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Ratings

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Louisville Gas & Electric Co.

January 24, 2025

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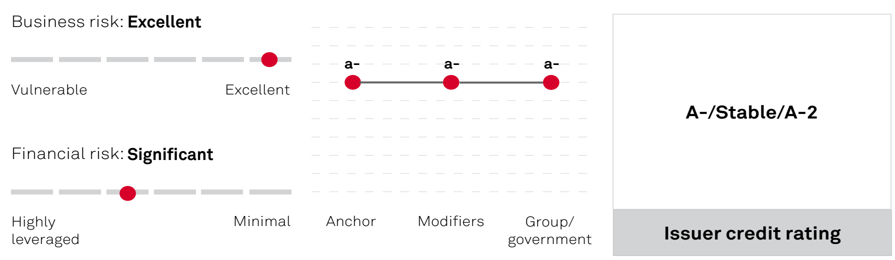
Ratings Score Snapshot



Credit Highlights

Overview

Key strengths	Key risks
Vertically integrated electric and natural gas distribution utility	Geographic concentration in Louisville, Ky., and modest customer base with limited scale
Credit-supportive regulatory environment in Kentucky	Negative discretionary cash flow from heightened capital spending and dividends
Balanced capital structure supports overall credit quality	70% of generation capacity is coal-fired, exposing the company to environmental compliance rules

Kentucky's constructive regulatory environment supports Louisville Gas & Electric Co.'s (LG&E's) credit quality. We view Kentucky's regulatory jurisdiction to be credit supportive for LG&E buoyed by use of forward test years for base rate cases, as well as the use of constructive recovery mechanisms such as environmental cost recovery surcharge, retired asset recovery rider, gas line tracker, and a pass-through fuel cost mechanism, all of which help mitigate regulatory lag and stabilize the company's operating cash flow.

Capital investment plan in Kentucky is underpinned by continued need to support future growth and maintain compliance with environmental standards. Capital spending in Kentucky, both for LG&E and Kentucky Utilities Co. (KU) (about $6.4 billion from 2024-2027), is primarily focused on system enhancements (generation investment, system hardening, digital transformation) and energy transition plans. These projects would allow LG&E to support demand growth, improve system reliability, and reduce emissions (aligning with parent PPL Corp.'s 2050 net zero ambition).

LG&E and KU recently filed an integrated resource plan with the KPSC demonstrating the need for additional generation needs due to anticipated growth from data center demand and economic growth. As per management, active data center requests in Kentucky have increased to nearly 3 gigawatts (GW) from 2 GW for the period 2026-2034. This is further underpinned by LG&E's recent announcement of supporting a 400-megawatt (MW) data center campus development in Louisville, with the first phase expected to be operational by late 2026 (130 MW). While there could be further upside to the current capital plan and this could potentially pressure credit metrics, S&P Global Ratings expects it will be partially offset by cash inflows in the form of authorized allowance for funds used during construction (AFUDC) for construction projects. Based on the current capital plan, we project LG&E's funds from operations (FFO) to debt will average 20%-21% through 2026.

LG&E and KU continue to progress toward reducing their coal-based generation exposure. In 2023, PPL Corp., which is also the parent company of KU, received regulatory approval from the Kentucky Public Service Commission (KPSC) to reduce its exposure to coal-fired generation by replacing it with a combination of gas-fired generation plants, solar, and battery storage. Subsequently, in February 2024, LG&E and KU entered into an agreement to begin construction of Mill Creek Unit 5 Generating Station. The natural gas combined-cycle facility will be jointly owned by LG&E (31%) and KU (69%), with an estimated project cost of about $1 billion, and commercial activities are expected to begin around mid-2027. This is part of the company's plan to replace about 600 MW of coal generation being retired by the end of 2027.

Outlook

The stable outlook on LG&E reflects our stable outlook on its ultimate parent, PPL Corp. We base this on our expectation that the parent's business risk profile will not weaken and consolidated financial measures will remain stable. Specifically, we expect PPL Corp.'s FFO to debt will remain in the 16%-18% range through 2025.

