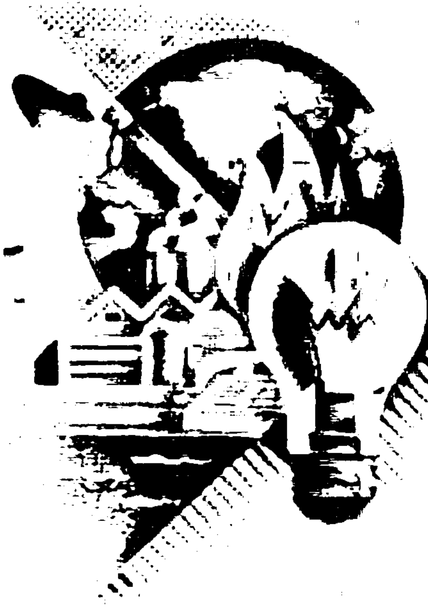
Exhibit No. ___(MPG-4)
Docket Nos. UE-060266/UG-060267
Witness: Michael P. Gorman

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. PUGET SOUND ENERGY, INC., Respondent.	**Docket No. UE-060266** **Docket No. UG-060267**

EXHIBIT NO. ____ (MPG-4)

CREDIT RATING REPORTS

July 19, 2006



Standard & Poor's

UTILITIES & PERSPECTIVES

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Downward Credit Pressure Continues on U.S. Power Industry

Rating activity was overwhelmingly negative for U.S. utilities (electric, gas, pipeline, and water) in this year's turbulent third quarter, with several companies experiencing numerous downgrades. Since July 1, 2002, there have been 57 downgrades among holding companies and operating subsidiaries, compared with just eight upgrades (three of which relate to Northern Natural Gas Co.). For the same period in 2001, there were only nine downgrades and five upgrades. The torrid pace of the previous six months (78 downgrades and six upgrades) continued in the third quarter, as did the steep credit decline that began in 2001, when Standard & Poor's recorded 81 downgrades and 29 upgrades. In addition, the third quarter witnessed many new CreditWatch listings and outlook revisions, most of which were negative.

Although U.S. power industry creditworthiness began to weaken before 2001, the California energy crisis and the Enron bankruptcy hastened the negative trend. The erosion can be traced mainly to:

- Weakening financial profiles;
- Loss of investor confidence that has affected liquidity and financing flexibility;
- Heightened business risk derived from more investment outside the traditional regulated utility business, particularly unregulated generation and energy trading and marketing;
- Capital and corporate restructuring efforts;
- Regulatory difficulties; and
- Mergers and acquisitions.

These trends, in turn, reflect companies' strategies to deal with an increasingly uncertain and competitive market, while also seeking to enhance shareholder value.

In just 12 months, the number of companies rated 'A' and above has significantly declined, while the number of firms rated 'BBB' and below has risen substantially. In this regard, about 49% of the industry now falls in the 'BBB' category rating, while a full 11% are rated below investment grade, including five companies that are rated 'D', compared with 40% and 5%, respectively, at the end of September 2001. The decline in the 'A' and 'AA' rating category has been precipitous, with just 40% of the industry carrying ratings of 'A' and above, versus 55% one year earlier. Notably, although the average rating for the power sector as a whole has slipped to 'BBB+', companies that continue to emphasize a vertically integrated structure are hanging onto an 'A-' average. But utility holding companies that have ventured too far afield from their core competencies have suffered weakening market capitalization and, in many instances, rating downgrades.

Despite the large number of rating downgrades and ongoing negative pressures on utility credit quality, the sector remains solidly investment grade. This is in line with the large percentage of companies (86%) that have average or above-average business profiles.

Capital Market Update

Financing activity declined in the past 12 months following a significant increase in 2001. The amount of long-term debt, hybrid preferred securities, and preferred stock issued during the first nine months of 2002 was about $56.9 billion, compared with approximately $61.2 billion issued in the same period in 2001. The decrease is attributable to a number of factors, among them capital market jitters, especially for those issuers that require access to the capital markets, a consequent heavier reliance on bank debt, sliding wholesale electricity prices, and reduced capital expenditures across all sectors, but most significantly as the result of the postponement or cancellation of planned new power plants.

Subpar Financial Measurements

A heavy debt burden has driven down key measures of bondholder protection in recent years. Total debt as a percentage of total capitalization was an aggressive 59.8% at June 30, 2002 (the latest period in which comparable data is available) compared with 54.9% almost four years earlier at year-end 1998. This debt level, while just one measure of financial health, is characteristic of a 'BB' rating category credit with an average business position. Much of the increase in leverage can be traced to debt raised at the parent or intermediate holding company level to fund unregulated activities. The material increase in leverage has not been offset by strengthening cash flows, and funds from operations to total debt has accordingly steadily declined, falling below 16% in June 2002 from 21% in 1998. This key financial ratio is also typical of a 'BB' category company. Funds flow coverage of interest and pretax interest coverage have also slipped, to 3.3 times (x) and 2.8x, respectively, for the rolling 12 months June 2002, from 3.9x and 3.1x in 1998. These levels are just suitable for companies in the 'BBB' rating group. However, the aforementioned ratios actually rose, although very slightly, in 2001 and June 2002 because of lower interest rates. Of course, there are several other financial and qualitative factors that determine credit quality, but given eroding financial parameters and riskier business profiles the median rating for the utility industry may eventually slip out of the high 'BBB' category.

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Looking Ahead

At the end of September 2002, just 48% of all utility rating outlooks were stable, compared with nearly 60% just one year ago. The decline is attributable mainly to the substantial increase in ratings that carry negative outlooks or are listed on CreditWatch. The percentage of outlooks that are negative has reached a high 31%, continuing to strongly overshadow positive outlooks, which stand at just 3%. This results mostly from a proliferation of higher-risk business strategies, constrained access to capital markets due to investor skepticism over accounting practices and disclosure, investigations on various regulatory levels, weak competitive positioning, and an anemic wholesale power market. The remaining 18% of companies are on CreditWatch—84% carry a negative listing, 9% positive, and 7% developing (which indicates that a rating may be raised, lowered, or remain unchanged). These percentages suggest that frequent rating changes will continue.

The Downgraded...

The ratings on Duke Energy Corp., Duke Capital Corp., Westcoast Energy Inc., Union Gas Ltd., and other related subsidiaries were lowered and removed from CreditWatch. The corporate credit rating for Duke Energy Trading and Marketing (DETM), which is 40% owned by Exxon Mobil Corp., was also lowered. Duke Energy Field Services LLC's rating was affirmed. The outlooks are stable.

