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Research Update:

Berkshire Hathaway Energy Co. Outlook Revised To Stable On Terminated Acquisition Agreement; Ratings Affirmed

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Research Update:

Berkshire Hathaway Energy Co. Outlook Revised To Stable On Terminated Acquisition Agreement; Ratings Affirmed

Overview

- Berkshire Hathaway Energy Co. (BHE) announced the termination of a definitive agreement with Energy Future Holdings Corp. (EFH) to acquire the reorganized EFH, including Oncor Electric Delivery Co. LLC (Oncor).
- 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 stable from negative on BHE and its U.S.-based utility subsidiaries.
- The stable outlook reflects our expectation that management will continue to focus on its core utility operations and reach constructive regulatory outcomes supporting the existing business risk profile. Although BHE has used significant debt leverage for acquisitions and capital investments, we expect credit measures to strengthen modestly, supporting the current rating. Under our base-case forecast, we expect adjusted funds from operations (FFO) to debt to average around 15% over the next few years.

Rating Action

On Aug. 22, 2017, S&P Global Ratings affirmed all ratings, including its 'A' issuer credit ratings on Berkshire Hathaway Energy Company (BHE) and all of BHE's U.S.-based regulated utility subsidiaries. We are revising the outlook to stable from negative on BHE and its U.S.-based 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.

Rationale

Berkshire Hathaway Energy announced that the definitive agreement to acquire the reorganized EFH has been terminated. If the acquisition had been completed, we projected that it would have modestly weakened financial measures, including our core ratio of adjusted FFO to debt. We had expected this to remain slightly above 13%, or at the very low end of our financial profile benchmark range. With the termination of the acquisition, we expect BHE's financial measures to remain in line with the current financial risk profile, with adjusted FFO to debt that we expect will average 15% over next two years.

We also affirmed our 'A' rating on BHE and U.S.-based subsidiaries. The affirmation is based on our expectation that BHE will continue to operate in a manner that will maintain an excellent business risk profile and preserve its financial risk profile assessment that we consider as significant.

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:

- Cash FFO of about $5.5 billion;
- Average expected credit facility availability of roughly $6.35 billion annually; and
- Cash and liquid investments of $800 million.

Principal liquidity uses:

- Debt maturities, including outstanding commercial paper, of about $4.3 billion; and
- Maintenance capital spending of about $4.5 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 falls toward the weaker end of the significant range.

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 attempted acquisition of a reorganized EFH, that may result in more volatile cash flow measures and incremental debt leverage.

Group rating methodology

We base our ratings on BHE on the consolidated group credit profile and application of our group ratings methodology. We assess BHE as a strategically important subsidiary of Berkshire Hathaway Inc. as it is important to Berkshire Hathaway's long-term strategy, is unlikely to be sold, and we expect that Berkshire Hathaway will continue to support BHE. As a result, our issuer credit rating (ICR) on BHE incorporates a three-notch uplift from its 'bbb' stand-alone credit profile (SACP).

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 stable outlook reflects our expectation that management will continue to focus on its core utility operations and reach constructive regulatory outcomes supporting the existing business risk profile. Although BHE has used significant debt leverage for acquisitions and capital investments, we expect credit measures to strengthen modestly, supporting the current rating. Under our base-case forecast, we expect adjusted FFO to debt to average about 15% over the next few years.

Downside scenario

We could lower ratings if core financial measures continuously underperform our base-case forecast and remain consistently at less credit-supportive levels, including adjusted FFO to debt of less than 13%. This could occur if rate-case outcomes are consistently weaker than expected, regulatory lag increases, or if capital spending increases and is primarily debt financed. Acquisition risk remains a consideration and could lead to a ratings change depending on the nature of a target entity, the financial risk profile at the time of the acquisition announcement, and the transaction financing.

Upside scenario

Given our assessment of business risk and expectations of financial performance, we do not expect higher ratings over the next few years. However, we could raise the ratings if the company's business risk profile strengthens, including if regulated utility operations materially increase as a percentage of total operations. We could also raise the ratings if business risk continues to focus on its core regulated utility operations, while financial measures strengthen and consistently exceed our base-case forecast, including adjusted FFO to total debt consistently above 20%, the high end of the significant financial risk profile category. Stronger financial measures could occur for various reasons, including through higher operating cash flow due to economic growth in the utilities' service territories, debt reduction with free operating cash flow, or greater equity funding of investments.

Ratings Score Snapshot

Corporate Credit Rating: A/Stable/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

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Ratings Affirmed; Outlook Action
                                        To                  From
Berkshire Hathaway Energy Company
Sierra Pacific Power Co.
PacifiCorp
MidAmerican Energy Co.
 Corporate Credit Rating                A/Stable/A-1        A/Negative/A-1

MidAmerican Funding LLC
 Corporate Credit Rating                A/Stable/--         A/Negative/--

NV Energy Inc.
Nevada Power Co.
 Corporate Credit Rating                A/Stable/NR         A/Negative/NR

Ratings Affirmed

Berkshire Hathaway Energy Company
 Senior Unsecured                       A-
 Commercial Paper                       A-1

MidAmerican Energy Co.
 Senior Secured                         A+
   Recovery Rating                      1+
 Commercial Paper                       A-1

MidAmerican Funding LLC
 Senior Secured                         A-

NV Energy Inc.
 Senior Unsecured                       A-

Nevada Power Co.
 Senior Secured                         A+
   Recovery Rating                      1+

PacifiCorp
 Senior Secured                         A+
   Recovery Rating                      1+
 Preferred Stock                        BBB+
 Commercial Paper                       A-1

Sierra Pacific Power Co.
 Senior Secured                         A+
   Recovery Rating                      1+
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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.