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Tear Sheet:

Enexis Holding N.V.

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We expect upcoming regulatory decisions on Dutch distribution system operators' (DSOs) remuneration to further improve Enexis' credit metrics. The July 2023 ruling of the Dutch Trade and Industry Appeal Tribunal (the "CBb") concluded favorable changes to the regulatory remuneration parameters for power distribution networks. We believe its implementation would lead to higher revenues for Enexis in the current regulatory period, 2022-2026. We expect to reassess our rating once the Dutch regulator ACM publishes its decision on the tariff settlement of this binding and non-contestable ruling, expected toward the end of the year.

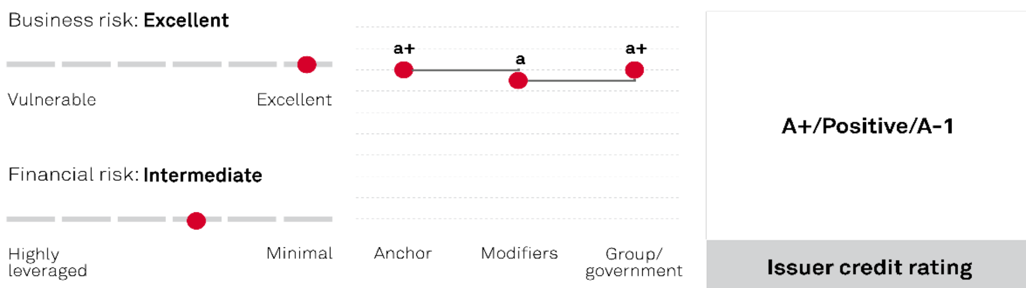
We forecast higher funds from operations (FFO) to debt, averaging 21% over 2023-2025, above our previous estimate of 18%. The CBb instructed ACM to use a more recent reference to determine efficiency costs--2021, rather than 2018-2020. Productivity changes will also be recalculated using 2017-2021 instead of 2004-2020. This will give Enexis extra revenues of about €700 million to be settled before December 2026, with upside in allowed revenues also flowing to the regulatory period starting 2027. We therefore forecast EBITDA to increase above €1.1 billion by the end of our 2023-2025 forecast period, from our previous expectation of €850 million, and FFO to reach about €0.9 billion compared to €700 million previously.

Growing investments to support the energy transition will lead to higher capex, but we think the Fudura disposal should support the spending in the short-term. We expect a sharp increase in investments, to €1.1 billion-€1.5 billion per year over 2023-2025 from €900 million in 2022. About one third of this will be fueled by cost inflation, while the rest comes from risen demand for infrastructure to facilitate the energy transition. Workforce and raw materials shortages could, however, slow its ambitious investment plans. We forecast Enexis will fund its short-term and post-2025 capital spending needs via the €1.3 billion sale proceeds from the disposal of Fudura's noncore energy services in 2022. The extra revenues from the CBb ruling should also support the generation of€600 million-€800 million average yearly operating cash flows over 2023-2025.

The Dutch framework protects Enexis' regulated network activities from spikes in energy costs for grid losses as well as rising interest rates and cost inflation. During 2022-2026, remuneration will cover--with a two-year lag--most of the difference in energy costs, and rising risk-free rates and costs of debt, while inflation effects are partly included in the update to the weighted-average cost of capital (WACC). 2022-2026 initially showed a decline in the nominal pre-tax WACC to 2.78% by year-end 2026 from 2.95% in 2022 for gas and power distribution. This is mitigated by the regulation allowing WACC ex-post adjustments for rising interest rates in cost of equity and cost of debt, with a lag of two years (so in 2024 WACC will be adjusted for rising yields in 2022). The revised nominal pre-tax WACC assumption should rise to 4.8% in 2026 from 2.9% in 2022. The regulatory WACC for electricity is calculated as real WACC plus 50% of inflation expectations, while the nominal WACC for gas includes a 12% higher inflation rate in 2023.

We view Enexis' financial policy and risk management as supportive. Enexis maintains a publicly stated financial policy of keeping an 'A' level rating. It has a very solid track record of prioritizing the reinforcement of its balance sheet over distributing dividends to shareholders. Though we view Dutch state support of maintaining a minimum 'A-' rating for Dutch DSOs as positive, we do not believe Enexis will call for state support in the medium term. We expect management would put in place sufficient credit remedy measures to postpone as much as possible any future need for state intervention.

