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CREDIT OPINION
8 November 2022

Update

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RATINGS

New York State Electric and Gas Corporation

Domicile	New York, United States
Long Term Rating	Baa1
Type	LT Issuer Rating
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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New York State Electric and Gas Corporation

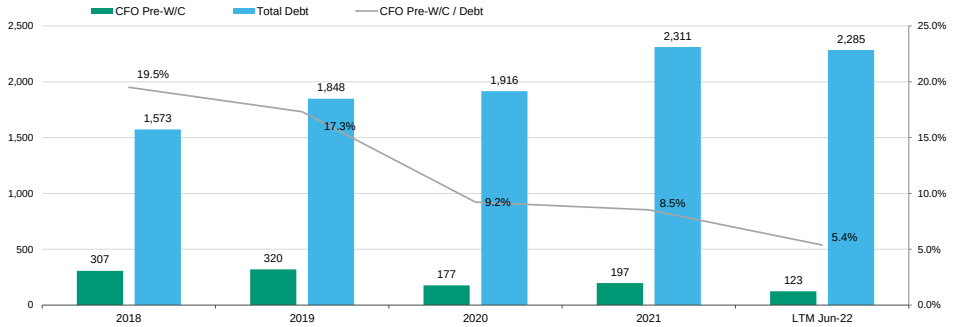
Update to credit analysis

Summary

New York State Electric and Gas Corporation's (NYSEG) credit profile reflects: 1) its low business risk transmission and distribution (T&D) operations, 2) a transparent regulatory framework with supportive cost recovery provisions and 3) several ring-fencing type provisions that are in place to insulate the utility from the higher business risk of its affiliates and parent company.

NYSEG's credit is constrained by extremely weak and declining financial metrics and the need for material cash flow improvement at a time of recessionary-type economic pressures. As such, material rate increases could prove challenging for the company's current rate case filing. Uncertainty also exists as to the future of its natural gas business and associated depreciation recovery as New York pursues a path toward reducing economy wide greenhouse gas emissions.

Exhibit 1
Historical CFO Pre-WC, Total Debt and CFO Pre-WC to Debt ($ MM)



Source: Moody's Financial Metrics

Credit strengths

» Low business risk transmission and distribution utility assets

» Operates under a revenue decoupling mechanism which helps to support fixed cost recovery, regardless of volumetric demand

» Ring-fencing type provisions and stand-alone liquidity provide some insulation from riskier affiliates

Credit challenges

» Weaker than expected financial metrics

» Increasing operating and capital costs amid customer affordability concerns

» Uncertainties surrounding New York energy policy and path toward decarbonization

Rating outlook

NYSEG's stable outlook considers that the company is in the midst of a material general rate case filing that will determine the future trajectory of its financial metrics. While metrics are very weak now, a credit supportive rate order could improve the ratio of CFO pre-WC to debt to above 14%.

Factors that could lead to an upgrade

» A material improvement in the credit supportiveness of NYSEG's political and regulatory framework

» Stronger financial metrics, such that its CFO pre-WC to debt ratio is 19% or higher on a sustained basis

Factors that could lead to a downgrade

» Inadequate rate relief provided by the current rate filing, such that CFO pre-WC to debt remains below 14%

» A lower degree of rate support in New York State, including as it pertains to the climate action measures under consideration by the state and NYPSC

Key indicators

New York State Electric and Gas Corporation's [1]

	Dec-18	Dec-19	Dec-20	Dec-21	LTM Jun-22
CFO Pre-W/C + Interest / Interest	5.0x	4.7x	3.2x	4.0x	2.8x
CFO Pre-W/C / Debt	19.5%	17.3%	9.2%	8.5%	5.4%
CFO Pre-W/C – Dividends / Debt	19.5%	11.9%	4.0%	-3.2%	-6.4%
Debt / Capitalization	45.1%	47.9%	43.5%	46.8%	43.4%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Source: Moody's Financial Metrics

Profile

New York State Electric & Gas (NYSEG) is the largest regulated electric and gas distribution utility subsidiary of Avangrid Networks Inc. (Networks, not rated), a direct subsidiary of Avangrid Inc. (Avangrid Baa2 stable). NYSEG's 2022 rate base is about $3.9 billion (nearly 80% electric and about 20% gas), or about 30% of Networks' total $13 billion rate base at September 2022. The company's operations are regulated by the New York Public Service Commission (NYPSC) and the Federal Energy Regulatory Commission.

