Rating Process Case Study

Differentiating Speculative Grade Issuers & Boyd Gaming Case Study

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FitchRatings

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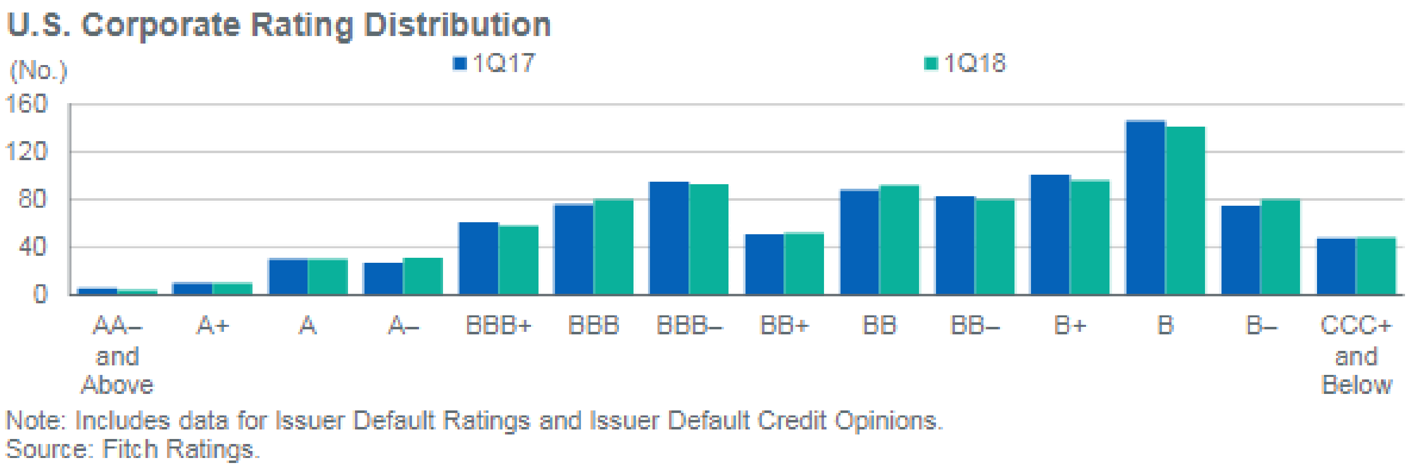
Corporate Rating Criteria



- Fitch's **Issuer Default Rating (IDR)** is an assessment of an issuer's vulnerability of default on financial obligations.
- The **ratings of individual debt issues** incorporate additional information on priority of payment and likely recovery in the event of default.

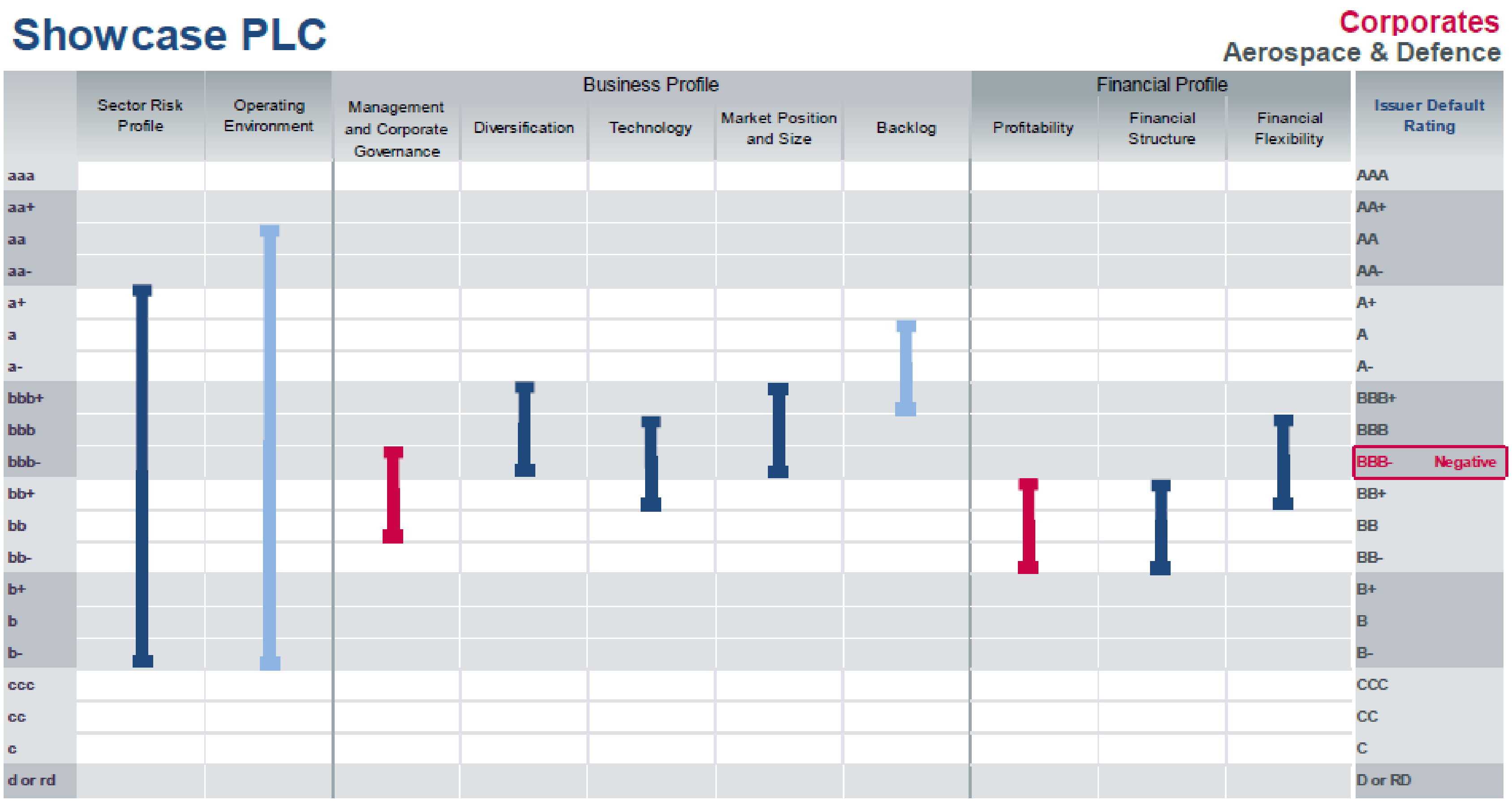
IDR (Default Risk) + Recovery = Instrument Rating

