

October 30, 2008

## Northeast Utilities

**Primary Credit Analyst:**

John Kennedy, New York (1) 212-438-7670; john\_kennedy@standardandpoors.com

### Table Of Contents

---

Major Rating Factors

Rationale

Outlook

# Northeast Utilities

## Major Rating Factors

### Strengths:

- Supportive regulatory regime in states;
- Low risk electric transmission and distribution business;
- Minimal competition; and
- Completion of the sale of the nonregulated business may improve business profile.

### Weaknesses:

- Still owns generation in New Hampshire;
- Large capital program for T&D operations (\$3 billion over the next several years); and
- Financial metrics weak for rating level.

Corporate Credit Rating
<i>Foreign Currency</i> BBB/Stable/--
<i>Local Currency</i> BBB/Stable/NR

## Rationale

The ratings on Northeast Utilities (NU) and its subsidiaries are based on the consolidated credit profile of the corporation. NU's subsidiaries are Connecticut Light & Power Co. (CL&P), Public Service Co. of New Hampshire (PSNH), Western Massachusetts Electric Co. (WMECO), and Yankee Gas Services Co.

NU's overall excellent business profile score reflects the strength of its regulated businesses. The utilities benefit from relatively supportive regulation in Connecticut, Massachusetts, and New Hampshire; management's focus on transmission and distribution (T&D); and low operational risk.

NU's business profile has improved with the sale of its competitive generation business. It used the approximately \$1 billion in proceeds (before taxes) to increase its capital investment in T&D infrastructure in its operating region. Total transmission capital spending could exceed \$3.0 billion in the 2008-2012 period. NU has a number of transmission-capital spending programs in the next few years. The first is a \$1.65 billion plan to improve transmission reliability in southwestern Connecticut. This includes the Bethel-to-Norwalk connection, which was completed in October 2006 for \$340 million. There are three other southwestern Connecticut programs currently under construction.

The other major program is the New England East-West Solution (NEEWS), a group of programs designed to improve transmission reliability and remove bottlenecks in Massachusetts and Connecticut. The NEEWS projects are currently in the planning stages, and are expected to cost about \$1.49 billion during the 2008-2013 period. NU is counting on its increased transmission investment to raise its rate base and earn strong returns. With an October 2006 ruling, the FERC allowed NU an 11.64% ROE on its existing transmission rate base and 12.64% on its new investments.

Capital spending at NU's distribution and generation unit will increase as well, to an estimated \$500 million in 2008. Aging equipment and increased summer peak load usage (despite overall flat residential use per customer) also require higher distribution spending. CL&P makes up the largest portion of the distribution segment. Its ROE for the past 12 months was below 8%, and is expected to improve slightly in 2008, while its authorized return is 9.4%.

CL&P already has some of the highest rates in the country, and may face some resistance in its attempts to raise rates significantly.

Total consolidated capital spending is expected to be about \$1.3 billion in 2008, versus expected cash from operations of \$450 million to \$500 million. The net cash flow to capital spending ratio could be about 40% in 2008, low for the rating.

NU's financial profile is slightly weak for the rating level. Adjusted funds from operations (FFO) interest coverage for the 12 months ended June 30, 2008, was 3.2x, and adjusted FFO to total debt was about 11.5%. Standard & Poor's expects credit protection measures to continue to be stretched for the rating level for the foreseeable future. However, the companies' business risk has improved as they have executed their strategy of becoming primarily a T&D-oriented group. Capital needs over the next several years will be heavy. Capital spending and dividends of \$6.5 billion over 2008-2012 will be funded with \$3.5 billion in cash from operations and about \$3.0 billion in new debt and equity offerings. The company forecasts that returns will improve once its rate base reflects the capital spending.

### Liquidity

NU has adequate liquidity, with bank lines of \$500 million at the holding company, \$400 million at the regulated companies. Both bank facilities mature in November 2010. Debt under the bank facility has been modest, and has been used primarily for LOCs issued for credit assurance for wholesale marketing contracts. Since NU completed the sale of the majority of the wholesale business, LOC issuance and draws under the line have been minimal.

## Outlook

The stable outlook on NU and its subsidiaries reflects Standard & Poor's expectation that the company's regulated businesses will dominate the business profile. In addition, the rating incorporates the expectation that NU will recover the costs of its construction program as the projects reach completion and that NU's financial measures will gradually improve. Factored into the stable outlook is the expectation of timely and adequate regulatory relief throughout the 2007-2012 period. Adverse rulings would be detrimental to current credit ratings and would precipitate a negative outlook and/or downgrade. The weak financial ratios for the rating also make the company susceptible to a negative rating action if its financial performance and consequent coverage measures deviate from current expectations. Given the financial strain imposed by the capital expenditure program, higher credit ratings are precluded at this time.