Lower ratings reflect a reassessment of Duke Energy's consolidated creditworthiness given the increasing risk of energy trading and merchant generation activities. The CreditWatch negative listing is removed because Standard & Poor's does not expect the outcome of the ongoing FERC and SEC investigations into "round-trip" trades to be onerous. Duke Energy has said that less than 1% of its trading revenues came from round-trip trades.

The downgrades also incorporate the financial implications of the current decline in wholesale electricity prices. This deterioration is mitigated by cash flow stability provided by Duke's regulated electric and gas pipeline businesses. Importantly, Duke continues to reduce capital expenditures commensurate with expected reduced cash flow from Duke Energy North America and DETM.

The ratings on Reliant Resources Inc. (RRI) and related entities remain on CreditWatch with negative implications following two downgrades this quarter, pending the refinancing of holding company debt and credit facilities ($5.9 billion, including a $1.4 billion synthetic lease) and debt at RRI subsidiary Orion Power Holdings and its respective subsidiaries ($1.3 billion net of cash). Ratings on RRI subsidiary Reliant Energy Power Generation Benelux B.V. are affirmed

Chart 1

Third Quarter Rating Actions

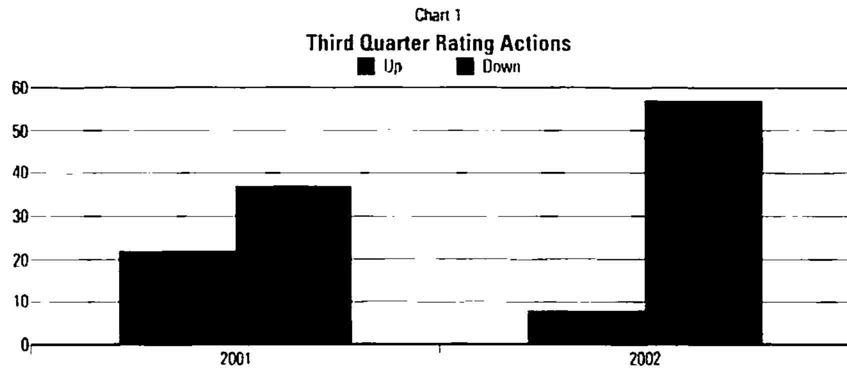
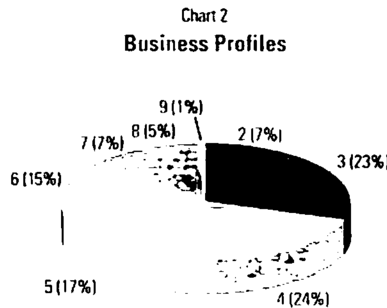


Chart 2

Business Profiles



Business profiles are categorized from "1" (strong) to "10" (weak)

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and remain on CreditWatch as RRI may implement a structure that would insulate this subsidiary.

The rating downgrades reflect increased collateral calls, expectations of a material weakening in credit protection mainly due to the likely increased cost of renewing the bank facilities and expected restrictions on upstreaming cash from Orion Power to RRI, which will limit RRI's ability to service holding company debt. RRI's financial profile is also weakened by the decline in wholesale operations, which is expected to be partially mitigated through 2005 by better-than-expected earnings from the company's Texas retail operations.

CenterPoint Energy Inc.'s (formerly Reliant Energy Inc.) board of directors voted to spin off RRI common stock to CenterPoint shareholders at its Sept. 5, 2002 meeting. Legal separation of the two entities occurred Sept. 30. This should facilitate the current refinancing efforts at both companies.

Ratings on The Williams Cos. Inc. and its subsidiaries were lowered twice in July, resulting in an aggregate five-notch downgrade to 'B+' from 'BBB'. The steep credit decline can be traced to the company's deteriorating liquidity position, as well as rating triggers associated with the AES Ironwood, AES Red Oak, and Georgia EMC tolling agreements, which may require Williams to provide LOCs to each entity. The ramifications of these requirements create significant uncertainty in Williams' financial position and warrant a rating in the 'B' category. These liabilities also add risk to Williams' ability to close on a potential $1.6 billion secured line of credit in the near term or to execute other options to meet liquidity needs. The ratings remain on CreditWatch with negative implications.

The CreditWatch direction on subsidiary Williams Gas Pipelines Central Inc. (Central) was changed to developing from negative on Sept. 17, reflecting the parent's definitive agreement to sell Central to Southern Star Central Corp., a subsidiary of AIG Highstar Capital L.P., for $380 million in cash and the assumption of $175 million in debt. The CreditWatch developing listing reflects the uncertainty surrounding the disposition of the $175 million of senior notes at Central. Assuming that the transaction closes, the rating could be raised, lowered, or withdrawn, depending on how the new owner structures the acquisition.

Dynegy Inc. and subsidiaries Dynegy Holdings Inc., Illinova Corp., and Illinois Power Co. had ratings lowered twice, resulting in a four-notch downgrade to 'B+'. The first downgrade to 'BB' from 'BBB-' was attributable to continuing erosion in Dynegy's core merchant energy business, difficulties in accessing the capital markets and a strained liquidity position. Despite cost savings and cutbacks in capital expenditures, including a reduction in the common dividend payout, needed incremental cash flow had been slow to

Chart 3
Third Quarter Rating Distributions

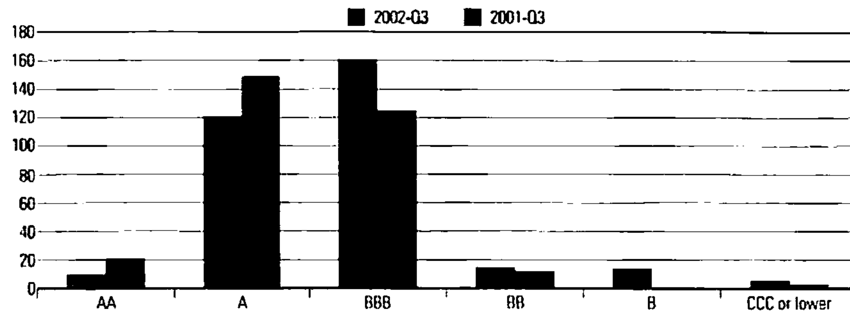
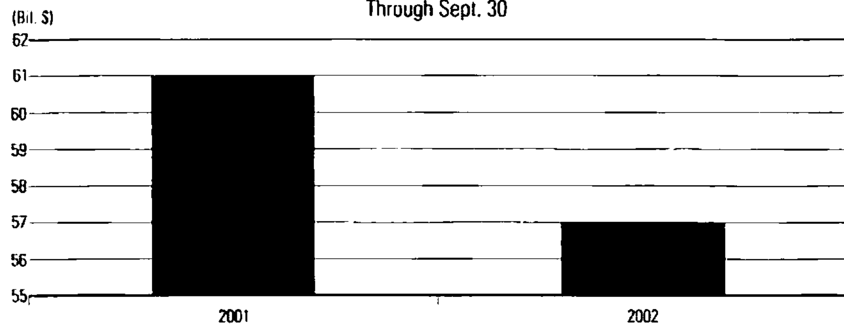


