



Fitch Affirms Big Rivers Electric Corp. at 'BBB-'; Outlook Stable

Fitch Ratings - New York - 04 December 2019:

Fitch Ratings has affirmed the ratings on the following bonds issued by Big Rivers Electric Corporation (BREC) at 'BBB-':

--\$83 million County of Ohio pollution control revenue bonds, series 2010A.

--Issuer Default Rating (IDR).

ANALYTICAL CONCLUSION

The 'BBB-' rating and IDR on Big Rivers Electric Corporation reflects the corporation's elevated but improving leverage profile in relation to its midrange revenue defensibility and strong operating risk profile. Fitch assesses Big River's three members to have midrange credit quality, which coupled with the absence of independent rate-setting authority, constrains the corporation's overall revenue defensibility.

The rating also reflects the corporation's consistently low operating cost burden and supportive regulatory regime. Lastly, Fitch views favorably the re-balancing of Big River's previously long resource position through a combination of greater contracted non-member sales and the retiring and/or idling of existing capacity, which should allow financial margins to remain stable and operating costs low. If margins remain strong and leverage declines further, upward rating movement is possible.

CREDIT PROFILE

Big Rivers Electric Corporation, a non-profit generation and transmission (G&T) cooperative formed in 1961, provides all-requirements wholesale electric and transmission service to three electric distribution cooperatives pursuant to all-requirements contracts through Dec. 31, 2043. The three members provide service to a total of approximately 117,000 retail customers located in 22 western Kentucky counties. Financial performance of the three distribution systems is satisfactory and provides sufficient support for the rating.

KEY RATING DRIVERS

Revenue Defensibility:: 'bbb'

Strong Contractual Framework, Midrange Member Credit Quality

Revenue defensibility is midrange despite otherwise very strong revenue source characteristics provided by all-requirements contracts. The midrange assessment principally reflects the credit quality of the three member utilities along with the regulatory framework within which Big Rivers and its customers operate. While the regulatory regime has been constructive historically, neither Big Rivers nor its three customers have autonomy over rate-setting.

Operating Risk:: 'a'

Coal-Dominated Resource Base, Low Cost Burden

The strong operating risk assessment begins with a low operating cost burden that has averaged 4.85 cents/KWh over the past five years. Operating cost flexibility assessment is neutral as Big River's has idled or retired 695 MWs of coal capacity over the past few years. As a result, reliance on coal-fired capacity is lower than historical amounts and sits just below Fitch's threshold for a neutral assessment. Management expects to add some renewable (solar) capacity over the next several years, which will further diversify the resource base.

Financial Profile:: 'bbb'

Improved Margins, Leverage to Decline

Big River's midrange financial profile reflects elevated but improving leverage ratios. The solid financial results achieved in fiscals 2017 and 2018 are expected to continue as Big Rivers provides contracted energy and capacity to Kentucky Municipal Energy Agency and the city of Owensboro, KY in 2019 and 2020, respectively. In addition, Fitch anticipates lower operating expenses from the reduction in capacity over the past few years coupled with higher non-cash expenses (depreciation) will lead to a further improvement in leverage over the next few years.

Asymmetric Additional Risk Considerations

There are no additional asymmetric risks affecting the rating.

RATING SENSITIVITIES

Improved Leverage: Big Rivers Electric Corporation's ratings and IDR could be upgraded if the financial profile is sustained and leverage continues its positive trend downward over time.

Member Credit Quality: The rating is also sensitive to changes in the credit quality of its three member customers. A shift in member credit quality in either direction could result in a change in Fitch's assessment of revenue defensibility and could lead to a change in the rating.

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 or transmission of electricity.

Revenue Defensibility

Strong Contractual Framework

Revenue source characteristics are very strong. All three of Big Rivers' customers are signed to long-term, all-requirements, take-and-pay power contracts. All costs associated with the delivery of power and energy/services, including debt service on the bonds, are billed to the customers on a monthly basis. There are no step-up provisions in the contracts for non-payment. However, given there are only three members, the rating on the bonds is heavily correlated to the credit quality of all three customers.

Rates are Regulated

The Kentucky Public Service Commission (KPSC) is charged with approving the wholesale and retail rates of Big Rivers' and its members. Wholesale rates charged to the members consist of a demand charge and an energy charge per kWh consumed as approved by KPSC. Big Rivers has certain approved riders including a fuel adjustment clause and an environmental surcharge, which helps provide timely pass-through of variable charges. Supportive regulatory policies and successful rate recovery efforts historically point to a constructive regulatory environment.

