Glitre Energi AS
Norway, Utilities

SCOPE BBB

Corporate profile

Glitre Energi AS is a Norwegian energy utility operating mainly in the former 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 26.5% ownership of Viken Fiber. Glitre Energi has an annual hydropower production of about 2.6 TWh and supplies energy to approximately 52,000 retail customers. In terms of distribution, the company builds and operates a roughly 8,100 km power grid serving around 97,000 customers. Glitre Energi is owned by Drammen municipality (50%) and 19 municipalities in the former Buskerud county (50%, via the company Vardar).

Key metrics

			Scope estimates	
Scope credit ratios	2018	2019	2020F	2021F
EBITDA/interest cover	7.7x	8.7x	5.2x	5.9x
Scope-adjusted debt (SaD)/EBITDA	3.6x	3.1x	5.5x	4.5x
Scope-adjusted funds from operations/SaD	7.8 %	31.0 %	8.3 %	19.1 %
Free operating cash flow/SaD	-4.9 %	20.9%	-2.4%	7.6%

Rating rationale

Scope Ratings has an BBB corporate issuer rating on Glitre Energi AS, as well as an S-2 short-term rating and a BBB senior unsecured rating. The ratings are currently under review for a developing outcome, following the latest development during H2 2020 where Glitre Energi and Agder Energi have been discussing and contemplating the possibility to merge its businesses.

The issuer rating is positively affected by Glitre Energi's share of monopolistic grid operations and relatively stable group profitability. The latter is influenced by the substantial hedging arrangement for its more volatile power generation business, which has helped the company to report group EBITDA margins of above 40% in the past. Glitre Energi's vertically integrated value chain supports our overall business risk assessment, although this is dampened slightly by low profitability in some non-core businesses. Limited geographical outreach for selected segments, some asset concentration risk, and a lack of flexibility in water-reservoir capacity (due to run-of-the-river power plants) also affect the company's business risk profile.

Glitre Energi's positive free operating cash flow (FOCF) over time supports its overall financial risk profile. However, its financial risk profile has deteriorated, following a recent spike in leverage and the expectation of negative FOCF this year. Based on the latest forward power prices and hedges in place, we expect the situation to return to more normalised levels next year, which will ease the downward pressure on the company's financial risk profile. As a result, we continue to assess Glitre Energi's overall financial profile as solid, with an average Scope-adjusted debt (SaD)/EBITDA ratio of around 4x (excluding the subordinated shareholder loan) and debt protection in the 5-7x range going forward.

As regards supplementary rating drivers, we used a bottom-up approach to assess Glitre Energi's parent support under our government related entity methodology. The one-notch uplift assigned to the standalone rating for municipality ownership has not changed.

Scope anticipates that post a potential LoI, a final agreement could take up to 6 months to be finalised before presented to the owners, by which time more information should be available on the companies' business and financing structure and the ratings review can

Ratings & Outlook

Issuer rating	BBB
Short-term rating	S-2
Senior unsecured rating	BBB

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Related Methodologies

Corporate Rating Methodology, Feb 2020

Rating Methodology European Utilities, Mar 2020

Government Related Entities Methodology, Jul 2020

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be completed. Scope also assume that the Norwegian authorities, in addition to the municipality owners will have to approve the transaction.

Under Review

Scope aims to resolve the review as soon as possible. The ratings could be confirmed if the ongoing merger talks fails and resulted in keeping the status quo. If the ongoing merger talks materialised in more specific results, the rating outcome would depend on the future operational and financial setup of a potentially merged group. All directions (positive, negative, neutral) could be possible.

