Eidsiva Energi AS
Norway, Utilities

SCOPE BBB+ STABLE

Corporate profile

Eidsiva is the largest electricity grid company in Norway following the transaction with Hafslund E-CO, effective since 30 September 2019. Today, Eidsiva has more than 900,000 grid customers and operates a grid network of more than 66,000 km. Activities in the group also include district heating, broadband and retail power sales. Eidsiva accounts for its 42.8% stake in power production company E-CO Energi AS as an associated company. Eidsiva is fully owned by Norwegian municipalities, through Innlandet Energi Holding (49.4%), Åmot municipality (0.6%) and the City of Oslo (50%). The latter through Hafslund AS and Hafslund E-CO AS.

Key metrics

			Scope estimates	
Scope credit ratios	**2018**	**2019[1]**	**2020F**	**2021F**
EBITDA/interest cover (x)	4.1x	5.0x	6.6x	6.6x
Scope-adjusted debt (SaD)/EBITDA	6.1x	9.5x	5.0x	5.1x
Scope-adjusted funds from operations/SaD	5.4%	7.4%	20.7%	16.9%
Free operating cash flow/SaD	-8.5%	-1.2%	3.8%	-2.1%

Rating rationale

Scope Ratings affirms the BBB+/Stable corporate issuer rating on Eidsiva Energi AS, as well as the BBB+ senior unsecured rating and the S-2 short-term rating.

The issuer rating of Eidsiva includes our assessment of the company's low business risks and more aggressive financial risk profile. From 2020 (the first fully integrated operational year for the new entity after the transaction) and beyond, we expect that more than 80% of Eidsiva's EBITDA will come from the monopolistic grid business, which is positive for the predictability of cash flow and thus also justifies Eidsiva's more aggressive financial risk profile. Eidsiva's domestic market dominance, good customer diversification and efficiency improvements are also key drivers in our business risk assessment. Further, we recognise the increasingly good returns in the company's fibre/broadband businesses, which coupled with its even lower industry risk profile of regulated grid operations, result in an overall favourable average industry risk assessment for Eidsiva.

Also positive for the financial risk profile is our expectation that cash flow will be more predictable and less volatile going forward. Leverage and debt protection in the short to medium term are forecasted at around 5x and 6.5x, respectively, which is more stable and better than historical figures. Free operating cash flow, however, is still expected to be marginal, due to extensive investment plans throughout 2021. In the current year, cash flow has been helped by the disposal of the Moelven shares. However, with sizeable dividend payouts planned and the prospect of lower dividends received from the E-CO Energi (due to lower forward power prices seen recently, we forecast discretionary cash flow to remain negative in the medium term.

[1] *Hafslund E-CO transaction accounted for as of 30 September 2019, i.e. somewhat distorted numbers.*

Ratings & Outlook

Corporate ratings	BBB+
Outlook	Stable
Short-term rating	S-2
Senior unsecured rating	BBB+

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Related Methodologies

European Utility Methodology, March 2019

Corporate Rating Methodology, March 2019

Government Related Entities Methodology

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In terms of liquidity, the transaction with Hafslund E-CO had the largest impact. Eidsiva financed the transaction payment last year with short-term loans, which have been and will continue to be refinanced with long-term loans. This had a negative effect on liquidity ratios at YE 2019. Despite this, with a new revolving credit facility in place and new long-term bonds placed already in 2020, the liquidity profile is improving as expected.

Outlook

The Stable Outlook reflects our expectation that the success so far in integrating Hafslund Nett and Eidsiva Nett will continue and the new Eidsiva group entity will thus generate a significant part of its EBITDA from monopolistic, regulated grid operations. The Outlook also assumes funds from operations and debt protection ratios will improve from 2020 (compared to the past) and that Eidsiva will continue to be owned by Norwegian municipalities.

A positive action could be warranted by a reduction in overall leverage, via positive free cash flow or asset disposals, exemplified by a Scope-adjusted leverage ratio (Scope-adjusted debt/EBITDA) of around 4x on a sustained basis.

A negative rating action could be triggered by a significantly weaker financial risk profile (coming from higher capex and dividend for instance), leading to sustained Scope-adjusted debt/EBITDA of well above 5.25x and interest cover of below 5x. In addition, it would be triggered if the company lost its GRE (Government Related Entity) status.