Determining IDR – Assessing Qualitative and Quantitative Factors

Key Rating Factors	
• Sector risk profiles	• Financial profile
• Country Risk	• Cash flows and profitability
• Management strategy/governance	• Financial structure
• Group structures	• Financial flexibility
• Business profile	

Corporate Rating Criteria

Rating Navigators provide *guidance* of the concepts of Fitch’s criteria to the issuers in the sector the Navigator covers. Emphasis on *guidance*, as Fitch’s ratings are not formulaic.



Corporate Rating Criteria

FitchRatings **Showcase PLC**

Corporates
Aerospace & Defence

Operating Environment

aa+	Economic Environment	bb	Below average combination of countries where economic value is created and where assets are located.
aa	Financial Access	bbb	Average combination of issuer specific funding characteristics and of the strength of the relevant local financial market.
	Systemic Governance	bbb	Systemic governance (eg rule of law, corruption; government effectiveness) of the issuer's country of incorporation consistent with 'bbb'.
B-			
ccc			

Management and Corporate Governance

bbb	Management Strategy	bb	Strategy generally coherent but some evidence of weak implementation.
bbb-	Corporate Governance	bb	Board effectiveness questionable with few independent directors. "Key man" risk from dominant CEO or shareholder.
bb+	Group Structure	a	Group structure shows some complexity but mitigated by transparent reporting.
bb	Financial Transparency	bbb	Good quality reporting without significant failing. Consistent with the average of listed companies in major exchanges.
bb-			

Diversification

a-	Geographic Diversification	bbb	Revenue base moderately well spread out geographically.
bbb+	Commercial vs Defense Split	bbb	Active in both commercial and defense segments although one dominates
bbb	Programme/Product Diversification	bbb	Active in a moderate number of programmes
bbb-	Aftermarket Presence	bbb	Moderate aftermarket presence
bb+	Customer Concentration (Non-Prime Suppliers)	bb	Exposure to a top customer ranges from 20% to 50%

Technology

bbb+	Level of Self-Funded R&D/History of	bb	Low level of self-funded R&D; little or no history of innovation.
bbb	Extent of High-Tech Production	bb	Poor pipeline of new high tech work; proprietary products account for a moderate portion of revenue.
bbb-	Fin. Exp. to New Tech Projects (Excl. Aircraft	b	Exposure to cost overruns of new technology programmes is significant.
bb+			
bb			

Market Position and Size

a-	Prime Contracting and Cost Competitiveness	bb	Supplier or non-prime contractor; wins few tenders; sub-contracts the majority of work.
bbb+	Market Position	bbb	Top five position in key segments of operation.
bbb	Flexibility	bbb	Cost can be reduced, however with six to 12 month delays. A sizable portion (30% - 40%) of work is performed by sub-contractors.
bbb-			
bb+			

Backlog

a+	Quality	bbb	History of some cancellations; mixed customer base.
a	Diversification	bb	Concentrated backlog with one or few customers dominant.
a-	Backlog/Revenue	bbb	Backlog-to-revenue around 1.5x
bbb+			
bbb			

Profitability

bbb-	FFO Margin	bb	8%
bb+	EBIT Margin	b	6%
bb	FCF Margin	bb	1%
bb-	Volatility of Profitability	bb	Higher volatility of profits than industry average.
b+	EBITDAR Margin	bbb	12%

Financial Structure

bbb-	Lease Adjusted FFO Gross Leverage	bb	4.0x
bb+	Lease Adjusted FFO Net Leverage	bb	3.0x
bb	Net Debt/(CFO - Capex)	b	6.0x
bb-	Lease Adjusted Debt/EBITDAR	bb	4.0x
b+	Lease Adjusted Net Debt/EBITDAR	b	4.5x

Corporate Rating Criteria

Sector Risk Profile

- Provides a typical rating range for issuers in a given industry.
- Upper boundary of the range is not a cap.
- Stable characteristics: few competitors, high barriers to entry, national dominance, and predictable demand levels.
- Riskier characteristics: industry in decline, highly competitive, capital intensive, cyclical and volatile.