Chart 4
Debt and Preferred Stock Issuance
Through Sept. 30



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materialize largely due to decreased marketing opportunities and lower power prices. Standard & Poor's again lowered the ratings to 'B+' following an analysis that cash flow deterioration continues unabated. Cash flow from Dynegy's merchant energy business is expected to decline even further because it is likely industry counterparties are engaging in only low-margin spot gas transactions, a trend that is expected to continue.

The ratings remain on CreditWatch with negative implications, reflecting lingering concerns regarding the firms' ability to access capital markets and/or execute asset sales necessary to preserve an adequate liquidity position to meet its obligations over the next 18 months. Resolution of the CreditWatch listing is predicated on Dynegy's execution of stated business objectives and its ability to meet debt maturities at a level that supports the current rating. A demonstrated ability to achieve these goals could result in ratings stability.

Ratings on Aquila Inc. and its subsidiaries were lowered due to a deteriorating financial profile stemming from its involvement in the energy marketing and trading business. The company's decision to abandon that business to focus on regulated utility operations and efforts to improve its financial condition through asset and equity sales were not sufficient to preserve its prior credit quality. The negative outlook can be attributable to the risk that the company will be unable to timely achieve the amount of asset sales necessary to pay down debt to a level appropriate for the new rating.

Kinder Morgan Energy Partners L.P.'s (KMP) ratings were lowered due to a decline in its business risk profile, as well as greater interdependence between KMP and Kinder Morgan Inc., which holds a general partnership interest in KMP. The outlook is stable.

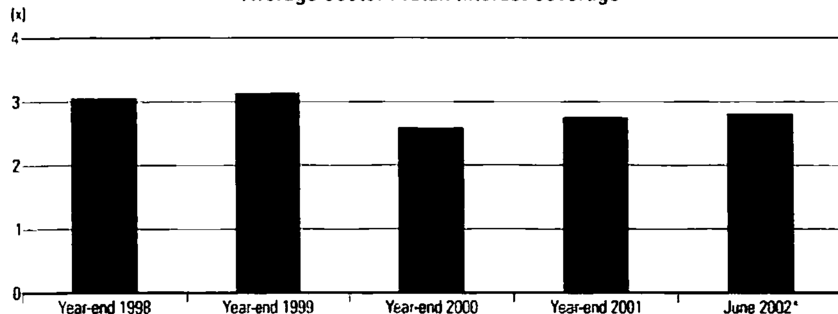
The ratings on CMS Energy Corp.'s subsidiaries Consumers Energy Co. and CMS Panhandle Pipeline Cos. were lowered to 'BB', in line with that of the parent. The downgrade reflects the company's use of the stock of subsidiary CMS Enterprises, which includes CMS Panhandle Pipeline, as security in certain bank facilities to obtain longer-term financing to weather its current liquidity position. In Standard & Poor's view, CMS Energy's actions indicate that the risk of default of CMS Energy and its affiliates is the same because the company relied on an operating subsidiary to meet its own financial commitments during a time of financial stress. The outlook is negative owing to the uncertainty posed by the SEC inquiry and CMS Energy's board of directors' special committee investigation into the round-trip trades. Additional challenges for CMS Energy include execution risk in completing planned asset sales, maintaining adequate liquidity over the near term, and generating cash flow and reducing debt sufficient enough to produce financial measures suitable for its current rating.

TECO Energy Inc. and affiliates saw their ratings lowered two notches owing to lower levels of consolidated cash flow, higher debt balances associated with commitments related to its power unit, and expected credit protection measures that are now commensurate with a 'BBB' corporate credit rating. The outlook for all entities is negative. Despite TECO's action plan and previously issued equity, depressed profitability at TECO Power Services (TPS), combined with weak power prices, presents significant challenges for the firm, including weaker interest coverages and execution risk. The outlook for all entities is negative, reflecting substantial execution risk that the company faces as it implements its action plan, and significant challenges related to activity at TPS, including construction commitments. Still, timely completion of TECO's monetization efforts, combined with successful navigation of TPS risks, could lead to ratings stability.

Allegheny Energy Inc. and its subsidiaries' ratings were lowered to 'BBB' from 'BBB+' on August 16 owing to a weakened financial profile caused by increasing debt leverage and a worse-than-expected downturn in the wholesale power market. Shortly after the close of the third quarter, Standard & Poor's again lowered its ratings to 'BB' from 'BBB' following the company's announcement that its principal credit agreements are under technical default. The ratings are on CreditWatch with negative implications, pending the outcome of the company's negotiations with its banks.

Chart 5

Average Sector Pretax Interest Coverage



*Indicates rolling 12 months

EOTT Energy Partners L.P. experienced a several notch downgrade this quarter with its corporate credit rating slipping to 'CCC' from 'B+'. On Oct. 1, the company's ratings were lowered to 'D' reflecting its failure to make a bond interest payment. The company will be utilizing the 30-day grace period and a forbearance on its bank credit facilities to attempt to reach an agreement on restructuring its debt and to resolve outstanding issues with Enron Corp. An Enron subsidiary is the general partner of EOTT. Since those efforts have been under way for months and have yet to produce any agreements, Standard & Poor's believes it is questionable whether the company will be able to successfully settle all of the necessary issues that will allow it to resume timely payments on its debt.

Lower ratings for SCANA Corp. and affiliates South Carolina Electric & Gas Co. and Public Service Co. of North Carolina Inc. reflect the parent's high debt leverage and the fact that management's previous plan to strengthen the balance sheet is being prolonged by the company's accelerating capital program and the delay in its ability to monetize all of its Deutsche Telekom shares (currently at a lower price than expected). These factors greatly hinder the company's ability to have its key financial ratios return to former levels of credit quality that support an 'A' ratings profile. The outlook is stable.

The ratings on Peoples Energy Corp. and subsidiaries Peoples Gas Light & Coke Co. and North Shore Gas were lowered several notches owing to deterioration in parent company Peoples Energy's consolidated financial profile, coupled with increasing business risk associated with the company's unregulated activities.