Downside scenario

We could lower our ratings on PPL Corp. and its subsidiaries over the next 24 months if:

- PPL's business risk remains unchanged; and
- Core credit ratios weaken such that PPL Corp.'s FFO to debt (S&P Global Ratings'-adjusted) falls consistently below 16%.

Upside scenario

Given our assessment of PPL Corp.'s business risk and our base-case assumptions, we do not anticipate raising our rating on PPL during the next 24 months. However, we could raise our ratings if:

- PPL Corp.'s FFO to debt (S&P Global Ratings'-adjusted) exceeds 21% on a consistent basis; and

- It maintains or improves its business risk.

Our Base-Case Scenario

Assumptions

- Gross margin growth primarily due to base-rate increases and timely cost recovery;
- Average annual capital spending of about $650 million-$700 million in 2025 and 2026 for upgrades to distribution equipment and improvements to generation assets to comply with environmental regulations;
- Annual dividends in the $190 million-$200 million range;
- Negative discretionary cash flow through 2026; and
- All debt maturities are refinanced.

Key metrics

Louisville Gas & Electric Co.--Key metrics*

	2023a	2024e	2025f	2026f
FFO to debt (%)	22.7	20-22	19-21	20-22
Debt to EBITDA (x)	3.4	3.5-4.0	3.5-4.0	3.5-4.0
FFO cash interest coverage (x)	7.2	6.0-7.0	5.5-6.5	6.0-6.5

*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast. FFO--Funds from operations.

Company Description

LG&E, which operates in and around Louisville, Ky., is a vertically integrated electric utility that serves about 436,000 customers and a natural gas distribution utility that serves about 335,000 customers. The company operates as a subsidiary of PPL Corp.

Peer Comparison

Louisville Gas & Electric Co.--Peer Comparisons

	Louisville Gas & Electric Co.	Southern Indiana Gas & Electric Co.	Wisconsin Public Service Corp.	Northern Indiana Public Service Co. LLC	NorthWestern Corp.
Foreign currency issuer credit rating	A-/Stable/A-2	BBB+/Negative/--	A-/Stable/A-2	BBB+/Stable/NR	BBB/Stable/A-2
Local currency issuer credit rating	A-/Stable/A-2	BBB+/Negative/--	A-/Stable/A-2	BBB+/Stable/NR	BBB/Stable/A-2
Period	Annual	Annual	Annual	Annual	Annual
Period ending	2023-12-31	2023-12-31	2023-12-31	2015-12-31	2023-12-31
Mil.	$	$	$	$	$
Revenue	1,613	731	1,681	2,222	1,422

Louisville Gas & Electric Co.--Peer Comparisons

EBITDA	758	271	624	652	525
Funds from operations (FFO)	580	197	524	506	389
Interest	110	60	101	92	144
Cash interest paid	94	51	98	84	137
Operating cash flow (OCF)	613	209	593	577	465
Capital expenditure	378	487	471	591	547
Free operating cash flow (FOCF)	235	(278)	122	(14)	(82)
Discretionary cash flow (DCF)	(92)	(371)	(133)	(39)	(236)
Cash and short-term investments	18	14	1	1	9
Gross available cash	18	14	1	1	9
Debt	2,559	1,201	2,424	2,310	2,911
Equity	3,172	1,325	2,554	2,156	2,785
EBITDA margin (%)	47.0	37.1	37.1	29.4	36.9
Return on capital (%)	7.8	6.0	8.0	8.9	5.8
EBITDA interest coverage (x)	6.9	4.5	6.2	7.1	3.6
FFO cash interest coverage (x)	7.2	4.9	6.4	7.0	3.8
Debt/EBITDA (x)	3.4	4.4	3.9	3.5	5.5
FFO/debt (%)	22.7	16.4	21.6	21.9	13.4
OCF/debt (%)	24.0	17.4	24.5	25.0	16.0
FOCF/debt (%)	9.2	(23.1)	5.0	(0.6)	(2.8)
DCF/debt (%)	(3.6)	(30.9)	(5.5)	(1.7)	(8.1)

Business Risk

Our assessment of LG&E's business risk profile primarily reflects the company's regulated operations, which comprise vertically integrated electric and natural gas distribution utilities, as well as Kentucky's generally constructive regulatory framework.