Big Rivers' last rate order, received in 2014, approved rates at levels that allowed it to cover total fixed costs on a self-sustaining basis. On the member level, rates are set for full cost recovery. However, while the regulatory environment for rate recovery has been supportive, approval of rate cases by an outside entity could result in delayed revenue recovery, potentially higher revenue variability and weaker overall revenue defensibility compared to non-regulated entities, and thus limits rate flexibility in Fitch's view.

Beginning in 2018, member rates have been set to allow Big Rivers to fully recover its costs from the members (i.e., there are no longer any deferred revenues), which is an important rating factor that underpins the investment grade rating. Fitch believes the stronger margins are sustainable over the intermediate term as Big Rivers begins to benefit for newly contracted sales. The average wholesale power cost to members declined in 2018 to \$71/MWh from about \$76/MWh the previous year. The member rate for 2019 is up to \$72.50 and is forecast to rise again in 2020 to just over \$73.00 but remain at this level for the next few years.

Midrange Purchaser Credit Quality

Revenue defensibility primarily reflects the member (purchaser) credit quality as evaluated using Fitch's purchaser credit index (PCI), which reflects the weighted average credit quality of the relevant obligors. Fitch's PCI score of 3.05 is based on an evaluation of all three member cooperatives; Meade County Rural Cooperative Corporation (Meade), KY comprising 16% of Big River's revenues; Kenergy Corporation, KY (Kenergy, 63% of revenues); and Jackson Purchase Energy Corporation, KY (Jackson, 21% of revenues). The overall scoring for each cooperative ranged from relatively strong to relatively weak.

The PCI takes into account the strength of the member's service area, retail rate competitiveness and ability to absorb rate increases through an analysis of its service area, as well as 2018 financial performance. Fitch assessed the service area characteristics for the two largest members to be midrange based on the relatively low median household income (MHI) and average to above average unemployment rates.

Contributing to Kenergy's midrange score are its proportionally low amount of revenues derived from residential users (23% of total coop revenues) and MHI that is just 84% of the US average. In addition, 2018 financial performance was weak. On the positive side, Kenergy's customer base is slowly growing and retail rates are very affordable. The weak score for Jackson is rooted in its even lower MHI (74% of the U.S. average), relatively high unemployment rate of 6.1%, high retail rates, and very weak 2018 margin and cash cushion. Meade's score was assessed to be the highest of the three, although as the smallest of Big Rivers' members, its strong overall credit profile factors less into the overall PCI.

The three member cooperatives serve small to mid-sized cities and counties, and are geographically located on Kentucky's western border. Economic activity throughout the state is relatively diverse but weighted more heavily in manufacturing and natural resources. Locally, growth in the population and customer base has been steady and the unemployment levels for the communities, while varied, are mostly moderate ranging from 4.4% to as high as 6.1%. A fairly robust transportation network provides access to larger metropolitan areas including Nashville, TN (to the south) and Louisville, KY as well as to St. Louis, MO (northwest) and Indianapolis, IN (north).

Operating Risk

Big River's strong operating risk assessment reflects a consistently low operating cost burden of about 5 cents/KWh since at least 2014. Operating costs are anticipated to remain low as resource capacity is expected to remain sufficient to meet existing member and newly added customer load and capital needs are manageable. In addition, power is supplied mainly by low-cost vintage generating units and contracted purchases, all of which is further supported by access to the MISO market.

Operating Cost Flexibility

Fitch assesses Big River's operating cost flexibility as neutral as its past reliance on coal-fired generation has declined. The assessment takes into account the corporation's current resource base that includes four owned generating facilities (all coal) as well as contracted hydroelectric capacity. In 2019, approximately 78% of total capacity is coal-fired, followed by hydro capacity at 16% and a small amount of natural gas.

Big Rivers currently owns and operates 1,000 MWs of net generating capacity consisting of the following coal-fired facilities: Green generating station, a two-unit 454 MW facility that has the ability to burn high Sulphur, low cost coal; Wilson generating station, a 417 MW single unit facility; and the smallest of BR's generating assets - Reid Station (130 MW). In addition, Big Rivers also receives power through contract with Southeastern Power

Administration (SEPA) for 178 MWs of hydroelectric capacity, bringing total current capacity to over 1,100 MWs. Big Rivers' 2017 decision to idle the 443 MW three-unit Coleman Station has helped improve its resource mix.