Avangrid is a publicly listed diversified utility holding company with the company's regulated operations accounting for about 80% of operating cash flow. Avangrid's primary owner is Iberdrola S.A. (Baa1 stable). Iberdrola owns an 81.6% stake in the company with the remaining 18.4% being held by the public. Iberdrola is a global diversified energy company primarily operating in Spain, the United Kingdom, the United States, Mexico and Brazil.

Detailed credit considerations

Financial metrics continue to be lower than expected

NYSEG's financial metrics are extremely weak and below our previous expectations of low-to-mid-teen's percentage range for the ratio of CFO pre-WC to debt. The current approximately 5% ratio is among the lowest in the industry, reflecting sizeable regulatory asset and liability fluctuations due to storm costs in Q2 2022 and rate mitigation measures implemented in NYSEG's 2020 rate order.

After the 2020 order, we projected that the CFO pre-WC to debt ratio would initially be weak for NYSEG's Baa1 rating, but that an improvement would occur year-over-year due to backloaded revenue increases through April 2023. The cash flow weakness of the rate plan is due to sizeable rate moderation measures enacted by the NYPSC (via "excess depreciation reserves" and the amortization schedule of regulatory assets and liabilities), in response to economic hardships of the COVID-19 pandemic.

Current rate case is critical for financial improvement

NYSEG's very weak financial profile makes its 2022 rate case filing extremely important to the credit trajectory of the company. In May 2022, NYSEG filed for electric and gas revenue increases of approximately $274 million and $43 million, respectively, which would result in average residential bill increases of 22.2% and 15.6%, respectively. In particular, the company cited that roughly 10% of the overall rate request, for both NYSEG and affiliate utility Rochester Gas & Electric (RG&E, Baa1 stable), is due to the residual rate pressure from the previous rate plan. The request was also based on 50% equity capitalization and a 10.2% ROE.

Despite the rationale put forth in NYSEG's filing, we see this level of rate increase as unlikely given the current economic pressures facing the company's customers and service territory. Along these lines, the NYPSC staff issued testimony in September 2022 recommending electric and gas revenue increases of around $220 million and almost $10 million, respectively (based on a 48% equity capitalization and 8.85% ROE).

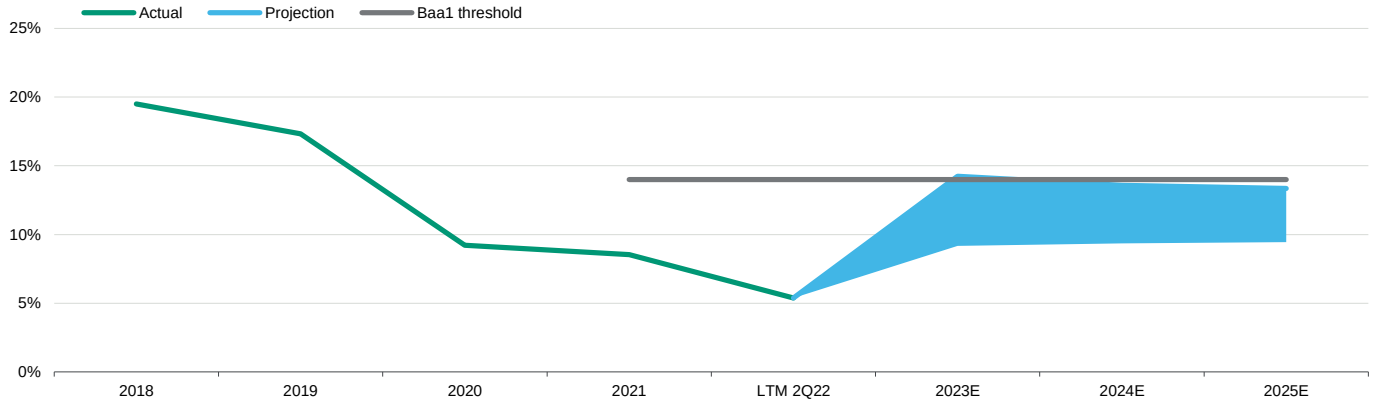
While the rate base, allowed ROE and equity layer are important factors for the company's financial profile, we view the ultimate NYPSC decisions around regulatory asset and liability amortization as more critical to the cash flow profile of the company.

