Østfold Energi AS
Kingdom of Norway, Utilities

SCOPE BBB+ STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2022**	**2023**	**2024E**	**2025E**
Scope-adjusted EBITDA interest cover	>20x	Net interest income	>20x	>20x
Scope-adjusted debt/EBITDA	Net cash	Net cash	0.6x	0.9x
Scope-adjusted free operating cash flow/debt	Net cash	Net cash	-60%	1%

Rating rationale

The rating reflects a standalone credit assessment of BBB and a one-notch uplift based on our assessment of parent support from the company's Norwegian municipal owners.

The business risk profile (assessed at BBB-) continues to reflect Østfold Energi's core exposure to low-cost, flexible and environmentally friendly hydropower generation (positive ESG factor), which has a favorable position in the merit order system and provides high profitability. Constraints includes the industry-inherent volatility in non-regulated power generation and low diversification compared to larger and more integrated utility peers.

The comparatively stronger financial risk profile (assessed at A) still supports the standalone credit assessment, driven by low leverage and good internal funding capacity over time.

Outlook and rating-change drivers

The Stable Outlook reflects our expectation that Østfold Energi will maintain strong credit metrics, with leverage (Scope-adjusted debt/EBITDA) remaining between 0.5x and 1.5x in the next few years amid higher-than-historical investments and more moderate power prices.

The upside scenario for the ratings and Outlook is:

1. A sustained net cash position, albeit deemed remote, as such leverage headroom likely could eventually be deployed for growth or shareholder remuneration.

The downside scenarios for the ratings and Outlook are (individually or collectively):

1. Sustained deterioration of leverage with Scope-adjusted debt/EBITDA above 2.5x.
2. Loss of government-related entity status (remote).

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
15 Nov 2024	Affirmation	BBB+/Stable
10 Nov 2023	New	BBB+/Stable

Ratings & Outlook

Issuer	BBB+/Stable
Short-term debt	S-2
Senior unsecured debt	BBB+

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Related Methodologies

General Corporate Rating Methodology; October 2023

European Utilities Rating Methodology; June 2024

Government Related Entities Methodology, September 2024

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Low-cost, flexible and environmentally friendly hydropower generation (positive ESG factor) with sizeable reservoirs • Strong financial risk profile with low leverage and good internal financing capacity over time • High profitability as measured by EBITDA margin and Scope-adjusted return on capital employed • Hedging policy which helps to mitigate some exposure to industry inherent volatility in the short-term • Long-term committed municipal owners with capacity and willingness to provide potential parent support	• Exposure to volatile power prices for unhedged power generation volumes • Asset concentration risk with power generation revolving around two key power plants – albeit partially mitigated by insurance for property damage and an adverse two-year standstill period • Low diversification by utility segment and geographical pricing market • Increased investments in the next years involving some execution risk related to growth projects

Positive rating-change drivers	Negative rating-change drivers
• A sustained net cash position, albeit deemed remote, as such leverage headroom is likely to eventually be deployed for growth or shareholder remuneration	• Sustained deterioration of leverage with Scope-adjusted debt/EBITDA above 2.5x • Loss of government-related entity status (remote)

Corporate profile

Østfold Energi is a Norwegian utility owned by Østfold county municipality (45%) and 13 municipalities within or in proximity to Østfold county municipality. Its main activity is hydropower generation in south Norway where it owns and operates mostly flexible hydro plants with installed capacity of 0.4 GW and an annual mean generation of around 1.6 TWh. It also owns 50% of Siso Energi and is engaged in district heating, wind and solar activities.

