Eidsiva Energi AS
Norway, Utilities

A- STABLE

Key metrics

			Scope estimates	
Scope credit ratios[1]	2021	2022	2023E	2024E
Scope-adjusted EBITDA/interest cover	7.4x	11.4x	7.5x	5.8x
Scope-adjusted debt/EBITDA	7.7x	3.7x	3.3x	3.5x
Scope-adjusted funds from operations (FFO)/debt	10%	24%	24%	19%
Scope-adjusted free operating cash flow (FOCF)/debt	-5%	9%	6%	1%

Rating rationale

The rating reflects a standalone credit assessment of BBB+ (up from BBB) and a one-notch uplift based on our assessment of parent support from Eidsiva's municipal owners.

The stronger standalone credit assessment is driven by our view of Eidsiva's stronger-than-anticipated financial risk profile, which is likely to be retained based on continued good performance in its regulated grid operations and sizeable cash dividends from its ownership in hydro power generator Hafslund Eco Vannkraft (HEV). This will likely provide ample operating cash flows to pursue relatively high grid investments and dividend payments while keeping leverage at stronger-than-anticipated levels, as exemplified by Scope-adjusted debt/EBITDA projected around 3.5x in the medium term. While cash dividends from HEV are subject to volatility and external factors such as achievable power prices in the generator's price region, we remain comfortable assessing the financial risk profile at BBB-, up from BB.

The business risk profile remains at A, underpinned by Eidsiva's dominant position as Norway's largest distribution system operator (DSO). Additionally, the company holds strong positions in its other business segments, including district heating and broadband.

Outlook and rating-change drivers

The Stable Outlook reflects our expectation that i) monopolistic, regulated grid operations will continue to contribute the most to EBITDA; ii) leverage remains around 3.5x on a sustained basis; iii) capital expenditure will remain high in the medium term; and iv) Eidsiva will remain municipality owned.

A positive action could be triggered by an improving financial risk profile, exemplified by Scope-adjusted debt/EBITDA sustained significantly below 3.0x, thanks to improved free operating cash flow and/or asset disposals.

A negative rating action could be triggered by a weakening financial risk profile, exemplified by Scope-adjusted debt/EBITDA sustained above 5.0x, which could be due to lower-than-expected power prices, higher-than-expected capex and/or extraordinary dividend payments. The loss of its government-related entity status could also trigger a negative rating action albeit deemed remote.

[1] 2021 restated, as Scope-adjusted metrics now include cash dividends from HEV

Ratings & Outlook

Issuer	A-/Stable
Short-term debt	S-1
Senior unsecured debt	A-

Analyst

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Related Methodologies

General Corporate Rating Methodology; October 2023

European Utilities Rating Methodology; March 2023

Government Related Entities Rating Methodology; July 2023

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Bloomberg: RESP SCOP

Rating history

Date	Rating action	Issuer rating & Outlook
24 Jan 2024	Upgrade	A-/Stable
25 Jan 2023	Affirmation	BBB+/Stable
24 Feb 2022	Affirmation	BBB+/Stable

Rating and rating-change drivers

Positive rating drivers

- Norway's largest regulated distribution system operator, with significant EBITDA from monopolistic power distribution
- Long-term committed municipal ownership resulting in a one-notch uplift using our Government Related Entities Rating Methodology
- Significant dividends from Eidsiva's 43.5% ownership in Norway's second largest hydro power producer HEV (positive ESG factor)
- Profitable broadband and bioenergy operations

Negative rating drivers

- Sizeable investments, resulting in pressure on FOCF and external funding requirements across the investment cycle
- Sizeable dividend payouts to municipal owners, despite higher-than-historical investments in the medium term