**Table 1**

<b>Northeast Utilities -- Peer Comparison*</b>			
<b>Industry Sector: Energy</b>			
	<b>--Average of past three fiscal years--</b>		
	<b>Northeast Utilities</b>	<b>NSTAR</b>	<b>Energy East Corp.</b>
Rating as of Oct. 28, 2008	BBB/Stable/NR	A+/Stable/A-1	BBB+/Stable/A-2
<b>(Mil. \$)</b>			
Revenues	6,438.4	3,184.1	5,235.8
Net income from cont. oper.	51.3	208.1	256.0

Table 1

<b>Northeast Utilities -- Peer Comparison*(cont.)</b>			
Funds from operations (FFO)	312.8	584.0	634.5
Capital expenditures	931.0	398.5	409.3
Cash and short-term investments	180.9	22.0	233.5
Debt	3,595.0	2,515.9	4,375.3
Preferred stock	96.8	35.8	20.5
Equity	2,655.3	1,514.4	2,910.4
Debt and equity	6,250.4	4,030.3	7,285.7
<b>Adjusted ratios</b>			
EBIT interest coverage (x)	1.9	3.5	2.2
FFO int. cov. (X)	2.5	5.1	2.9
FFO/debt (%)	8.7	23.2	14.5
Discretionary cash flow/debt (%)	(21.7)	(12.1)	(1.4)
Net cash flow / capex (%)	22.2	113.7	114.7
Total debt/debt plus equity (%)	57.5	62.4	60.1
Return on common equity (%)	0.9	13.0	8.7
Common dividend payout ratio (un-adj.) (%)	208.1	63.8	64.6

\*Fully adjusted (including postretirement obligations).

Table 2

<b>Northeast Utilities -- Financial Summary*</b>					
<b>Industry Sector: Energy</b>					
<b>--Fiscal year ended Dec. 31--</b>					
	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
Rating history	BBB/Stable/NR	BBB/Stable/NR	BBB/Stable/NR	BBB+/Negative/NR	BBB+/Stable/NR
<b>(Mil. \$)</b>					
Revenues	5,559.6	6,621.9	7,133.6	6,422.9	5,807.6
Net income from continuing operations	251.5	131.7	(229.2)	116.6	121.2
Funds from operations (FFO)	564.7	27.2	346.5	479.9	568.8
Capital expenditures	1,101.0	893.3	798.9	696.6	557.5
Cash and short-term investments	15.1	481.9	45.8	47.0	43.4
Debt	3,773.7	3,362.2	3,649.2	3,558.7	3,047.4
Preferred stock	58.1	116.2	116.2	116.2	116.2
Equity	2,971.9	2,914.4	2,079.7	1,979.7	2,008.8
Debt and equity	6,745.6	6,276.6	5,729.0	5,538.3	5,056.2
<b>Adjusted ratios</b>					
EBIT interest coverage (x)	2.6	1.5	1.6	2.0	1.9
FFO int. cov. (x)	3.6	1.2	2.6	3.5	4.5
FFO/debt (%)	15.0	0.8	9.5	13.5	18.7
Discretionary cash flow/debt (%)	(30.3)	(17.9)	(16.2)	(10.9)	(5.6)
Net Cash Flow / Capex (%)	40.6	(9.6)	32.4	56.6	87.9
Debt/debt and equity (%)	55.9	53.6	63.7	64.3	60.3
Return on common equity (%)	7.6	4.0	(10.6)	4.7	4.9

Table 2

Northeast Utilities -- Financial Summary*(cont.)					
Common dividend payout ratio (un-adj.) (%)	47.9	85.2	(38.2)	68.8	60.3

\*Fully adjusted (including postretirement obligations).

Table 3

## Reconciliation Of Northeast Utilities Reported Amounts With Standard &amp; Poor's Adjusted Amounts (Mil. \$)\*

--Fiscal year ended Dec. 31, 2007--

## Northeast Utilities reported amounts

	Debt	Shareholders' equity	Revenues	Operating income (before D&A)	Operating income (before D&A)	Operating income (after D&A)	Interest expense	Cash flow from operations	Cash flow from operations	Dividends paid	Capital expenditures
Reported	4,634.3	3,030.0	5,822.2	1,046.6	1,046.6	539.6	240.2	248.4	248.4	121.0	1,114.8
<b>Standard &amp; Poor's adjustments</b>											
Trade receivables sold or securitized	20.0	--	--	--	--	--	1.0	--	--	--	--
Operating leases	129.0	--	--	30.8	8.1	8.1	8.1	22.6	22.6	--	3.7
Intermediate hybrids reported as equity	58.1	(58.1)	--	--	--	--	2.8	(2.8)	(2.8)	(2.8)	--
Postretirement benefit obligations	7.2	--	--	3.9	3.9	3.9	--	22.9	22.9	--	--
Capitalized interest	--	--	--	--	--	--	17.5	(17.5)	(17.5)	--	(17.5)
Securitized utility cost recovery	(1,177.2)	--	(262.6)	(262.6)	(262.6)	(61.6)	(61.6)	(201.0)	(201.0)	--	--
Power purchase agreements	70.0	--	--	4.1	4.1	4.1	4.1	--	--	--	--
Asset retirement obligations	32.3	--	--	1.3	1.3	1.3	1.3	2.1	2.1	--	--
Reclassification of nonoperating income (expenses)	--	--	--	--	--	61.6	--	--	--	--	--
Reclassification of working-capital cash flow changes	--	--	--	--	--	--	--	--	490.0	--	--
Total adjustments	(860.7)	(58.1)	(262.6)	(222.6)	(245.2)	17.5	(26.7)	(173.8)	316.3	(2.8)	(13.8)