Financial overview

			Scope estimates		
Scope credit ratios	**2022**	**2023**	**2024E**	**2025E**	**2026E**
Scope-adjusted EBITDA/interest cover	>20x	Net interest income	>20x	>20x	19.0x
Scope-adjusted debt/EBITDA	Net cash	Net cash	0.6x	0.9x	1.2x
Scope-adjusted free operating cash flow/debt	Net cash	Net cash	-60%	1%	2%
Scope-adjusted EBITDA in NOK m					
EBITDA	2,072	1,236	653	628	615
Other items[1]	72	4	30	30	30
Scope-adjusted EBITDA	**2,144**	**1,240**	**683**	**658**	**645**
Funds from operations in NOK m					
Scope-adjusted EBITDA	2,144	1,240	683	658	645
less: Scope-adjusted interest	(13)	3	(10)	(27)	(34)
less: cash tax paid per cash flow statement	(432)	(1,388)	(649)	(270)	(242)
Other non-operating charges before FFO	135	(172)	-	-	-
Funds from operations (FFO)	**1,834**	**(317)**	**24**	**361**	**369**
Free operating cash flow in NOK m					
Scope-adjusted FFO	1,834	(317)	24	361	369
Change in working capital	20	(80)	-	-	-
less: capital expenditure (net)	(184)	(134)	(250)	(350)	(350)
less: lease amortisation	(4)	(5)	(5)	(5)	(5)
Free operating cash flow (FOCF)	**1,666**	**(535)**	**(231)**	**6**	**15**
Net cash interest paid in NOK m					
Net cash interest per cash flow statement	10	(6)	7	24	31
Add: pension interest	2	3	3	3	3
Net cash interest paid	**13**	**(3)**	**10**	**27**	**34**
Scope-adjusted debt in NOK m					
Reported gross financial debt	425	426	426	676	926
less: cash and cash equivalents	(1,700)	(721)	(119)	(175)	(252)
add: non-accessible cash	52	32	32	32	32
add: pension adjustment	48	44	44	44	44
Scope-adjusted debt	**(1,175)**	**(219)**	**383**	**577**	**750**

[1] Dividends received from associated companies.

Table of Content

Environmental, social and governance (ESG) profile[2]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)	Green leaf	Labour management		Management and supervision (supervisory boards and key person risk)	Grey leaf
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)	Grey leaf
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)	Grey leaf
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	Grey leaf

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

Clean energy generation

Østfold Energi's business model is mainly exposed to clean, low-cost hydropower generation. This limit transition and stranded risk and should support future cash flow through high utilisation factors of power plants with a continued, strong position in the merit order. The company supplements its core hydropower business with other types of sustainable energy generation.

We consider the company's large-scale hydropower generation to underpin its government-related entity status, as those assets are required to have at least two-thirds public ownership.

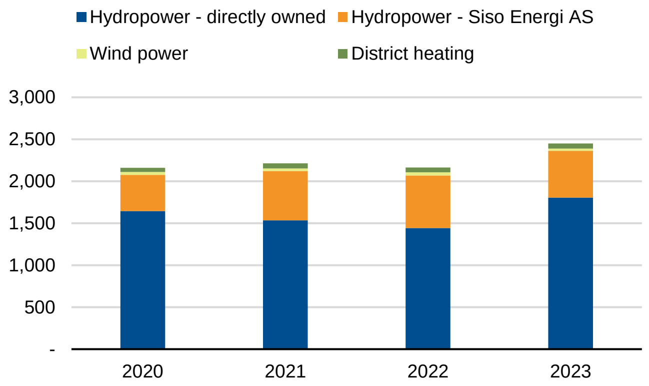
[2] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BBB-

Industry-inherent volatility in non-regulated power generation

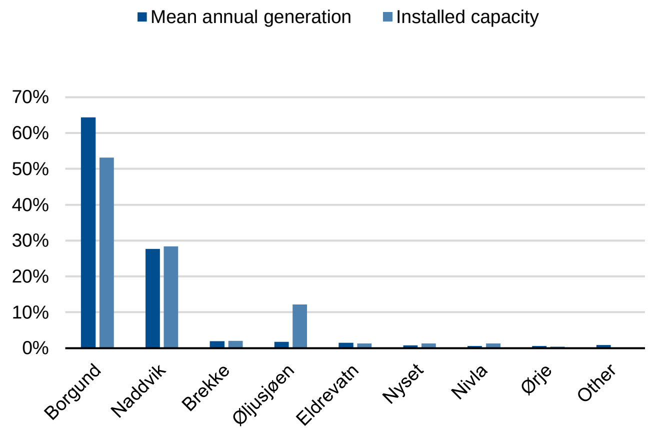
As an almost pure-play power generator, Østfold Energi's financial performance is closely linked to achievable power prices, which are inherently volatile. Its district heating business is more stable with high entry barriers but is comparatively small in terms of contribution to cash flow.

