

MOODY'S

INVESTORS SERVICE

Rating Action: Moody's downgrades FirstEnergy Solutions' CFR to Ca from Caa1 and maintains negative outlook

Global Credit Research - 23 Jan 2018

New York, January 23, 2018 -- Moody's Investors Service, ("Moody's") downgraded FirstEnergy Solutions Corp.'s (FES) corporate family rating (CFR) to Ca from Caa1 and the probability of default rating (PDR) to Ca-PD from Caa1-PD. FES's rating outlook remains negative. FES' speculative grade liquidity rating was also downgraded to SGL-4 from SGL-3. The three-notch downgrade reflects the increased likelihood of a default occurring within the next few months.

Downgrades:

..Issuer: Beaver (County of) PA, Industrial Devel Auth

...Senior Secured Revenue Bonds, Downgraded to B3(LGD1) from B1(LGD1)

...Senior Unsecured Revenue Bonds, Downgraded to Ca(LGD4) from Caa1(LGD4)

..Issuer: Bruce Mansfield Unit 1

...Senior Secured Pass-Through, Downgraded to Ca(LGD4) from Caa1(LGD4)

..Issuer: FirstEnergy Solutions Corp.

... Probability of Default Rating, Downgraded to Ca-PD from Caa1-PD

... Speculative Grade Liquidity Rating, Downgraded to SGL-4 from SGL-3

... Corporate Family Rating, Downgraded to Ca from Caa1

...Senior Unsecured Regular Bond/Debenture, Downgraded to Ca(LGD4) from Caa1(LGD4)

..Issuer: Ohio Air Quality Development Authority

...Senior Secured Revenue Bonds, Downgraded to B3(LGD1) from B1(LGD1)

...Senior Unsecured Revenue Bonds, Downgraded to Ca(LGD4) from Caa1(LGD4)

..Issuer: Ohio Water Development Authority

...Senior Secured Revenue Bonds, Downgraded to B3(LGD1) from B1(LGD1)

...Senior Unsecured Revenue Bonds, Downgraded to Ca(LGD4) from Caa1(LGD4)

..Issuer: Pennsylvania Economic Dev. Fin. Auth.

...Senior Secured Revenue Bonds, Downgraded to B3(LGD1) from B1(LGD1)

...Senior Unsecured Revenue Bonds, Downgraded to Ca(LGD4) from Caa1(LGD4)

Outlook Actions:

..Issuer: FirstEnergy Solutions Corp.

...Outlook, Remains Negative

RATINGS RATIONALE

"Both the probability of default and expected losses are high," stated Moody's analyst Jairo Chung. FES's parent FirstEnergy Corp. announced that it has formed a restructuring working group in anticipation of FES

either restructuring its debt or filing for bankruptcy in the near future. The newly formed restructuring group will advise FirstEnergy on its strategy to exit the merchant power generation business. Moody's expects the likelihood of FES repaying its \$98.9 million senior unsecured bond maturity on April 2nd is very low. Moody's views the formation of the restructuring working group as an indication that FES is getting closer to default.

In addition, there are no clear avenues for additional regulatory or political intervention aimed at providing any additional cash flows to FES. The two previous regulatory intervention opportunities failed to be implemented, including state legislation in Ohio and federal plans through the Federal Energy Regulatory Commission's (FERC) and the Department of Energy (DOE).

The Ca CFR and Ca-PD PDR reflect Moody's expectation that the probability of FES defaulting on its April bond payment is very high, and expected loss for the senior unsecured bonds to range 50% and 70%.

Rating Outlook

The negative outlook reflects the higher certainty around FES' unwillingness to make its next bond payment due in April 2018.

Liquidity

FES's speculative grade liquidity rating was lowered to SGL-4 from SGL-3. The SGL-4 reflects FES' inadequate internally generated cash flow, the likely covenant violation that will occur with a default, and the need to rely on its external sources of financing to cover its costs. Furthermore, Moody's believes FES has a very limited alternative liquidity sources such as asset sale, to raise cash.

FES has access to a secured credit facility with FirstEnergy for \$500 million and additional credit support for \$200 million, all of which is utilized to cover surety bond obligations. The credit facility is secured by the first mortgage bonds issued by two of FES' subsidiaries, FirstEnergy Nuclear Generation (NG) and FirstEnergy Generation (FG). In the case of restructuring or bankruptcy filing, it is uncertain whether this credit facility will continue to be treated as secured in a liability waterfall. For the period ending 30 September 2017, FES had all \$500 million available under this facility. However, FES's ability to use more than \$100 million is limited because FES must maintain a minimum availability of \$400 million to provide support for NG. FES continues to participate in the FirstEnergy's unregulated money pool for liquidity to supplement for the limit on its use of the secured credit facility. As of 30 September 2017, FES, its subsidiaries, and FENOC had net \$67 million borrowings in aggregate from the money pool.

Factors That Could Lead to an Upgrade

A rating upgrade is unlikely. However, if there are power market improvements that results in sustained improvements in FES' credit fundamentals, a rating upgrade could be considered.

Factors That Could Lead to a Downgrade

FES's CFR will be downgraded further if the company files for bankruptcy protection or restructures its debt through a distressed exchange.

FirstEnergy Solutions Corp. is a wholly-owned subsidiary of FirstEnergy Corp. and is a regional competitive electric producer and provider in the PJM Interconnection market. FES controls approximately 10.2 GW of power generation capacity, including super-critical coal-fired generation (3,690 MW), nuclear generation (4,048 MW), sub-critical coal-fired generation (1,256 MW), gas- and oil-fired generation (690 MW) and renewable generation (496 MW).

The principal methodology used in these ratings was Unregulated Utilities and Unregulated Power Companies published in May 2017. Please see the Rating Methodologies page on www.moody.com for a copy of this methodology.

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