Not included in the assessment cost flexibility assessment is the capacity from the coal-fired plant owned by the city of Henderson, KY. Pursuant to a long-standing agreement with Henderson, Big Rivers received the surplus energy from the plant after Henderson's own retail needs were met, which had been roughly equivalent to 180MW-190MW per year. The Henderson plant was no longer capable of providing economical, continuous and reliable operation, leading both parties to agree to de-commission it in early 2019. The retirement of the Henderson plant, which was approved by regulators in late 2018, resulted in the elimination of a net operating loss on the asset of roughly \$13 million annually.

Environmental Considerations

The Commonwealth of Kentucky does not currently have a renewable portfolio standard. However, Big Rivers issued a request for proposal to add up to 150 MWs of solar capacity. The expectation is to enter into a 20 year purchase power agreement at a fixed price. A short list of respondents and potential projects is currently being evaluated. The additional capacity is not expected to be available for at least several years. However, once available, capacity from coal resources will decline to around 70%.

Capital Planning and Management

Capital planning and management are assessed to be midrange. Big Rivers has an exceptionally high, Fitch-calculated average age of plant of 49 years in 2018, which indicates high life-cycle needs. This is somewhat offset by capital spending that has averaged 131% of annual depreciation over the past five years and an anticipated acceleration in annual depreciation expense and approval to treat several of its generating facilities as regulatory assets is received over the near term.

The regulatory asset designation will allow Big Rivers to include a larger proportion of the depreciation of these assets in its rating case with regulators for enhanced future cost recovery. Management anticipates capital spending for 2019-2023 to total a fairly sizeable \$355 million, which continues a recent trend of sound capital reinvestment undertaken over the past few years. Roughly \$250 million in additional debt is expected to be issued to fund the proposed capital spending.

Reduction in Long Generation Portfolio Position

Big Rivers historically provided capacity and energy to its members through a combination of multiple owned generation stations, including a leased facility (Henderson Station 2) and power purchases. After the loss of load attributable to the two large aluminum smelters, system peak demand declined to around 650 MWs, or roughly half of historical demand, leading to a very long resource position. To address this, Big Rivers implemented a mitigation plan with the goal of achieving financial savings and benefits that would help lower member rates. The plan included aggressively marketing the excess power under intermediate-term contracts and through spot sales in MISO.

More recently, growth in the existing customer base coupled with the signing of bi-lateral contracts with Kentucky Municipal Energy Agency (KyMEA, A/Stable), a consortium of Nebraska-based utilities, and full requirements sales to the city of Owensboro, KY (beginning in 2020) significantly increases contracted (non-member) sales and lowers reliance on short-term markets. In addition, the idling of the capacity at Coleman station and de-commissioning of the Henderson plant reduces total capacity to a manageable reserve of around 10% of total expected peak demand by 2020 (1,179 MW of capacity vs 1,026 MW of peak demand).

Operations at the Coleman plant (443 MW) were initially idled in 2014. Coleman is expected to be retired in the near term.

The wholesale customers in Nebraska began receiving energy in 2018, but full requirements capacity and energy totaling 85 MWs will phase in over time. KYMEA's 100 MW of firm purchases began May 1, 2019 and is followed by the city of Owensboro's agreement to purchase full requirements (165 MW) from Big Rivers beginning in mid-2020. The inclusion of these intermediate term contracts brings some predictability to the revenue base, which coupled with the idling and retiring of certain generating assets right-sizes the total resource needs relative to member and contracted demand. Big Rivers is expected to add up to 150 MW of solar in the coming years, 100 MW of which will be used to meet the expected 200 MWs of new demand from Nucor Steel.

Financial Profile

Improved Financial Results

Big Rivers filed a rate case with the Kentucky Public Service Commission (KPSC) in 2013 requesting an increase in rates to levels that would provide full cost recovery of system obligations. The KPSC granted the new rates in 2014, but the full effect of the increases were not realized until fiscal 2017, as previously set aside reserves were used to keep member rates low over several years leading up to 2017.