Country Risk

- Tied to the country where the issuer operates with two impacts
  - Operating Environment
  - Transfer and Convertibility Risk

Management Strategy

- Ability to create a healthy business mix, maintain operating efficiency, and strengthen the market position.
- Financial performance over time and future strategy and past record relative to goals.
- Risk tolerance, in particular relative to M&A and expansion financing.

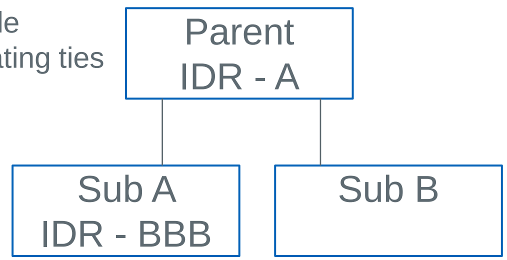
Corporate Governance

- Asymmetric rating consideration. Good governance is credit neutral while weaker governance is a negative.
- Main characteristics Fitch focuses on:
  - Governance/Group Structure: checks against conflicts of interest (e.g. management compensation, board make up, key-man risk, etc.).
  - Financial Transparency: high quality and timely financial reporting.

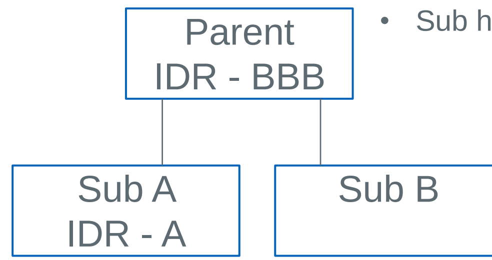
Group Structure – parent-sub linkage, JV/minority ownership adjustments

Parent Subsidiary Linkage

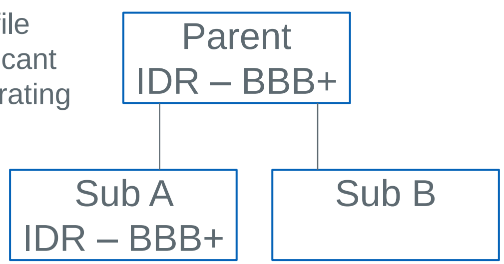
- Stronger Parent / Weaker Subsidiary
- Weak Linkage - Emphasis on de-consolidated financial profiles
- No guarantee, sub has little strategic value, little operating ties



- Weaker Parent / Stronger Subsidiary
- Weak Linkage – Emphasis on de-consolidated financial profiles
- Sub has strong ring fencing



- Stronger Parent / Weaker Subsidiary
- Strong Linkage - Emphasis on consolidated financial profile
- Guarantee, sub has significant strategic value and/or operating ties



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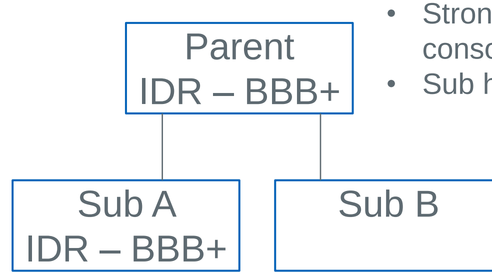


Corporate Rating Criteria

Business Profile

- Ability to withstand competitive pressures
  - Position in key markets
  - Level of product dominance
  - Ability to influence price
- Maintaining a high level of operating performance
  - Diversification by product, geography and customers/suppliers
  - Comparative cost position
- Size – if confers major advantages in terms of operating efficiency, economies of scale, financial flexibility, and competitive position.
- Business Profile factors and sub-factors will be customized per sector for the purpose of the Sector Navigators.

Corporate Rating Criteria

Financial Profile

- Quantitative aspect of analysis focuses on an issuer’s financial profile and it ability to service its obligations from a combination of internal and external resources.
- Emphasis on cash-flow measures of earnings, coverage and leverage (e.g. FFO, EBITDA, etc).
- As a rule of thumb sectors with more stable cash flows can handle more debt at the same rating level.
- ‘Forward-Looking Through-the-Cycle Approach’ – Fitch analysts use COMFORT model to standardize at least three years of historical financial metrics and 3-5 years of forecasted metrics.
  - Meant to illustrate a typical economic cycle
  - Also create a stress scenario, meant to show a downgrade scenario

Financial Profile (cont'd)