UGI Corp.'s electric utility affiliate UGI Utilities Inc. saw its ratings lowered due to increasing business risk at the parent. The stable outlook mirrors that of parent UGI Corp. and reflects its ability to continue to manage the challenges of a growing propane business while adequately maintaining the utility's financial condition.

Lower ratings for Empire District Electric Co. reflect a downward trend in the company's financial profile that was not adequately stemmed in recent regulatory actions. The outlook is stable.

NRG's Precipitous Credit Decline

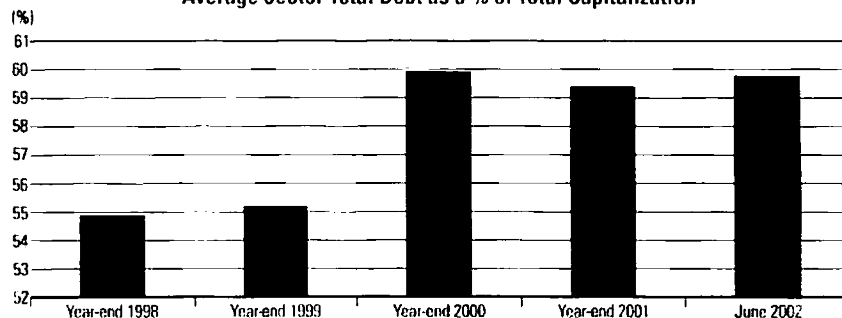
NRG Energy Inc., the independent power producer subsidiary of Xcel Energy Inc., experienced the most dire credit spiral this quarter, with its corporate credit rating lowered to 'D' from a 'BBB-'.

On June 3, 2002, Xcel completed a tender for the shares of NRG that it did not already own. Xcel's management then began to re-integrate NRG into Xcel. Xcel proposed improving NRG's financial position through significant asset sales and a cash infusion from Xcel. (Before the tender offer, NRG was rated 'BBB-', mainly reflecting its stand-alone credit quality. However, the rating always incorporated some level of implicit support from Xcel.) On June 24, 2002, Standard & Poor's lowered its corporate credit rating on Xcel and its subsidiaries, including NRG, to 'BBB'. The levelization of the ratings reflected repurchase of all NRG shares and the reintegration of the business into Xcel's corporate structure.

Notwithstanding Xcel's restructuring plan, NRG's financial position worsened as a result of low wholesale prices and a heavy debt burden. Exacerbating low operating cash flow was the uncertainty of the timing and amount of asset sales, which were not occurring quickly. NRG's own financial problems began to affect Xcel and its utility subsidiaries' access to capital. Xcel management's support for NRG accordingly began to wane, and with it Standard & Poor's perspective on the levelization of all Xcel's corporate credit ratings. Thus, Standard & Poor's undertook a series of negative rating actions on NRG alone. The downgrades were initially prompted by the poor cash flow position of NRG, and subsequently by the substantial equity calls triggered by the downgrade process (when NRG fell below investment grade, several financing arrangements required capital to be posted). As a result, NRG is currently rated purely on a stand-

Chart 6

Average Sector Total Debt as a % of Total Capitalization



alone basis. On Sept. 16, 2002, NRG's corporate credit rating was lowered to 'D', reflecting a default on four separate issues of corporate and project-level debt service.

The Few Upgrades...

The ratings on LG&E Energy Corp. and its subsidiaries were raised and removed from CreditWatch. The rating action followed the July 1, 2002 acquisition of LG&E's parent company Powergen PLC group by the German utility company E.ON AG, and a review by Standard & Poor's of the operational and financial linkages between the companies. The ratings reflect LG&E's lower stand-alone credit quality, offset by the benefit of being part of the stronger E.ON group. The implied support from E.ON is based on the expectation that LG&E will play an important and long-term role in E.ON's strategy to expand its presence in the U.S. The outlook is stable and reflects the expectation that E.ON will support LG&E's funding requirements, including the refinancing of maturing debt at the E.ON level.

Higher ratings for American Transmission Co. can be traced to favorable FERC rate treatment, organizational efficiencies, and stronger financial measures. The outlook is stable owing to expectations for continued reliable operations and supportive regulation. Also, it is expected that the capital expenditure program will not stress the company's financials and that the member/owner companies will continue to support credit quality.

Mixed Rating Actions

Northern Natural Gas Co. (NNG) experienced numerous rating actions. On July 2, its ratings were raised to 'BBB-' from 'CC' due to the expiration of Enron Corp.'s option to repurchase NNG, which ensured that the firm remained a wholly owned subsidiary of Dynegy Inc. for the time being. Subsequently, on July 25, NNG's ratings were lowered to 'B+', reflecting Dynegy's inability to execute on asset divestitures, including the expected partial monetization of NNG. Because Standard & Poor's viewed the sale as being uncertain, NNG's creditworthiness was considered to be commensurate with the consolidated credit rating of Dynegy. On Aug. 23, NNG's ratings were raised back to 'BBB-' following MidAmerican Energy Holdings Co.'s closing on the purchase of the pipeline from Dynegy. Lastly, on Sept. 25, 2002, NNG's ratings were raised three notches to 'A-' following its change of ownership. NNG is now a wholly owned subsidiary of NNGC Acquisition LLC, which in turn is a wholly owned subsidiary of MidAmerican Energy Holdings. Because of a ring-fencing structure that protects NNG from credit events at the MEHC parent, the rating on NNG is higher than that of its parent. The outlook is stable.

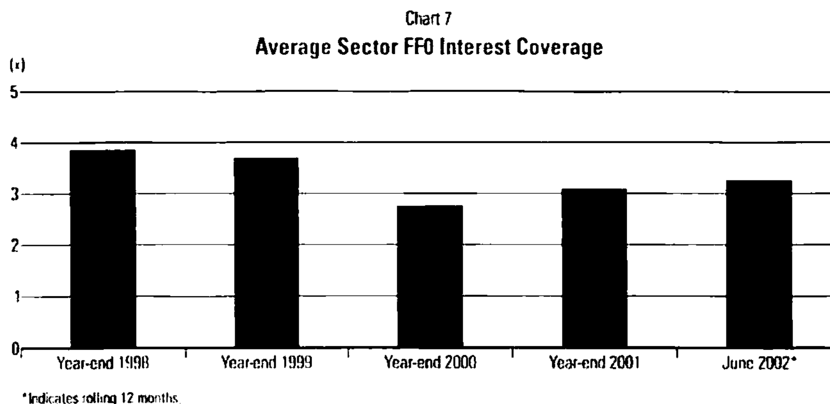
CreditWatch Listings Heat Up

Following a revision in its credit outlook to negative from stable early in August, the ratings on El Paso Corp. and its affiliates were placed on CreditWatch with negative implications on Sept. 23 as a result of the FERC Administrative Law Judge's recommendation that fines be imposed for withholding capacity and exercising market power in California. Standard & Poor's will review the firm's response to regulatory pressures, as well as 2003 projected cash flow and capital spending at the pipeline, exploration and production units, and gathering and processing units. The potential for lower credit ratings is possible after Standard & Poor's review, which will be completed before the end of 2002.