Fitch-calculated debt service coverage improved to 1.30x in fiscal 2017 (and to 1.36x in 2018) from very weak levels previously, and coverage of full obligations improved to 1.28x by 2018. Audited fiscal year Sept. 30, 2019 results are not expected to be available for several months, but are anticipated to be sound once again. The improved performance over the past few years is largely attributable to the full implementation of the cooperative's risk mitigation strategy and approved rate plan.

However, the mitigation reserves have been fully utilized and Fitch believes the improved leverage ratios that have resulted from a steady decline in net debt and rise in funds available for debt service (FADS) over the past few years is likely to continue. Cash remains near historical norms and at 57 days cash on hand is considered neutral to the financial profile assessment. A \$100 million senior secured credit agreement provides added liquidity.

Fitch Analytical Stress Test (FAST) Base and Rating Case Analysis

Fitch's base case is based on Big River's financial pro forma for fiscal years 2019 - 2023, which conservatively incorporates a slight decline in energy and revenues followed by limited growth through the forecast and annual spending for capital improvements totaling \$356 million through 2023. The base case assumes \$294 million of outstanding principal will be retired (including cash defeasances) although a portion of the capital plan will be funded with additional debt.

The Fitch base case aligns with Big Rivers' forecasted margins, which includes a decline in operating expenses related to the closure of Station 2 in 2019, and regulatory approval to treat station 2 as a regulatory asset, a rise in annual depreciation beginning in 2019, and an expected increase in sales related to Owensboro, KY and the expected opening of a new facility by Nucor Steel in 2022. The base case shows a decline in leverage in year one (2019) to 6.9x followed by a further modest decline in the leverage ratio throughout the remainder of the forward look.

For the rating case, the FAST incorporates a stress in sales in the first two years aggregating to 16% before a return to sales growth in years three through five. The previously mentioned base case assumptions are also

applied. The result of the stress is an increase in the leverage ratio to 9.1x in year two before an expected return of sales growth and presumed rate increases that would allow the utility to maintain at least a minimal amount of cash in subsequent years. Fitch believes the above stress-induced leverage ratio would remain fully supportive of the current rating. However, if actual leverage declines as projected in the base case, a higher rating could be warranted.

Debt Profile

The debt profile is neutral to the rating. Big Rivers had approximately \$760 million in total outstanding debt as of fiscal year-end 2018. All of the outstanding debt is fixed rate maturing no later than 2032 and includes a large bullet maturity of \$245 million due in 2023. Management expects to cash-fund roughly half of this payment and refinance the rest with long-term, fully amortizing bonds.

In addition to the sources of information identified in Fitch's applicable criteria specified below, this action was informed by information from Lumesis.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3 - ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY/DEBT	RATING	PRIOR
Big Rivers Electric Corporation (KY)	LT IDR BBB- ● Affirmed	BBB- ●
Big Rivers Electric Corporation (KY) /Senior Secured Obligation/1 LT	LT BBB- ● Affirmed	BBB- ●

Additional information is available on www.fitchratings.com

FITCH RATINGS ANALYSTS

Primary Rating Analyst
Andrew DeStefano
Director
+1 212 908 0284
Fitch Ratings, Inc.
Hearst Tower 300 W. 57th Street

New York 10019

Secondary Rating Analyst
Parker Montgomery
Associate Director
+1 212 908 0356

Committee Chairperson
Kathy Masterson
Senior Director
+1 512 215 3730

MEDIA CONTACTS

Sandro Scenga
New York
+1 212 908 0278
sandro.scenga@thefitchgroup.com

Applicable Criteria

U.S. Public Power Rating Criteria (pub. 03 Apr 2019)
Public Sector, Revenue-Supported Entities Rating Criteria (pub. 07 Nov 2019)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Policy

DISCLAIMER

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTPS://WWW.FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://www.fitchratings.com/understandingcreditratings). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT WWW.FITCHRATINGS.COM. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. DIRECTORS AND SHAREHOLDERS RELEVANT INTERESTS ARE AVAILABLE AT [HTTPS://WWW.FITCHRATINGS.COM/SITE/REGULATORY](https://www.fitchratings.com/site/regulatory). FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

COPYRIGHT

Copyright © 2019 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and

distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001

Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

SOLICITATION STATUS

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

Endorsement Policy

Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the EU Regulatory Disclosures page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.

Fitch Updates Terms of Use & Privacy Policy

We have updated our Terms of Use and Privacy Policies which cover all of Fitch Group's websites. Learn more.