Given the uncertainty associated with the regulatory accounts and political influence over bill rate mitigation, we project NYSEG's cash flow under multiple scenarios. These scenarios range from an essentially neutral regulatory asset/liability contribution (i.e., where cash flow is primarily driven by rate base, allowed returns and capitalization) to one maintaining the average cash outflow NYSEG experienced in the 2020-LTM 2Q22 period in long-term regulatory accounts (including other long-term assets and liabilities), or about $150 million per annum. The resulting CFO pre-WC to debt ratio range of these scenarios is seen in the exhibit below. Our estimates indicate that NYSEG may find it challenging to maintain cash flow to debt ratios above its 14% financial metric threshold for a possible downgrade.

At the same time, we note that if NYSEG is awarded largely what it requested in the filing, including recovery of the residual items from the 2020 order, CFO pre-WC to debt ratios will likely outperform these scenarios and be in the mid-to-high teen's percent range. We also note that the company froze its pension in Q1 2022, which will help to temper the amount of debt imputed in our adjusted metrics and improve leverage ratios, all else being equal.

Exhibit 3

NYSEG's ratio of CFO pre-WC to debt is expected to remain below historical levels through 2023



The financial metric threshold indicated is one of several factors that could cause a downgrade if the metric is below that level for a sustained period of time.
Source: Moody's Financial Metrics and Moody's projections

Regulatory framework offers a strong suite of cost recovery provisions

A significant aspect of NYSEG's credit support resides in the transparency of the NYPSC regulatory framework, which includes a suite of cost recovery mechanisms that allow the company to recover various costs on a timely basis. The most important features are a forward-looking test year (for most expenses and all planned capital expenditures), full recovery of purchased electric and natural gas costs and electric and gas revenue decoupling mechanisms (RDMs) for the majority of customers. Utilities within the state have often operated under multiyear rate plans, which allows recovery of projected capital and operating costs commensurate with the spend.

These features provide quick cost recovery that had historically underpinned stable and predictable financial metrics. The RDMs, in particular, help to provide stable gross margin regardless of the volume sold to customers. This is an important feature, since it should keep the company's financial profile intact as the industry transitions to a more efficient and distributed network.

While the multiyear nature of rate plans has been a material positive for several years, we acknowledge that today's rising cost environment could expose a utility to inadequate rates if inflationary pressures (including higher interest rates) continue, and if that is not adequately encapsulated within the rate plan. NYSEG has tried to address this risk by including an inflation factor and reconciliation mechanism in its current rate filing.

Longer-term challenges face NYSEG's gas business, but electric business should benefit

Part of NYSEG and RG&E's existing rate plans includes a commitment to a zero-net increase in natural gas volumes through April 2023. According to the agreement, this means that weather-normalized levels of billed gas use for NYSEG and RG&E will not exceed gas use of approximately 56 million dekatherms for NYSEG and around 53 million dekatherms for RG&E.

We expect the trend of curbing demand to continue and lead to longer-term challenges for NYSEG's and RG&E's collective gas business, as the companies and stakeholders attempt to meet the goals of New York's Climate Leadership and Community Protection Act (CLCPA). The CLCPA targets 100% zero-emission electricity by 2040 and an 85% reduction of greenhouse gas emissions by 2050.

Along these lines, a 22 member New York Climate Action Council (CAC) is tasked with making recommendations for achieving these goals and issued a Draft Scoping Plan in December of 2021. The plan included various emission reduction scenarios, all of which pointed to a material downsizing of the fossil gas system (mostly via electrification), which raises credit risk for state gas distribution companies. Dialogue around the specific requirements of the Draft Scoping Plan have been ongoing and a Final Scoping Plan is expected at year-end 2022. We also expect that it will take some time for the NYPSC to understand the ramifications of the CAC's Final Plan and institute rulemaking for utilities to follow.