The ratings on Cleco Corp. and its utility, Cleco Power LLC, were placed on CreditWatch with negative implications to reflect the worsening credit quality of the counterparties in the company's tolling agreements and financing risk associated with the Acadia power project.

The tolling agreement with Williams Energy Marketing on Cleco's Evangeline project could be affected by the eroding credit quality at The Williams Cos. Inc., which is deeply speculative grade. Cleco also has tolling agreements with other counterparties that are experiencing deteriorating creditworthiness, which could affect the expected cash flows from the projects that contribute support for Cleco's

Chart 7
Average Sector FFO Interest Coverage



*Indicates rolling 12 months.

current ratings. Cross-default provisions in Cleco's corporate credit facility may also be triggered by credit events at one or more of the power projects.

Current ratings are also predicated on the completion of nonrecourse financing of the Acadia power project, which is questionable. If Acadia-related debt remains fully recourse to Cleco, credit protection measures for Cleco would not support current ratings.

Resolution of the CreditWatch listing will occur when the impact of the credit deterioration at Williams on the Evangeline project becomes clearer and when substantial progress has been achieved in Acadia's re-financing.

Nicor Inc. and subsidiary Nicor Gas Co. had their ratings placed on CreditWatch with negative implications following accounting problems and losses related to the Nicor's 50% ownership in Nicor Energy LLC, a retail energy marketing joint venture with Dynegy Inc., possible improper behavior in the company's performance-based rate program, and the immediate and severe negative market reaction to the company's announcements. Although the losses recorded are mainly noncash, relatively small for the consolidated entity, and have not affected the company's robust financial profile and solid liquidity position, the potential for further disclosures could result in subsequent charges and restatements.

The ratings on Pennsylvania Suburban Water Co. were placed on CreditWatch with negative implications owing to parent Philadelphia Suburban Corp.'s agreement to purchase AquaSource Utility Inc., a DQE Inc. subsidiary, for $205 million. The transaction is expected to close in the second half of 2003. Of credit concern is the potential for consolidated financials to weaken if the transaction is largely debt-financed.

More Negative Outlooks

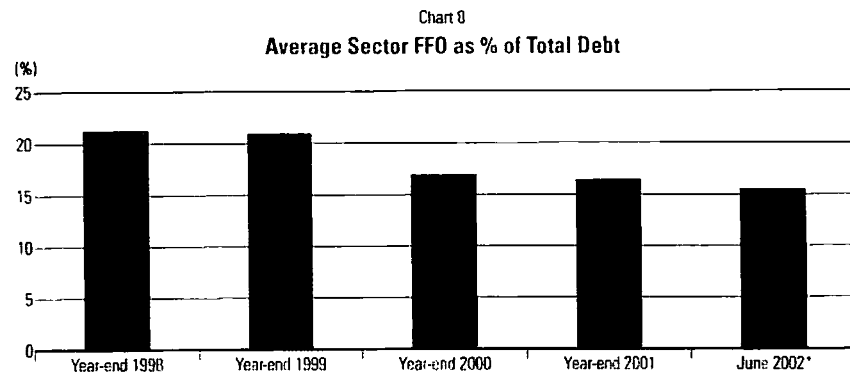
PPL Corp. and its subsidiaries, except PPL Electric Utilities which is structurally ring-fenced, had their outlooks changed to negative from stable, reflecting PPL's deteriorating credit profile that has resulted primarily from declining wholesale electricity prices and also from setbacks in its international operations, particularly in Brazil. PPL's management will also have to balance the level of debt financing in its capitalization with the pace of its growth strategy.

The credit outlook on TXU Corp. was revised to negative from stable, reflecting a deterioration in TXU Europe Ltd.'s creditworthiness. TXU Europe represents about one-third of TXU Corp.'s global income and has more than one-half of all its customers. TXU Australia Holdings (Partnership) L.P., which represents a much smaller percentage of assets and customers, is also highly leveraged. The ratings of both subsidiaries benefit from the relatively strong cash flow and improving financial profile of TXU US Holdings, which owns the electric and gas distribution businesses in Texas. TXU US Holdings will reduce debt by over $1 billion when securitized in 2003 and 2004. Debt is also being reduced with proceeds from the sale of generating plants in the U.K. and Texas, and from the issuance of common stock and convertible debt. Debt will continue to be reduced using cash flow and the conversion of existing securities. However, with the diminished prospects for profitability in Europe, and the likelihood of limited returns from the Australian operations in the short-to-medium term, it is less likely that strengthening financials in the U.S. will be sufficient to support the current corporate credit rating for the consolidated company.

The ratings on Puget Energy Inc. and subsidiary Puget Sound Energy Inc. (Puget) were affirmed and removed from CreditWatch, reflecting an agreement among various parties to Puget's interim and general rate requests. Recent resolution of the utility's general rate case with the Washington Utilities and Transportation Commission is considered by Standard & Poor's to be supportive of Puget's credit quality. Yet, the outlook is negative owing to weak financial measures and concern that Puget Energy and the utility might not be able to achieve current projections, which indicate that both entities should achieve financial targets commensurate with current ratings by 2004 and 2005.

Chart 8

Average Sector FFO as % of Total Debt



*Indicates rolling 12 months.

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Rating Stability

The ratings on Northwest Natural Gas Co. were removed from CreditWatch with negative implications, where they were placed Oct. 8, 2001, following the company's announcement that it agreed to purchase Portland General Electric Co., a unit of Enron Corp. On May 17, 2002, Enron and Northwest Natural mutually agreed to terminate the contract following Enron's inability, following its bankruptcy, to satisfy the terms of the contract as originally agreed upon. The sale contract's termination was subject to bankruptcy court approval, which was formally given on June 20, 2002 and was effective July 1, 2002. The outlook is stable.

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Research:

Industry Report Card: U.S. Electric/Water/Gas

Publication date: 04-Jan-2005

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Commentary/Key Trends

Rating actions in the regulated U.S. utility (electric, gas, pipeline, and water) and merchant power sectors over the past few months were fairly balanced. Since the last report card (for the third quarter of 2004), there were nine upgrades and eight downgrades.

