

RatingsDirect®

Research Update:

EMG Utica 'B' Rating Affirmed, Outlook Stable; Senior Debt Rating Raised To 'B+' On Improved Recovery Expectations

Primary Credit Analyst:

Michael Pastrich, New York 212-438-0604; michael.pastrich@spglobal.com

Secondary Contact:

Mike Llanos, New York (1) 212-438-4849; mike.llanos@spglobal.com

Table Of Contents

Overview

Rating Action

Rationale

Outlook

Recovery Analysis

Related Criteria

Ratings List

Research Update:

EMG Utica 'B' Rating Affirmed, Outlook Stable; Senior Debt Rating Raised To 'B+' On Improved Recovery Expectations

Overview

- Significant debt paydown in 2017 has resulted in improved financial ratio projections at EMG Utica LLC, with debt to EBITDA now expected to be in the 1.5x-2x range over the next few years. We also have increased confidence that dividend coverage ratios provide sufficient headroom to shield the company during times of moderate stress.
- We are affirming the 'B' corporate credit rating on EMG Utica LLC. The outlook remains stable.
- At the same time, we are revising the recovery rating on the company's \$325 million senior secured term loan B to '2' from '3' and raising the issue-level rating on the debt to 'B+' from 'B'.
- The stable outlook reflects our belief that the company will have adequate liquidity to meet its financial obligations over the next 12 months with interest coverage in excess of 10x and a debt-to-EBITDA ratio in the 1.5x-2x area.

Rating Action

On Jan. 18, 2018, S&P Global Ratings affirmed its 'B' corporate credit rating on EMG Utica LLC. The outlook is stable.

At the same time, we raised our issue-level rating on EMG Utica's \$325 million senior secured term loan B to 'B+' from 'B'. We also revised the recovery rating on the term loan to '2' from '3', reflecting our expectation of substantial (70%-90%; rounded estimate: 80%) recovery in the event of default.

Rationale

EMG Utica LLC is rated under S&P Global Ratings' non-controlling equity interest (NCEI) criteria, which are used to rate debt instruments issued by entities that own shares in one or more other entities (the investee company). The 'B' corporate credit rating on the company reflects the differentiated credit quality between it and its investee company, MarkWest Utica EMG LLC, of which EMG Utica owns a 44.3% interest. The differentiation reflects the structural subordination of the company relative to MarkWest Utica and the discretionary dividends that it does not control.

The main factors behind EMG Utica's rating include the cash flow stability of its underlying investment, the level of influence on MarkWest Utica's corporate governance and financial policy, EMG Utica's financial ratios, and EMG Utica's ability to liquidate investments to repay debt.

We assess cash flow stability as neutral, which is an improvement from our previous assessment of negative. MarkWest Utica's cash flows are relatively stable and backed by long-term contracts (remaining tenor of about 11-12 years) with 100% fixed fee-based cash flows. The marginal improvement in counterparty creditworthiness and absence of a financial covenant that could limit dividends from MarkWest Utica support the assessment. At the same time, the company is exposed to volumetric risk given that most contracts are structured as acreage dedications rather than minimum volume commitments, which we view more favorably. Despite MarkWest Utica's competitive advantage in its area of operation, we believe some cash flow volatility is likely during periods of commodity price volatility.

We assess corporate governance and financial policy as negative. In our view, EMG Utica has limited influence on the board or management of MarkWest Utica. MarkWest Energy Partners L.P., the partner in the joint venture, has more control over EBITDA generation and dividends as the operator and majority owner.

We assess financial ratios as positive, which is an improvement over our previous assessment of neutral. Our forecast assumes stand-alone debt to EBITDA in the 1.5x-2x range, with interest coverage ratio of about 10x over the next few years. The cash flow sweep has helped to significantly reduce debt, resulting in approximately \$38 million of debt reduction in the first three quarters of 2017, which has led to incremental improvement in leverage ratios over the last year.

We base the negative assessment on the ability to liquidate investments on the fact that MarkWest Utica is not publicly traded and it would be difficult to accurately forecast asset valuations relative to debt.

Liquidity

We assess EMG Utica's liquidity as adequate. We forecast liquidity sources to exceed uses by more than 1.5x for the next 12 months. Although this normally maps to a higher liquidity assessment, qualitative factors limit our assessment at adequate, specifically the lack of a satisfactory standing in the capital markets.

Principal liquidity sources:

- Projected funds from operations of about \$90 million, and
- Debt service reserve account of about \$5 million.

Principal liquidity uses:

- Mandatory debt amortization of about \$2 million, and
- Dividends of about \$15 million.

Covenants

Covenants include a maximum leverage ratio of 4.5x and an interest coverage ratio of 3x. We expect EMG Utica to maintain an EBITDA cushion in excess of 15% with its financial covenants.

Modifiers

The positive comparable rating assessment reflects the fact that the ultimate parent of MarkWest Utica's majority owner is a master limited partnership. Therefore, we expect the partnership would maintain or increase distributions over time and thus would require the same from the investments it controls. In addition, there is a six-month debt service reserve throughout the loan's life, which we view as positive for creditworthiness. This positive assessment provides a one notch uplift to reach the final rating.

Outlook

The stable rating outlook on EMG Utica reflects our belief that the company will have adequate liquidity to meet its financial obligations over the next 12 months with interest coverage in excess of 10x and a debt-to-EBITDA ratio in the 1.5x-2x range.

Downside scenario

Though unlikely due to the robust metrics, we could lower the ratings if dividends became curtailed such that interest coverage fell below 1.5x.

Upside scenario

Higher ratings are unlikely over the next year, due to the company's limited scale and our view that MarkWest Utica's cash flows are dependent on counterparties with lower ratings. We could consider higher ratings if our view of MarkWest Utica's creditworthiness improved.

Recovery Analysis

Key analytical factors

- We use a discrete asset valuation approach to value EMG Utica's interest in MarkWest Utica EMG in the event that EMG Utica defaults.
- We simulate a default arising from declining commodity prices that result in lower throughput volumes at EMG Utica's investee company, MarkWest Utica EMG LLC. The lower volume throughput leads MarkWest to sharply reduce its dividend, resulting in EMG being unable to service its debt. Our default scenario does not assume a default at MarkWest Utica EMG.
- The term loan holds a first-priority perfected lien on substantially all of the capital stock of the joint venture held by the borrower as well as its ownership interest in the joint venture.

Simulated default assumptions

- Simulated year of default: 2020
- EBITDA at emergence: About \$24.5 mil.
- EBITDA multiple: 7x

Simplified waterfall

- Net enterprise value (after 3% admin. costs): \$165 mil.
- Valuation split (obligors/non-obligors): 100%/0%
- Secured first-lien debt: \$200 mil. (includes six months of prepetition interest)
- Recovery expectations: '2' (70%-90%; rounded estimate: 80%)

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Corporates - General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- General Criteria: Methodology For Companies With Noncontrolling Equity Interests, Jan. 5, 2016
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed

EMG Utica LLC		
Corporate Credit Rating		B/Stable/--

Upgraded; Recovery Rating Revised

	To	From
EMG Utica LLC		
Senior Secured	B+	B
Recovery Rating	2(80%)	3(60%)

Certain terms used in this report, particularly certain adjectives used to

Research Update: EMG Utica 'B' Rating Affirmed, Outlook Stable; Senior Debt Rating Raised To 'B+' On Improved Recovery Expectations

express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

Copyright © 2017 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.