Figure 1: Energy generation volume by technology, GWh



Sources: Østfold Energi, Scope

Figure 2: Directly owned hydropower generation by power plant



Sources: Østfold Energi, Scope

Consolidated mean annual hydropower volume of 1.6 TWh

Østfold Energi has an annual mean hydropower generation volume of about 1.6 TWh in south Norway from directly owned hydro plants. In addition, it owns 50% of Siso Energi, which operates two hydro plants in north Norway that generate around 1.1 TWh in a normal year.

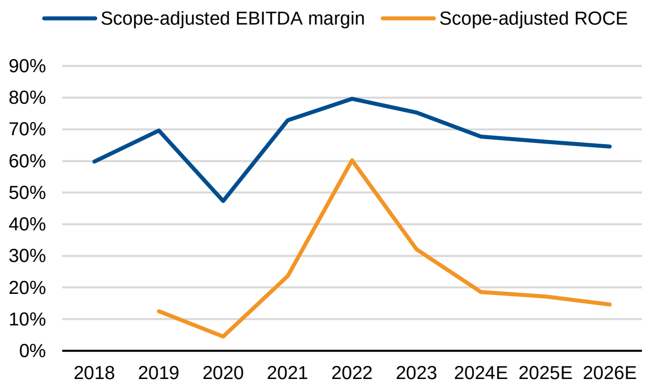
Small size balanced by strong merit order position

The company is a small power generator in Norway by market share. We still assess Østfold Energi's market positioning as good, owing to its low-cost and flexible hydropower generation, which holds a strong position in the merit order and can provide peak-load capacity.

Mainly operating in Norway's NO5 bidding zone

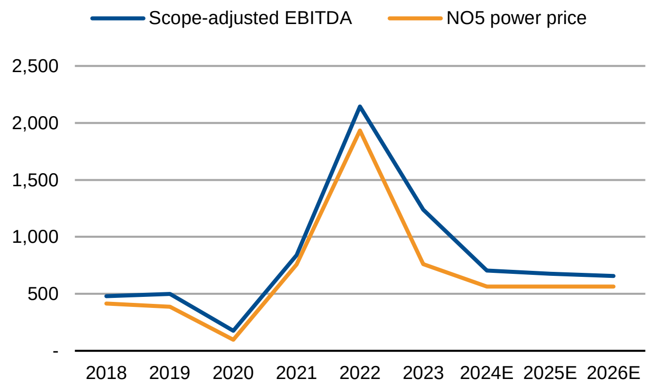
Østfold Energi's hydropower generation is mainly located in southwest Norway (NO5 bidding zone). In terms of pricing risk, this regional concentration is partly mitigated by exposure to surrounding power markets in the Nordics and Europe through interconnectors.

Figure 3: Profitability



Sources: Østfold Energi, Scope estimates

Figure 4: Scope-adjusted EBITDA (NOK m) versus the average power price in NO5 (NOK/MWh)



Sources: Østfold Energi, Nordpool, Scope estimates

Asset concentration risk

Østfold Energi's power generation portfolio is concentrated around its two largest hydropower plants. These constitute around 90% of its mean annual production. This constrains asset diversification. However, with regards to adverse scenarios, we assess a mitigating impact from insurance that cover property damage and a standstill period of up to two years. There is no cumulative standstill risk as the plants are operationally independent of each other.

Dividend income from associated companies

Historically, Østfold Energi's cash flow has benefited from regular dividends from associated companies, of which Zephyr has been the most important, with a contribution of NOK 186m over 2018-2023.

Strong profitability

The business risk profile remains supported by strong profitability given the core exposure to low-cost hydro. We note that Østfold Energi's margins continue to normalise as power prices have gradually become more moderate. The EBITDA margin has declined from a peak of 80% in 2022 to 75% in 2023 and further to 72% in H1 2024. We expect the margin to stabilise in a range of 65%-70% in the current power price environment.

Financial risk profile: A

Unchanged financial risk profile

The financial risk profile remains strong, and is unchanged at A, reflecting low leverage and good internal financing capacity over time. Østfold Energi has historically maintained relatively conservative credit metrics. This has supported its ability to handle fluctuations in power prices.