Positive rating-change drivers

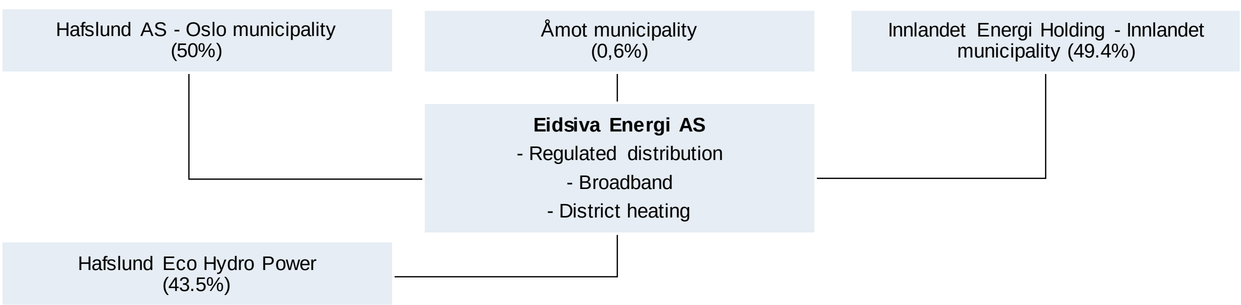
- Improving FOCF, or asset disposals, reducing Scope-adjusted debt/EBITDA significantly below 3.0x, sustained

Negative rating-change drivers

- Weaker financial risk profile for a prolonged period, with Scope-adjusted debt/EBITDA significantly above 5.0x
- Loss of municipal ownership and government-related entity status (remote)

Corporate profile

Figure 1: Eidsiva company overview



Sources: Eidsiva, public

Eidsiva Energi AS is Norway's largest DSO with more than 980,000 connection points, serving almost 2m individuals through a distribution network of over 66,000 km. In addition, the company also has a profitable district heating operation with an annual volume of around 450 GWh per annum and is Norway's third largest provider of broadband services to over 88,000 customers through its collaboration with Norwegian broadband provider Altibox. In 2022, Eidsiva had a turnover of EUR 990m, an EBITDA of EUR 293m and a net income of EUR 191m.

Eidsiva holds a 43.5% ownership in Norway's second largest hydro power producer HEV 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% through Hafslund).

Financial overview

			Scope estimates		
Scope credit ratios	**2021**	**2022**	**2023E**	**2024E**	**2025E**
EBITDA/interest cover	7.4x	11.4x	7.5x	5.8x	7.1x
Scope-adjusted debt/EBITDA	7.7x	3.7x	3.3x	3.5x	3.4x
Scope-adjusted FFO/debt	10%	24%	24%	19%	22%
Scope-adjusted FOCF/debt	-5%	9%	6%	1%	5%
Scope-adjusted EBITDA in NOK m					
EBITDA	1,811	3,297	3,822	4,064	4,429
Dividends received (mainly HEV)	380	1,194	950	750	650
Scope-adjusted EBITDA	**2,191**	**4,491**	**4,772**	**4,814**	**5,079**
FFO in NOK m					
Scope-adjusted EBITDA	2,191	4,491	4,772	4,814	5,079
less: (net) cash interest paid	-296	-590	-638	-836	-717
less: cash tax paid per cash flow statement	-289	35	-330	-774	-528
Other cash flow changes (including from associates)	105	135	0	0	0
FFO	**1,711**	**4,071**	**3,804**	**3,204**	**3,834**
FOCF in NOK m					
FFO	1,711	4,071	3,804	3,204	3,834
Change in working capital	-94	85	82	-16	-31
less: capital expenditure (net)	-2,533	-2,635	-3,000	-3,000	-3,000
FOCF	**-916**	**1,521**	**886**	**188**	**803**
Net cash interest paid in NOK m					
Net cash interest per cash flow statement	296	394	638	836	717
Change in other items	0	0	0	0	0
Net cash interest paid	**296**	**394**	**638**	**836**	**717**
Scope-adjusted debt in NOK m					
Reported gross financial debt	17,405	19,231	17,369	18,444	18,793
less: cash and cash equivalents	-555	-2,673	-1,655	-1,717	-1,669
add: non-accessible cash[2]	57	88	90	90	90
add: pension adjustment[3]	0	0	0	0	0
Other items	0	0	0	0	0
Scope-adjusted debt	**16,907**	**16,646**	**15,804**	**16,817**	**17,214**

[2] Restricted cash includes collateral provided for future tax payments.
[3] No pension adjustment since 2020 as Eidsiva's pension assets fully cover its pension liabilities.