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, who are willing and capable to provide potential parent support	• Limited geographical diversification outside main local regions in Norway • Low profitability in power sales and limited contribution from share of non-core businesses • No water reservoir capacity and some asset concentration risk at power plants

Rating-change drivers

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

Financial overview, numbers in NOK m

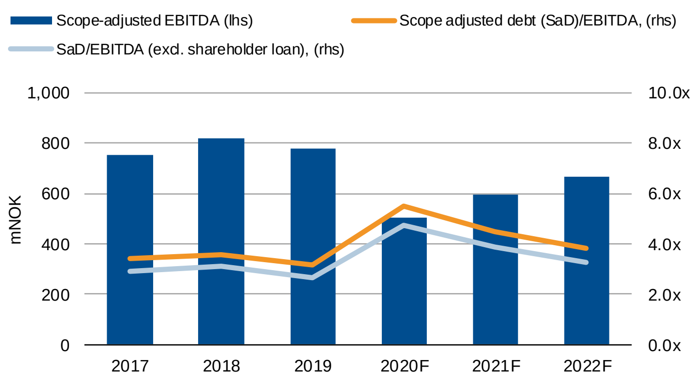
			Scope estimates	
Scope credit ratios	**2018**	**2019**	**2020F**	**2021F**
EBITDA/interest cover	7.7x	8.7x	5.2x	5.9x
Scope-adjusted debt/EBITDA	3.6x	3.1x	5.5x	4.5x
Scope-adjusted debt (excl. sub. shareholder loan) / EBITDA	3.1x	2.7x	4.7x	3.9x
Scope-adjusted FFO/Scope-adjusted debt	7.8 %	31.0 %	8.3 %	19.1 %
FOCF/Scope-adjusted debt	-4.9 %	20.9%	-2.4%	7.6%
Scope-adjusted EBITDA				
EBITDA	794	779	505	595
Operating lease payments in respective year	25	-	-	-
Scope-adjusted EBITDA	**820**	**779**	**505**	**595**
Scope-adjusted funds from operations				
EBITDA	794	779	505	595
less: (net) cash interest as per cash flow statement	-87	-88	-96	-99
less: cash tax paid as per cash flow statement	-150	-310	-313	-55
add: depreciation component operating leases	15	-	-	-
Other items	-344	372	129	65
Scope funds from operations (FFO)	**229**	**754**	**226**	**505**
Scope-adjusted debt				
Reported gross debt	2,323	2,232	2,596	2,396
Cash, cash equivalents	-103	-225	-266	-163
cash not accessible	59	34	35	35
Pension adjustment	43	32	29	26
Operating lease obligation	229	-	-	-
Subordinated owner loan	374	374	374	374
Scope-adjusted debt (SaD)	**2,926**	**2,447**	**2,767**	**2,668**

Operational developments since our previous rating report

With 2020 coming to an end, it is clear that the achieved power prices in Glitre's service territory will be substantially below our expectations last year. This will affect cash flow generation negatively, particularly within the company's hydro power production segment. Still, Glitre's hedging activities have significantly improved achieved prices compared to spot prices, and current hedges in place also provide some protection from downside risk going forward. As the hydro power production segment's EBITDA has decreased, its relative contribution to overall group EBITDA this year has fallen. Despite more stable grid profitability this year, Glitre's financial risk profile has deteriorated, as evidenced by the spike in its leverage ratio and the expectation of negative FOCF this year.

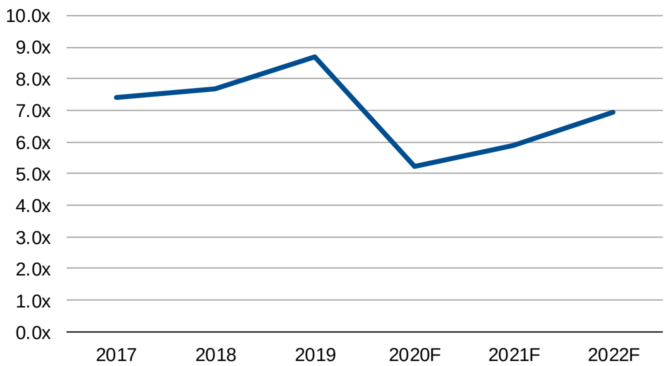
The company's ambition is still to reduce the underlying volatility in production by hedging a relatively high percentage of anticipated production next year (around 50%), and then reducing this in the following years. In addition to the Nasdaq contracts, Glitre also uses over-the-counter or bilateral hedging agreements.

