

# Credit Trends in the Gas Sector Amidst the Financial Crisis

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**Moody's Investors Service**

## Overview

### Financial crisis no broad impact on gas credit quality

- Short-term stable sector outlook based on reasonable rate treatment.
- Utilities as “safe haven” for investors.
- Cost of new debt higher but little impact on credit metrics.
- LDCs’ upcoming capital requirements more manageable and certain than for electric utilities and pipelines.



## Credit Perspective on ROE

ROE – indicator of regulatory support and management's investment record

- Allowed ROEs outside 10% industry average – analyzed for impact on earnings stability and cash flow.
- Rate designs that improve stability: decoupling, weather normalization.
- Mechanisms that conserve liquidity: fuel cost recovery and trackers that minimize working capital needs, infrastructure trackers that enable faster recovery of capital outlays.



## ROE – Indicator of Credit Trends

- ROE – indicator of profitability, the basis of cash flow.
- LDCs' peer ratings trended down toward mean of A3 over past decade.
- Very low allowed ROE presents credit risk: subsequent base rate filing, regulatory lag.



## Immediate Fallout from the Financial Crisis

Credit crisis – challenges for a capital intensive business

- LDC business model results in negative free cash flow.
- Capex being curtailed, deferred.
- Liquidity: debt maturities, bank facility renewals.
- Back in vogue: secured debt, operating company debt.



## Long-Term Implications

- More scarce capital allocated to favorable jurisdictions: “virtuous circle” of utility reinvestment, service/reliability, stakeholder satisfaction.
- Parent allocates capital away from LDC to higher risk businesses – negative halo effect, dividend pressure.
- Parent decides to sell LDC – M&A event risk.



## Conclusions

- No immediate impact foreseen from the credit crisis on LDC credit quality.
- Stable sector outlook based on assumption of continued reasonable regulatory support.
- Rate case cycle – regulatory risk returns as catalyst for change in credit ratings, cost of capital.



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