Table of Content

Environmental, social and governance (ESG) profile[4]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend
Green leaf (ESG factor: credit positive)
Red leaf (ESG factor: credit negative)
Grey leaf (ESG factor: credit neutral)

ESG profile supportive of market position, profitability, cash flow and access to funding

Although the majority of Eidsiva's operation revolves around regulated power distribution, the company's ownership in Norway's second largest hydro power producer HEV is a credit-positive ESG factor. The ownership strengthens the company's ESG profile, supporting both current and future cash flow and access to funding.

Further, the Norwegian government relies heavily on regulated distributors to reach its stated climate goals[5] by 2030. This is because those goals rely heavily on new intermittent generation and the electrification of Norwegian industry, both of which will lead to an increased strain on power grids. Eidsiva has shown that it will honour its role in achieving these goals, as one of Norway's DSO, by investing heavily in its power grids over the medium term. We believe this contributes positively to solidifying its status as a government-related entity.

Norwegian utilities generally have sustainable profiles but are still subject to regulatory and reputational risks. This became clear during 2022, when extraordinarily high electricity prices brought attention to Norway's publicly owned power sector. It was further exemplified in September 2022, when the government imposed a temporary windfall tax on electricity generators (ended in Q4 2023) because of the soaring prices and permanently raised the resource rent tax rate on hydro generation assets. Eidsiva as a company is not directly impacted by these windfall taxes, but indirectly through its ownership in HEV.

Considering the extraordinary circumstances, and the temporary nature of the windfall tax, we do not consider this a shift in the regulatory environment. Historically, the regulatory environment has been very stable, something we do not see changing. This stability is reflected through the industry and market assessments.

[4] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e., those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.
[5] www.regjeringen.no/en/aktuelt/norways-new-climate-target-emissions-to-be-cut-by-at-least-55-/id2944876/

Business risk profile: A

Blended industry risk profile: A+

Eidsiva is vertically integrated and horizontally diversified (Figure 2). Each of these segments has its own distinct industry risk fundamentals, and we therefore apply a blended industry risk profile. In addition, cash dividends from HEV have grown following recent years' surging power prices. As we expect sizeable contributions from HEV in the medium term, the industry risk from HEV (unregulated generation) is included when assessing Eidsiva's industry risk. Still, regulated power distribution remains the largest contributor with 68% of average Scope-adjusted EBITDA, but the inclusion of the exposure to unregulated generation through HEV leads to an assessment of Eidsiva's industry risk at A+ (down from AA-).

Strong market position, driven by its regulated monopolistic position in power distribution

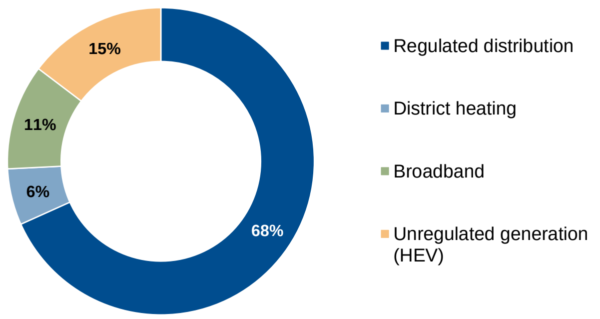
Eidsiva has a very strong market position, driven by its regulated monopolistic position in power distribution. It also benefits from strong and partly protected positions in both broadband and district heating. Eidsiva's long-standing minority shareholding in Norway's largest unregulated generator (HEV) also contributes favourably.

