

**Rating Action: Moody's changes Georgia Power outlook to negative, affirms Southern with stable outlook**

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Global Credit Research - 20 Mar 2017

**Approximately \$8 billion of debt securities affected**

New York, March 20, 2017 -- Moody's Investor Service changed the rating outlook of Georgia Power Company to negative from stable while affirming the utility's ratings, including its A3 senior unsecured and Issuer Rating. Moody's affirmed the ratings of its parent company, The Southern Company (Southern), including its Baa2 senior unsecured rating and Prime-2 short-term rating for commercial paper, with a stable outlook. Moody's also affirmed the ratings of Southern Electric Generating Company, including its A1 senior unsecured rating, with a stable outlook.

**RATINGS RATIONALE**

"The negative outlook on Georgia Power reflects the increased credit and regulatory risk facing the company due to the uncertain future of Westinghouse, the construction contractor building the new Vogtle nuclear units, and its parent company Toshiba", said Michael G. Haggarty, Associate Managing Director.

Toshiba Corporation (Toshiba, Caa1, ratings on review), is actively considering a sale or other strategic options for its US nuclear unit Westinghouse Electric Company LLC (Westinghouse, unrated), and has recently hired US bankruptcy lawyers to explore these options. In our opinion, these developments raise questions regarding the companies' ability and willingness to physically complete the Vogtle project under the current arrangements, which could ultimately shift some of the risks of nuclear construction, and the potential for further cost increases, back to Georgia Power.

The Vogtle units are being constructed for Georgia Power and its municipal and cooperative utility partners under a fixed price engineering procurement construction (EPC) contract, with guaranteed completion dates and associated liquidated damage provisions that materially place the risks of future cost overruns and delays on Westinghouse. Westinghouse's obligations have been guaranteed by its parent, Toshiba, but the value of the guarantee could be diminished by Toshiba's weakened financial condition.

Last week, Toshiba delayed the release of its third quarter financial results for the second time while it further investigates accounting issues relating to Westinghouse's 2015 acquisition of CB&I Stone & Webster. The acquisition, and the related assumption of obligations to complete the Vogtle and VC Summer nuclear units in the US, is believed to be the primary determinant of Toshiba's forecasted full year impairment loss of more than \$6 billion.

In the event Westinghouse were to become unable or unwilling to complete the projects as currently contracted, including the potential for a bankruptcy filing, we anticipate Georgia Power would evaluate alternatives. These may include completing the project itself, or engaging other contractors, which could result in additional costs or delays for Georgia Power and its rate payers. Georgia Power is currently in the process of reviewing the detail supporting Westinghouse's recently revised forecasted in-service dates of December 2019 and September 2020 for the two Vogtle units, in part to assess the potential for additional delays or cost increases.

We expect Georgia Power to review these alternatives with its utility partners on the project, the Georgia Public Service Commission (GPSC), and the US Department of Energy (DOE), which guarantees \$2.6 billion of loans from the US Federal Financing Bank. In the event certain mandatory prepayment events occur under the DOE loan agreement, including the termination of the Vogtle EPC contract, Georgia Power could be required to prepay the outstanding amount over five years with level principal amortization.

The rating affirmation considers that the obligations under Westinghouse's fixed price EPC contract are currently guaranteed by Toshiba, which could mitigate additional project costs that might arise in the event Westinghouse was rendered unable or unwilling to fulfill its obligations. The affirmation assumes the guarantee from Toshiba remains in place and that Toshiba continues as a going concern. The ratings affirmation also reflects the credit supportive regulatory environment in Georgia and the state's support of nuclear construction

as evidenced by the recent regulatory settlement on Vogtle costs, which we viewed as credit positive.

The negative outlook also considers cash flow coverage metrics that have declined as the Vogtle project has proceeded, with Georgia Power's CFO pre-working capital to debt falling from the 26%-27% range from 2011-2013 to 23% on average from 2014-2016 and 21% at 31 December 2016. This ratio is now slightly below our methodology rating guidelines of between 22% and 30% for the A rating category, a significant credit weakness considering the higher risk entailed in the new nuclear construction project. Georgia Power also exhibits a somewhat constrained liquidity position, particularly considering its large construction program, with approximately half of its \$1.75 billion of bank credit facilities dedicated to providing liquidity support for variable rate demand bonds.

The affirmation of Southern's ratings with a stable outlook considers the increased size, scale, and diversity of the company's business following the acquisition of a natural gas local distribution company and other natural gas assets last year, and the continued growth of subsidiary Southern Power Company's (Baa1 stable) largely contracted renewable energy business. Although Georgia Power remains Southern's largest subsidiary and the biggest source of dividends, the credit strength and overall growth of the company's other businesses has reduced the relative impact of Georgia Power and the Vogtle new nuclear construction project on the parent. Although parent company debt increased significantly following the natural gas acquisitions in 2016, Southern is appropriately positioned at its current Baa2 rating level considering our projection of a CFO pre-working capital to debt ratio of above 15%.

The affirmation of the ratings Southern Electric Generating Company (A1 senior unsecured, A2 Issuer Rating), which is 50% owned by Georgia Power and 50% owned by Alabama Power Company (A1 senior unsecured, stable), reflects the unconditional guaranty of its debt by Alabama Power.

#### Rating Outlook

The negative rating outlook incorporates a view that Toshiba could file Westinghouse into a chapter 11 bankruptcy proceeding, thereby calling into question the ability to complete the Vogtle project under the current arrangements. This will, in turn create disruptions to the construction progress and result in additional costs to complete the project, which will trigger a higher level of regulatory scrutiny. The negative outlook also assumes that Georgia Power will maintain a financial profile consistent with its existing metrics, including the steady production of CFO pre-working capital to debt in the low 20% range; and that the GPSC will continue to provide transparent and timely recovery of its Vogtle costs.