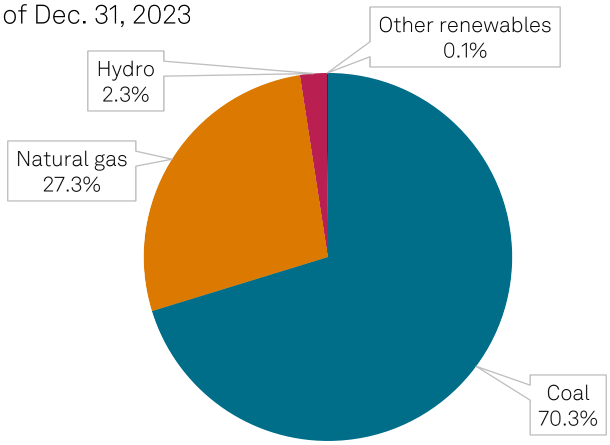
With a base of about 436,000 electric and about 335,000 natural gas customers, LG&E has limited scale. Residential and commercial customers generate about 75%-80% of LG&E's revenues, helping the company generate steady cash flows. Our assessment also incorporates the company's moderate operating diversity due to LG&E's electric and natural gas operations.

The company has about 2,800 MW of generation capacity, including sizable coal-fired generation that contributes nearly 70% of its total generation capacity. There is greater operating risk from these generation assets than LG&E's transmission and distribution operations. The company has been upgrading its coal-fired generation plants to comply with environmental regulations. While the capital costs for these upgrades continue, they have diminished over time and now account for about 10% of the total $6.4 billion capex amount (2024-2027). LG&E can recover these costs through the environmental cost-recovery mechanism, which limits the company's regulatory lag and supports its credit profile. The company is regulated by the KPSC and benefits from other mechanisms, such as a gas line tracker and a pass-through fuel cost mechanism, which help stabilize its operating cash flow.

Moreover, LG&E's low-cost generation and efficient operations contribute to the overall competitive rates the company offers its customers.

Louisville Gas & Electric Co. generation mix

As of Dec. 31, 2023



Source: Company filings.

Financial Risk

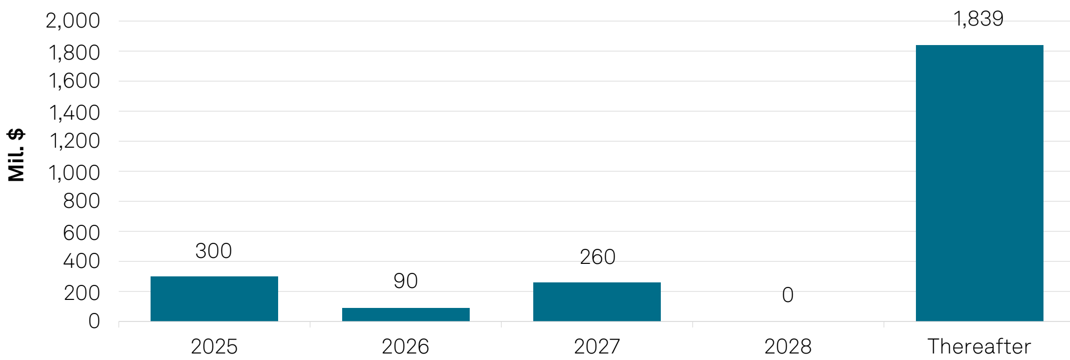
Under our base-case scenario, we assume LG&E's FFO to debt (S&P Global Ratings'-adjusted) will be in the 19%-22% range through 2026. We expect stability because the company benefits from recovery mechanisms, such as the environmental cost rider, as well as formulaic transmission rates and forward test years for rate cases. LG&E's ongoing discretionary cash flow deficits because of its heightened capital spending, which we expect it will fund at least partially with debt, offset these strengths. We anticipate the company's debt to EBITDA will be in the 3.5x-4.0x range through 2026. LG&E's supplemental FFO cash interest coverage ratio, which we expect will be in the range of 6.0x-6.5x through 2026, further bolsters the financial risk profile.

We assess LG&E's financial risk profile using our medial volatility financial benchmarks, reflecting lower risk regulated utility operations and effective management of regulatory risk. These benchmarks are more relaxed than those used for typical corporate issuers.