Figure 1: Scope-adjusted leverage (x) and EBITDA (NOK m)



Source: Scope estimates

Figure 2: EBITDA/Interest cover (x)



Source: Scope estimates

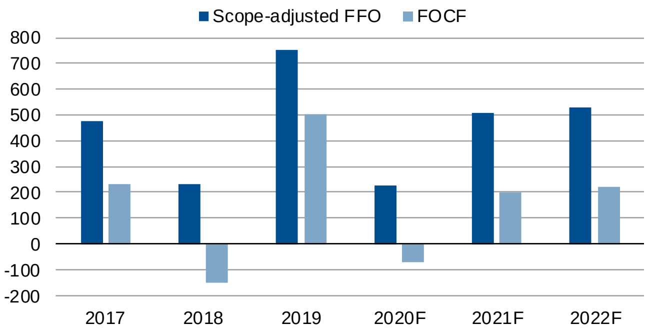
Updated forecast

We have updated our financial forecast for Glitre, following our review of recent performance and market conditions. Our projections do not assume any structural transactions. Based on the latest forward power prices and hedges in place, we expect leverage to return to more normalised levels as early as next year, which will ease the current downward pressure on Glitre's financial risk profile.

We expect power prices to recover in 2021, based on updated forward market data as of early Dec 2020. Glitre's hedging level for the next three years indicates less downside risk for 45%-55% of expected production in 2021 and 2022. The assumed recovery in prices could also be helped by the new power cable to Germany, which will be in place next year, and our assumption of a lower hydrological surplus in the market, which has been a drag this year.

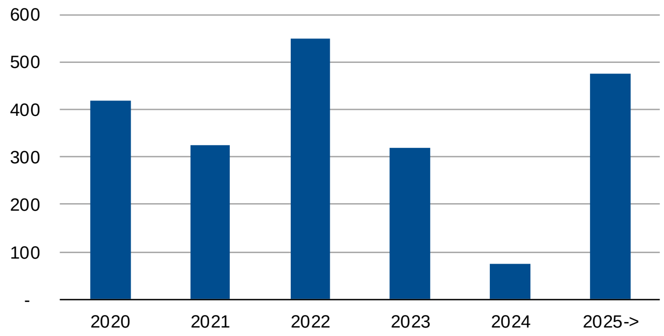
Looking at cash flows and capex figures over time, Glitre's free operating cash flow has been positive (with the exception of 2018 and 2020) and we project that it will continue to be so in the coming years. Capex and divided estimates are NOK 300m p.a. and approx. 60% of net income respectively. If we include dividend pay-outs, discretionary cash flow is expected to be positive in 2021 and 2022, making the dip in 2020 temporary.

Figure 3: Cash flow development (NOK m)



Source: Scope estimates

Figure 4: Debt maturity profile, as at Sept 2020 (NOK m)



Source: Scope estimates

Summary of business and financial risk profiles

Our business risk profile assessment for Glitre Energi has not changed over the year and is currently stronger than its financial risk profile. The company's business risk profile is supported by historically stable profitability margins and a well-integrated business model, with a large share of monopolistic power distribution and the hedging of more volatile power production output.

Supplementary rating drivers

We continue to use a bottom-up approach to analyse Glitre Energi's parent support. The one-notch uplift assigned for municipality ownership remains unchanged. As of 2020, the new indirect owners of Glitre Energi are the underlying municipalities in Buskerud (instead of the county municipality) through direct owner Vardar.

Long-term and short-term debt ratings

The senior unsecured rating is in line with the issuer rating. The S-2 short-term rating reflects the company's sufficient short-term debt coverage and good access to banks and debt capital markets. Despite Glitre Energi's lower internal liquidity ratio at present (due to maturing debt), overall liquidity is adequate and justifies the affirmation of our S-2 short-term rating, in accordance with our methodology.

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