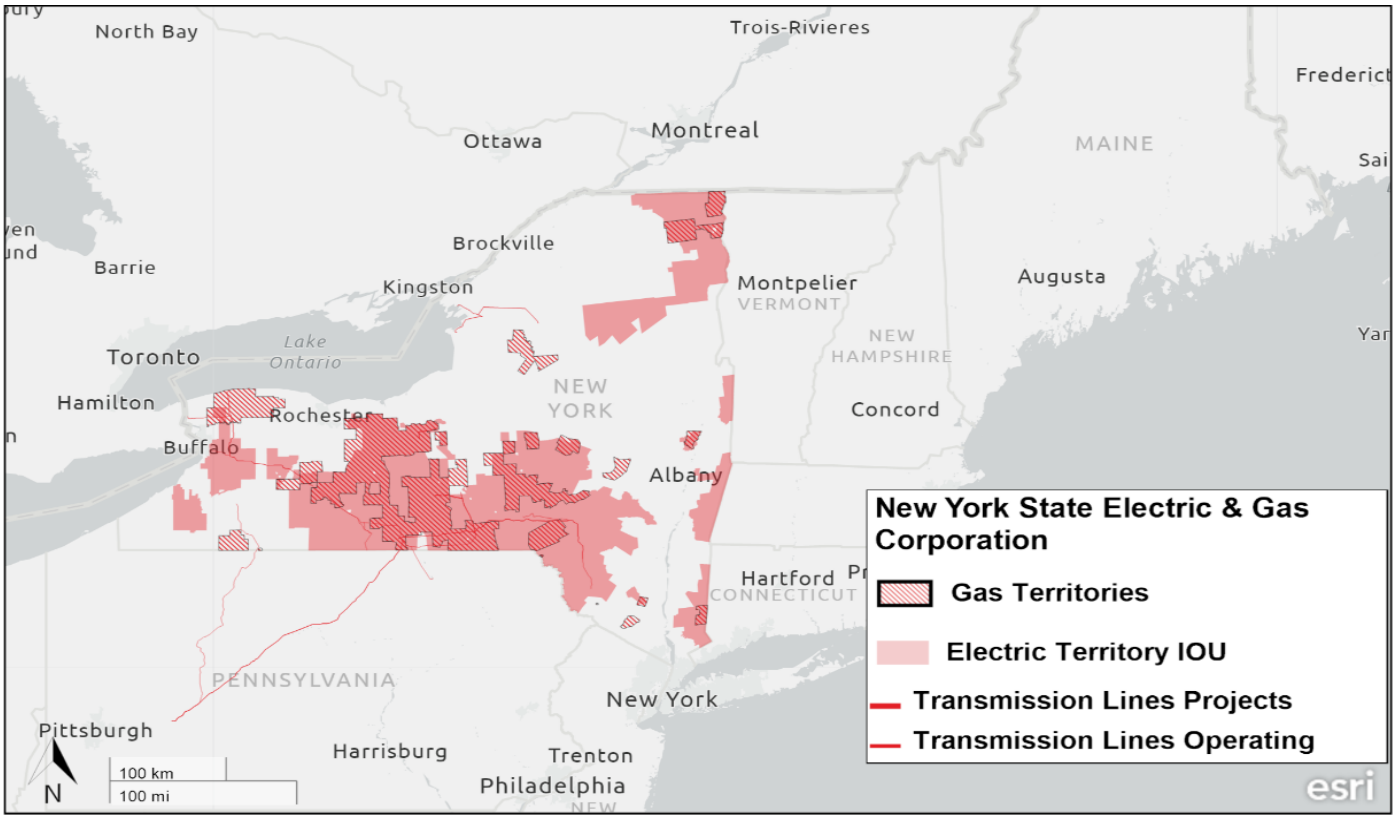
The NYPSC rulemaking is the most important aspect of this process from a credit perspective, since it will determine how utilities recover the costs to comply with the state's energy future, including addressing stranded asset risk associated with what appears to be a waning gas industry. To date, the NYPSC has provided incremental clarity around gas planning issues, by way of a May 2022

order that prescribes how state LDCs are to plan, operate and communicate with regulators in order to provide adequate service to meet customer demand, while also making progress to comply with CLCPA mandates. The Gas System Planning Process includes requirements such as a Long-Term Plan filing made every three years, with annual updates to be provided to the NYPSC. It also provides instructions on cost/benefit analyses of alternative investments (including non-pipeline alternatives and initial looks into nascent fuels such as renewable natural gas and hydrogen) as well as cost recovery and incentive mechanisms for these alternatives.

However, the downsizing of natural gas systems will also provide sizeable growth opportunities for NYSEG, which has good overlap of service territories, as seen in the exhibit below.