Debt maturities

Louisville Gas & Electric Co. debt maturity schedule

As of Sept. 30, 2024



Source: Company filings.

Louisville Gas & Electric Co.--Financial Summary

Period ending	Dec-31-2018	Dec-31-2019	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023
Reporting period	2018a	2019a	2020a	2021a	2022a	2023a
Display currency (mil.)	$	$	$	$	$	$
Revenues	1,496	1,500	1,456	1,569	1,798	1,613
EBITDA	613	657	675	681	732	758
Funds from operations (FFO)	533	577	529	551	591	580
Interest expense	89	98	97	91	96	110
Cash interest paid	73	78	83	78	84	94
Operating cash flow (OCF)	454	503	490	463	548	613
Capital expenditure	554	482	456	466	371	378
Free operating cash flow (FOCF)	(100)	21	34	(3)	177	235
Discretionary cash flow (DCF)	(256)	(161)	(127)	(195)	(98)	(92)
Cash and short-term investments	10	15	7	9	93	18
Gross available cash	10	15	7	9	93	18
Debt	2,223	2,347	2,488	2,492	2,471	2,559
Common equity	2,687	2,762	2,948	3,079	3,166	3,172
Adjusted ratios						
EBITDA margin (%)	40.9	43.8	46.4	43.4	40.7	47.0
Return on capital (%)	8.0	7.8	7.6	7.1	7.6	7.8
EBITDA interest coverage (x)	6.9	6.7	7.0	7.5	7.7	6.9
FFO cash interest coverage (x)	8.3	8.4	7.4	8.1	8.1	7.2
Debt/EBITDA (x)	3.6	3.6	3.7	3.7	3.4	3.4
FFO/debt (%)	24.0	24.6	21.3	22.1	23.9	22.7
OCF/debt (%)	20.4	21.4	19.7	18.6	22.2	24.0

Louisville Gas & Electric Co.--Financial Summary						
FOCF/debt (%)	(4.5)	0.9	1.4	(0.1)	7.2	9.2
DCF/debt (%)	(11.5)	(6.9)	(5.1)	(7.8)	(3.9)	(3.6)

Reconciliation Of Louisville Gas & Electric Co. Reported Amounts With S&P Global Adjusted Amounts (Mil. $)

		Debt	Shareholder Equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
Financial year	Dec-31-2023										
Company reported amounts		2,469	3,172	1,613	735	433	102	758	609	166	378
Cash taxes paid		-	-	-	-	-	-	(84)	-	-	-
Cash interest paid		-	-	-	-	-	-	(93)	-	-	-
Lease liabilities		15	-	-	-	-	-	-	-	-	-
Operating leases		-	-	-	5	1	1	(1)	4	-	-
Accessible cash and liquid investments		(18)	-	-	-	-	-	-	-	-	-
Asset-retirement obligations		67	-	-	4	4	4	-	-	-	-
Nonoperating income (expense)		-	-	-	-	4	-	-	-	-	-
Debt: Debt serviced by third parties		26	-	-	-	-	-	-	-	-	-
EBITDA: other income/ (expense)		-	-	-	14	14	-	-	-	-	-
D&A: other		-	-	-	-	(14)	-	-	-	-	-
Interest expense: other		-	-	-	-	-	3	-	-	-	-
Total adjustments		90	-	-	23	9	8	(178)	4	-	-
S&P Global Ratings adjusted		**Debt**	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from Operations**	**Operating cash flow**	**Dividends**	**Capital expenditure**
		2,559	3,172	1,613	758	442	110	580	613	166	378

Liquidity

We base our short-term 'A-2' rating on LG&E on our long-term issuer credit rating on the company. As of Sept. 30, 2024, we assess LG&E’s stand-alone liquidity as adequate because we expect the company’s liquidity sources will be more than 1.1x its uses over the next 12 months and meet its cash outflows even if its EBITDA declines by 10%. We believe the company's predictable regulatory framework provides LG&E with cash flow stability, even in times of economic stress.

