Glitre Energi AS
Norway, Utilities

SCOPE BBB Stable

Corporate profile

Glitre Energi AS (Glitre) is a Norwegian energy utility operating mainly in the Buskerud county and Hadeland area. It is vertically integrated, with activities primarily in power production, distribution and power sales but also in broadband services through its 29% ownership of Viken Fiber. Glitre has an annual hydropower production of about 2.4 TWh and supplies energy to more than 50,000 retail customers. In terms of distribution, the company builds and operates a roughly 8,100 km power grid serving 90,000 customers. Glitre is owned by Drammen municipality (50%) and Buskerud county municipality (50%, via the company Vardar).

Key metrics

			Scope estimates	
Scope credit ratios	**2016**	**2017**	**2018F**	**2019F**
EBITDA/interest cover (x)	6.2x	7.4x	7.4x	7.6x
Scope-adjusted debt (SaD)/EBITDA	3.8x	3.4x	3.6x	3.4x
Scope-adjusted FFO/SaD	19.9 %	20.3 %	16.3 %	16.3 %
Free operating cash flow/SaD	9.2 %	11.1 %	4.6 %	4.7%

Rating rationale

Scope Ratings affirms its BBB corporate issuer rating on Glitre Energi AS, as well as the S-2 short-term rating and BBB senior unsecured ratings.

The issuer rating continues to be driven by Glitre's meaningful share of monopolistic grid operations and relatively stable overall profitability and cash flow. The latter is helped by the substantial hedging of its more volatile power generation business. Glitre's vertically integrated value chain supports our overall business risk assessment, though dampened slightly by low profitability in power sales and some non-core businesses. Limited geographical outreach for selected segments, certain asset concentration risk, and lack of flexibility in water-reservoir capacity (due to run-of-the-river power plants) are also affecting the business risk profile.

The company's positive free operating cash flow is viewed supportive by us when assessing the overall financial risk profile of Glitre. Although we expect certain credit metrics to slightly worsen at YE 2018 compared to at YE 2017, the overall credit trend from 2019 looks solid, helped by an anticipated normal production level output. The average SaD/EBITDA of around 3.6x and debt protection ratios of above 7x, outperformed our previous estimates slightly, but still places Glitre well within the BBB area for a vertically integrated utility, according to our methodology.

Liquidity remains sufficient and covers short term debt maturities well, supported by a newly refinanced NOK 1.0bn long-term credit line that remains undrawn, available cash and access to bond and bank debt.

Ratings & Outlook

Corporate ratings	BBB
Short-term rating	S-2
Senior unsecured rating	BBB

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Related methodologies

European Utilities, January 2018

Government-Related Entity, July 2018

Scope rates Glitre Energi at BBB/Stable, 4 Jan 2018

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Outlook

The Stable Outlook reflects our expectations that Glitre will continue to be a diversified utility, with operations in power production, distribution and sales; to fund its medium-term planned capex programme using internally generated cash flow; and to reduce volatility via power production hedging. As a result, we anticipate key credit metrics to remain largely unchanged in the medium term. The Outlook is also based on our expectation that Glitre will continue to be owned by Norwegian municipalities.

A positive rating action could be warranted if Glitre were to materially increase the share of its distribution business or deleverage to a SaD/EBITDA of below 3.0x on a sustainable basis.

A negative rating action is possible if the company were to participate in a debt-financed structural transaction that either substantially weakened its business risk profile or resulted in a SaD/EBITDA of well above 4x and prolonged negative free operating cash flow generation.

Rating drivers

Positive rating drivers	Negative rating drivers
• Well-integrated business model, with large share of monopolistic power distribution • Cost-efficient and environmentally friendly hydropower production, with good and relatively stable profitability development due to established hedging agreements • Long-term, committed municipality owners which are willing and able to provide potential parent support	• Limited geographical diversification outside main local regions in Norway • Low profitability in power sales and limited contribution from its share of non-core businesses • No water reservoir capacity and some asset concentration risk at its power plants

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Increasing share of distribution business • Improved financial risk profile, exemplified by a deleveraging to a SaD/EBITDA ratio of below 3.0x on a sustainable basis	• Debt-financed transaction that weakens either its business risk profile or financial risk profile • A weaker credit profile with a SaD/EBITDA ratio of well above 4x and prolonged negative free operating cash flow