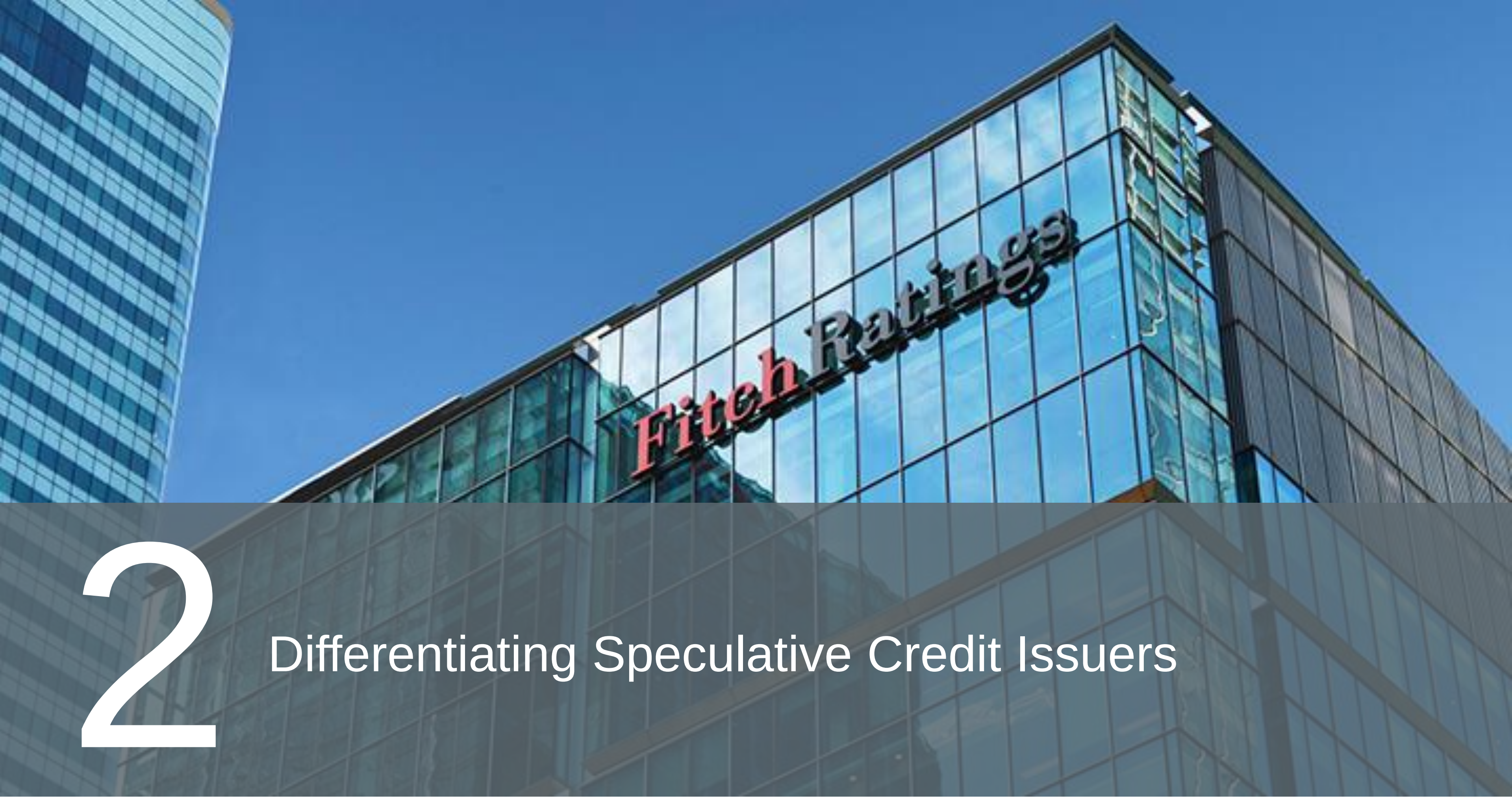
- Cash Flows and Profitability
  - Affect the maintenance of operating facilities, internal growth and expansion, access to capital, and the ability to withstand downturns.
  - Focus on sustainability and stability – supports ability to service debt and finance operations and capital requirements.

- Financial Structure
  - Level of dependence on external financing.
  - Industries differ in their need for capital and their capacity for debt.

Corporate Rating Criteria

Financial Profile (cont'd)

- Financial Flexibility
  - Issuer financial discipline and policy
  - Ability to control capital spending
  - Broad access to capital and diversification of funding sources
  - Strong liquidity – cash on hand, FCF, committed lines of credit
  - Debt mix: unsecured vs. secured & fixed vs. variable
  - Amortization/maturity schedule



2 Differentiating Speculative Credit Issuers

Differentiating Speculative Credit Issuers

Rating Definitions

B: Highly speculative	‘B’ ratings indicate that material default risk is present, but a limited margin of safety remains. Financial commitments are currently being met; however, capacity for continued payment is vulnerable to deterioration in the business and economic environment.
CCC: Substantial credit risk	Default is a real possibility.
CC: Very high levels of credit risk	Default of some kind appears probable.
C: Exceptionally high levels of credit risk	A default or default-like process has begun, or the issuer is in standstill, or for a closed funding vehicle, payment capacity is irrevocably impaired.

Differentiating Speculative Credit Issuers

Relative Importance of Factors in Determining Ratings

Higher ● **Moderate** ● **Lower** ●

	B+ vs B	B vs B-	B- vs CCC+	CCC+ vs CCC-
Business Model	Higher	Moderate	Moderate	Lower
Strategy	Higher	Moderate	Moderate	Lower
Cash flow	Higher	Higher	Moderate	Moderate
Leverage profile	Moderate	Higher	Higher	Moderate
Governance and financial policy	Moderate	Moderate	Moderate	Moderate
Refinancing risk	Lower	Moderate	Higher	Higher
Liquidity	Lower	Moderate	Higher	Higher