With 66,000 km of distribution network, over 980,000 connection points, and approximately 2 million customers in its service area, Eidsiva is Norway's largest DSO (Figure 3). In addition, the structural aspects of Eidsiva's service area are strong, as it is an economically growing area that includes the Norwegian capital city of Oslo. This is favourable in terms of the predictability and projected growth of future cash flows.

Norway's third largest provider in district heating and in broadband services

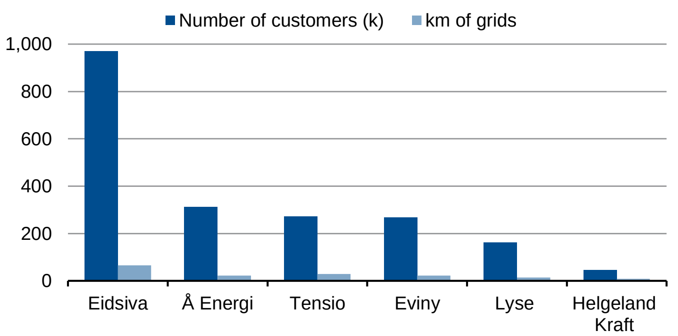
Eidsiva is the third largest district heating provider in Norway, with an annual production of around 450 GWh. It is also Norway's third-largest provider of broadband services, with over 88,000 broadband customers through its collaboration with Norwegian broadband provider Altibox. Albeit smaller, we positively incorporate both segments in our assessment of Eidsiva's diversification and market position.

Figure 2: 2019-2025E average Scope-adjusted EBITDA contribution by business segment



Sources: Eidsiva, Scope estimates

Figure 3: Norwegian distribution system operators, grid size and customers



Sources: Eidsiva, Scope

Eidsiva's positions in district heating and broadband services are further reinforced by high barriers to entry. The company has made significant investments in developing fiber and district heating infrastructure in its service territory, which would be a costly endeavor for new entrants. As a result, new competitors are unlikely to enter these markets, and Eidsiva's operations in these areas are somewhat shielded from direct competition.

Proposal by Norwegian Communications Authority may increase competition in broadband

For broadband services, this may change in the next couple of years, as a recent proposal by the Norwegian Communications Authority would require regional broadband providers with strong market positions to open their networks to other providers. While this would likely impact Eidsiva's broadband operations, it is expected to have a moderate impact on its profitability, as it would still receive compensation from other providers utilising its fiber network.

Regulated distribution, a stabilising force for the overall business

The regulatory framework for power distribution in Norway allows for timely cost coverage. This means that underlying profitability and cash flow over time are dictated by state-set tariffs rather than short-term market fluctuations. Eidsiva's core business in power distribution is therefore a stabilising force and a robust source of cash flow for the overall business.

However, as changes in a company's costs can only be passed on to end-customers through tariff changes in following years, this system also impacts short-term profitability when cost greatly decrease or increase in a short period of time.

Short-term profitability hindered in 2021/22

Indeed, Eidsiva's short-term profitability was hindered in 2021/22, as the surging power prices led to a sharp increase in costs to cover grid losses as well as higher operational costs. Despite rising costs, Eidsiva opted to delay tariff adjustments in 2022 to mitigate the burden on Norwegian households, negatively impacting its inter-year profitability.

Support scheme implemented in H2 2022

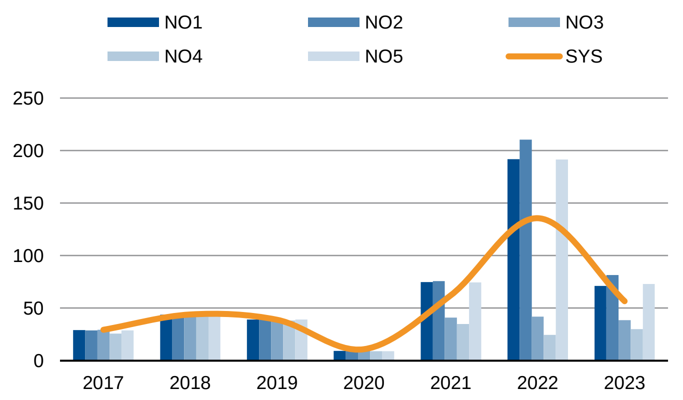
The company's profitability was at a record low when the Norwegian government and the Norwegian transmission system operator (Statnett SF) put in place a temporary scheme to alleviate the pressure on Norwegian grid operators: tariffs imposed by Statnett on local grid operators were reduced and congestion income was directly transferred from Statnett to local grid operators to compensate for the inflated costs[6]. As the largest DSO in Norway, Eidsiva greatly benefited from this scheme and ended 2022 on a stronger note than expected in our last review.

