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Trending Topics from J.P. Morgan Corp Fin Advisory | Week of May 28, 2018

2. Tax reform ripple effects on ratings?

Key Takeaways

- While Moody's has already shown upgrade/downgrade triggers with and without repatriation tax liability (a topic previously covered in this distribution), agencies have increasingly commented on more specific impacts from tax reform.
- Union Pacific's recent downgrade threshold shift at Moody's from 2.0x to 2.25x serves as relevant case study of potential future adjustments to come.

In a recently published Moody's piece, the agency explicitly discussed Union Pacific's re-evaluation of its capital structure in light of the U.S. Tax Cuts and Jobs Act. This re-evaluation includes looking at the currently targeted threshold of leverage below 2.0x. Since Union Pacific has the majority of earnings generated in the U.S. and, as a railway company, is a highly capital intensive business, it stands to benefit considerably from tax reform. While the re-evaluation was done at the company, it is also notable that Moody's reacted with the threshold shift based on what the company articulated.

It is worth considering Union Pacific as a case study of how rating agencies may continue to shift their coverage and thought process behind ratings thresholds as companies re-evaluate capital allocation policy post tax reform.

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