Rating drivers

Positive rating drivers	Negative rating drivers
• Norway's largest grid company, with a significant EBITDA share from monopolistic power distribution (more than 80%) • Long-term, supportive and committed municipality owners • High dividend inflow from its 42.8% ownership in Norway's second largest hydropower production company, as well as profitable broadband and bioenergy businesses	• Ongoing sizeable investment phase, resulting in negative free cash flow and external funding requirements • Somewhat aggressive financial credit ratios expected in the short term • Some integration risk during the implementation process of the transaction

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Reduced leverage via positive free cash flow or asset disposals • Scope-adjusted debt/EBITDA of around 4x on a sustained basis	• Significantly weaker financial risk profile, exemplified by a Scope-adjusted debt/EBITDA of well above 5.25x for a prolonged period and interest cover of below 5x • Losing its GRE status

Financial overview

			Scope estimates	
Scope credit ratios	**2018**	**2019**	**2020F**	**2021F**
EBITDA/interest cover (x)	4.1x	5.0x	6.6x	6.6x
Scope-adjusted debt (SaD)/EBITDA	6.1x	9.5x	5.0x	5.1x
Scope-adjusted funds from operations/SaD	5.4%	7.4%	20.7%	16.9%
Free operating cash flow/SaD	-8.5%	-1.2%	3.8%	-2.1%
Scope-adjusted EBITDA in NOK m	**2018**	**2019**	**2020F**	**2021F**
EBITDA	1,346	1,422	2,717	2,850
Operating lease payments in respective year	54	-	-	-
Scope-adjusted EBITDA	**1,400**	**1,422**	**2,718**	**2,852**
Scope-adjusted funds from operations in NOK m	**2018**	**2019**	**2020F**	**2021F**
EBITDA	1,346	1,422	2,717	2,850
less: (net) cash interest as per cash flow statement	-585	-335	-410	-430
less: cash tax paid as per cash flow statement	-110	-172	-229	-254
add: depreciation component, operating leases	35	-	-	-
Other items (incl. dividend from E-CO Energi)	-224	80	736	300
Scope-adjusted funds from operations	**462**	**995**	**2,814**	**2,465**
Scope-adjusted debt in NOK m	**2018**	**2019**	**2020F**	**2021F**
Reported gross financial debt	8,240	14,938	15,208	15,996
less: cash and cash equivalents	-366	-1,490	-1,625	-1,406
add: cash not accessible	70	35	35	35
add: pension adjustment	210	0	0	0
add: operating lease obligations	409	-	-	-
Scope-adjusted debt	**8,586**	**13,483**	**13,618**	**14,625**

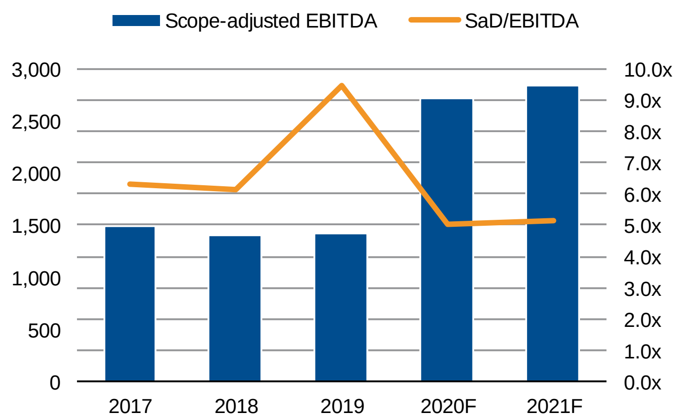
Key developments in Eidsiva since Scope's update in July 2019

The transaction between Eidsiva Energi and Hafslund E-CO is now complete and effective since 30 September 2019, in accordance with the previous agreement. Further information is available in our rating report dated 3 July 2019 and our rating action dated 26 March 2019.

The transaction has reduced the relevance of FY 2019 results, as these include only the three-month figures of Hafslund Nett and a gain from the de-consolidation of the Eidsiva Power production unit. Thus, it is more important to review recent cash flow and funding developments.

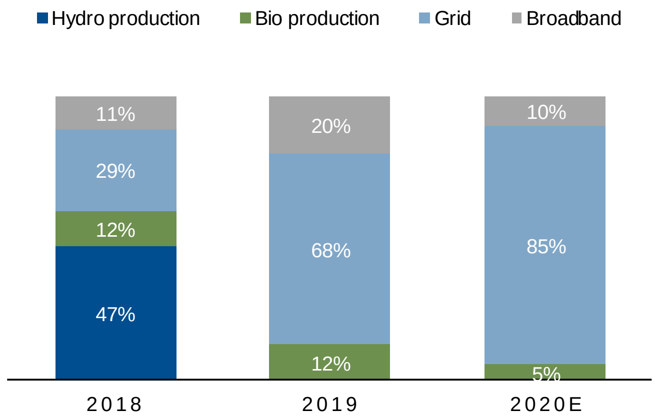
The transaction has resulted in Eidsiva's Scope-adjusted debt increasing by around NOK 5bn from YE 2018 to YE 2019, driven by bank loans, NIB loans, commercial paper, green bonds and normal bonds. We anticipate the loan portfolio's maturity to continue to increase throughout 2020, which will lead to improved internal and external liquidity ratios. The inclusion of almost NOK 1.6bn of leases in 2019 (to reported debt) was also higher than our previous adjustment for operating leases, which had a negative impact on our assessment.

