FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms APUC and LUCo at 'BBB'; Downgrades APCo to 'BBB-'; Removes Evolving Watch

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Fitch Ratings - New York - 19 Mar 2024: Fitch Ratings has affirmed the Long-Term Issuer Default Ratings (IDRs) of Algonquin Power & Utilities Corp. (APUC) and its regulated utility subsidiary, Liberty Utilities Co. (LUCo) at 'BBB'. The Rating Outlook for APUC and LUCo is Stable.

In addition, Fitch has removed Algonquin Power Co. (APCo) from Rating Watch Evolving and has downgraded APCo's Long-Term IDR to 'BBB-' from 'BBB' and its Short-Term IDR to 'F3' from 'F2'. APCo has been assigned a Stable Rating Outlook. The downgrade reflects uncertainty about APCo's future capitalization, higher than expected leverage and weaker financial performance linked to 2023 wind resources below long-term average.

Fitch has also affirmed the debt security ratings for APUC, LUCo, Liberty Utilities Finance GP1 (Liberty Finance) and the companies' Short-Term IDRs at 'F2', and has downgraded APCo's debt security rating to 'BBB-' from 'BBB'.

APUC's Stable Rating Outlook and ratings affirmation is contingent on the company's ability to right size its capital structure and bring the leverage down in line with the current ratings following the sale of its Renewable Energy Group. Delay in the sale announcement and closure and/or less than expected proceeds could result in sustained leverage outside of APUC's current ratings threshold. However, this is not Fitch's base case at this time.

KEY RATING DRIVERS

Algonquin Power & Utilities Corp.

Transition to Fully Regulated Business: Following the expected divestiture of renewable assets, APUC's business risk profile will be supported by stable and predictable earnings from LUCo's regulated utility operations, which are expected to contribute about 85% of EBITDA post non-regulated assets divestiture. The remainder of EBITDA is coming from regulated businesses in Canada, Bermuda and Chile, supporting fully regulated low risk business profile with stable and predictable cash flows.

On Aug. 10, 2023, the company announced its plans to sell its Renewable Energy Group and transition into a fully regulated utility business. The company plans to use the sale proceeds to deleverage, and depending on the ultimate proceeds, buyback shares, to the extent that it maintains leverage metrics consistent with its current credit ratings.

Diversified Asset Base: LUCo benefits from its diversified portfolio of regulated utility operations across 13 states. LUCo was built from several acquisitions, most significantly of The Empire District Electric Company (Empire District), a Missouri electric utility, on Jan. 1, 2017. Empire District accounts for approximately more than 40% of LUCo's EBITDA.

APUC's integrated electric operations account for approximately 58% of rate base, natural gas distribution operations account for approximately 22%, and water and wastewater operations account for approximately 20% of rate base. This asset diversification mitigates the company's exposure to any regional or state specific shocks that could affect cash flows. Although APUC benefits from regulatory diversification, it owns utilities that, in Fitch's view, operate in somewhat less constructive regulatory environments. APUC's largest utility operates in Missouri.

Elevated Credit Metrics: APUC's leverage metrics over the past three years have remained high for its rating, with its 2023 FFO leverage rising to 7.9x. APUC's parent level debt is currently approximately 40% of total, higher than its peers at around 20%. However, Fitch expects this to decrease to approximately 30% in the forecast period as the company transitions into a fully regulated business.

APUC's ability to return to credit metrics commensurate with its 'BBB' rating will depend on its ability to execute the sale of the renewable's energy group. Delay in the potential sales process could weigh on the company's credit rating; however, it does not currently.

Upon completion of the Renewable Energy Group sale, Fitch expects the company to deleverage and remain below its current leverage sensitivity threshold of 5.8x FFO leverage over the forecast period. Given persistent high leverage, absence of the asset sales would require a significant equity issuance and/or capital expenditure cuts in order to support current ratings.

Parent/Subsidiary Linkage: Parent and subsidiary linkage exists between APUC and LUCo as determined by Fitch's "Parent and Subsidiary Linkage Rating Criteria". Fitch determines APUC's standalone credit profile (SCP) based on consolidated financial metrics.