Exhibit 4

NYSEG's Service Territory has a high amount of overlap between electric and gas operations



Source: S&P Global Market Intelligence

Ring-fencing type mechanisms are positive, but do not completely separate NYSEG's credit profile from that of its parents

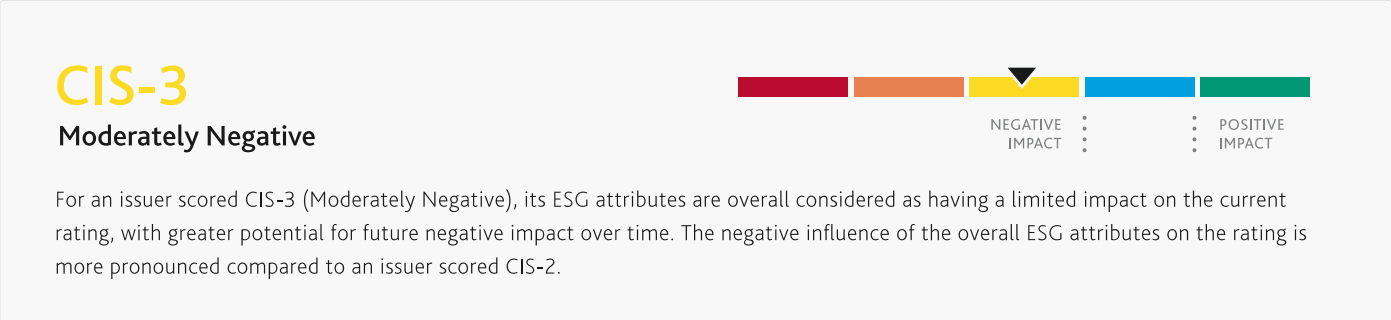
NYSEG benefits from a suite of ring-fencing type measures that help to insulate the company from the higher business risk of its unregulated affiliate and parent company. Some of the key provisions are: the imposition of a minimum equity ratio tied to the capital structure used in establishing NYSEG's rates, a prohibition on lending to unregulated affiliates and a "Special Preferred Share" provision, that add a significant impediment to NYSEG becoming part of a voluntary bankruptcy proceeding.

While NYSEG is well positioned to withstand some pressure from a credit deterioration at AGR, NYSEG's parent, and/or Iberdrola, AGR's majority owner, it is not fully immune should the credit quality of either entity drop materially.

ESG considerations

NYSEG's ESG Credit Impact Score is CIS-3 (Moderately Negative)

Exhibit 5
ESG Credit Impact Score



Source: Moody's Investors Service

NYSEG's ESG Credit Impact Score is moderately negative (**CIS-3**), reflecting highly negative environmental risks, highly negative social risks and moderately negative exposure to governance risks.

Exhibit 6
ESG Issuer Profile Scores

Source: Moody's Investors Service

Environmental

NYSEG's highly negative exposure to environmental risks (**E-4** issuer profile score) is driven by its geographical concentration in New York, which exposes the company to material and extreme weather events. This is somewhat counterbalanced by the company's asset profile as a regulated electric and gas transmission and distribution utility.

Social

Exposure to social risks is highly negative (**S-4** issuer profile score) reflecting the fundamental utility risk that demographics and societal trends could include social pressures or public concern around affordability, utility reputational or environmental concerns. In turn, these pressures could result in adverse political intervention into utility operations or regulatory changes, which we have seen in New York. These risks will be prominent in NYSEG's current general rate case filing in New York, which include significant proposed increases in capital spending for system resiliency and energy transition. Going forward, the utility could be further challenged by higher operating expenses related to inflation, rising interest rates and state carbon transition policies.

Governance

NYSEG's governance is driven by that of its parent, Avangrid. Avangrid's moderately negative governance risks (G-3 issuer profile score) stem from high management turnover – including its third CEO in as many years – which creates uncertainty around risk categories such as management credibility and track record. Avangrid's governance risks are also associated with having a majority owner (i.e., Iberdrola SA (Baa1 stable, **CIS-3**), which owns 81.5% of Avangrid; the remaining 18.5% is owned by public shareholders). These risks are weighed against the extensive industry experience of Avangrid's new CEO and CFO as well as Iberdrola's supportive ownership

practices, including access to its expertise for conducting major projects such as offshore wind. While we view Iberdrola as providing supportive help to Avangrid's board and management, we regard Avangrid as having distinct long-term financial policies and practices.

ESG Issuer Profile Scores and Credit Impact Scores for NYSEG are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page NYSEG on MDC and view the ESG Scores section.

