Fitch Affirms DTE Energy, DTE Electric Co. and DTE Gas Co.'s Ratings; Outlook Stable

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NEW YORK--(BUSINESS WIRE)--Fitch Ratings has affirmed the long-term Issuer Default Rating (IDR) of DTE Energy Co. DTE) at 'BBB', and those of its regulated subsidiaries, DTE Electric Co. (DECo) and DTE Gas Co. (DTE Gas) at 'BBB+'. The Rating Outlook for all entities is Stable. More than $8 billion of consolidated long-term debt is affected by today's rating action. DTE's 'F2' short-term rating is largely derived from the stable cash flows from its higher rated utility subsidiaries. For a full list of rating actions see the end of the press release.

The Stable Outlook reflects the predictable earnings and cash flows of DTE's two regulated utility companies. DECo is the primary driver of consolidated cash flows and comprised approximately 79% of consolidated EBITDAR for the last 12 months (LTM) ending Sept. 30, 2014.

DTE's current ratings reflect the low risk of its regulated operations, a large capex program focused on growing utility and pipeline investments, a constructive regulatory environment, and an improving economy. Current ratings assume a reasonable outcome in DECo's pending general rate case (GRC) and a timely return on invested capital. Credit concerns include a high level of parent-only debt (approximately $1.8 billion), moderate regulatory lag, and the future effects of more stringent environmental regulations on DECo's predominantly coal-fired power generation portfolio. The ratings also consider the solid operating performance of the company's regulated and non-regulated operations, and the expectation that the company will continue to effectively manage the risks associated with its growing pipeline investments. Fitch's considers DTE's increasing investments in the Gas Storage and Pipeline (GSP) business segment as favourable due to long-term contractual arrangements, low regulatory risk and higher returns on equity (ROE).

Key Rating Drivers

First GRC Filing in Over 4 Years: In December 2014, DECo filed its 2015 GRC with the Michigan Public Service Commission (MPSC) requesting a $370 million rate increase predicated on a 10.75% ROE and a 50% equity layer. The filing is based on a forward-looking test year and the rate increase primarily reflects $2.8 billion in new net plant additions. The new plant additions include the planned purchase of the 732MW natural gas-fired Renaissance Power Plant from LS Power Group for $240 million as well as the planned purchase of a 300MW Michigan-based simple-cycle natural gas-fired power plant. DECo plans to self-implement rates on or after July, 1, 2015, subject to refund, and a decision by the MPSC is expected by December.

Fitch has conservatively modeled a 10% ROE for DECO which approximates recent industry averages. The expiration of securitization charges, renewable surcharge reductions and a continued low-commodity environment provides DECo sufficient headroom to seek base rate increases without significant pressure on retail rates. In DECo's GRC filing, net rates for residential customers are expected to increase modestly by 3% while rates for commercial and large industrial customers are expected to decrease by 7% and 18%, respectively. For the LTM period ending Sept. 30, 2014, DECo's earned ROE was approximately 10.7%, slightly above its current authorized ROE of 10.5%.

New Infrastructure Recovery Mechanism (IRM) Filing at DTE Gas: In November, DTE Gas filed with the MPSC to double the pace of its pipe replacement program to 160 miles a year, resulting in an annual investment of $130 million per year beginning in January 2016, an annual increase of $50 million over current levels. Fitch expects a decision by the MPSC by the end of this year and DTE Gas expects new rates effective July 2016. Fitch views the adoption of the IRM by the MPSC as part of DTE Gas' 2012 GRC settlement as indicative of continued regulatory support. In Fitch's view, the IRM reduces future regulatory lag leading to timely rate base and earnings growth and obviates the need for GRC filings through 2016.

Potential Elimination of Retail Open Access in MI: Recently, talks about customer choice have centered on eliminating retail open access and moving Michigan's electricity market to full regulation after a previous bill introduced in the U.S. House to raise the customer choice cap beyond 10% did not get any traction. If retail open access was eliminated it could result in customers coming back to DECo amid tightening capacity markets in MISO, necessitating the need for new generation investments such as the planned purchase of the 732MW gas fired

Renaissance Power Plant. Fitch views the elimination of customer choice as positive for DECo.