Differentiating Speculative Credit Issuers

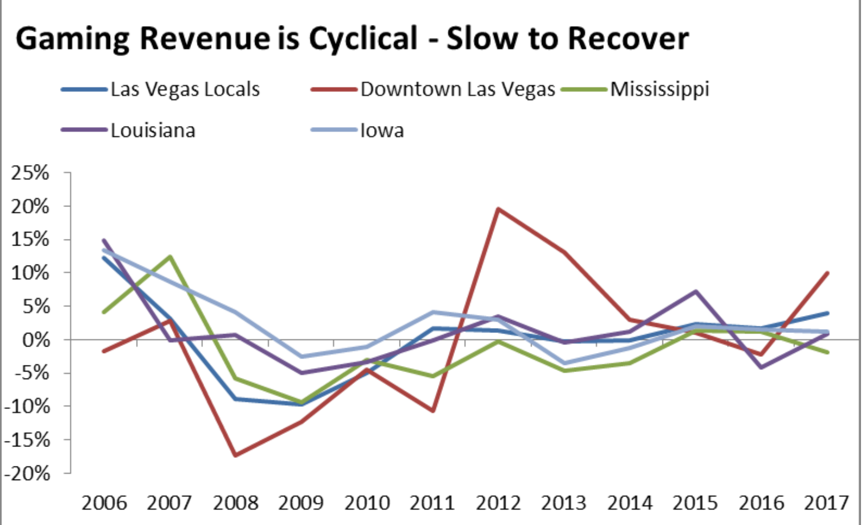
Key Rating Considerations for Highly Speculative Credits

Factor	B+	B	B-	CCC+	CCC	CCC-	CC
Business Model	Robust	Sustainable	Intact	Redeemable	Compromised	Disrupted	Irredeemable
Strategy Execution risk	Limited	Moderate	Meaningful	Challenging yet achievable	Uncertain	Highly speculative	Not credible
Cash flow profile	Consistently positive	Neutral to positive	Volatile	Mostly negative	Constantly negative	Accelerating cash outflows	Irreversible outflow
Leverage profile	Clear deleveraging path	Deleveraging	High but sustainable	Significant outlier	Unsustainable	Disproportion-ate and increasing	Unrecoverable
Governance / financial policy	Committed	Some commitment to deleveraging	Aggressive	Ineffective	Uncommitted	Hostile	Inevitable balance sheet restructuring
Refinancing risk	Limited	Manageable	High	Off market options	Excessive	Unavailable	Imminent
Liquidity	Comfortable	Satisfactory	Limited	Minimal headroom	Poor / Partly Funded	Unfunded	De facto insolvent

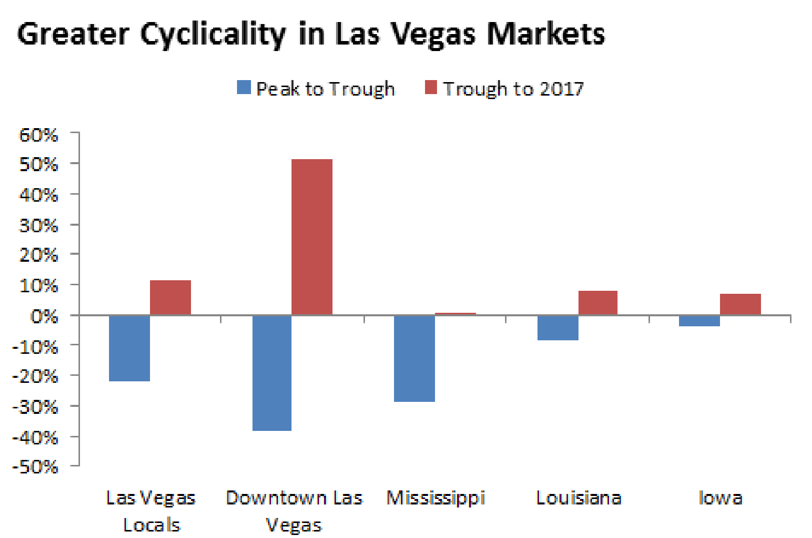
3 Boyd Gaming Corp. Case Study

Summary of Rating Drivers

- Exposure to cyclical industry
- Tepid sector outlook for regional gaming
- High adjusted leverage, but declining
- Strong free cash flow supports capital intensity / shareholder returns.
- Increasing diversification



Note: Annual change in gross gaming revenues. Major markets Boyd operates in shown.



Note: 'Peak to Trough' years correspond with the last recession.

Qualitative Assessment

WEAKER

STRONGER

Competitive Environment

No barriers to entry					Low likelihood of new entrats
Market oversaturation, declining					Min. supply growth, underpentrated
Aggressive promotional activity					Product quality/loyalty demand drivers

Market Position

Small player					Market leader, competitively protected
Negative brand ID					Effective brands & loyalty program
Low quality reducing revenues					High quality, consistent reinvestment