A few noteworthy trends have emerged as important factors for credit quality. These include the rising importance of regulatory decisions in certain states, the acceleration of merger and acquisition activity, a low interest rate regimen, and attractive debt capital markets that allow many issuers to refinance at favorable rates. Despite these trends, challenges associated with weak financial credit measures and stagnant power markets in many regions pressure the financial performance of certain issuers.

Regulatory treatment has become a more prevalent ratings driver in certain jurisdictions. Filings and rulings on rate proceedings in states such as Arizona, Oregon, Missouri, and Texas could affect ratings in the near term. In addition, the opposing views of certain state regulatory bodies and the FERC on issues, such as restructuring the regional transmission systems and incorporating certain merchant plants of affiliated companies in the rate base, will likely lead to a protracted struggle among those regulatory bodies for oversight.

Regulatory decisions were meaningful factors in the downgrades of DTE Energy Co. (BBB/Stable/A-2) and IDACORP Inc. (BBB+/Stable/A-2). In the case of IDACORP, a disappointing regulatory decision compounded by weak credit measures led to the downgrade. For Detroit Edison Co., a unit of DTE Energy, despite the granting of a rate order that provided a substantial increase in rates and contained many favorable characteristics, the credit measures would not improve enough in the near term to be commensurate with the ratings.

Another development that has become a more prominent ratings issue is merger and acquisition activity. Recently, Exelon Corp. (A-/Watch Neg/A-2) announced a merger with Public Service Enterprise Group Inc. (BBB/Watch Dev/A-3) that would create the industry's largest utility holding company. Exelon's ratings were placed on CreditWatch with negative implications while PSEG's ratings were placed on CreditWatch with developing implications. The ratings on NUI Utilities Inc. (A-/Negative/--) and the outlook on AGL Resources Inc. (A-/Negative/A-2) were also affected by their transaction, which was completed in December. In addition, Illinois Power Co. (A-/Negative/--) was upgraded, upon the completion of its acquisition by Ameren Corp. (A-/Negative/A-2). While it is unclear whether these transactions presage a rise in merger and acquisition activity, there apparently is increasing interest.

The number of rating actions during 2004 declined dramatically from the past few years. The number of rating actions (upgrades and downgrades) is only about one-third of the previous two years. This is

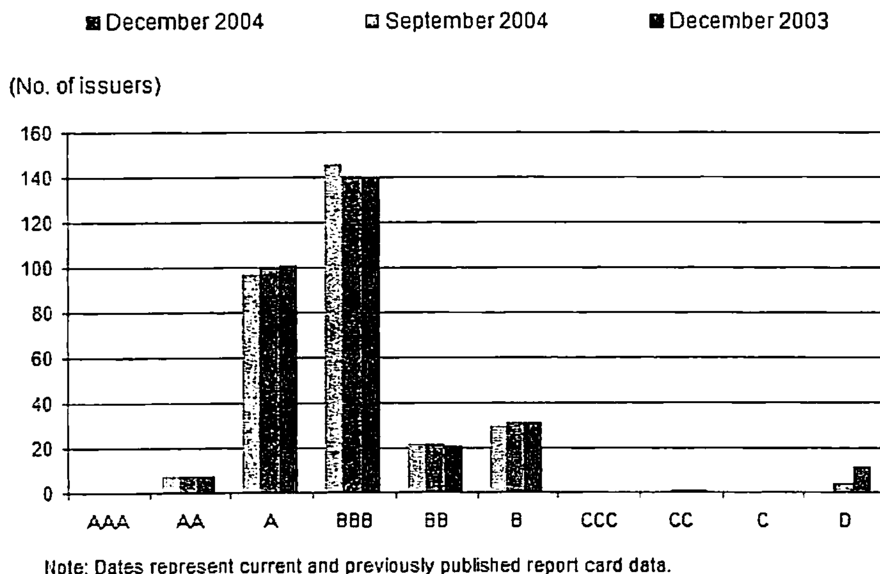
indicative of a measure of rating stability, which is indeed apparent in rating outlooks, 56% of which are stable. This is also a reflection of slowly stabilizing credit measures as many management teams have made "balance sheet repair" a key business objective. For example, Duke Energy Corp.'s outlook was revised to positive in recognition of significant debt reduction in 2004 and improved credit measures.

Still, weak credit measures and financial performance leave certain issuers susceptible to rating downgrades. The existing financial weakness of many utilities results primarily from high debt levels and cash flow stress associated with unsuccessful forays into more competitive businesses. Consequently, 37% of rating outlooks are negative or on CreditWatch with negative implications. Moreover, despite the current industry trend of "back-to-basics," it is very possible in the longer term that the competition for capital and investor interest will embolden companies to embrace growth strategies that could erode credit quality.

Companies with merchant exposure continue to experience volatile cash flows and regulatory uncertainty. The operating environment remains challenging. The creditworthiness of many purely merchant power companies is constrained by burdensome debt levels and insufficient cash flow from operations. Faced with the prospect of stagnant power markets in many regions, cash flow measures are likely to remain weak until wholesale electricity margins materially improve. The only bright spot in this otherwise dim market are merchant coal and nuclear plants that are benefiting from their lower cost of generation in markets, where elevated gas prices set power prices.

Chart 1

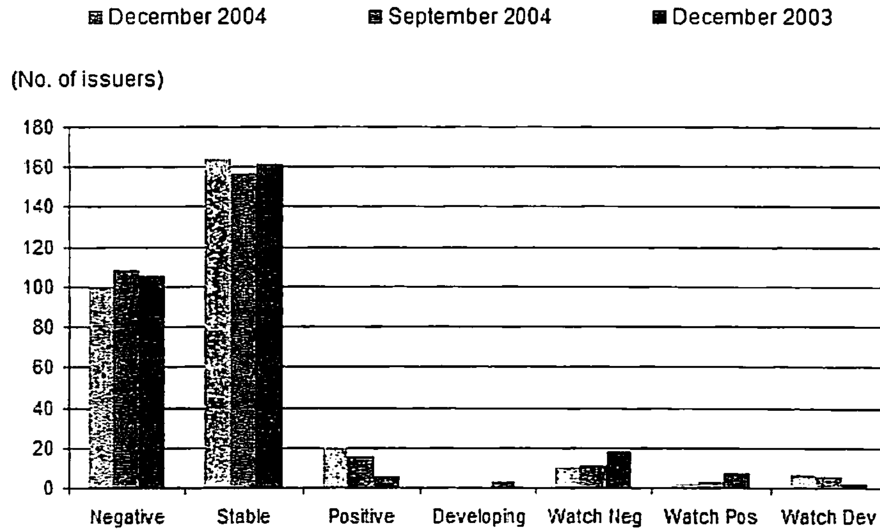
U.S. Utilities Long-Term Ratings Distribution



Note: Dates represent current and previously published report card data.