New MI Energy Legislation Expected in 2015: In December 2014, Michigan Governor Rick Snyder broadly outlined the state's future energy policy goals by 2025 and indicated he would like to have new energy legislation in place this year when current Renewable Portfolio Standards and Energy Efficiency targets end. The governor emphasized the increased use of cleaner natural gas and wind resources while reducing the state's reliance on less efficient coal generation and indicated he would seek to increase RPS and EE targets through 2025. DTE recovers its renewable investments under an annual renewable surcharge subject to MPSC approval. DTE expects natural gas-fired generation along with renewables to approximate up to 50% of total generating capacity by 2030, a material improvement from 10% in 2013 and in line with the governor's energy policy goals. Fitch views DTE's investments in renewable energy as favorable and, via the renewable energy surcharge, provides earnings growth in between GRC proceedings.

Constructive Regulatory Environment: Fitch views the regulatory environment in Michigan as constructive. The current regulatory framework allows for full pass-through of fuel and purchased power costs, reasonable ROE, forward-looking test years and a timely resolution of rate proceedings. In addition, DECo and DTE Gas have the ability to file rate cases with self-implementation if the ROE dips below the authorized level (currently at 10.5%). Furthermore, a revenue-decoupling mechanism and IRM at DTE Gas helps to reduce exposure to regulatory lag.

Growth in Diversified Businesses; GSP Segment Growing: Fitch expects a strong growth in DTE's non-utility businesses, which will be driven by the GSP and Power and Industrial (P&I) business segments.

DTE plans to spend $1.2 billion through 2017 on new pipeline and gathering investments in the Marcellus and Utica Shale basins to meet growing shipper demand, levels approximately 61% higher than the preceding three-year period. DTE is currently moving forward with plans to build and increase capacity of its Nexus and Vector pipelines to move Utica and Southwest Marcellus shale gas to markets in the U.S. Midwest, including Chicago, Ohio and Michigan, and Ontario, Canada. DTE completed a FERC pre-filing for the Nexus pipeline in the fourth quarter of 2014 (4Q'14) and has an in-service target date during 4Q'17. Agreements with several local distribution companies (LDCs) and key shippers have been executed. DTE is also making investments to expand capacity on its Bluestone and Millennium pipelines in the Marcellus Shale basin. The Bluestone expansion is expected to be completed by the 2Q'16. Fitch views DTE's increasing investments in the FERC-regulated GSP segment as favorable due to higher ROE, lower regulatory risk, and long-term contractual arrangements.

The P&I segment is supported by long-term power purchase agreement contracts with limited commodity risk. DTE's GSP and P&I segments comprised 11% and 10% of consolidated net income for 2013, respectively, and Fitch expects these business segments may contribute up to 15% each of consolidated net income by 2019.

High Capex: Capital investments are expected to total approximately $7.2 billion through 2017, levels approximately 20% higher than the preceding three year period. Of the total capex, DECo plans to spend $4.7 billion, primarily on new generation, distribution investments and environmental compliance. DTE Gas plans to spend $1 billion on distribution system enhancements including storage and transportation projects. Due to the large capex program, both the regulated utilities will need equity support from the parent through 2017 to help maintain their balanced capital structures. In addition, growing natural gas pipeline investments will render DTE to be FCF negative in the intermediate term, in Fitch's view. DTE will need to fund the deficit by a roughly 50% mix of debt and equity to maintain the present balanced capital structure. Fitch anticipates annual equity issuances at DTE totaling roughly $300 million per year through 2017 through its Dividend Reinvestment Programs (DRIP) and employee pension programs and approximately $300 million increase in parent only long-term debt per annum.

Modest Weakness in Credit Metrics: Fitch forecasts DTE's credit metrics to remain commensurate with Fitch's 'BBB' IDR guidelines for utility companies but anticipates the large capital spending program to modestly pressure leverage metrics. Fitch calculates DTE's EBITDAR coverage ratio at 4.9x for the LTM period ending Sept. 30, 2014 and leverage as measured by debt-to-EBITDAR at 3.9x. Going forward, Fitch expects consolidated debt-to-EBITDAR to increase to 4.2x through 2017 due to investments associated with the large capex program and moderate regulatory lag. Fitch also expects funds from operations (FFO)/Debt metrics to average 23% through 2017, in line with management's FFO/Debt target of 20% to 22%.

