From: Simon, Timothy A.
Sent: 3/16/2011 5:07:39 PM
To: Cherry, Brian K (/O=PG&E/OU=CORPORATE/CN=RECIPIENTS/CN=BKC7); Simon, Timothy A. (timothy.simon@cpuc.ca.gov)
Cc: Koss, Kenneth L. (kenneth.koss@cpuc.ca.gov)
Bcc:
Subject: Re: S&P Ratings Action

Brian,

This is concerning, but somewhat predictable. I would like to meet with you and your treasury team to dig deeper into the financial ratings.

Regards,

From: Cherry, Brian K
To: Simon, Timothy A.
Sent: Wed Mar 16 15:59:27 2011
Subject: FW: S&P Ratings Action

From: Harvey, Kent M
Sent: Wednesday, March 16, 2011 2:00 PM
To: Darbee, Peter; Johns, Christopher; Cherry, Sara A; Bottorff, Thomas E; Cherry, Brian K
Subject: Fw: S&P Ratings Action

FYI, Kent

From: Redacted
Sent: Wednesday, March 16, 2011 01:54 PM
To: Harvey, Kent M; Togneri, Gabriel
Cc: Bijur, Nicholas M.; Steel, Brian; Redacted Redacted DeSanze, Christine M. (Law); Hayes, Kathleen (Law); Ludemann, Doreen (Law); Dore, Jay; Redacted Redacted Chakravarty, Prateek
Subject: S&P Ratings Action

Kent,

Just a few minutes before market close today, S&P officially released its latest credit update. I have attached the report for your review along with some of our initial thoughts.

Action Summary

- Ratings outlook revised to "negative" from "stable"
- Business profile revised to strong from excellent
- Liquidity revised from "adequate" to "less than adequate" with the expectation that upon successful refinance of the credit facilities liquidity will be revised back to "adequate"
- Current long term ratings remain at BBB+ with risk or lower rating over the next 18 months

Fixed Income market reaction

I talked to some of our capital markets bankers after the release went public and we have not seen any immediate impact to both our CDS levels or credit spreads, we are at levels similar to yesterday, but given the late press release we will probably have to wait till tomorrow morning to refresh our thoughts.

The rationale behind the decision was the same as what Nick had shared with you yesterday but just to re-summarize.

Rationale for rating action

San Bruno – According to S&P, San Bruno situation seems to have taken a life of its own.

1) Concerns around federal/state scrutiny on PG&E operations

a. Public and regulatory sentiment is at its lowest in years

b. CPUC is under significant political pressure as evidence by strong language in the recent order (This creates a high uncertainty around punitive damages/fines that CPUC may assess that S&P imagines to be large and extremely uncertain).

2) Management is in a tough spot

i. Level of scrutiny is too great

ii. It will be difficult for management to contest the charges

iii. Issues lead S&P to believe that management has not focused on gas operations which has severely damaged its credibility

3) Heavy Capex program, RPS, and rate pressures further complicate the variability of outcome and weaken the business profile

4) Direct Cost Estimates – There sense is that this will be a moving number with a high level of variability and if it is large enough it materially impacts the business profile of the company

5) Third Party Liability Costs –S&P feels comfortable that PG&E can expect to receive insurance proceeds to repay third party claims.

Regards,

Redacted

Treasury | Pacific Gas and Electric Company

Office: Redacted
e-mail:

<<S&P PGE negative outlook 03-16-2011.pdf>>