Chart 2

U.S. Utilities Outlook Distribution



Note: Dates represent current and previously published report card data.

Issuer Review

Table 1 U.S. Electric/Water/Gas			
Issuer	Corporate credit rating*	Analyst	Comment
AES Corp. (The)	B+/Positive/--	Taylor	Standard & Poor's expects AES to continue on its path of parent level debt reduction going forward and that the company can lower parent level debt to about $4.5 billion over the next 12 to 18 months, in which case an upgrade to 'BB-' is likely. Fairly sizable distributions from developing economies such as Venezuela, Nigeria, and Argentina in 2004 are helpful, but expectations of continuing dividends from these economies present risk. AES may begin to ramp up equity investment in new projects in the near future.
Indianapolis Power & Light Co.	BB+/Positive/--	Eiseman	See The AES Corp.
IPALCO Enterprises Inc.	BB+/Positive/--	Eiseman	See The AES Corp.
AGL Resources Inc.	A-/Negative/A-2	Messer	The negative outlook reflects AGL's challenge of successfully realizing cost savings at NUI and Standard & Poor's expectation that cash flow to total debt and debt leverage are likely to remain weak for the 'A-' category through 2007. Standard & Poor's estimates that interest coverage ratios will be between 3.5x and 3.7x in 2005 and remain appropriate for the 'A-' rating category; however, funds from operations to average total debt is expected to remain weak (between 18% and 20%) through 2007.
Atlanta Gas Light Co.	A-/Negative/--	Messer	See AGL Resources Inc.
Allegheny Energy Inc.	B+/Positive/--	Hsieh	Allegheny has stabilized its credit profile and paved the way for financial recovery in the coming years. The company continues to make progress bolstering its balance sheet. The company's stated goal is to pay down $1.5 billion of debt by the end of 2005. With $200 million of equity issued in October, the company has paid down $900 million of debt to date, and is likely to pay down another $200 million of debt in the first quarter of 2005 with proceeds from asset sales.

Blue Chip Economic Indicators

Top Analysts' Forecasts Of The U.S. Economic Outlook For The Year Ahead

Vol. 31, No. 3
March 10, 2006

Long-Range Consensus U.S. Economic Projections

II. For comparison, this table includes some of the long-range consensus projections found on the preceding page, plus the latest long-range projections from the Bush Administration[1] and the Congressional Budget Office (CBO)[2].

ECONOMIC VARIABLE		2008	2009	2010	2011	2012	Five-Year Averages 2008-12	Five-Year Averages 2013-17
		Percent Change, Full Year-Over-Prior Year						
1. Real GDP	**CONSENSUS**	**3.1**	**3.1**	**3.1**	**2.9**	**3.0**	**3.1**	**3.0**
(chained, 2000 dollars)	Bush Admin.[1,3]	3.3	3.1	3.1	3.1	na	3.2	na
	CBO[2,3]	3.4	3.3	3.0	2.8	2.7	3.0	2.6
2. GDP Chained Price Index	**CONSENSUS**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**
	Bush Admin.[1,3]	2.1	2.1	2.1	2.1	na	2.1	na
	CBO[2,3]	1.8	1.8	1.8	1.8	1.8	1.8	1.8
3. Nominal GDP	**CONSENSUS**	**5.3**	**5.3**	**5.2**	**5.1**	**5.2**	**5.2**	**5.2**
(current dollars)	Bush Admin.[1,3]	5.5	5.3	5.3	5.3	na	5.4	na
	CBO[2,3]	5.3	5.2	4.9	4.6	4.5	4.9	4.4
4. Consumer Price Index	**CONSENSUS**	**2.3**	**2.3**	**2.3**	**2.3**	**2.3**	**2.3**	**2.4**
(for all urban consumers)	Bush Admin.[1,3]	2.4	2.4	2.4	2.5	na	2.4	na
	CBO[2,3]	2.2	2.2	2.2	2.2	2.2	2.2	2.2
		Annual Average						
5. Treasury Bills, 3-Month	**CONSENSUS**	**4.7**	**4.7**	**4.7**	**4.5**	**4.6**	**4.6**	**4.6**
(percent per annum)	Bush Admin.[1,3]	4.3	4.3	4.3	4.3	na	4.3	na
	CBO[2,3]	4.4	4.4	4.4	4.4	4.4	4.4	4.4
6. Treasury Notes, 10-Year	**CONSENSUS**	**5.4**	**5.5**	**5.5**	**5.4**	**5.5**	**5.5**	**5.5**
(yield per annum)	Bush Admin.[1,3]	5.5	5.6	5.6	5.6	na	5.6	na
	CBO[2,3]	5.2	5.2	5.2	5.2	5.2	5.2	5.2
7. Unemployment Rate	**CONSENSUS**	**4.8**	**4.8**	**4.9**	**4.9**	**5.0**	**4.9**	**4.9**
(% of civilian labor force)	Bush Admin.[1,3]	5.0	5.0	5.0	5.0	na	5.0	na
	CBO[2,3]	5.1	5.2	5.2	5.2	5.2	5.2	5.2

III. In this table, we compare the results of our most recent survey with those of our survey in October 2005[4].

ECONOMIC VARIABLE		2008	2009	2010	2011	2012	Five-Year Averages 2008-12	Five-Year Averages 2013-17
		Percent Change, Full Year-Over-Prior Year						
1. Real GDP	**March Consensus**	**3.1**	**3.1**	**3.1**	**2.9**	**3.0**	**3.1**	**3.0**
(chained, 2000 dollars)	October Consensus	3.2	3.1	3.3	3.2	na	na	na
2. GDP Chained Price Index	**March Consensus**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**	**2.1**
	October Consensus	2.3	2.2	2.3	2.2	na	na	na
3. Nominal GDP	**March Consensus**	**5.3**	**5.3**	**5.2**	**5.1**	**5.2**	**5.2**	**5.2**
(current dollars)	October Consensus	5.5	5.4	5.5	5.4	na	na	na
4. Consumer Price Index	**March Consensus**	**2.3**	**2.3**	**2.3**	**2.3**	**2.3**	**2.3**	**2.4**
(for all urban consumers)	October Consensus	2.5	2.5	2.4	2.5	na	na	na
		Annual Average						
5. Treasury Bills, 3-Month	**March Consensus**	**4.7**	**4.7**	**4.7**	**4.5**	**4.6**	**4.6**	**4.6**
(percent per annum)	October Consensus	4.4	4.3	4.4	4.4	na	na	na
6. Treasury Notes, 10-Year	**March Consensus**	**5.4**	**5.5**	**5.5**	**5.4**	**5.5**	**5.5**	**5.5**
(yield per annum)	October Consensus	5.3	5.3	5.4	5.4	na	na	na
7. Unemployment Rate	**March Consensus**	**4.8**	**4.8**	**4.9**	**4.9**	**5.0**	**4.9**	**4.9**
(% of civilian labor force)	October Consensus	4.9	4.9	5.0	4.9	na	na	na