LUCo's IDR is the same as APUC's. If Fitch were to consider LUCo's SCP stronger than APUC's, the linkage would follow a weak parent/strong subsidiary approach. Emphasis would be placed on the utilities' low-risk regulated operations across a number of utilities in U.S. The legal ring-fencing factor would be considered "open" due to LUCo being a holding company. The access & control factor would be considered "porous" as APUC centrally manages the treasury function for its subsidiaries and is the sole source of equity.

However, LUCo previously issued long-term debt through Liberty Finance and is planning to issue long-term debt directly through LUCo going forward. Fitch considers LUCo strategically important to APUC, accounting for a majority of APUC's consolidated EBITDA. Fitch would not rate APUC's Long-Term IDR higher than LUCo's; however, LUCo's Long-Term IDR could be up to one notch higher than APUC's.

Parent and subsidiary linkage exists between APUC and APCo. Fitch considers APCo's SCP weaker than APUC's given it's higher leverage and weaker non-regulated business performance, and follows a strong parent/weak subsidiary approach. Fitch considers legal incentive to be low because APUC does not guarantee APCo's debt. Strategic and operational incentives are also considered to be low due APUC's current plans to sell the renewables business in 2024. Therefore, APCo's Long-Term IDR is determined by its SCP.

Liberty Utilities Co.

Diversified Portfolio of Utilities: LUCo's rating reflects the company's low-risk regulated electric, natural gas, water and wastewater utility operations and adequate financial profile. LUCo benefits from its diversified portfolio of regulated utility operations across 13 states. This asset diversification mitigates the company's exposure to any regional or state-specific shocks that could affect cash flows.

LUCo was built up through several acquisitions, most significantly of The Empire District Electric Company (Empire District) in 2017, which operates in Missouri, accounts for more than 40% of LUCo's EBITDA. Historically, LUCo has been acquisitive, primarily looking for smaller utility systems that could benefit from operational efficiencies. Fitch does not expect any material acquisitions over the forecast period following the termination of the Kentucky Power acquisition last year.

Balanced Regulatory Environment: Fitch views LUCo's overall regulatory environment as balanced. The company's authorized ROEs range from 8.9% - 9.7% across its jurisdictions, averaging 9.4%, which is modestly below industry averages. Empire Electric, the largest of LUCo's utilities, is authorized an ROE of 9.3% and a 50% equity ratio. The company had recently completed several rate cases, including CalPeco Electric Systems (CalPeco Electric) authorizing an annual revenue increase of $27.0 million in 2023.

The company is currently involved in several regulatory proceedings requesting $105.8 million in total revenue increases, including New York Water with a $39.7 million rate case, and EnergyNorth Gas for $27.5 million. Fitch assumes regulatory outcome in line with the historical results. Fitch believes LUCo's balanced and diversified regulatory environment supports its solid business risk profile.

The company has invested approximately $500 million towards the implementation of a new ERP system. This investment has not yet been added into its rate base and management expects it can do so with its current/future rate case filings. Reduction in regulatory lag related to its investment in the ERP system would be credit positive for LUCo moving forward.

Manageable Wildfire Risk: In recent years, severe weather and wildfires that cause major damages and claims against utility companies have become more frequent. On Nov. 17, 2020, the Mountain View Fire broke out in CalPeco Electric (Wholly owned by LUCo) system's service territory in California. The cause of the fire remains under investigation and CAL Fire has not yet released its final report. The company is currently named in 21 lawsuits in connection with the wildfire seeking damages.

During 2023, the company accrued an estimated loss of $66 million related to the Mountain View Fire. The company had wildfire liability insurance that is expected to apply up to applicable policy limits. LUCo's ownership in CalPeco benefits from legal ring-fencing which should protect the parent LUCo from damages in excess of its investment in CalPeco.

Empire District, the largest utility owned by LUCo operates in the state of Missouri which has relatively moderate to low wildfire risk. With insurance coverage to protect against wildfire damages and ongoing wildfire mitigation investment, Fitch believes LUCo's wildfire risk to be manageable.

Adequate Financial Metrics: LUCo's financial profile is supported by stable and predictable earnings from regulated utility operations. Fitch expects 2023 FFO leverage at 4.9x, in line with historical results. Fitch projects LUCo's FFO leverage to average around 5.0x, in line with the ratings, over the forecast. The company benefits from the more regular rate case filings and 2024 securitization proceeds at Empire District. LUCo's overall regulatory environment is considered balanced, although it has recently been affected by regulatory lag on its implementation of a new ERP system.

