FITCH AFFIRMS BIG RIVERS ELECTRIC CORP. AT 'BB'; OUTLOOK STABLE

Fitch Ratings-New York-04 February 2016: Fitch Ratings affirms its 'BB' rating on the following bonds issued by Big Rivers Electric Corporation (Big Rivers):

--$83.3 million County of Ohio pollution control revenue bonds series 2010A.

The Rating Outlook is Stable.

SECURITY

The bonds are secured by a mortgage lien on substantially all of the Big Rivers' owned tangible assets, which include the revenue generated from the wholesale sale and transmission of electricity.

KEY RATING DRIVERS

OUTLOOK REMAINS STABLE: The Stable Outlook reflects the beneficial results of Big Rivers' mitigation plan, which was put in place following the termination of power supply contracts with two large aluminum smelters. Cost reductions, idling of generation, rate increases, and off-system sales and use of reserve funds have combined to provide improved financial stability.

IMPORTANCE OF WHOLESALE MARKET SALES: While termination of the smelter agreements has eliminated exposure to volatile smelter sales, it leaves Big Rivers with a significant amount of surplus power for sale. A level of success has been achieved in marketing this power both on a contract basis and into the Midcontinent ISO (MISO) spot market, but short-term sales expose the cooperative to greater risk. Big Rivers is aggressively pursuing other contract sales opportunities.

SUPPORTIVE REGULATION: Big Rivers and its three member systems are rate regulated by the Kentucky Public Service Commission (KPSC). Rate increases and supportive regulatory policies, in conjunction with the cooperative's mitigation plan, should allow Big Rivers to meet its near-term financial goals.

ADEQUATE LIQUIDITY: Unrestricted cash and equivalents totaled about $50 million at year-end 2015. Higher cash balances are expected in 2016 and longer term, unrestricted balances are expected to be in excess of $60 million. A $130 million senior secured credit agreement provides added liquidity.

RATING SENSITIVITIES
ADDITIONAL CONTRACT SALES: Increasingly positive results brought about by Big Rivers Electric Corporation's mitigation plan, particularly additional longer-term capacity contract sales, could result in a credit upgrade.

LESS FAVORABLE REGULATORY SUPPORT: A reversal of supportive regulatory policy by the Kentucky Public Service Commission, in the wake of weaker energy sales or impediments to the mitigation plan could adversely impact Big Rivers' financial position and its rating.

CREDIT PROFILE

Big Rivers, a generation and transmission (G&T) cooperative, provides all-requirements wholesale electric and transmission service to three electric distribution cooperatives pursuant to contracts through Dec. 31, 2043. These distribution members provide service to a total of about 114,000 retail customers located in 22 western Kentucky counties. Kenergy Corporation, the largest of the three systems, previously served two large smelters (approximately 65% of G&T revenues), prior to termination of these contracts. This has resulted in a change to Big Rivers' customer profile which is now more residentially based. Financial performance of the three distribution systems is satisfactory and provides adequate support.

System peak demand, net of smelter load, is now around 700 megawatts (MW), approximately half of historical demand. Big Rivers is working aggressively to market the excess power under intermediate-term contracts and through spot sales in MISO. Big Rivers has implemented a mitigation plan with the goal of achieving financial savings and benefits that would help lower member rates. The cooperative's indenture and loan agreements require a margin for interest ratio (MFIR) of at least 1.10x each year.

IDLING OF GENERATION
With the end of the smelter agreements, Big Rivers no longer has an immediate market for power from the 443 MW coal-fired Coleman Station, which began operation in 1969. The plant has been idled and the cooperative continues to evaluate the best use of this facility.

Big Rivers has also considered idling Wilson Station (417 MW). However, this more cost-efficient plant continues to operate, since it affords greater operating flexibility and the ability to sell power when demand is sufficient and pricing attractive. Excess capacity and associated energy is sold under contract, through the spot market or retained for future contracted sales.

RATE ADJUSTMENTS
With the loss of smelter load and revenue, Big Rivers needed to increase its rates and modify its rate structure among its remaining customers. Following KPSC approved rate increases, wholesale base rates (excluding smelters) now approximate $75 per MWH. By 2020, rates are forecast at about $80 per MWH, and projected to remain fairly steady thereafter. The large industrial rate 'All-In' (net) for 2016 is estimated at $63.88 per MWH and for 2020 is estimated at $66.01. Rural retail customers typically pay about 3.5 cents per KWH in addition to the wholesale rate charged.

In 2009, concurrent with the unwinding of a generating asset lease transaction between Big Rivers and E.ON U.S., the KPSC issued rate orders designed to be sufficient to support the cooperative's financial viability, including the establishment of several reserve funds. These funds will be fully utilized by mid-2016. Thus, Big Rivers' financial forecast will no longer include these restricted reserves. Once the reserves are fully utilized, the average rural rate is expected to be approximately 11.6 cents per KWH. Management hopes to maintain member rate stability by crediting future surplus revenues to member rates.

FINANCIAL FORECAST
Big Rivers' previous financial results were affected by a number of unusual events, making it difficult to assess the cooperative's normalized financial performance. Fitch calculated debt service coverage (DSC) was below 1x in calendar years 2012 and 2013, reflecting termination of the smelter agreements, but improved in 2014 helped by implementation of the mitigation plan and enhanced sales brought on by unusually cold weather. Starting in 2016, when restricted reserves are fully utilized and the impact of non-member sales become clearer, a truer picture of the utility's financial standing is likely.

Big Rivers' current financial forecast for 2015 through 2019 assumes total annual operating revenues of around $450 million and annual net margins in excess of $12 million, including an amount of hedged and non-hedged off-system sales. This is forecasted to produce a times interest earned ratio (TIER) of about 1.30x and DSC in the area of 1.25x. The KPSC previously authorized a TIER of 1.30x. While Big Rivers believes rates now in place are sufficient to sustain business operations and maintain reasonable financial ratios, a comprehensive energy sales program remains an important part of the cooperative's business model.

Unrestricted cash and equivalents totaled around $50 million at year-end 2015. On March 5, 2015, the cooperative closed on a new three-year $130 million CFC-led syndicated credit facility. The expanded facility is designed to provide approximately $100 million for normal operating requirements and $30 million to be used as a bridge loan for environmental expenditures, pending RUS long-term financing.

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Applicable Criteria
Revenue-Supported Rating Criteria (pub. 16 Jun 2014)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=750012
U.S. Public Power Rating Criteria (pub. 18 May 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=864007