Diversification

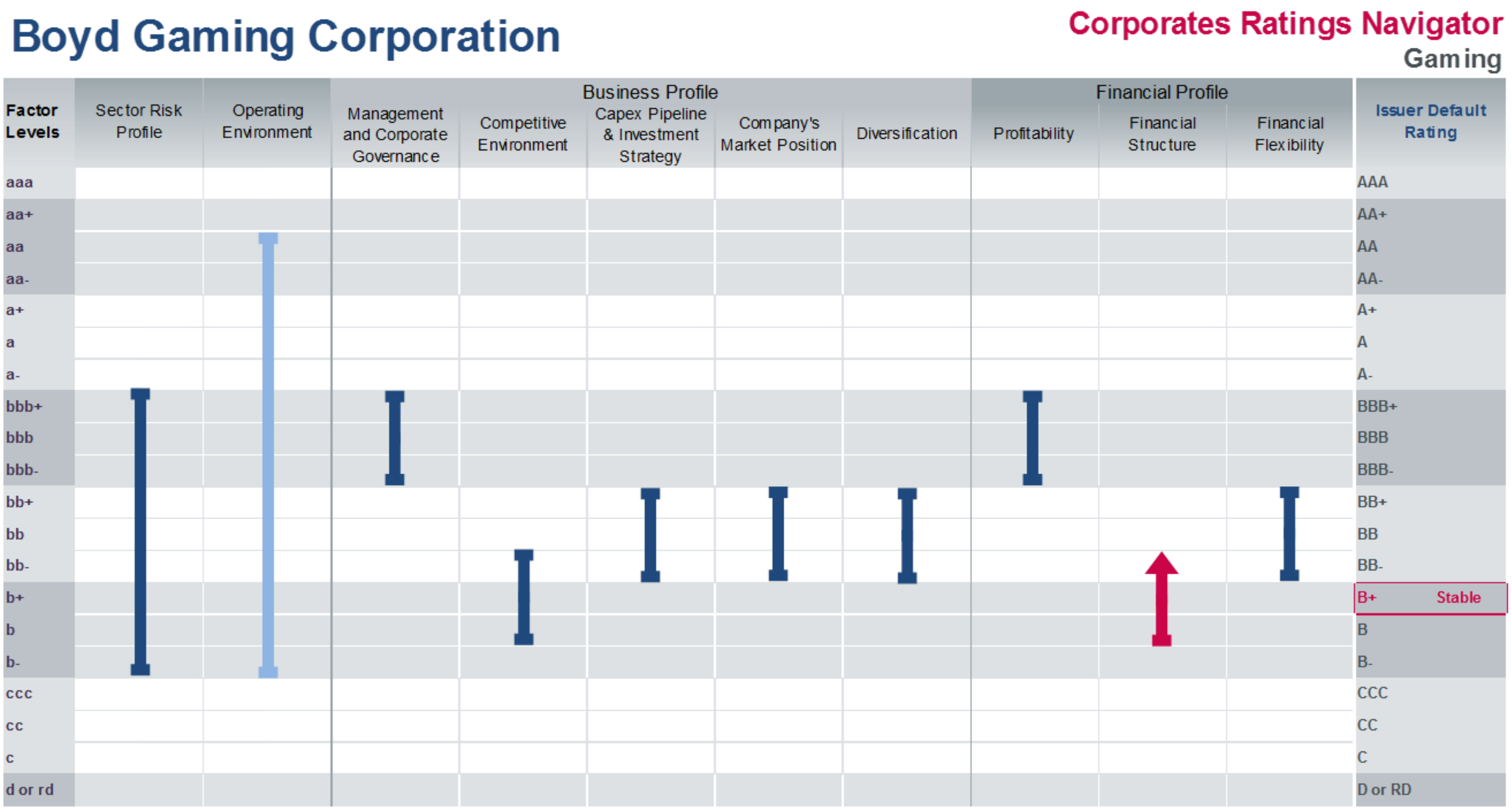
Geographically concentrated					Several markets, potentially international
Primarily gaming oriented					Strong non-gaming diversification

Differentiation at Lower End of Rating Spectrum

Considerations	B+	B	B-	CCC+	CCC	CCC-	CC	Trend	Fitch's View
Business Model	Robust	Sustainable	Intact	Redeemable	Compromised	Disrupted	Irredeemable	◀▶	U.S. regional markets face secular challenges, though BYD has exposure to the more robust Las Vegas Locals market.
Strategy/ Execution Risk	Limited	Moderate	Meaningful	Challenging Yet Achievable	Uncertain	Highly Speculative	Not Credible	◀▶	History of M&A transactions.
Cash Flow	Consistently Positive	Neutral to positive	Volatile	Mostly negative	Constantly negative	Accelerating cash outflow	Irreversible Outflow	▲	Fitch expects annual FCF to increase towards $300 million by 2020.
Leverage Profile	Clear deleveraging path	Deleveraging capacity	High but sustainable	Significant outlier	Unsustainable	Disproportionate and increasing	Unrecoverable	◀▶	Public commitment to reach debt/EBITDA of '4x-5x' but recent acquisitions slow de-leveraging path.
Governance and Financial Policy	Committed	Some commitment to deleveraging	Aggressive	Ineffective	Uncommitted	Hostile	Inevitable Balance Sheet Restructuring	◀▶	Would temporarily increase leverage above target range for strategic growth opportunities.
Refinancing Risk	Limited	Manageable	High	Off Market Options	Excessive	Unavailable	Imminent	◀▶	BYD does not have any meaningful maturities until 2021 when the revolver and term loan A mature.
Liquidity	Comfortable	Satisfactory	Limited	Minimal Headroom	Poor/Partly funded	Unfunded	De Facto Insolvent	◀▶	Ample level of excess cash (net of cage cash) and revolver availability.
CONCLUSION	B+								

