



Mr. Jeff DeRouen  
Executive Director  
Kentucky Public Service Commission  
211 Sower Boulevard  
P. O. Box 615  
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March 15, 2011

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COMMISSION

**LG&E and KU Energy LLC**  
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Re: *Joint Application of PPL Corporation, E.ON AG, E.ON US Investments Corp., E.ON U.S. LLC, Louisville Gas and Electric Company and Kentucky Utilities Company For Approval of An Acquisition of Ownership and Control of Utilities – Case No. 2010-00204*

Dear Mr. DeRouen:

Pursuant to the Commission's Order of September 30, 2010, in the above-referenced proceeding, PPL Corporation, LG&E and KU Energy LLC, Louisville Gas and Electric Company, and Kentucky Utilities Company ("the Companies") hereby report to the Commission and interested Parties any credit rating agency downgrade of PPL or any of PPL's Kentucky-based operating subsidiaries. Attached is a copy of a report issued on March 2, 2011. The Companies are filing this notice pursuant to Appendix A, Section 3.5 of the Order.

Please confirm your receipt of this filing by placing the stamp of your Office with date received on the extra copy.

Should you have any questions regarding this information, please contact me at your convenience.

Sincerely,

Rick E. Lovekamp

cc: Dennis G. Howard II, AG  
Michael L. Kurtz, KIUC

### Research Update:

## PPL Corp. Is Lowered To 'BBB' And Placed On CreditWatch Negative After Acquisition Announcement

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## Research Update:

# PPL Corp. Is Lowered To 'BBB' And Placed On CreditWatch Negative After Acquisition Announcement

## Overview

- We lowered our ratings on diversified energy company PPL Corp. (PPL) and its affiliates PPL Energy Supply (PPL Energy), LG&E and KU Energy LLC (LKE), Louisville Gas & Electric Co. (LG&E), and Kentucky Utilities Co. (KU) to 'BBB' from 'BBB+'.
- We lowered the rating on PPL subsidiary PPL Electric Utilities (PPLEU) to 'BBB' from 'A-'.
- At the same time we placed all the 'BBB' ratings on CreditWatch with negative implications.
- The short-term ratings on Kentucky Utilities, Louisville Gas & Electric, and PPLEU are 'A-3'.
- The downgrades and CreditWatch listing follow PPL's proposed acquisition of E.ON UK's Central Networks West PLC (CNW) and Central Networks East PLC (CNE).

## Rating Action

On March 2, 2011, Standard & Poor's Ratings Services lowered the corporate credit ratings on PPL Corp. (PPL) and its affiliates PPL Energy Supply (PPL Energy), LG&E and KU Energy LLC (LKE), Louisville Gas & Electric Co. (LG&E), and Kentucky Utilities Co. (KU) to 'BBB' from 'BBB+' and placed these ratings on CreditWatch with negative implications. We also lowered the rating on PPL subsidiary PPL Electric Utilities (PPLEU) to 'BBB' from 'A-'. The ratings actions follow PPL's planned acquisition of E.ON UK's Central Networks West PLC (CNW) and Central Networks East PLC (CNE), two distribution networks in the United Kingdom. The CreditWatch listing is directly related to the execution of the financing plan for the acquisition, which includes a commitment by the company for a substantial issuance of equity. Resolution of the CreditWatch will depend on the ability of the company to complete its financing activities consistent with our expectations for the 'BBB' ratings. Allentown, Pa.-based PPL has about \$12.7 billion of long-term debt, including \$1.63 billion of junior subordinated notes.

The CreditWatch listing will remain until demonstrated progress on the permanent financing plan has been executed in line with our expectations. The acquisition requires large permanent financing that has attendant execution risks, and we will monitor PPL's ability to finalize this permanent financing. We could remove the CreditWatch listing and assign a stable outlook if financing is consistent with our expectation. We could lower the ratings if PPL is unable to fully execute its permanent financing plan in a

credit-supportive manner consistent with our expectations for 'BBB' ratings.

## **Rationale**

PPL's purchase price of E.ON UK's Central Networks utilities includes the assumption of \$800 million of public debt and cash of \$5.6 billion (excluding related transaction expenses and fees) that will be funded through a combination of cash, common equity issuance at PPL, unsecured debt at CNW and CNE, and unsecured debt at an intermediate holding company (generically called UK Holdings) that will own CNW and CNE. In addition, PPL will issue equity units at PPL Capital Funding, which will likely receive high equity credit under our rating criteria. This acquisition will raise PPL's regulated cash flows to approximately 75% from the current level of 60%. Before PPL bought the Kentucky utilities, its regulated cash flows comprised less than 30%. The ratings change reflects our revisions, in accordance with our criteria, of PPL's business risk profile to excellent from strong and the company's financial risk profile to aggressive from significant.