For the LTM ending Sept. 30, 2014, DECo's EBITDAR coverage was 6.7x and leverage, as measured by debt-to-EBITDAR, was 3.2x. Going forward, Fitch expects EBITDAR coverage ratios to remain above 6x and anticipates debt-to-EBITDAR to increase modestly to 3.4x through 2017 due to increased capital investments.

For the LTM ending Sept. 30, 2014, DTE Gas' EBITDAR coverage ratio was 7x and debt-to-EBITDAR was 3x. Going forward, Fitch expects EBITDAR coverage measures to remain above 5x and anticipates debt-to-EBITDAR to weaken to approximate 4x through 2017 due to the large capex program.

Sufficient Liquidity and Manageable Maturities: DTE has approximately $1.2 billion of total liquidity available under its respective credit agreements as of Sept. 30 2014, including $60 million of cash and cash equivalents. DTE's consolidated $1.8 billion five-year unsecured revolving credit facilities mature in 2018 and are composed of $1.2 billion at DTE, $300 million at DECo, and $300 million at DTE Gas. The facilities have a maximum debt-to-capitalization covenant of 65% and, as of Sept. 30, 2014, DTE was in compliance with consolidated debt-to-capitalization of 50.2% under its credit agreement. Debt maturities over the next four years are manageable and are as follows (excluding securitization maturities): $150 million in 2015, $451 million in 2016, no maturities in 2017, and $400 million in 2018. Maturing debt will be funded through a combination of internal cashflows and external debt refinancings.

RATING SENSITIVITIES

DTE Energy, Inc.

Future developments that either individually or combined could lead to positive rating actions include:

--Sustained debt-to-EBITDAR in the 3.50x-3.75x range.

Future developments that either individually or combined could lead to negative rating actions include:

--Sustained debt-to-EBITDAR above 4.25x. Fitch expects consolidated credit metrics to be pressured through 2017 as a result of high capex at the utilities. Persistently weak consolidated leverage metrics beyond Fitch's current forecast period could lead to negative rating action for DTE.

DTE Electric Co.

Future developments that either individually or combined could lead to positive rating actions include:

--The elimination of DECO's retail open-access program;

--Sustained Debt-to-EBITDAR at 3.5x or below.

Future developments that either individually or combined could lead to negative rating actions include:

--An unexpected outcome in DECO's pending GRC that limits the utility's ability to recover cost of capital investments in a timely manner;

--An adverse change in Michigan's regulatory climate;

--Sustained debt-to-EBITDAR metrics in the 3.75x-4.00x range.

DTE Gas Co.

Future developments that either individually or combined could lead to positive rating actions include:

--A constructive outcome in DTE Gas' pending IRM filing;

--Sustained debt-to-EBITDAR metrics at 3.5x or below.

Future developments that either individually or combined could lead to positive rating actions include:

An unexpected adverse change in the regulatory environment that limits the utility's ability to recover cost of capital investments in a timely manner;

--Sustained debt-to-EBITDAR metrics in the 3.75x-4.00x range.

Fitch has affirmed the following ratings with a Stable Outlook:

DTE

--Long-term IDR at 'BBB';

--Senior unsecured notes at 'BBB';

--Junior subordinated notes at 'BB+';

--Short-term IDR at 'F2';

--Commercial paper at 'F2'.

DTE Gas Co.

--Long-term IDR at 'BBB+';

--Senior secured at 'A';

--Short-term IDR at 'F2';

--Commercial paper at 'F2'.

DECO

--Long-term IDR at 'BBB+';

--Senior secured at 'A';

--Short-term IDR at 'F2';

--Commercial paper at 'F2'

Additional information is available at 'www.fitchratings.com'.

Applicable Criteria and Related Research:

--'Rating U.S. Utilities, Power and Gas Companies' (March 11, 2014);

--'Corporate Rating Methodology' (May 28, 2014);

-'Recovery Ratings and Notching Criteria for Utilities' (Nov. 18, 2014).

Applicable Criteria and Related Research:

Recovery Ratings and Notching Criteria for Utilities

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=813608

Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=749393

Rating U.S. Utilities, Power and Gas Companies (Sector Credit Factors)

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=735155

Additional Disclosure

Solicitation Status

http://www.fitchratings.com/gws/en/disclosure/solicitation?pr_id=978155

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