Source: Fitch

Corporates Rating Navigator for Boyd



Peer Analysis

	Penn National Gaming	Pinnacle Entertainment	Penn National	Boyd Gaming	Caesars Entertainment	MGM Resorts International
	Stand-Alone	Stand-Alone	Pro Forma for PENN/PNK merger	Pro forma for recent acquisitions	Consolidated and Pro Forma for acquisitions	Consolidated
IDR/IDCO	b*/stable	b*/stable	---	B+/Stable	b+*/stable	BB/Stable
Statement Date	9/30/2017	9/30/2017	Pro Forma 2017	Pro Forma	Pro Forma	12/31/2017
Assets	25	16	41	29	33	
Markets	Multiple regional, 1 Las Vegas Strip asset, 1 other Las Vegas asset	Multiple regional	Multiple regional, 1 Las Vegas Strip asset, 1 other Las Vegas asset	Multiple regional, multipel Las Vegas Locals, multiple Downtown Las Vegas	Multiple regional, multiple Las Vegas Strip	Multiple regional, multiple Las Vegas Strip, 2 Macau
# of Leases	1	2	3	1	3	---
% EBITDAR subject to lease	85%	100%	~100%	23%	54%	---
Revenue	3,122	2,578	5,036	2,945	8,566	10,775
Growth	3.2%	12.1%	N/A	N/A	N/A	14.0%
EBITDAR	874	703	1,451	857	2,351	2,520
EBITDAR Margin	28.0%	27.3%	28.8%	29.1%	27.4%	23.4%
Rent Expense	(452)	(407)	(797)	(136)	(727)	0
EBITDA	422	297	654	721	1,624	2,520
EBITDA Margin	13.5%	11.5%	13.0%	24.5%	19.0%	23.4%
Total Debt	1,351	834	2,530	4,046	9,734	13,018
Adjusted Debt	4,962	4,073	8,906	5,134	15,553	---
Total Leverage	3.2x	2.8x	3.9x	5.6x	6.0x	5.2x
Adjusted Leverage	5.7x	5.8x	6.1x	6.0x	6.6x	---
CFFO	375	234	505	455	1,197	2,206
Capex	(102)	(81)	(175)	(141)	(670)	(1,864)
Dividends	0	0	0	(150)	0	(422)
FCF	273	153	330	164	527	(80)
FCF Margin	8.7%	5.9%	6.6%	5.6%	6.2%	-0.7%
Capital Intensity	-3.3%	-3.1%	-3.5%	-4.8%	-7.8%	-17.3%

Qualitative and Quantitative Comparison

- Portfolio size, diversification, and quality
- Leverage metrics and trajectory, adjusted for Master Lease rental payments
- EBITDA and free cash flow margins

Rating Sensitivities

	Penn National Gaming	Pinnacle Entertainment	Penn National	Boyd Gaming	Caesars Entertainment	MGM Resorts International
	Stand-Alone	Stand-Alone	Pro Forma for PENN/PNK merger	Pro forma for recent acquisitions	Consolidated and Pro Forma for acquisitions	Consolidated
IDR/IDCO Triggers						
BB	---	---	---	---	---	Current IDR
BB-	---	---	Diversification away from master leases; FCF growth. De-leveraging is limited due to impact from rental payments.	Gross leverage below 5.0x; adj. leverage around 5.0x; discretionary FCF exceeding $300MM, stable/growing regional markets.	Adjusted leverage below 5.0x; Discretionary FCF above $600MM, positive operating trends.	Gross leverage exceeding 6.0x, weaker operating performance, large debt funded transaction, more aggressive financial policy.
B+	Materially de-levering (adj. lev @5.9x), FCF growth ($250MM currently), diversifying away from master lease.	material reduction in adj. leverage (6.1x currently); FCF margin approaching 10%, diversification away from master lease.	Current IDCO	Current IDCO	Current IDCO	---
B	Current IDCO	Current IDCO	Adjusted leverage above 6.5x, discretionary FCF $250MM, weaker operating trends.	Gross leverage above 6.0x, adj. leverage increasing to 6.0x, discretionary FCF $150MM, operating pressure, REIT spinoff.	Adjusted leverage above 6.5x, discretionary FCF $400MM, weaker operating trends.	---
B-	Adjusted leverage in high 6x or low 7x, operating challenges pressuring FCF.	Material increase in adj. leverage, FCF margin approaching 2%, prolonged recession or secular pressure.	---	---	---	---

Companies of similar size and market exposure should have similar leverage sensitivities at the same rating level.

This can be adjusted slightly for individual characteristics.

<u>Examples</u>

- MGM can withstand higher leverage at ‘BB-’ level given international exposure and favorable domestic mix.
- Caesars and PENN can withstand higher leverage at ‘B+’ level relative to Boyd given diversification, stronger FCF, and sizeable loyalty programs.