Figure 1: Scope-adjusted leverage development (NOK m)



Source: Company, Scope

Figure 2: Share of group EBITDA development (in %)



Source: Company, Scope

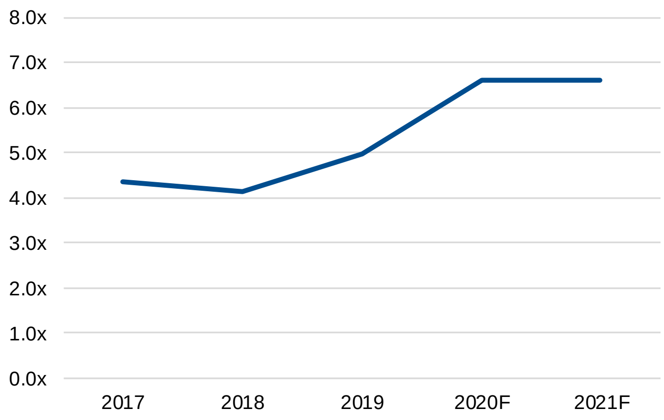
Updated Scope forecast

We have updated our financial forecast for Eidsiva after reviewing the actual figures of the transaction (as per the group's Q4 report), its recent operating performance and the current market conditions. Overall, we forecast somewhat lower profitability and slightly higher capex, which are negative for key credit ratios compared to our previous forecasts. Still, the postponement until 2020 of cash flow from Eidsiva's associate company will be offset by higher-than-expected cash inflow from the Moelven shares, meaning the revised 2020 figure for free operating cash flow remains generally in line with previous estimates.

With current power prices lower than last year's levels (affecting the potential dividend from the associated company) and with the company's investment spending expected to increase slightly in 2021 (mainly in Hafslund Nett), we expect deleveraging in the medium term to be slower than previously forecasted. Our base case expects leverage to stay slightly above 5x, interest cover at somewhat below 7x, and funds from operations/Scope-adjusted debt at around 16% from 2021. These revised levels have no negative impact on the current rating.

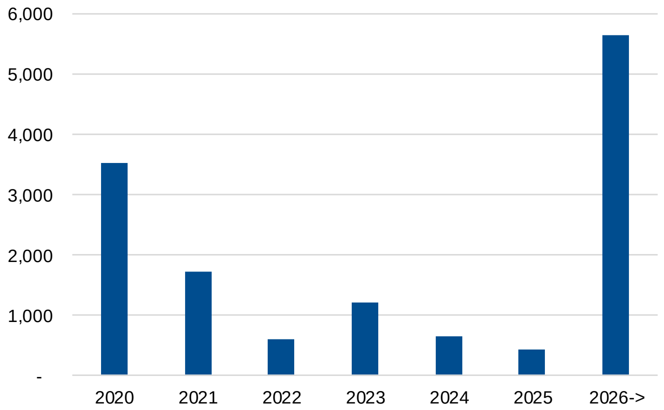
Eidsiva Energi's liquidity totalled NOK 2.7bn (cash and undrawn credit lines) at the end of Q4 2019, which was lower than its short-term debt balance (NOK 5.5bn). Since then, the company has arranged new long-term funding (NOK 2bn) and increased its undrawn credit facility (to NOK 2bn maturing in 2022). Although, further loans still need to be refinanced in 2020, we assess liquidity as adequate, based on the proven access to various debt markets. Looking into 2021, the refinancing need will become smaller but will remain noticeable as we do not project positive discretionary cash flow.

Figure 3: EBITDA/net interest expense (x)



Source: Company, Scope

Figure 4: Debt maturity profile, at late Feb 2020 (NOK m)



Source: Company, Scope

Summary of business and financial risk profiles

Our assessment of Eidsiva's business risk profile (A rated) has not changed. Eidsiva is still Norway's largest grid company, with a significant EBITDA share from monopolistic power distribution. Our financial risk profile assessment (BB) is also unchanged from last year, although we note that the expected deterioration in leverage metrics will be slower than previously anticipated. Still, these revised credit metrics figures are not putting negative pressure on the current rating.

Supplementary rating drivers

We continue to use our bottom-up approach to analyse Eidsiva Energi's parent support, and the one-notch uplift assigned for municipality ownership has not changed. Still, the transaction with Hafsund E-CO, through which the City of Oslo indirectly became a 50% owner (via Hafslund E-CO and Hafslund AS), is seen as positive for the potential capacity for financial support in the future. Moreover, the fact that the former single individual Eidsiva municipality owners have been combined into a new holding company is seen as neutral, but gives impression of more united.

Although Eidsiva's financial policy requires no rating adjustment, we note the M&A risk arising from the company's outspoken ambitions. Our new projections assume no more structural transactions, but we note that the company is still open to participating in the further consolidation of the Norwegian utility sector. Still, we consider these strategic ambitions in the context of management's dedication to maintaining a solid financial strength, and thus its desire to protect its investment grade rating.

Short-term rating

Despite the reduction in Eidsiva's internal liquidity ratio, due to the high portion of maturing short-term debt, most of which relates to the Hafslund transaction, this ratio has already improved significantly in the last six months, and we expect this to continue throughout 2020 as planned. Thus, taking into account the company's access to capital markets and the new and increased undrawn credit facility, we view overall liquidity as adequate and affirm our S-2 short-term rating.

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