Liquidity analysis

While internal sources and uses of funds will depend upon the result of NYSEG's current rate case, we expect NYSEG to produce $350 - $400 million of cash flow, compared to around $700 million that the company is including in their long-term outlook, resulting in negative free cash flow of about $300 - $350 million before any upstreamed dividends to Avangrid. We expect NYSEG's dividend policy to be driven by maintaining its regulatory allowed capital structure, which could mean that NYSEG pays no dividends, or even that Avangrid infuses equity into the utility to help fund capital needs and balance NYSEG's growing debt.

Avangrid employs a centralized approach to managing its liquidity. To the extent possible given certain regulatory restrictions, Avangrid aims to concentrate its cash at the holding company and primarily conduct its short-term borrowings through Avangrid. The utilities optimize their cash balances through a virtual money pool arrangement. Under the terms of this agreement, utilities may lend to each other but not to their unregulated affiliates or parent. These terms meet a regulatory requirement set at the time of Avangrid's acquisition of the utility companies which prohibits utilities from lending to unregulated affiliates, including Avangrid. To the extent that additional liquidity is required, NYSEG borrows under a bilateral loan agreement with Avangrid.

From an external liquidity standpoint, Avangrid and its regulated utility subsidiaries, including NYSEG, are parties to a $3.575 billion revolving credit facility that expires in November 2026. NYSEG's minimum sublimit under the facility is $400 million. We view management's efforts to formalize a minimum sublimit as helpful in providing visibility into what amounts of the shared facility are dependably allocated to the utility. Given Avangrid's centralized liquidity management philosophy and the virtual money pool of its utilities, we view the bank facility as effectively serving as a committed lender of last resort.

The bank credit facility does not include an ongoing material adverse change clause and the only financial covenant is a maximum allowed debt to capitalization ratio of 65%. We understand that, as of 30 September 2022, each company was in compliance with this covenant.

NYSEG's next long term debt maturity is $200 million of senior notes due May 2023.

Iberdrola also provides incremental liquidity to Avangrid

Aside from cash balances and utility dividends, Avangrid has access to both $2.5 billion of the aforementioned shared $3.575 billion facility. At 30 September 2022, there was $375 million of commercial paper outstanding, backstopped by the facility.

Avangrid is also party to a notional cash pooling arrangement along with other Iberdrola subsidiaries. Parties to the agreement, including Avangrid, may deposit funds with or borrow from the pool, provided that the net balance of funds deposited or borrowed by all pool participants in the aggregate is not less than zero. This agreement provides Avangrid with a third avenue for liquidity, supplementing its access to the debt and equity capital markets.

Lastly, Avangrid also has a $500 million credit facility with Iberdrola Financiacion, S.A.U., a company of the Iberdrola Group, which expires in June 2023.

Rating methodology and scorecard factors

Methodology Scorecard Factors
New York State Electric and Gas Corporation

Regulated Electric and Gas Utilities Industry [1][2]	Current LTM 6/30/2022		Moody's 12-18 Month Forward View As of Date Published	
Factor 1 : Regulatory Framework (25%)	**Measure**	**Score**	**Measure**	**Score**
a) Legislative and Judicial Underpinnings of the Regulatory Framework	A	A	A	A
b) Consistency and Predictability of Regulation	Baa	Baa	Baa	Baa
Factor 2 : Ability to Recover Costs and Earn Returns (25%)				
a) Timeliness of Recovery of Operating and Capital Costs	Aa	Aa	Aa	Aa
b) Sufficiency of Rates and Returns	Baa	Baa	Baa	Baa
Factor 3 : Diversification (10%)				
a) Market Position	Baa	Baa	Baa	Baa
b) Generation and Fuel Diversity	N/A	N/A	N/A	N/A
Factor 4 : Financial Strength (40%)				
a) CFO pre-WC + Interest / Interest (3 Year Avg)	3.6x	Baa	3x - 5x	Baa
b) CFO pre-WC / Debt (3 Year Avg)	9.6%	Ba	9% - 14%	Baa
c) CFO pre-WC – Dividends / Debt (3 Year Avg)	1.9%	Ba	6% - 11%	Baa
d) Debt / Capitalization (3 Year Avg)	43.1%	A	45% - 50%	A
Rating:				
Scorecard-Indicated Outcome Before Notching Adjustment		Baa1		Baa1
HoldCo Structural Subordination Notching	0	0	0	0
a) Scorecard-Indicated Outcome		Baa1		Baa1
b) Actual Rating Assigned		Baa1		Baa1