Table 3

**Reconciliation Of Northeast Utilities Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. \$)\*(cont.)**
**Standard & Poor's adjusted amounts**

	Debt	Equity	Revenues	Operating income (before D&A)	EBITDA	EBIT	Interest expense	Cash flow from operations	Funds from operations	Dividends paid	Capital expenditures
Adjusted	3,773.7	2,971.9	5,559.6	824.1	801.5	557.1	213.5	74.7	564.7	118.2	1,101.0

\*Northeast Utilities reported amounts shown are taken from the company's financial statements but might include adjustments made by data providers or reclassifications made by Standard & Poor's analysts. Please note that two reported amounts (operating income before D&A and cash flow from operations) are used to derive more than one Standard & Poor's-adjusted amount (operating income before D&A and EBITDA, and cash flow from operations and funds from operations, respectively). Consequently, the first section in some tables may feature duplicate descriptions and amounts.

**Ratings Detail (As Of October 30, 2008)\***
**Northeast Utilities**

Corporate Credit Rating

*Foreign Currency*

BBB/Stable/--

*Local Currency*

BBB/Stable/NR

Senior Unsecured (3 Issues)

BBB-

**Corporate Credit Ratings History**

27-May-2005

*Foreign Currency*

BBB/Stable/--

14-Apr-2004

BBB+/Negative/--

08-Nov-2001

BBB+/Stable/--

27-May-2005

*Local Currency*

BBB/Stable/NR

14-Apr-2004

BBB+/Negative/NR

08-Nov-2001

BBB+/Stable/NR

**Business Risk Profile**
**1 2 3 4 5 6 7 8 9 10**
**Financial Risk Profile**

Aggressive

**Related Entities**
**Connecticut Light & Power Co.**

Issuer Credit Rating

BBB/Stable/NR

Preferred Stock (8 Issues)

BB+

Senior Secured (3 Issues)

AA/Negative

Senior Secured (15 Issues)

BBB+

Senior Unsecured (5 Issues)

BBB-

**Public Service Co. of New Hampshire**

Issuer Credit Rating

BBB/Stable/--

Senior Secured (2 Issues)

BBB

Senior Secured (4 Issues)

BBB+

Senior Unsecured (5 Issues)

AA/Negative

Senior Unsecured (1 Issue)

AAA

**Western Massachusetts Electric Co.**

Issuer Credit Rating

BBB/Stable/NR

Senior Unsecured (5 Issues)

BBB

**Yankee Gas Services Co.**

Issuer Credit Rating

BBB/Stable/--

**Ratings Detail** (As Of October 30, 2008)\***(cont.)**

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

Copyright © 2008 Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P). S&P and/or its third party licensors have exclusive proprietary rights in the data or information provided herein. This data/information may only be used internally for business purposes and shall not be used for any unlawful or unauthorized purposes. Dissemination, distribution or reproduction of this data/information in any form is strictly prohibited except with the prior written permission of S&P. Because of the possibility of human or mechanical error by S&P, its affiliates or its third party licensors, S&P, its affiliates and its third party licensors do not guarantee the accuracy, adequacy, completeness or availability of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. S&P GIVES NO EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall S&P, its affiliates and its third party licensors be liable for any direct, indirect, special or consequential damages in connection with subscriber's or others use of the data/information contained herein. Access to the data or information contained herein is subject to termination in the event any agreement with a third-party of information or software is terminated.

Analytic services provided by Standard & Poor's Ratings Services (Ratings Services) are the result of separate activities designed to preserve the independence and objectivity of ratings opinions. The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision. Ratings are based on information received by Ratings Services. Other divisions of Standard & Poor's may have information that is not available to Ratings Services. Standard & Poor's has established policies and procedures to maintain the confidentiality of non-public information received during the ratings process.

Ratings Services receives compensation for its ratings. Such compensation is normally paid either by the issuers of such securities or third parties participating in marketing the securities. While Standard & Poor's reserves the right to disseminate the rating, it receives no payment for doing so, except for subscriptions to its publications. Additional information about our ratings fees is available at [www.standardandpoors.com/usratingsfees](http://www.standardandpoors.com/usratingsfees).

Any Passwords/user IDs issued by S&P to users are single user-dedicated and may ONLY be used by the individual to whom they have been assigned. No sharing of passwords/user IDs and no simultaneous access via the same password/user ID is permitted. To reprint, translate, or use the data or information other than as provided herein, contact Client Services, 55 Water Street, New York, NY 10041; (1)212.438.9823 or by e-mail to: [research\\_request@standardandpoors.com](mailto:research_request@standardandpoors.com).