Liberty Finance is a financing vehicle for LUCo and until now has been used to issue long-term senior unsecured debt for LUCo. With the recent issuance and going forward LUCo is planning to issue senior unsecured debt only at LUCo. All remaining outstanding debt of Liberty Finance is fully and unconditionally guaranteed by LUCo and ranks pari passu with LUCo's senior unsecured debt. Liberty Finance senior unsecured debt rating is 'BBB+'. The senior unsecured ratings for operating utilities receive a one notch uplift relative to the IDR as per Fitch's criteria.

Algonquin Power Co.

Leverage Elevated: Fitch has downgraded APCo's ratings due to the higher than expected leverage driven by higher operational costs and lower resource generation vs. Fitch's previous projections. Following a year of challenging weather resources for the renewable energy business, APCo's FFO leverage has elevated to 9.6x in our 2023 forecast, well above negative sensitivity threshold and Fitch projections. In addition, going forward EBITDA contribution is projected to be lower than Fitch previously expected due to a shift in the strategy pending sale of the business.

Given APUC's announced plan to sell the business, the creditworthiness of the ultimate buyer, business capitalization post sale and the parent-subsidiary linkage relationship with the buyer will guide APCo's ratings. Fitch expects to have more clarity on the transaction in the next three to six months, with company management targeting a potential transaction announcement in mid-2024.

Diversified Long-term Contracted Assets: Approximately 84% of APCo's electrical output is sold pursuant to long-term contractual arrangements with a production-weighted average remaining contract life of 10 years as of Dec. 31, 2023. This provides a long timeline of relatively stable cash flows. APCo owns 46 power facilities totaling 2.7GW of net generation capacity, which provides for meaningful asset diversification. Three-quarters of APCo's EBITDA is derived from U.S.-based assets, with the remainder from Canadian assets.

APCo has a strong pipeline of over approximately 8GW of solar and wind projects, more than half of which have site certainty and are in interconnection queues. Approximately

300MW of solar projects in various stages are under construction.

DERIVATION SUMMARY

Algonquin Power & Utilities Corp.

APUC is positioned slightly weaker compared to other 'BBB' rated holding companies in Fitch's coverage universe, such as CMS Energy Corporation (CMS; BBB/Stable) and American Electric Power Company, Inc. (AEP; BBB/Stable), but stronger than Emera Incorporated (Emera; BBB/Negative). Fitch expects APUC's proportion of consolidated EBITDA from regulated utility operations following renewable assets divestiture to be in line with its peers CMS, AEP and Emera, at which 95% or more of earnings come from regulated operations.

FFO leverage metrics are weaker than those of CMS and AEP, which are projected to average roughly 5.0x and 5.8x, respectively, over the next few years. Emera's FFO leverage is projected to remain elevated at approximately 6.5x in2024. Fitch projects APUC's FFO leverage will improve to roughly 5.7x in 2026 as the company transitions to a fully regulated business and uses divestiture proceeds to reduce parent level debt.

APUC has the most geographically diverse asset mix compared with peers, as it operates across more than a dozen states in the U.S., Canada, Bermuda and Chile. APUC also benefits from industry diversification, as it owns electric, natural gas and water utilities. The portfolio compares favorably with larger single-state utilities from a diversification perspective, but its larger peers may benefit more from efficiencies of scale. APUC also owns utilities that operate in somewhat less constructive regulatory environments, in Fitch's view, with APUC's largest utility operating in Missouri.

AEP is also well diversified geographically, with a much larger scale of operations than APUC. CMS owns a single-state utility in a constructive regulatory environment in Michigan. Emera operates in a few states in the U.S., Canada and the Caribbean, with the primary earnings driver coming from its largest utility operating in a very constructive Florida regulatory environment with strong customer growth.

AEP's and CMS's parent-level debt is expected to be approximately 20% over the forecast period. Emera's parent-level debt is expected to be higher at approximately 40% to 50%. APUC's parent debt is also elevated at roughly 40% of total debt and is projected to decrease to 30% as it transitions into a fully regulated utility company following the sale of its Renewable Energy Group.