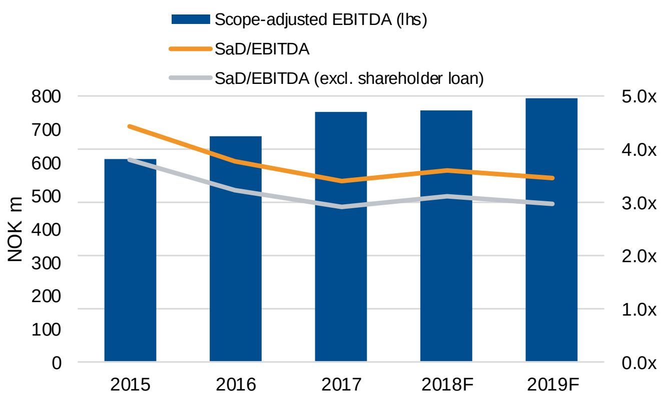
Financial overview

			Scope estimates	
Scope credit ratios	**2016**	**2017**	**2018F**	**2019F**
EBITDA/interest cover (x)	6.2x	7.4x	7.4x	7.6x
Scope-adjusted debt/EBITDA	3.8x	3.4x	3.6x	3.4x
Scope-adjusted debt (excluding shareholder loan)/EBITDA	3.2x	2.9x	3.1x	3.0x
Scope-adjusted FFO/Scope-adjusted debt	19.9 %	20.3 %	16.3 %	16.3 %
FOCF/Scope-adjusted debt	9.2 %	11.1 %	4.6 %	4.7%
EBITDA	483	564	570	608
Operating lease payments in respective year	192	167	164	164
Scope-adjusted EBITDA	**675**	**731**	**734**	**772**
EBITDA	675	731	734	772
less: (net) cash interest as per cash flow statement	-127	-89	-93	-97
less: cash tax paid as per cash flow statement	-70	-141	-252	-288
add: depreciation component operating leases	0	14	14	15
Other items	35	6	42	54
Scope funds from operations (FFO)	513	521	443	456
Reported gross debt	2,491	2,688	2,475	2,375
Cash, cash equivalents	-478	-763	-370	-244
cash not accessible	19	40	20	20
Pension adjustment	52	58	55	52
Operating lease obligation	114	167	166	163
Subordinated owner loan	374	374	374	374
Scope-adjusted debt (SaD)	**2,572**	**2,565**	**2,721**	**2,741**

Operational developments since Scope's previous rating report

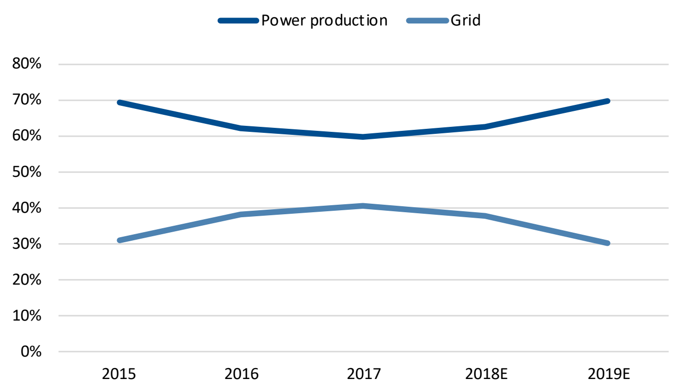
During the first nine months of 2018, Glitre's overall performance was slightly better than our expectations, but with mixed underlying factors. This year, Glitre's hydro production was low (mainly due to a very dry Q3, with output 30% below the levels during the same period in 2017) but realised power prices were higher. The positive market price effects were dampened by the company's normal high hedging levels it had going into 2018. Still, we are in favour of Glitre's ambitions to reduce underlying volatility in production. With the higher forward price curve we see in today's market, we anticipate the company's average realised prices to also fall below market prices in 2019. Results in the distribution grid segment have largely aligned with company plans, while retail power sales division reported a small profit. Overall, we continue to favour its vertically integrated business model, as it helps to stabilise profitability.