Profitability improved as of Q3 2023

As of Q3 2023 power prices were substantially lower than for the same period in 2022. This impacted Eidsiva directly through lower profitability in district heating and indirectly through reduced earnings in HEV. In parallel, the grid business benefited from lower grid losses, lower overhead costs, and improved cost coverage as 2021/22's cost levels, higher interest rates, higher inflation, all were incorporated in the state set revenue cap and allowed rate of return calculation. Therefore, the company's grid business reported a strong EBITDA margin of 42% at Q3 2023 (21% at Q3 2022).

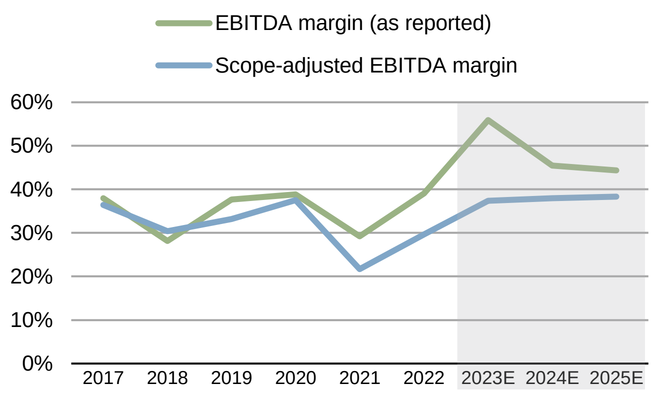
The remaining segments delivered EBITDA margins around 40% and contributions from HEV were already above year-end 2022 levels, as HEV's profits were less impacted by legacy hedges and fair value adjustments than in 2022. In sum, Eidsiva reported an EBITDA margin of 67% at Q3 2023 (40% if income associated companies was excluded).

Figure 4: Average yearly power prices in Norway, EUR/MWh



Sources: Eidsiva, Scope estimates

Figure 5: Historical and projected EBITDA margins[7]



Sources: Eidsiva, Scope estimates

[6] www.regjeringen.no/no/aktuelt/pressemelding-flaskehalsinntekter/id2942438/
[7] Reported EBITDA margin includes income from associated companies (mainly comprises of P&L contributions from HEV).

Increasing underlying profitability expected in the coming years

Going forward we anticipate that Eidsiva's income will rise, driven by sustained high investments in grid infrastructure and the inclusion of recent years' higher-than-historical cost levels in the state's revenue cap calculation. Further, we expect that Eidsiva's profitability will improve in the medium term due to the following factors: i) Transfers of congestion income from the Norwegian TSO in 2023, ii) Improved cost coverage through the inclusion of recent year's cost levels, rising interest and rising inflation in the state set allowed revenues and allowed return calculations, iii) Continued higher-than-historical power prices, resulting in higher-than-historical cash dividends from HEV, and iv) Synergies realised upon completion of a larger IT project in 2023.

However, some factors are expected to negatively impact EBITDA: i) No transfers of congestion income from the Norwegian TSO for 2024 and 2025, ii) Inflationary pressure on wages and other operational expenses, and iii) Continued higher-than-historical power prices, leading to higher-than-historical cost associated to grid losses and service costs.