Recovery Analysis

Segment	EBITDAR	Stress	Stressed EBITDAR	Rent	Stressed EBITDA	Multiple	Enterprise Value
Las Vegas Locals	255	25%	191	0	191	7.0	1,337
Downtown	54	20%	43	0	43	6.0	260
Midwest & South	364	20%	291	0	291	6.5	1,894
Pinnacle Assets	197	20%	158	(105)	53	6.0	316
Valley Forge	40	20%	32	0	32	6.0	192
Corporate	(73)	21%	(58)	0	(58)	6.6	(377)
Total	**837**	**21%**	**658**	**(105)**	**553**	**6.6**	**3,622**

Recovery Analysis

($ Mil., Except Where Noted; Issuer Default Rating: B+)

Distressed EV As a GC		Comments
Going Concern EBITDA	553	Annualized acquisition results with 20%-25% stress depending on market
EBITDA Multiple (x)	6.6	Weighted average of market multiples (6x–7x).
Additional Value from Affiliates, Minority Interest, Other	0	—
Going Concern Enterprise Value	**3,622**	—
Less: Administrative Claims (10% of EV)	362	—
EV Available for Claims	3,259	—

Priority	Amount	Concession Allocation	Value Recovered	Recovery (%)	Recovery Rating	Notching	Rating
Sr. Secured (First Lien)	2,144	0	2,144	100	RR1	3	BB+
Sr. Unsecured[a]	2,350	0	1,115	47	RR4	0	B+

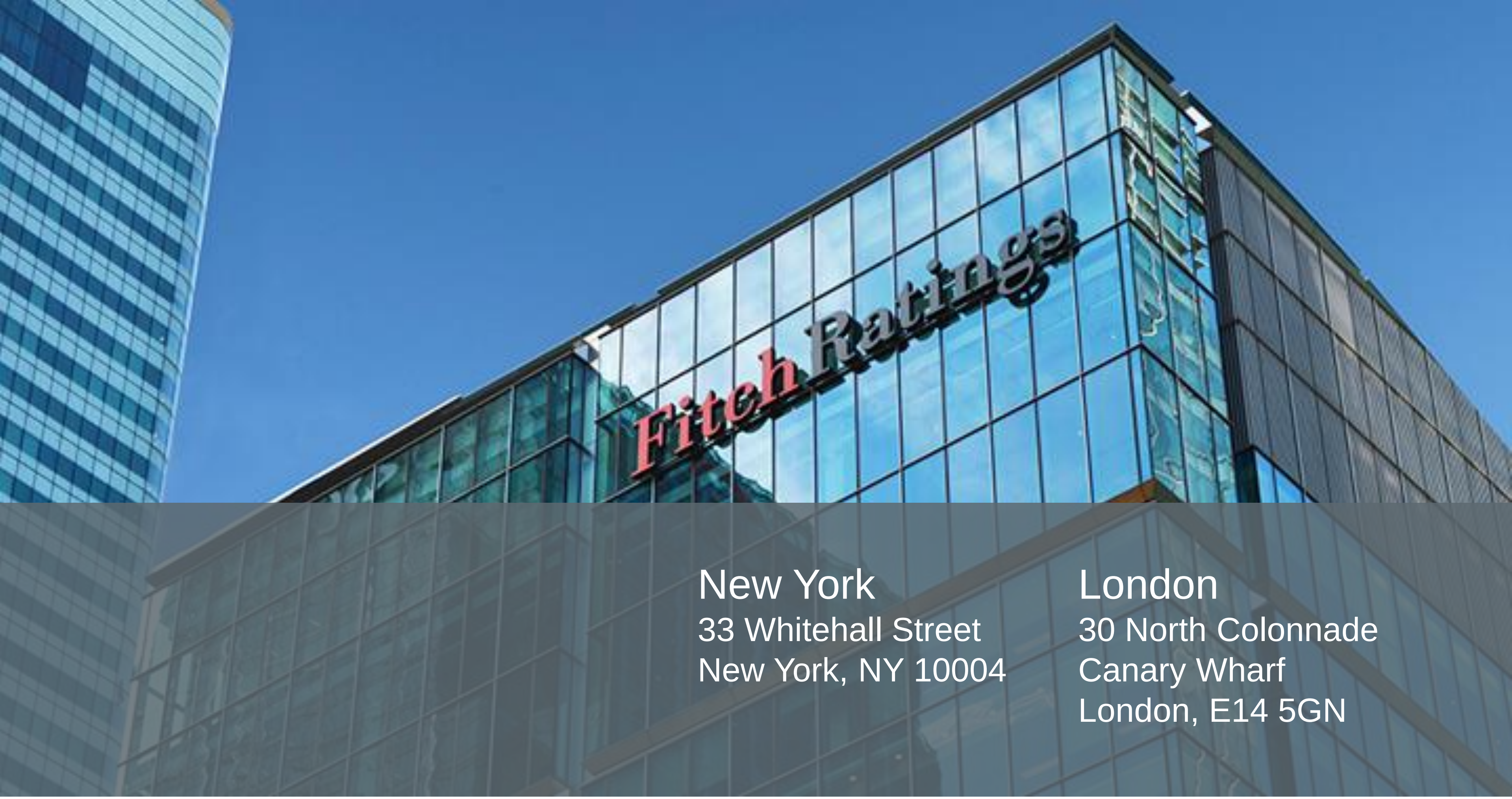
[a]Includes $850 million in incremental unsecured debt for acquisitions, which is Fitch's assumption. EV – Enterprise value. GC – Going concern.
Source: Fitch Ratings.

Segment-level analysis to derive going concern enterprise value

- EBITDAR stresses to reflect moderate recessionary environment of high single-digit to low double-digit revenue declines, assuming 50% flowthough.
- Range of segment EV multiples reflect differing asset quality, competitive environment, and operating cost structure.

Recovery waterfall guides issue-specific notching from IDR

- Assumes 10% administrative claims (standard).
- Assumes full draw on revolver ($775 million for Boyd).



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