Liberty Utilities Co

LUCo benefits from significant geographic and regulatory diversification. The company consists of electric, natural gas, and water and wastewater utilities in 13 states. This portfolio compares favorably with larger single-state utilities from a diversification perspective, although its larger peers may benefit more from efficiencies of scale. A significant amount of LUCo's EBITDA is exposed to Missouri, which historically has had a somewhat challenging regulatory environment, although it became more balanced in recent years.

Peer Southwestern Public Service Company (SPS; BBB/Stable) is an integrated electric utility that operates in two states, Texas and New Mexico, with more challenging regulatory environments. SPS lacks the diversification of LUCo, but it is a larger utility that also benefits from being a subsidiary of higher-rated Xcel Energy Inc. (BBB+/Negative), a much larger and fully regulated utility family. Fitch views Wildfire risks for SPS's to be higher than LUCo's in light of recent wildfires within SPS's service territory. LUCo's financial metrics are weaker than those of SPS. Fitch forecasts LUCo's FFO leverage to remain in line with the ratings through 2028. Fitch expects SPS's FFO leverage to average roughly 4.0x over the forecast period.

Algonquin Power Co.

APCo benefits from having approximately 84% of its generation under long-term contractual arrangements with investment-grade counterparties, mitigating some of the risk associated with its unregulated operations. The average length of its long-term contractual arrangements is approximately 10 years, which provides APCo with a good runway of relatively predictable cash flows.

Southern Power Company (BBB+/Stable) has a similarly percentage of generation under long-term contracts. APCo owns and operates approximately 2.7GW of net generation capacity spread across 11 U.S. states and six Canadian provinces, providing beneficial geographic diversification. Southern Power has a much larger generation portfolio with more than 12.5GW of generation capacity in 14 states across U.S. Southern Power's financial metrics are stronger than APCO's, with FFO leverage projected in the range of 3.0x-4.0x over 2024-2025.

KEY ASSUMPTIONS

Algonquin Power & Utilities Corp.

--Divestiture of all non-regulated businesses, proceeds used to deleverage the balance sheet;

--Approximately $1 billion annual capex run rate post sale of the renewables group;

--$1.15 billion of convertible equity converts in 2024;

--Dividend 4% yield in 2024 and forward;

--Securitization debt and related revenue to serve the debt is excluded from the FFO Leverage calculation;

--Interest rates for newly issued debt at around 6% over the forecast period.

RATING SENSITIVITIES

Algonquin Power & Utilities Corp.

Factors that could, individually or collectively, lead to a positive rating action/upgrade:

--Consolidated FFO leverage expected to remain at less than 4.8x on a sustained basis following full divestiture of the non-regulated operations.

Factors that could, individually or collectively, lead to a negative rating action/downgrade:

--Consolidated FFO leverage expected to exceed 5.8x on a sustained basis following full divestiture of the non-regulated operations;

--An additional increase to the ratio of parent-level debt to consolidated debt;

--A downgrade of LUCo's Long-Term IDR would result in a commensurate downgrade of APUC's Long-Term IDR.

Algonquin Power Co.

Factors that could, individually or collectively, lead to a positive rating action/upgrade.

--FFO leverage expected to remain at less than 4.5x on a sustained basis.

Factors that could, individually or collectively, lead to a negative rating action/downgrade:

--FFO leverage expected to exceed 6.0x on a sustained basis;

--A significant decrease in the percentage of generation under long-term contracts.

Liberty Utilities Co.

Factors that could, individually or collectively, lead to a positive rating action/upgrade:

--FFO leverage expected to remain at less than 4.8x on a sustained basis.

Factors that could, individually or collectively, lead to a negative rating action/downgrade:

--FFO leverage expected to exceed 5.8x on a sustained basis;

--Adverse regulatory decisions that result in less-timely cost recovery or significantly weaker financial metrics;

--A two-notch downgrade of APUC's Long-Term IDR would result in a downgrade of LUCo's Long-Term IDR.

LIQUIDITY AND DEBT STRUCTURE

Algonquin Power & Utilities Corp.