Expected reported EBITDA margins between 56-44%

In conclusion, profitability is expected to remain good in the medium term, with Scope-adjusted EBITDA margin increasing towards 38% in 2025E, compared to 30% in 2022 and 35% on average historically.

Financial risk profile: BBB-

Assumptions & adjustments

To assess Eidsiva's creditworthiness, we look at key credit metrics such as leverage and debt protection supplemented by our assessment on internal funding capacity and liquidity.

We have made the following adjustments and assumptions in our base case:

- Updated price scenario;
- Adjusted contribution from HEV;
- Incorporated repayment of a NOK 2bn loan given to HEV by Eidsiva in 2023;
- No more transfers of congestion income from the Norwegian TSO after 2023;
- Higher effective cost of debt.

Improved leverage, around 3.5x in the medium term

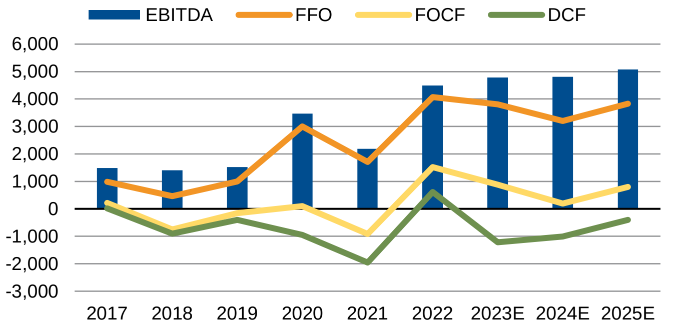
Eidsiva's financial risk profile reflects our expectation that profitability in its regulated grid operations will remain good, cash dividends from HEV will remain above historical averages and that the company will invest around NOK 3bn per annum and pay out dividends of around 50% of net income.

We expect Eidsiva's leverage to decrease from 3.7x at year-end 2022 to 3.3x at YE 2023E before stabilising around 3.5x in the medium term. However, we note uncertainties regarding the tail end of our forecast, as deleveraging is partly driven by assumptions of higher-than-historical contributions from HEV. These contributions will vary with Nordic energy prices, which are volatile. Excluding such contributions, the projections show a deleveraging to around 4.0x, which is still stronger than projected during last year's review.

Pressure on interest coverage following rising interest rates and lower interest income

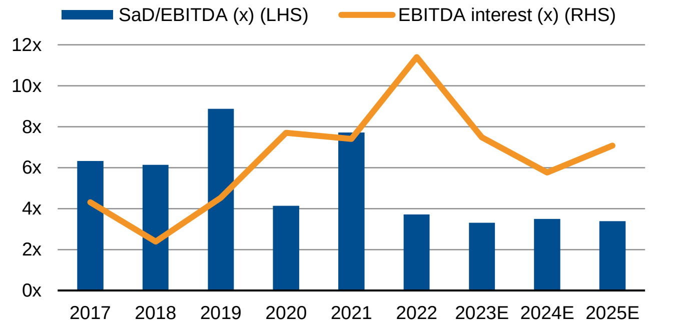
In parallel, the projected interest coverage will weaken from 11.4x in 2022 to 7.5x in 2023E, before reaching a low of 5.8x in 2024E. This decline is primarily attributed to the loss of interest income from the NOK 2bn loan given to HEV by Eidsiva which was repaid in April 2023. Additionally, rising interest rates will impact the portion of the company's financing that is floating rate (five out of 19 bonds), but this effect is moderate in comparison to the decrease in interest income.

Figure 6: Scope-adjusted cash flows (NOK m)



DCF = discretionary cash flow
Sources: Eidsiva, Scope estimates

Figure 7: Scope-adjusted leverage and interest coverage



Sources: Eidsiva, Scope estimates

Cash flow positively impacted by government support scheme and contributions from HEV

In addition to robust cash flows from Eidsiva's operations, FFO and FOCF will benefit from contributions from HEV throughout the forecast and from the government support scheme in 2023E (Figure 6). The resulting projections show a low in 2024E, when higher-than-historical tax payments are due (based on 2023E's earnings) before strengthening again in 2025E.

