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Summary:
Enexis Holding N.V.

Primary Credit Analyst:
Karin Erlander, London (44) 20-7176-3584; karin_erlander@standardandpoors.com

Secondary Contact:
Mark J Davidson, London (44) 20-7176-6306; mark_j_davidson@standardandpoors.com

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Credit Rating: A+/Positive/--

Rationale

The ratings on Dutch electricity and gas distribution network company Enexis Holding N.V. and its subsidiary Enexis B.V. (jointly Enexis) reflect Standard & Poor's Ratings Services' view of the company's "excellent" business risk profile and "intermediate" financial risk profile.

Our assessment of Enexis' business risk profile as "excellent" reflects its natural monopoly status in its license areas, its low-risk regulated electricity and gas distribution network businesses, and its high quality network assets. The majority of Enexis' activities, including its electricity and gas tariffs, are regulated by the Dutch Ministry of Economic Affairs and the Dutch regulator, Energiekamer. These strengths are partly offset by the regulatory tariff reset risk every third year; exposure to incentive-based regulation that can impose challenging efficiency requirements; and the potential for further consolidation in the Dutch energy network sector, in which we anticipate Enexis would take an active part.

The "intermediate" financial risk profile continues to reflect Enexis' stable and predictable operating cash flow, our view that Enexis' credit metrics have strengthened due to tariff increases for the 2011-2013 regulatory period, and the company's well-spread maturity profile. It also takes into account a sizable capital expenditure (capex) program of about €850 million over 2012 and 2013, and the risk that investments could increase above our base-case projections due to acquisitions or higher-than-anticipated investments in smart meters.

The 'A+' rating on Enexis is based on the company's stand-alone credit profile, which we assess at 'a+', and on our opinion that there is a "moderate" likelihood that its owners would provide timely and sufficient extraordinary support in the event of financial distress. In accordance with our criteria for government-related entities, our view of a "moderate" likelihood of extraordinary support is based on our assessment of Enexis':

- "Important" role, given its strategic importance to the province and municipality owners, as the monopoly provider of gas and electricity distribution services in its license areas; and
- "Limited" link to the owners, given the dispersed ownership structure. Enexis' owners are the provinces of Noord Brabant (31%), Overijssel (19%), Limburg (16%), Groningen (6%), and Drenthe (2%), as well as other provinces and 116 municipalities in the region.

S&P base-case operating scenario

We project that Enexis' revenues, excluding further consolidation, will increase by an average of 5% per year through 2013, from €1.3 billion reported in 2011, and that the company's EBITDA margin will remain about 51% in 2013, which compares with less than 50% in 2010 and 51% in 2011.

Enexis' revenues increased 9% to €1.3 billion, and operating profit increased by 15% to €403 million in 2011, compared with 2010. We believe that Enexis will be able to sustain this level of earnings given the approved regulated tariffs through 2013 and the company's ongoing cost-saving program. Cost savings reduced operating costs by more than €24 million in 2011.

Revenues are also likely to increase as a result of the consolidation of the Dutch gas distribution network operator Intergas that Enexis acquired in May 2011. At the end of February 2012, Enexis announced the intention to acquire N.V. Rendo, the owner and operator of a gas and electricity distribution network in the north of The Netherlands. This is a relatively small network with an annual turnover of about €30 million, and we do not believe that the proposed acquisition would change our view on Enexis' business or financial risk profiles. However, the acquisition makes strategic sense and could provide some synergies because Rendo is situated within Enexis' existing service area.

S&P base-case cash flow and capital-structure scenario

We believe that Enexis will continue to participate in the consolidation of the distribution network sector in The Netherlands, but that investment will be more spread out over time, thereby limiting the near-term effect on the company's credit metrics. We also view positively that Enexis has built up a cash balance for this purpose, further mitigating any detrimental effect that a large acquisition may have on the credit metrics.

Our view is that, as a result of these developments, Enexis' will be able to sustain Standard & Poor's-adjusted funds from operations (FFO) to debt of more than 20% over the next few years.

Enexis' funds from operations (FFO) increased by 33% in 2011, to €639 million, compared with 2010. This amount of cash flow amply covered the €193 million acquisition of Intergas and Enexis' capital expenditures (capex) in 2011, which totaled €445 million (or €358 million net of customer contributions toward the capex).

At the same time, Enexis' debt remained largely unchanged at €1.9 billion as of year-end 2011, compared with year-end 2010. As a result, Enexis' FFO-to-debt ratio exceeded 33% at year-end 2011. Positively, the company repaid a €450 million shareholder loan in January 2012 that was due to expire in September 2012, thereby reducing refinancing risk. The loan was redeemed using the proceeds from a 10-year €300 million bond issued in January 2012.

Liquidity

We assess Enexis's liquidity position as "adequate" as defined in our criteria, supported by our view that Enexis' liquidity sources will exceed its funding needs by more than 1.2x in the next 12 months. At the same time, we consider that the consolidation of the Dutch distribution network sector could incur cash outflows to cover potential acquisitions, and note that Enexis has built up its cash balances for this purpose.

As of March 31, 2012, we estimate that Enexis' liquidity sources over the next 12 months will exceed €1.2 billion under our base-case scenario. These include:

- Unrestricted cash and short-term marketable securities of about €263 million.
- Access to an undrawn €450 million committed credit facility expiring in 2015. We believe that Enexis will maintain substantial headroom under the financial covenants in its credit facility documentation.
- Annual FFO of about €500 million.

We estimate that Enexis' liquidity needs--excluding potential cash outflows linked to the sector consolidation--will exceed €550 million in the 12 months to March 31, 2013, including:

- Working capital of about €20 million.
- Capex of close to €420 million.
- Dividend payments of about €115 million.

Outlook

The positive outlook reflects our view that Enexis will continue to report solid cash flow coverage of debt metrics over the medium term. We believe that an increase in earnings and operating cash flows is likely through 2013, due to pre-approved regulatory tariffs, ongoing cost savings, and the consolidation of Intergas.

We would consider a one-notch upgrade to 'AA-' if we assess that the company's financial risk profile is likely to have strengthened on a sustainable basis, particularly if the company is able to sustain adjusted FFO to debt of about 25%, while maintaining an unchanged business risk profile.

However, we would likely revise the outlook to stable if we believe that the company is likely to recapitalize its balance sheet to be in line with its publicly stated minimum FFO-to-debt ratio requirement of 20%. Such a recapitalization could in our view occur either through further sector consolidation in The Netherlands, an extraordinary dividend distribution, or negative regulatory intervention.

Related Criteria And Research

All articles listed below are available on RatingsDirect on the Global Credit Portal, unless otherwise stated.

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Sept. 28, 2011
- Principles Of Credit Ratings, Feb. 16, 2011
- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria Methodology: Business Risk/Financial Risk Matrix Expanded, May 27, 2009
- 2008 Corporate Criteria: Analytical Methodology, April 15, 2008
- 2008 Corporate Criteria: Ratios And Adjustments, April 15, 2008

Additional Contact:
Infrastructure Finance Ratings Europe; InfrastructureEurope@standardandpoors.com