmerican Funding LLC		
NV Energy Inc.		
Nevada Power Co.		
Corporate Credit Rating	A/Negative/--	A/Stable/--
Berkshire Hathaway Energy Company		
Senior Unsecured	A-	
Commercial Paper	A-1	
Iowa-Illinois Gas & Electric Co.		
Senior Unsecured	A/A-1	
MidAmerican Energy Co.		
Senior Secured	A+	
Recovery Rating	1+	
Senior Unsecured	A/A-1	
Commercial Paper	A-1	

MidAmerican Funding LLC	
Senior Secured	A-
Midwest Power Systems Inc.	
Senior Secured	A/A-1
NV Energy Inc.	
Senior Unsecured	A-
Nevada Power Co.	
Senior Secured	A+
Recovery Rating	1+
PacifiCorp	
Senior Secured	A+
Recovery Rating	1+
Senior Secured	A+/A-1
Recovery Rating	1+
Preferred Stock	BBB+
Commercial Paper	A-1
Sierra Pacific Power Co.	
Senior Secured	A+
Recovery Rating	1+
Senior Secured	A+/A-1
Recovery Rating	1+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.