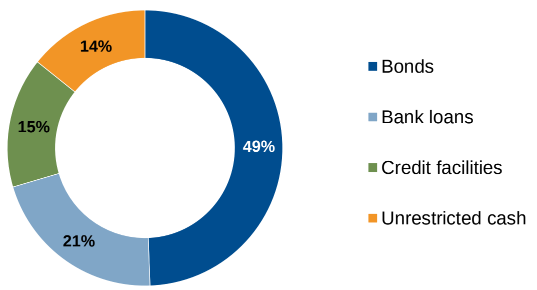
Negative discretionary cash flow due continued dividends

Lastly, we forecast negative discretionary cash flow for 2023-2025, due the timing of taxes and our expectations that Eidsiva will pay dividends to its municipal owners whilst upholding its capital expenditure programme.

Diverse funding mix and balanced maturity profile

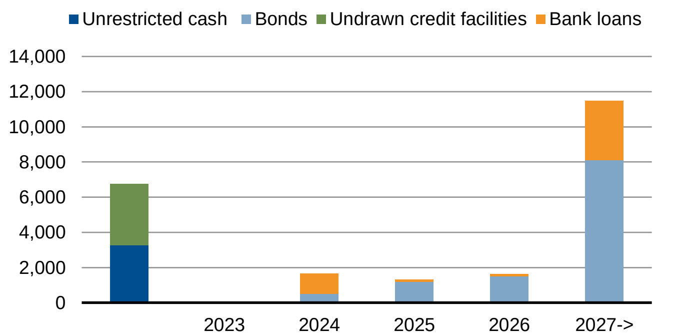
Eidsiva has access to a diverse range of funding sources (including bonds, overdraft facilities and bank loans), facilitated by its investment-grade credit rating, municipal ownership, and a balanced debt maturity profile (Figures 8 and 9).

Figure 8: Funding mix, Q3 2023



Sources: Eidsiva, Scope

Figure 9: Debt maturity profile (NOK m), Q3 2023



Sources: Eidsiva, Scope

Adequate liquidity

To accommodate higher net working capital requirements (due to higher cost associated to grid losses), Eidsiva increased its committed credit facilities to NOK 3.5bn in 2022. In addition to unutilised facilities Eidsiva had NOK 3.3bn in unrestricted cash at Q3 2023 compared to total maturities of NOK 1.7bn in 2024.

Eidsiva's liquidity remains adequate, with a liquidity (internal and external) cover of over 200%.

Balance in NOK m	2022	2023E	2024E
Unrestricted cash (t-1)	498	2,585	1,565
Open committed credit lines (t-1)	2,500	3,500	3,500
FOCF (t)	1,521	886	188
Short-term debt (t-1)	2,221	2,578	241
Coverage	**>200%**	**>200%**	**>200%**

Supplementary rating drivers: +1 notch

Government-related entity status warrants a one-notch uplift from the BBB+ standalone credit assesment

Eidsiva is fully owned by municipalities in its service territory. Using our Government Related Entity Rating Methodology, we apply a bottom-up approach to assess Eidsiva's parental support.

We anticipate a high capacity and medium willingness of the public sponsors to provide financial support, if needed. We therefore grant a one-notch rating uplift to Eidsiva's standalone credit assessment.

No adjustment for financial policy

We make no adjustment for financial policy and highlight management's dedication to maintaining the company's financial strength and its desire to protect an investment grade rating. Still, we acknowledge the company's history of consolidating the Norwegian utility sector and the continued dividend payments to its municipal owners.

Long-term and short-term debt ratings

Senior unsecured debt rating: A-

The A- rating for senior unsecured debt is in line with the issuer rating.

Short-term debt rating: S-1

The short-term debt rating of S-1 is based on the A-/Stable issuer rating, sufficient short-term debt coverage and good access to both bank and bond financing.

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