Ratings Score Snapshot



Recent Research

- Update: Enexis Holding N.V., Jan. 3, 2023
- Dutch Energy Network Enexis Outlook Revised To Stable On Fudura Sale, Expected State Support; Affirmed At 'A+/A-1', Aug. 9, 2022
- Dutch Networks Stedin, Alliander And Enexis Ratings Affirmed On Government Support; Enexis Outlook Revised To Positive, Feb. 14, 2023
- Utilities Handbook 2023: Western Europe Regulated Power, Oct. 18, 2023
- Industry Top Trends Update Europe: Utilities, July 18, 2023

Company Description

Enexis engages in the installation, maintenance, operation, and development of distribution grids for electricity and gas in the Netherlands. Through its main subsidiary, Enexis Netbeheer B.V., the company's electricity grid covers 144,200 kilometers (km) with 2.9 million connection points (cps), while its gas grid covers 46,200 km with 2.3 million cps, making it the second largest Dutch DSO after Alliander (as of year-end 2022).

Through its network, the company provides electricity and gas in the Dutch provinces of Groningen, Drenthe, Overijssel, Noord-Brabant, and Limburg. After the Fudura sale, less than 5% of Enexis' revenue is derived from other utility services. These nonregulated businesses are complementary to the core activities. Enexis is owned by the Provinces of Noord-Brabant (30.8%), Overijssel (19.7%), Limburg (16.1%), and Groningen and Drenthe (9%), and the rest is owned by 86 smaller municipalities.

Outlook

The positive outlook on Enexis reflects our expectation that the company will be able to maintain average FFO to debt well above 18% over the current regulatory period, after spiking at about 32% in 2022 due to the exceptional cash-in from the Fudura sale. Although Enexis has incremental debt needs due to the intensive capex program under the Dutch government's energy transition plan, we expect it will maintain significant financial headroom above the 18% threshold for the current rating. We expect that the effects of higher energy costs will be manageable for Enexis in the long term, thanks to hedging in place and cost recovery throughout the regulatory framework.

We do not foresee Enexis calling for state support in the medium term, though we view as positive the framework agreement whereby the state commits to ultimately support DSOs' capital adequacy at a minimum 'A-' or equivalent rating level.

Downside scenario

We would revise the outlook on Enexis to stable if we assessed that its FFO to debt was likely to decline and remain below 18%. This could stem from a higher-than-expected increase in debt and shareholder distributions or a decrease in operating margins resulting from worse-than-expected price volatility or adverse regulatory decisions like a lack of compensation for energy purchase costs to cover grids losses in 2024.

A one-notch downward revision of the SACP, although unlikely, would lead us to lower the issuer credit rating by one notch, barring any change in our view of extraordinary government support. In contrast, a one-notch downgrade of the Netherlands would not result in a downgrade of Enexis, all things remaining equal.

Upside scenario

We could raise the rating if we thought Enexis could sustain adjusted FFO to debt comfortably above 23% with no deterioration in business risk.

Key Metrics

Enexis Holding N.V.--Forecast summary

Period ending	Dec-31-2021	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025
(Mil. EUR)	2021a	2022a	2023e	2024f	2025f
EBITDA	732	712	550-650	800-900	1,100-1,200
Net capital expenditure (capex)	763	775	900-1,00	1,250-1,350	1,350-,1,450
Free operating cash flow (FOCF)	(149)	(223)	(600)-(400)	(700)-(500)	(600)-(400)
Dividends	80	105	150-250	0-100	0-100
Discretionary cash flow (DCF)	(229)	(328)	(800)-(600)	(800)-(600)	(700)-(500)
Debt	3,037	1,965	2,600-2,800	3,300-3,500	3,900-4,100
Debt/EBITDA (x)	4.1	2.8	4.5-5.0	4.3-3.8	3.2-3.7
FFO/debt (%)	20.7	31.4	18-22	19-23	22-26

Financial Summary

Enexis Holding N.V.--Financial Summary

Period ending	Dec-31-2017	Dec-31-2018	Dec-31-2019	Dec-31-2020	Dec-31-2021	Dec-31-2022
Reporting period	2017a	2018a	2019a	2020a	2021a	2022a
Display currency (mil.)	EUR	EUR	EUR	EUR	EUR	EUR
Revenues	1,380	1,445	1,491	1,516	1,634	1,705
EBITDA	699	760	710	622	732	712
Funds from operations (FFO)	576	621	600	545	630	618
Interest expense	67	66	58	45	42	31
Cash interest paid	63	66	60	39	37	39
Operating cash flow (OCF)	583	616	539	610	614	552
Capital expenditure	514	558	638	738	763	775
Free operating cash flow (FOCF)	69	58	(99)	(127)	(149)	(223)
Discretionary cash flow (DCF)	(35)	(45)	(221)	(233)	(229)	(328)
Cash and short-term investments	286	31	62	47	107	867
Gross available cash	286	31	62	47	107	867
Debt	2,303	2,344	2,640	2,684	3,037	1,965
Common equity	3,808	4,024	4,112	4,366	4,491	5,691
Adjusted ratios						
EBITDA margin (%)	50.7	52.6	47.6	41.0	44.8	41.8
Return on capital (%)	5.7	6.6	5.4	3.6	4.4	3.7
EBITDA interest coverage (x)	10.4	11.5	12.3	13.9	17.3	22.7
FFO cash interest coverage (x)	10.1	10.4	11.1	15.1	17.9	16.7
Debt/EBITDA (x)	3.3	3.1	3.7	4.3	4.1	2.8
FFO/debt (%)	25.0	26.5	22.7	20.3	20.7	31.4
OCF/debt (%)	25.3	26.3	20.4	22.7	20.2	28.1
FOCF/debt (%)	3.0	2.5	(3.8)	(4.7)	(4.9)	(11.3)
DCF/debt (%)	(1.5)	(1.9)	(8.4)	(8.7)	(7.5)	(16.7)

