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Summary:

Consolidated Edison Co. of New York Inc.

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Credit Rating: A/Negative/A-2

Rationale

The ratings on Consolidated Edison Co. of New York Inc. (CECONY) reflect the consolidated rating of its parent, Consolidated Edison Inc. (Con Edison). The ratings also reflect Con Edison's Orange and Rockland Utilities Inc. subsidiary and the parent's nonregulated activities, which include retail and wholesale services and operation of infrastructure projects. Con Edison's and CECONY's excellent business risk profiles stem from a historically supportive regulatory environment and a conservative strategy as a transmission and distribution (T&D) company.

To address its significant capital needs, CECONY filed with the New York State Public Service Commission for an electric rate increase of $1.2 billion effective April 1, 2008, based on an ROE of 11.5% and a common equity ratio of 48.7%. However, an Administrative Law Judge has recommended a significantly lower rate increase, about $600 million, or half of the company's request and a common equity ratio of 49.65%. The largest factor contributing to the difference is the Judge's recommendation of a 9% ROE. A decision is expected in March 2008.

CECONY accounts for about 90% of Con Edison's total assets, revenues, and operating income. CECONY's electric and gas operations are low risk, reflecting Con Edison's strategy to own and operate electric and gas T&D assets in the Northeast. CECONY's mostly underground service network and the capability of each of its independent networks to operate without two primary feeders enable CECONY to have some of the industry's lowest power interruption metrics.

Con Edison's nonregulated activities account for about 5% of revenues and net income and consist of energy-related services (resale of 9.1 million megawatt-hours for the nine months ended Sept. 30, 2007, and 10.6 million megawatt-hours in 2006), ownership and operation of electric generation facilities (1,668 MW), and energy-related operations and risk-management services.

Con Edison's planned sale of 1,706MW of merchant generation capacity for $1.477 billion will support credit quality. The sale, which is expected to close in the first half of 2008, will generate $667 million of net cash flow, after repayment of project debt, taxes, and transaction expenses.

The sale benefits Con Edison's credit profile because it will moderate business risk, allowing the company to further focus on its regulated transmission and distribution operations, and provide cash to repay debt and fund other capital spending, obviating the need for some external financing.

The company's wholly-owned subsidiary, Consolidated Edison Development, owns the assets, which consist of five generation facilities in New England, New Jersey, and Maryland.

As of Sept. 30, 2007, Con Edison had adjusted debt to capital of about 53%, adjusted funds from operations (FFO) interest coverage of 3.0x, and adjusted FFO to total debt of 16%. With adjusted debt to capital of about 52%, adjusted FFO interest coverage of 4.1x, and adjusted FFO to total debt of about 19%, CECONY's credit ratios are marginally stronger than those of its parent. Leverage and interest coverage ratios are expected to remain weak for the current rating in 2008 as capital project and the need to access external funding will offset increases in sales and rates. However, maintaining the current ratings hinges on a favorable rate agreement for CECONY, its ability to recover outage-related costs, and continued improvements in total leverage.

Although Con Edison recovers its underfunded pension and post-retirement benefit obligations through regulatory deferrals, the utility's combined pension and other post-retirement obligations were underfunded by about $480 million ($285 million at CECONY).

Short-term credit factors

The short-term rating on Con Edison and its subsidiaries is 'A-2', reflecting the company's adequate liquidity and the expectation of continued stable cash flows to fund dividends and capital spending. As of Sept. 30, 2007, Con Edison and its subsidiaries had $192 million of unrestricted cash ($66 million at CECONY) and about $1.9 billion available under its $2.25 billion revolving credit facility, which matures in June 2011. Con Edison's borrowings under the revolving credit facility are limited to $1 billion, and CECONY's borrowings are limited to $1.5 billion. Con Edison primarily uses the revolving credit facility to support its commercial paper obligations, of which $350 million was outstanding as of Sept. 30, 2007.

Consolidated cash flow from operations for the 12 months ended Sept. 30, 2007 was about $1.7 billion ($1.4 billion from CECONY). Future debt and equity issuances will be required to fund annual capital spending of about $2.5 billion (2008 estimate), common dividends of more than $500 million per year ($350 million to $400 million of dividends paid annually to Con Edison from CECONY), and debt maturities of $507 million in 2008. Standard & Poor's expects Con Edison to fund acquisitions of nonregulated business opportunities conservatively, and that these investments will account for only a small percentage of consolidated cash flows and capital commitments.

Outlook

The outlook is negative. Con Edison's consolidated financial ratios are weak for the current rating, partly due to costs related to service disruptions during the summer of 2006. We expect financial metrics to somewhat improve in 2008, given CECONY's regulatory rate increase. If regulatory relief allows Con Edison to generate and maintain FFO to total debt of about 15% and FFO interest coverage above 3.5x by the end of 2008, we could revise the outlook to stable. However, a downgrade could occur if these ratios do not appear achievable due to funding higher-than-expected outage-related costs, significantly lower-than-anticipated rate relief in 2008, or implementation of a higher-risk strategy.