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



Source: Company, Scope

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



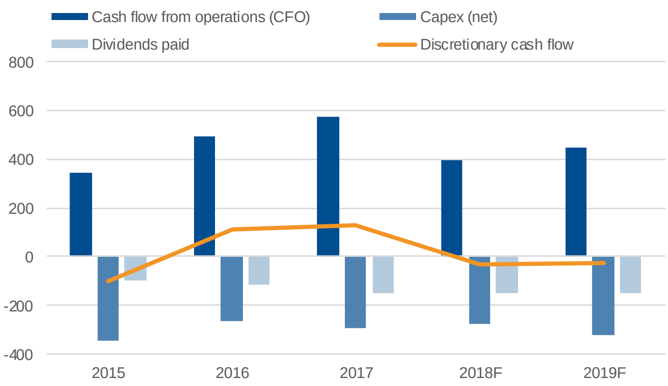
Source: Company, Scope

Updated Scope forecast

Our financial performance forecast for Glitre has been updated with new estimates for power prices and anticipated volume; while other areas are largely left unchanged. Overall, we expect group credit metrics in 2019 to be a bit more conservative than we had anticipated last year, helped by slightly higher power price assumptions. This will also affect cash flow positively, although higher taxes paid reduces the net effect to some degree. The improvement in EBITDA is mainly expected from hydropower production; therefore Glitre's profitability will be increasingly driven from a more volatile source next year we assume (see Figure 2). In this EBITDA figure, Viken Fiber (associated company) is not included (whose dividend contribution to Glitre is also expected to rise next year).

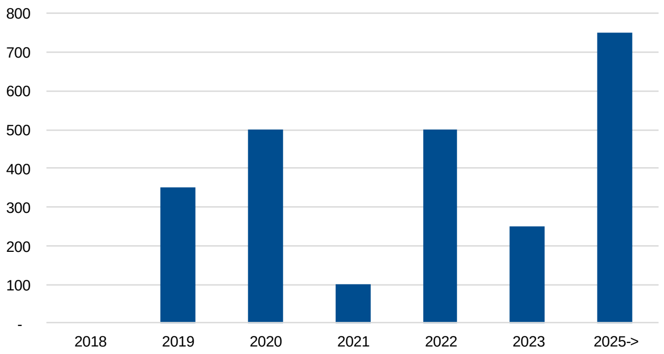
Glitre's liquidity remains more than sufficient with NOK 1.6bn in cash and available credit lines, which cover short- to medium-term debt maturities well. As illustrated in Figure 3, we anticipate free operating cash flow to stay positive and discretionary cash flow to break even short-term. Separately, we foresee increased event risk in Glitre going forward, due to several proposed and in-process mergers and divestments in the Norwegian utility market. Our projections do not currently assume any such transactions, but as the company has been open to selling non-core assets in the past, we anticipate that selected transactions in the coming years are likely.

Figure 3: Cash flow development (NOK m)



Source: Company, Scope

Figure 4: Debt maturity profile, as mid-Dec 2018 (NOK m)



Source: Company, Scope

New government-related entity methodology from Scope

On 13 July 2018, Scope published its new government-related entity methodology, which now also applies to Glitre alongside the utility-specific rating methodology. The new methodology is used to assess the level of support and the corresponding uplift from the standalone rating. We use the bottom-up approach to analyse Glitre, and the one-notch uplift assigned for the ultimate 100% municipality ownership has not changed since the last review.

To assess the likelihood of support, we considered Glitre's importance in Norway, political willingness for financial support, and the potential for political or investor turmoil should support be withheld. The owners' willingness has been demonstrated in the past, by the partial conversion of a shareholder loan into equity to improve certain credit metrics in 2015. Further, Norway's Industrial Licensing Act, which states that hydropower assets must be owned two-thirds by the public at all times, as well as monopoly regulations governing the grid business, confirm our assessment.

Based on the GRE methodology grid, we assess both the capacity and likelihood of government support at 'medium' and give a one-notch uplift to Glitre's standalone rating of BBB-.

Finally, we also highlight the effects from the Norwegian government's ongoing process to merge municipalities and county municipalities - with Buskerud county municipality to be merged with Akershus and Østfold in 2020 to create Viken. A consequence for Glitre will be having the underlying municipalities in Buskerud as new indirect owners instead of the county municipality; while another consequence is the potential for future merger of assets between Vardar and Glitre. While the latter does not necessarily constitute any parent support effect, the change in indirect ownership to the underlying municipalities does, but will not affecting our one-notch rating uplift assigned.

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