Peer Comparison

Enexis Holding N.V.--Peer Comparisons

	Enexis Holding N.V.	Alliander N.V.	Stedin Holding N.V.	TenneT Holding B.V.	N.V. Nederlandse Gasunie
Foreign currency issuer credit rating	A+/Positive/A-1	A+/Watch Pos/A-1	A-/Stable/A-2	A-/Stable/A-2	AA-/Stable/A-1+

Enexis Holding N.V.--Peer Comparisons

Local currency issuer credit rating	A+/Positive/A-1	A+/Watch Pos/A-1	A-/Stable/A-2	A-/Stable/A-2	AA-/Stable/A-1+
Period	Annual	Annual	Annual	Annual	Annual
Period ending	2022-12-31	2022-12-31	2022-12-31	2022-12-31	2022-12-31
Mil.	EUR	EUR	EUR	EUR	EUR
Revenue	1,705	2,150	1,333	8,286	2,354
EBITDA	712	773	437	254	1,345
Funds from operations (FFO)	618	653	372	(224)	1,114
Interest	31	49	52	329	70
Cash interest paid	39	60	49	247	95
Operating cash flow (OCF)	552	562	276	999	1,406
Capital expenditure	775	1,229	700	4,412	417
Free operating cash flow (FOCF)	(223)	(667)	(425)	(3,414)	989
Discretionary cash flow (DCF)	(328)	(766)	(432)	(3,603)	771
Cash and short-term investments	867	204	53	1,282	472
Gross available cash	867	204	53	1,282	472
Debt	1,965	3,314	3,678	21,297	3,597
Equity	5,691	4,622	3,092	6,631	6,304
EBITDA margin (%)	41.8	36.0	32.8	3.1	57.2
Return on capital (%)	3.7	4.2	1.5	(3.7)	9.6
EBITDA interest coverage (x)	22.7	15.9	8.4	0.8	19.1
FFO cash interest coverage (x)	16.7	11.8	8.7	0.1	12.7
Debt/EBITDA (x)	2.8	4.3	8.4	83.8	2.7
FFO/debt (%)	31.4	19.7	10.1	(1.0)	31.0
OCF/debt (%)	28.1	17.0	7.5	4.7	39.1
FOCF/debt (%)	(11.3)	(20.1)	(11.5)	(16.0)	27.5
DCF/debt (%)	(16.7)	(23.1)	(11.7)	(16.9)	21.4

Environmental, Social, And Governance

ESG factors have an overall neutral influence on our credit rating analysis of Enexis. The company is one of the most relevant stakeholders for the Dutch government to deliver on its energy transition objectives. Its pivotal role entails collaborating with Dutch local governments, industries, and communities to integrate new renewable capacity into its grid while managing congestion. We believe this will stimulate Enexis' electricity grid deployment by expanding its regulatory asset base over the next decade. In our opinion, the critical role of its electricity infrastructure more than compensates for the more uncertain long-term prospects of its gas grid, as the country strives to phase out gas by 2050 and embrace renewable gases.

Given the sharp rise in power and gas prices, political scrutiny on affordability remains high in Europe. Although we consider that there could be negative government intervention in the sector, we believe any potential negative impact is amply covered by a supportive regulatory framework.

Rating Component Scores

Foreign currency issuer credit rating	A+/Positive/A-1
Local currency issuer credit rating	A+/Positive/A-1
Business risk	Excellent
Country risk	Very Low
Industry risk	Very Low
Competitive position	Excellent
Financial risk	Intermediate
Cash flow/leverage	Intermediate
Anchor	a+
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Satisfactory (no impact)
Comparable rating analysis	Negative (-1 notch)
Stand-alone credit profile	a

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012

- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010