Our revision of the business profile to excellent reflects the addition of fully regulated distribution utilities that have credit-supportive U.K. regulation and no commodity exposure, since power for retail customers is procured by nonaffiliated retail suppliers. The Central Networks utilities are contiguous to PPL's existing U.K. utilities. After the acquisition of CNE and CNW, we expect U.K. operations to be about 30% of PPL's consolidated cash flow. With this transaction, we are viewing all of PPL's utility assets as part of a consolidated entity, whereas previously we considered only the quality of the utility's dividends to its parent. The stability of CNE and CNW along with existing utility assets in the U.K., Kentucky, and Pennsylvania, which we assess as excellent, will more than offset the business risk profile, which we assess as satisfactory, of PPL Energy's merchant generation, resulting in an excellent business profile. We expect the merchant generation business to comprise less than 25% of pro forma consolidated cash flows.

Our revision of the financial risk profile to aggressive reflects in part the company's financial policies toward acquisitions, including funding with aggressive levels of hybrid securities. Furthermore, due to the company's strategy to focus on fully regulated operations and also expand its U.K. presence, we are incorporating consolidated financial measures for PPL in our analysis. When reviewing the financial metrics, we are now including all cash flows and debt obligations from the U.K. utilities and PPLEU in PPL's financial measures. We expect consolidated financial measures, including ratios of debt to EBITDA, funds from operations (FFO) to total debt, and debt to capital, to range in the aggressive category of our financial risk profile. Debt to EBITDA should range between 4x and 5x, while we expect the percentage of FFO to debt to be in the mid-teens. These measures will support ratings at the 'BBB' level on successful completion of the permanent financing.

### Short-term credit factors

Standard & Poor's currently views PPL's liquidity as strong under its corporate liquidity methodology, which categorizes liquidity in five standard descriptors. Our assessment of liquidity as strong supports PPL's 'BBB' issuer credit rating. Projected sources of liquidity--mainly operating cash flow and available bank lines--exceed projected uses--mainly necessary capital expenditures, debt maturities, and common dividends--by more than 1.5x. The ratio of sources over uses would be positive even after a 50% EBITDA decline. Additional factors that support the liquidity are PPL's ability to absorb high-impact, low-probability events with limited need for refinancing, its flexibility to lower capital spending, its sound bank relationships, its solid standing in credit markets, and its generally prudent risk management.

### CreditWatch

The CreditWatch listing will remain until demonstrated progress on the permanent financing plan has been executed in line with our expectations. The acquisition requires large permanent financing that has attendant execution risks, and we will monitor PPL's ability to finalize this permanent financing. We could remove the CreditWatch listing and assign a stable outlook if financing is consistent with our expectation. We could lower the ratings if PPL is unable to fully execute its permanent financing plan in a credit-supportive manner consistent with our expectations for 'BBB' ratings.

### Related Criteria And Research

- "Criteria Methodology: Business Risk/Financial Risk Matrix Expanded," May 27, 2009
- "2008 Corporate Criteria: Analytical Methodology," April 15, 2008
- "2008 Corporate Criteria: Ratios And Adjustments," April 15, 2008

### Ratings List

Downgraded; CreditWatch Action

	To	From
PPL Corp. Corporate Credit Rating	BBB/Watch Neg/--	BBB+/Stable/--
PPL Capital Funding Inc. Senior Unsecured	BBB-/Watch Neg	BBB
Junior Subordinated	BB+/Watch Neg	BBB-
PPL Energy Supply LLC Corporate Credit Rating	BBB/Watch Neg/--	BBB+/Stable/--
Senior Unsecured	BBB/Watch Neg	BBB+
PPL Electric Utilities Corp. Corporate Credit Rating	BBB/Watch Neg/A-3	A-/Stable/A-2

*Research Update: PPL Corp. Is Lowered To 'BBB' And Placed On Credit Watch Negative After Acquisition Announcement*

Senior Secured	BBB+/Watch Neg	A-
Recovery Rating	1	1
Preference Stock	BB+/Watch Neg	BBB
Commercial Paper	A-3/Watch Neg	A-2
LG&E and KU Energy LLC		
Corporate Credit Rating	BBB/Watch Neg/--	BBB+/Stable/--
Senior Unsecured	BBB-/Watch Neg	BBB
Louisville Gas & Electric Co.		
Corporate Credit Rating	BBB/Watch Neg/--	BBB+/Stable/--
Senior Secured	A-/Watch Neg	A
Recovery Rating	1+	1+
Kentucky Utilities Co.		
Corporate Credit Rating	BBB/Watch Neg/A-3	BBB+/Stable/A-2
Senior Secured	A-/Watch Neg	A
Recovery Rating	1+	1+

Complete ratings information is available to subscribers of RatingsDirect on the Global Credit Portal at [www.globalcreditportal.com](http://www.globalcreditportal.com). All ratings affected by this rating action can be found on Standard & Poor's public Web site at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

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