In addition, the company has the ability to absorb high-impact, low-probability events. This reflects its recently upsized $600 million syndicated credit facility expiring December 2029. Furthermore, we believe LG&E could scale back its high capital spending during stressful periods, which indicates its limited need for refinancing under such conditions. Lastly, our assessment reflects the company's generally prudent risk management, sound relationships with banks (composed of a diversified banking group), and generally satisfactory standing in the credit markets.

Wholistically, these factors support our use of slightly lower thresholds to assess LG&E's liquidity compared with the thresholds we use for typical corporate borrowers. Overall, we believe the company will likely be able to withstand adverse market circumstances over the next 12 months with sufficient liquidity to meet its obligations. The company's next large long-term debt maturity of $300 million is in 2025, which we expect LG&E will proactively address in advance of its scheduled due date.

Principal liquidity sources

- Estimated cash FFO of about $560 million;
- Cash and liquid investments of about $10 million as of Sept. 30, 2024; and
- Revolving credit facility availability of $600 million as of Jan. 2, 2025.

Principal liquidity uses

- $300 million due in 2025;
- Capital spending of about $570 million; and
- Dividends of about $195 million.

Environmental, Social, And Governance

Environmental factors are a negative consideration in our credit rating analysis of LG&E, given its significant exposure to coal-based power generation. About 70% of its total generation capacity of about 2,800 MW is coal-fired, which represents an environmental risk. Over the longer term, the company expects to replace much of its coal-based generation with a combination of natural gas and renewables.

Group Influence

Under our group rating methodology, we consider LG&E to be a core subsidiary of parent PPL Corp. The core status reflects our view that LG&E is highly unlikely to be sold, has a strong long-term commitment from senior management, is successful at what it does, and contributes materially to the group. Given its core subsidiary status and our 'a-' group credit profile on PPL Corp., our long-term issuer credit rating on LG&E is 'A-'.

Issue Ratings--Recovery Analysis

Key analytical factors

LG&E's first-mortgage bonds benefit from a first-priority lien on substantially all the utility's real property owned or subsequently acquired. Collateral coverage of more than 1.5x supports a recovery rating of '1+' and an issue-level rating one notch above the long-term issuer credit rating.

Rating Component Scores	
Foreign currency issuer credit rating	**A-/Stable/A-2**
Local currency issuer credit rating	**A-/Stable/A-2**
Business risk	**Excellent**
Country risk	Very Low
Industry risk	Very Low
Competitive position	Strong
Financial risk	**Significant**
Cash flow/leverage	Significant
Anchor	**a-**
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Neutral (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	**a-**

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | Utilities: Collateral Coverage And Issue Notching Rules For '1+' And '1' Recovery Ratings On Senior Bonds Secured By Utility Real Property, Feb. 14, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Industry Credit Outlook North America Regulated Utilities, Jan 14, 2024
- PPL Electric Utilities Corp., June 25, 2024

Ratings Detail (as of January 24, 2025)*		
Louisville Gas & Electric Co.		
Issuer Credit Rating		A-/Stable/A-2
Commercial Paper		
Local Currency		A-2
Senior Secured		A
Issuer Credit Ratings History		
01-Jun-2015	*Foreign Currency*	A-/Stable/A-2
10-Jun-2014		BBB/Watch Pos/A-2
15-Apr-2011		BBB/Stable/A-2
01-Jun-2015	*Local Currency*	A-/Stable/A-2
10-Jun-2014		BBB/Watch Pos/A-2
15-Apr-2011		BBB/Stable/A-2
Related Entities		
Kentucky Utilities Co.		
Issuer Credit Rating		A-/Stable/A-2
Commercial Paper		
Local Currency		A-2
Senior Secured		A
PPL Capital Funding Inc.		
Issuer Credit Rating		A-/Stable/A-2
Senior Unsecured		BBB+
PPL Corp.		
Issuer Credit Rating		A-/Stable/A-2
PPL Electric Utilities Corp.		
Issuer Credit Rating		A/Stable/A-1
Commercial Paper		
Local Currency		A-1
Senior Secured		A+
Rhode Island Energy		
Issuer Credit Rating		A-/Stable/A-2
Commercial Paper		
Local Currency		A-2
Preferred Stock		BBB
Senior Secured		A
Senior Unsecured		A-

Ratings Detail (as of January 24, 2025)*

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.