Main assumptions

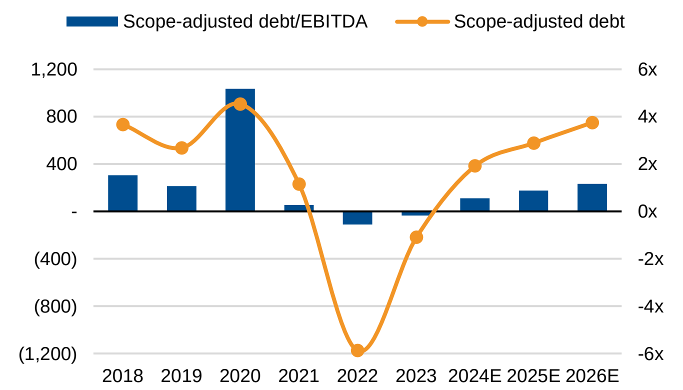
Our financial projections for 2024-2026 are mainly based on:

- An average power price in NO5 of around NOK 550/MWh
- Annual hydropower volumes (consolidated) of around 1.6 TWh
- Total investments of around NOK 1bn
- Maintenance of the dividend policy with payouts equal to 65% of the preceding year's net income

Net cash position of NOK 0.2bn at YE 2023

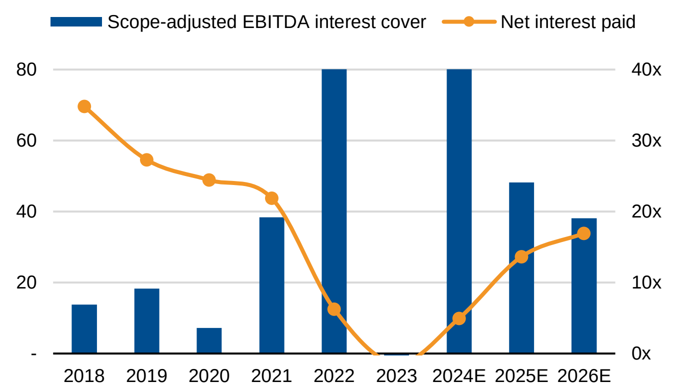
As of YE 2023, the company had a net cash position (as measured by Scope-adjusted debt) of NOK 0.2bn. Given the more moderate power prices in southwest Norway and the company's plans for higher-than-historical capex in 2024-2026, we expect a gradual increase in Scope-adjusted debt to around NOK 400m by YE 2024 and around NOK 750m by YE 2026.

Figure 5: Leverage (rhs) and Scope-adjusted debt (NOK m, lhs)



Sources: Østfold Energi, Scope estimates

Figure 6: EBITDA interest coverage (rhs) and Scope-adjusted interest (NOK m, lhs)



Sources: Østfold Energi, Scope estimates

Leverage expected to remain strong, although weakening

The gradual increase in Scope-adjusted debt is likely to result in a similar trajectory for leverage. However, as the company is mostly deploying its significant cash accumulation over 2021-2023 (Figure 5), we still expect leverage to remain strong, with Scope-adjusted debt/EBITDA projected to have an upward trend within a range of 0.5x-1.5x in the forecast period.

Debt protection to exceed 10x

Østfold Energi's debt protection (EBITDA interest cover) remains comfortable. In 2023, the company had a net interest income. While we expect a weakening in the next few years given an increasing debt exposure, the ratio is still likely to consistently exceed a level of 10x.