#### Factors that Could Lead to an Upgrade

An upgrade of Georgia Power is unlikely considering the negative rating outlook, the higher uncertainty associated with the Vogtle new nuclear project and the utility's declining metrics. The outlook could be revised to stable if the financial situation at Westinghouse and Toshiba improves while their commitments to the Vogtle project were maintained.

Southern's rating could be upgraded if there is a substantial reduction of parent company debt levels; if the Vogtle project and Mississippi Power Company's (Ba1, negative) Kemper plant reach commercial operation without significant additional delays or cost increases; if one or more of its major utilities is upgraded (Alabama Power, Georgia Power, Southern Power Company, or Southern Company Gas Capital); or if consolidated credit metrics return to level more appropriate for a Baa1 rating, including CFO pre-working capital to debt in the 20% range.

#### Factors that Could Lead to a Downgrade

Georgia Power's rating could be downgraded if Toshiba files for bankruptcy; if there are further delays or cost increases on the project; if there is a decrease in the level of regulatory, political, public, or partner support for the project; or if we expect the utility's CFO pre-working capital to debt ratio to remain below 22% for a sustained period.

Southern's rating could be downgraded if there are material additional debt financed acquisitions; if parent company debt increases materially above the current 25% of consolidated debt level; if one or more of its larger subsidiaries is downgraded (Alabama Power, Georgia Power, Southern Power Company, or Southern Company Gas Capital); or if consolidated coverage metrics show a decline below the levels incorporated in our current projections, including cash flow from operations pre-working capital to debt below 15% for an extended period.

Outlook Actions:

- ..Issuer: Georgia Power Company
- ....Outlook, Changed To Negative From Stable
- ..Issuer: Southern Company (The)
- ....Outlook, Remains Stable
- ..Issuer: Southern Elect Generating Co
- ....Outlook, Remains Stable

Affirmations:

- ..Issuer: Appling County Development Authority, GA
- ....Senior Unsecured Revenue Bonds, Affirmed A3
- ....Senior Unsecured Revenue Bonds, Affirmed VMIG 2
- ..Issuer: Bartow County Development Authority, GA
- ....Senior Unsecured Revenue Bonds, Affirmed A3
- ....Senior Unsecured Revenue Bonds, Affirmed VMIG 2
- ..Issuer: Burke County Development Authority, GA
- ....Senior Unsecured Revenue Bonds, Affirmed A3
- ....Senior Unsecured Revenue Bonds, Affirmed VMIG 2
- ..Issuer: Coweta County Development Authority, GA
- ....Senior Unsecured Revenue Bonds, Affirmed A3
- ....Senior Unsecured Revenue Bonds, Affirmed VMIG 2
- ..Issuer: EFFINGHAM COUNTY INDUSTRIAL DEVELOPMENT AUTHORITY,
- ....Senior Unsecured Revenue Bonds, Affirmed A3
- ....Senior Unsecured Revenue Bonds, Affirmed VMIG 2
- ..Issuer: Floyd County Development Authority, GA
- ....Senior Unsecured Revenue Bonds, Affirmed A3
- ....Senior Unsecured Revenue Bonds, Affirmed VMIG 2
- ..Issuer: Georgia Power Company
- .... Issuer Rating, Affirmed A3
- ....Senior Unsecured Shelf, Affirmed (P)A3
- ....Junior Subordinate Shelf, Affirmed (P)Baa1
- ....Preferred Shelf, Affirmed (P)Baa2
- ....Preference Shelf, Affirmed (P)Baa2
- ....Preference Stock Preference Stock, Affirmed Baa2
- ....Pref. Stock Non-cumulative Preferred Stock, Affirmed Baa2

...Senior Unsecured Bank Credit Facility, Affirmed A3  
...Senior Unsecured Regular Bond/Debenture, Affirmed A3  
..Issuer: Heard County Development Authority, GA  
...Senior Unsecured Revenue Bonds, Affirmed A3  
...Senior Unsecured Revenue Bonds, Affirmed VMIG 2  
..Issuer: Monroe County Development Authority, GA  
...Senior Unsecured Revenue Bonds, Affirmed A3  
...Senior Unsecured Revenue Bonds, Affirmed VMIG 2  
..Issuer: Southern Company (The)  
... Commercial Paper, Affirmed P-2  
...Junior Subordinated Regular Bond/Debenture, Affirmed Baa3  
...Junior Subordinate Shelf, Affirmed (P)Baa3  
...Senior Unsecured Shelf, Affirmed (P)Baa2  
...Senior Unsecured Bank Credit Facility, Affirmed Baa2  
...Senior Unsecured Regular Bond/Debenture, Affirmed Baa2  
..Issuer: Southern Elect Generating Co  
... Issuer Rating, Affirmed A2  
...Senior Unsecured Regular Bond/Debenture, Affirmed A1  
..Issuer: Wilsonville (Town of) AL, I.D.B.  
...Senior Unsecured Revenue Bonds, Affirmed A1

The principal methodology used in these ratings was Regulated Electric and Gas Utilities published in December 2013. Please see the Rating Methodologies page on [www.moodys.com](http://www.moodys.com) for a copy of this methodology.

The Southern Company is a utility holding company headquartered in Atlanta, Georgia and the parent company of utility subsidiaries Alabama Power Company, Georgia Power Company, Gulf Power Company, Mississippi Power Company, Southern Company Gas, Southern Gas Capital, Northern Illinois Gas Company, Southern Electric Generating Company, wholesale power company Southern Power Company, and commercial paper issuer Southern Company Funding Corporation.

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