Moody's Investors Service

Global Credit Research
Credit Opinion
16 DEC 2005

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Credit Opinion: Union Electric Company

Union Electric Company

St. Louis, Missouri, United States

Ratings

Category	Moody's Rating
Outlook	Rating(s) Under Review
Issuer Rating	*A2
First Mortgage Bonds	*A1
Senior Secured	*A1
Senior Unsecured Shelf	*(P)A2
Subordinate	*A3
Preferred Stock	*Baa1
Commercial Paper	*P-1
Parent: Ameren Corporation	
Outlook	Rating(s) Under Review
Issuer Rating	*Baa1
Sr Unsec Bank Credit Facility	*Baa1
Senior Unsecured	*Baa1
Subordinate Shelf	*(P)Baa2
Preferred Shelf	*(P)Baa2

Commercial Paper	*P-2

Union Electric Capital Trust I

Outlook	Rating(s) Under Review
Bkd Preferred Shelf	*(P)A3

* Placed under review for possible downgrade on December 15, 2005

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Key Indicators

Union Electric Company	3Q05 LTM	2004	2003	2002
Adjusted Funds from Operations + Adjusted Interest / Adjusted Interest [1]	7.73	7.01	7.06	6.47
Adjusted Funds from Operations / Adjusted Debt [2][3]	35%	30%	31%	30%
Retained Cash Flow / Adjusted Debt [3]	23%	17%	19%	17%
Adjusted Debt / Adjusted Capitalization [3][4]	45%	46%	44%	44%
Common Dividends / Net Income Available for Common	78%	84%	65%	89%
Net Income Available for Common / Common Equity	13%	13%	16%	13%

[1] Interest is adjusted to include preferred dividends and lease payments [2] Preferred dividends have been deducted from FFO [3] Adjusted debt includes 8x next year's operating leases [4] Adjusted capitalization reflects the adjustments made to debt

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Credit Strengths

The credit strengths of AmerenUE (Union Electric Company) include:

- Strong and stable debt service coverage measures

- Solid balance sheet with moderate, though increasing, leverage

- Low cost generating assets and competitive rates

- New fuel, purchased power, and environmental cost recovery mechanism passed in Missouri

- Potentially improving regulatory situation in Missouri

Credit Challenges

The credit challenges of AmerenUE (Union Electric Company) include:

- Negative free cash flow due to a large environmental capital expenditure program

- Additional leverage incurred to finance these capital expenditures

- Increasing pension, employee benefit, insurance and nuclear operating costs

- Rising coal and transportation prices are hurting margins

- Regulatory risk with regard to potential rate case in 2006 and MPSC enactment of cost recovery mechanism

Rating Rationale

AmerenUE's A1 senior secured debt rating reflects the company's strong debt service coverage measures, good financial metrics, conservative management, and low production costs. The rating also reflects high capital expenditures for new generating capacity, for environmental compliance, to upgrade its transmission and distribution system, and for the replacement of steam generators at the Callaway nuclear plant, which will negatively affect cash flow and coverage ratios going forward.

AmerenUE's cash flow has traditionally been strong and stable, although it has fallen short of covering dividends and high capital expenditures for several years, resulting in negative free cash flow over the last three years. AmerenUE's capital expenditures were $629 million during the first three quarters of 2005, up from $374 million over the same period last year. To finance higher capital expenditures, AmerenUE's debt to capitalization ratio has increased from its historical 40% range and to approximately 45%, and is expected to remain in this range going forward.

AmerenUE has experienced the adverse effects of a slow economy, rising employee benefit costs, and higher insurance and security costs in recent years. In addition, the company expects coal prices to increase significantly in 2006 and 2007. AmerenUE is also one of a declining number of single asset nuclear plant operators in the country, with its Callaway nuclear plant experiencing an overall decline in performance during 2004, resulting in significant unanticipated replacement power and maintenance costs last year.

AmerenUE operates under a rate plan which was approved by the MPSC in 2002 and which includes a rate moratorium through July 1, 2006. The company expects to submit a cost of service study shortly, at which point it will determine if it will file for a rate increase in 2006. On July 14, 2006, the governor signed legislation permitting the state's utilities, including AmerenUE, to apply to the MPSC for fuel, purchased power, and environmental cost recovery. With coal and coal transportation prices rising, the enactment of recently passed cost recovery mechanisms by the MPSC is an important credit consideration.

Rating Outlook

The rating is on review for possible downgrade, reflecting our expectation of some deferral of expected rate increases for Ameren's Illinois utilities and the likelihood that if the operating cash flow of the Illinois utilities declines, Ameren would need to rely on its Missouri operations for a larger share of cash flow and upstreamed dividends to meet parent company obligations. The review will focus on the prospects for a resolution of the on-going dispute in Illinois, clarity regarding the amount and timing of any related rate increases, the mechanisms for ultimate recovery of the utilities' increased costs and investment outlays, and the regulatory climate for the utilities going forward.

What Could Change the Rating - UP

The review for downgrade limits the near term upside potential for the rating.

What Could Change the Rating - DOWN

Regulatory environment for Ameren's Illinois utilities deteriorates further, a material deferral of power costs in Illinois results in an increased reliance by Ameren on dividends from its Missouri utility, a decline in AmerenUE's cash flow coverage measures, including FFO/Interest below 5.0x, FFO/Debt below 20%; an increase in debt to capitalization above the 45% range; a continuation of higher operating expense trends; unanticipated capital expenditure requirements; a lengthy unanticipated outage at the Callaway nuclear plant.