Adequate Liquidity: Fitch considers APUC's liquidity adequate. On March 31, 2023, APUC's senior unsecured revolving credit facility was amended and restated to increase the borrowing capacity to $1.0 billion from $500.0 million with a new maturity date of March 31, 2028. As of Dec. 31, 2023, APUC's $1.0 billion senior unsecured corporate revolving credit facility had $779.1 million drawn and $2.4 million of outstanding LOCs. As of Dec. 31, 2023, the company had issued $35.5 million of LOCs from its $75.0 million uncommitted LOC facility. Long-term debt maturities are manageable.

Liberty Utilities Co.

Adequate Liquidity: Fitch considers LUCo's liquidity to be adequate. LUCo primarily meets its short-term liquidity needs through the issuance of CP under its $500 million CP program. LUCo also has a $1.0 billion senior unsecured revolving credit facility (RCF) that matures on April 29, 2027. The company also has access to a $1.0 billion delayed draw term facility maturing on Oct. 25, 2024.

As of Dec. 31, 2023, LUCo's $1.0 billion senior unsecured revolving credit facility had $371.0 million drawn and $39.2 million of outstanding LOCs. As of Dec. 31, 2023, LUCo had $481.7 million of commercial paper issued and outstanding. LUCo's $500.0 million short-term credit facility had $125 million drawn and no outstanding letters of credit. LUCo's $1.0 billion delayed draw term facility had $610.4 million drawn. On Jan. 12, 2024 the company issued $500 million and $350 million of senior unsecured notes used to repay its debt including credit facility balances. LUCo requires modest cash on hand to fund its operations. Long-term debt maturities over the next five years are manageable.

Algonquin Power Co.

Adequate Liquidity: Fitch considers APCo's liquidity adequate. APCo's liquidity is primarily supported by a $500 million senior unsecured syndicated revolving credit facility (RCF) that matures July 22, 2027. APCo had $262.6 million drawn and $6.6 million in outstanding LOC as of Dec. 31, 2023. APCo has $600 million of LOC facilities made up of a $250 million uncommitted bilateral LOC facility and a $350 million uncommitted LOC facility. As of Dec. 31, 2023 APCo LOC had $385.4 million in outstanding LOC.

ISSUER PROFILE

Algonquin Power & Utilities Corp. (APUC) is a diversified international generation, transmission and distribution utility and power holding company. APUC is domiciled in Ontario, Canada, but more than 90% of APUC's consolidated EBITDA is derived from the company's U.S. operations.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means 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. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Algonquin Power Co.	LT IDR	BBB- Rating Outlook Stable	Downgrade	BBB
	ST IDR	F3	Downgrade	F2
senior unsecured	LT	BBB-	Downgrade	BBB
Liberty Utilities Finance GP1				
senior unsecured	LT	BBB+	Affirmed	BBB+
Liberty Utilities Co.	LT IDR	BBB Rating Outlook Stable	Affirmed	BBB Rating Outlook Stable
	ST IDR	F2	Affirmed	F2
senior unsecured	LT	BBB+	Affirmed	BBB+
senior unsecured	ST	F2	Affirmed	F2
Algonquin Power & Utilities Corp.	LT IDR	BBB Rating Outlook Stable	Affirmed	BBB Rating Outlook Stable

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Corporate Hybrids Treatment and Notching Criteria (pub. 12 Nov 2020)

Parent and Subsidiary Linkage Rating Criteria (pub. 16 Jun 2023)

Corporates Recovery Ratings and Instrument Ratings Criteria (pub. 13 Oct 2023) (including rating assumption sensitivity)

Corporate Rating Criteria (pub. 03 Nov 2023) (including rating assumption sensitivity)

Sector Navigators – Addendum to the Corporate Rating Criteria (pub. 03 Nov 2023)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Algonquin Power & Utilities Corp.	EU Endorsed, UK Endorsed
Algonquin Power Co.	EU Endorsed, UK Endorsed
Liberty Utilities Co.	EU Endorsed, UK Endorsed
Liberty Utilities Finance GP1	EU Endorsed, UK Endorsed

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The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. For more details on sector-specific best- and worst-case scenario credit ratings, please see Best- and Worst-Case Measures under the Rating Performance page on Fitch's website.

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