Almost NOK 1bn of capex in 2024-2026

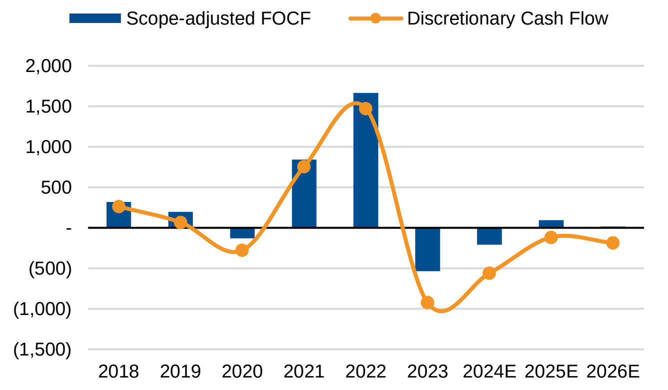
Forecasted capex amounts to almost NOK 1bn over 2024-2026, of which a high share is committed projects. The construction of a new hydropower plant, Gravdalen, is the largest project, with an estimated expenditure of NOK 0.5bn. The construction commenced in 2024 and is expected to be completed in Q3 2026, adding around 60 GWh of new power generation volumes.

Likely some dependence on external financing in the next few years

Free operating cash flow is expected be slightly negative in 2024-2026, on average, despite deductions for the investment in Gravdalen under the resource rent tax regime. The pressure on free operating cash flow is driven by growth capex and it also reflects high taxes paid in 2024 based on the strong result in 2023.

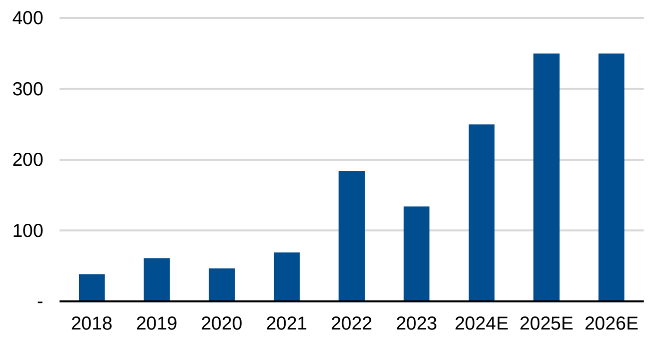
While much of the forecasted growth capex is likely to be funded internally, we expect that maintenance of the dividend policy and potential business acquisitions will require external financing in 2024-2026.

Figure 7: Scope-adjusted cash flows, NOK m



Sources: Østfold Energi, Scope estimates

Figure 8: Capex, NOK m



Sources: Østfold Energi, Scope estimates

Adequate liquidity

Liquidity is adequate. The NOK 400 million bond with maturity in August 2025 is expected to be refinanced with a similar debt instrument. The bond is currently the only outstanding debt of the company.

In our view, external financing for growth investments and refinancing should not be a problem. This is based on our assessment that Østfold Energi has good access to bank and capital market financing.

Balance in NOK m	2023	2024E	2025E
Cash and cash equivalents (t-1)	1,700	721	119
Non-accessible cash (t-1)	(52)	(32)	(32)
Open committed credit lines (t-1)	250	250	250
Free operating cash flow	(535)	(231)	6
Short-term debt (t-1)	-	-	400
Coverage, internal	**No ST debt**	**No ST debt**	**23%**
Coverage, internal + external	**No ST debt**	**No ST debt**	**86%**

Supplementary rating drivers: +1 notch

Supplementary rating drivers

Østfold Energi's financial policy has no credit impact beyond that reflected in our assessment of the financial risk profile. The company's dividend policy stipulates a payout ratio of 65% of the preceding year's net profit and a goal of maintaining an investment grade credit rating.

The issuer rating incorporates a one-notch uplift to the standalone credit assessment of BBB considering the company's status as a government-related entity. We have applied the bottom-up approach using the framework outlined in Scope's Government Related Entities Methodology. The conclusion of a one-notch uplift reflects the public sponsor's 'high' capacity and 'medium' willingness to provide support. In addition to some importance for the policy objectives of its owners, we note that Østfold Energi's large hydropower plants are required to be at least two-thirds owned by the state or municipalities. The rating uplift is in line with other Norwegian utilities rated by us with majority or full public ownership but no explicit guarantees on their debt or financial support.

Long-term and short-term debt ratings

Senior unsecured debt rating: BBB+

We have affirmed the instrument rating of BBB+ on senior unsecured debt, in line with the issuer rating.

Short-term debt rating: S-2

The affirmed S-2 short-term debt rating is based on the underlying BBB+/Stable issuer rating and reflects adequate short-term debt coverage as well as adequate access to bank and capital markets financing.

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