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
[2] As of 6/30/2022(L)
[3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.
Source: Moody's Financial Metrics

Appendix

Exhibit 8

Cash Flow and Credit Metrics [1]

CF Metrics	Dec-18	Dec-19	Dec-20	Dec-21	LTM Jun-22
As Adjusted					
FFO	**327**	**267**	**300**	**320**	**350**
+/- Other	-20	53	-123	-123	-228
CFO Pre-WC	**307**	**320**	**177**	**197**	**123**
+/- ΔWC	103	-48	69	195	90
CFO	**409**	**272**	**245**	**392**	**213**
- Div	0	100	100	270	270
- Capex	524	611	689	792	756
FCF	**-114**	**-438**	**-543**	**-669**	**-813**
(CFO Pre-W/C) / Debt	19.5%	17.3%	9.2%	8.5%	5.4%
(CFO Pre-W/C - Dividends) / Debt	19.5%	11.9%	4.0%	-3.2%	-6.4%
FFO / Debt	20.8%	14.5%	15.6%	13.8%	15.3%
RCF / Debt	20.8%	9.0%	10.4%	2.2%	3.5%
Revenue	1,694	1,548	1,564	1,804	2,044
Interest Expense	77	86	79	67	69
Net Income	53	82	145	159	189
Total Assets	5,561	5,926	6,451	6,961	7,190
Total Liabilities	4,124	4,471	4,557	4,997	4,921
Total Equity	1,437	1,455	1,895	1,964	2,269

[1] All figures and ratios are calculated using Moody's estimates and standard adjustments. Periods are Financial Year-End unless indicated. LTM = Last Twelve Months.
Source: Moody's Financial Metrics

Exhibit 9

Peer Comparison Table [1]

	New York State Electric and Gas Corporation Baa1 (Stable)			Central Hudson Gas & Electric Corporation Baa1 (Stable)			Consolidated Edison Company of New York, Inc. Baa1 (Stable)			Orange and Rockland Utilities, Inc. Baa2 (Stable)		
(In US millions)	FYE Dec-20	FYE Dec-21	LTM Jun-22	FYE Dec-20	FYE Dec-21	LTM Jun-22	FYE Dec-20	FYE Dec-21	LTM Jun-22	FYE Dec-21	FYE Dec-21	LTM Jun-22
Revenue	1,564	1,804	2,044	712	796	921	10,647	11,716	12,448	862	941	1,022
CFO Pre-W/C	177	197	123	129	160	124	2,200	2,693	3,326	169	191	185
Total Debt	1,916	2,311	2,285	878	1,030	1,079	20,710	20,296	21,065	1,211	1,128	1,149
CFO Pre-W/C + Interest / Interest	3.2x	4.0x	2.8x	4.7x	5.4x	4.3x	3.8x	4.3x	5.0x	4.6x	5.0x	5.0x
CFO Pre-W/C / Debt	9.2%	8.5%	5.4%	14.7%	15.6%	11.5%	10.6%	13.3%	15.8%	14.0%	16.9%	16.1%
CFO Pre-W/C – Dividends / Debt	4.0%	-3.2%	-6.4%	14.7%	15.6%	11.5%	5.9%	8.4%	11.1%	9.9%	12.3%	11.4%
Debt / Capitalization	43.5%	46.8%	43.4%	44.1%	45.8%	45.5%	49.3%	46.8%	47.2%	51.3%	47.4%	47.6%

[1] All figures & ratios calculated using Moody's estimates & standard adjustments. FYE = Financial Year-End. LTM = Last Twelve Months. RUR* = Ratings under Review, where UPG = for upgrade and DNG = for downgrade
Source: Moody's Financial Metrics

Ratings

Exhibit 10

Category	Moody's Rating
NEW YORK STATE ELECTRIC AND GAS CORPORATION	
Outlook	Stable
Issuer Rating	Baa1
Senior Unsecured	Baa1
ULT PARENT: IBERDROLA S.A.	
Outlook	Stable
Issuer Rating	Baa1
Senior Unsecured MTN -Dom Curr	(P)Baa1
ST Issuer Rating	P-2
PARENT: AVANGRID, INC.	
Outlook	Stable
Issuer Rating	Baa2
Senior Unsecured	Baa2
Commercial Paper	P-2

Source: Moody's Investors Service

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