[1]*Budget of the United States Government, Fiscal Year 2007*, Office of Management and Budget. February 2006. [2]*The Budget and Economic Outlook: Fiscal Years 2007-2016;* Congressional Budget Office, February 2006. [3]The Bush Administration's forecast only extends through 2011, so averages for the 2008-2012 period are based on the forecast for the four-year period 2008-2012. CBO's forecast only extends through 2016, so averages for the 2013-2017 period are based on the forecast for the four-year period 2013-2016. [4]*Blue Chip Economic Indicators*, October 10, 2005.

Aspen Publishers

Blue Chip Financial Forecasts

Top Analysts' Forecasts Of U.S. And Foreign Interest Rates, Currency Values And the Factors That Influence Them

Vol. 25, No. 7 July 1, 2006

Wolters Kluwer
Law & Business

Consensus Forecasts Of U.S. Interest Rates And Key Assumptions[1]

	History								Consensus Forecasts-Quarterly Avg.					
	Average For Week Ending				Average For Month			Latest Q*	3Q	4Q	1Q	2Q	3Q	4Q
Interest Rates	June 16	June 9	June 2	May 26	May	Apr.	Mar.	2Q 2006	2006	2006	2007	2007	2007	2007
Federal Funds Rate	5.00	4.99	5.01	4.98	4.94	4.79	4.59	*4.91*	5.3	5.4	5.4	5.2	5.1	4.9
Prime Rate	8.00	8.00	8.00	8.00	7.93	7.75	7.53	*7.89*	8.3	8.4	8.4	8.2	8.1	8.0
LIBOR, 3-mo.	5.34	5.28	5.25	5.21	5.18	5.07	4.92	*5.18*	5.5	5.6	5.5	5.4	5.2	5.1
Commercial Paper, 1-mo.	5.10	5.02	4.99	4.98	4.95	4.80	4.61	*4.93*	5.4	5.5	5.4	5.3	5.1	5.0
Treasury bill, 3-mo.	4.89	4.86	4.84	4.83	4.84	4.72	4.63	*4.81*	5.2	5.3	5.2	5.1	4.9	4.8
Treasury bill, 6-mo.	5.16	5.06	5.05	5.01	5.01	4.90	4.79	*5.00*	5.3	5.4	5.4	5.2	5.1	5.0
Treasury bill, 1 yr.	5.13	5.04	5.03	4.99	5.00	4.90	4.77	*4.99*	5.3	5.4	5.4	5.3	5.2	5.1
Treasury note, 2 yr.	5.09	5.00	5.00	4.96	4.97	4.89	4.73	*4.96*	5.3	5.3	5.3	5.2	5.1	5.0
Treasury note, 5 yr.	5.02	4.95	4.99	4.95	5.00	4.90	4.72	*4.96*	5.3	5.3	5.3	5.2	5.2	5.1
Treasury note, 10 yr.	5.05	5.01	5.08	5.05	5.11	4.99	4.72	*5.05*	5.3	5.3	5.3	5.3	5.3	5.3
Treasury note, 30 yr.	5.09	5.07	5.18	5.15	5.20	5.06	4.73	*5.12*	5.3	5.4	5.4	5.4	5.4	5.3
Corporate Aaa bond	5.83	5.81	5.91	5.90	5.95	5.84	5.53	*5.88*	6.2	6.3	6.3	6.3	6.3	6.2
Corporate Baa bond	6.71	6.67	6.75	6.72	6.75	6.68	6.41	*6.71*	7.1	7.2	7.2	7.2	7.2	7.1
State & Local bonds	4.58	4.48	4.57	4.52	4.59	4.58	4.44	*4.57*	4.9	5.0	5.0	5.0	5.0	5.0
Home mortgage rate	6.63	6.62	6.67	6.62	6.60	6.51	6.32	*6.58*	6.8	6.9	6.9	6.9	6.8	6.8
	History								Consensus Forecasts-Quarterly Avg.					
	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q*	3Q	4Q	1Q	2Q	3Q	4Q
Key Assumptions	2004	2004	2005	2005	2005	2005	2006	2006	2006	2006	2007	2007	2007	2007
Major Currency Index	86.5	81.9	81.3	83.5	84.7	85.8	84.9	*82.1*	81.9	81.1	80.6	79.9	79.6	79.5
Real GDP	4.0	3.3	3.8	3.3	4.1	1.7	5.3	*2.9*	2.9	2.9	2.8	2.9	3.0	3.1
GDP Price Index	1.5	2.7	3.1	2.6	3.3	3.5	3.3	*3.0*	2.4	2.4	2.5	2.3	2.2	2.2
Consumer Price Index	2.1	3.6	2.3	3.8	5.5	3.3	2.2	*4.4*	2.7	2.5	2.5	2.4	2.4	2.3

[1]Individual panel members' forecasts are on pages 4 through 9. Historical data for interest rates except LIBOR is from Federal Reserve Release (FRSR) H.15. LIBOR quotes available from *The Wall Street Journal*. Definitions reported here are same as those in FRSR H.15. Treasury yields are reported on a constant maturity basis. Historical data for the U.S. Federal Reserve Board's Major Currency Index is from FRSR H.10 and G.5. Historical data for Real GDP and4.64 GDP Chained Price Index are from the Bureau of Economic Analysis (BEA). Consumer Price Index (CPI) history is from the Department of Labor's Bureau of Labor Statistics (BLS). **Interest rate data for 2Q 2006 based on historical data through the week ended May 16th. .Data for 2Q 2006 Major Currency Index also is based on data through week ended May 16th. Figures for 2Q 2006 Real GDP, GDP Chained Price Index and Consumer Price Index are consensus forecasts based on a special question survey this month of the panel members.*