Credit Rating Announcement

14 October 2022

Scope affirms its A-/Stable issuer rating on Tensio AS

Stable operating performance achieved, and on course to meet targeted leverage multiple of 5x by year end.

The latest information on the rating, including rating reports and related methodologies, is available on this LINK.

Rating action

Scope Ratings GmbH (Scope) has affirmed its A-/Stable issuer rating on Norwegian utility company Tensio AS.

Rating rationale

The affirmation of the issuer rating reflects Tensio's continued strong business risk profile, despite the expectation of a higher leverage this year. The latter is in line with Scope expectations, and admittedly also in line with management's established financial policy and leverage target. With YE2021 leverage (Scope-adjusted Debt/EBITDA) ending at 3.8x, Scope anticipates the ratio will be close to 5x at year-end 2022, following another recapitalisation transaction this year (NOK 250m pay-out). The special dividend relates back to the establishment of Tensio, when combining the two grid companies was done without transferring much debt from the two owners. With the company's leverage target of 5x reaching this year, Scope's expectations are that the company will operate around this leverage in the medium term and start with ordinary dividends ahead.

Tensio's strong business risk profile is underpinned by the utility's undiluted exposure to regulated power distribution, which is associated with minimal industry risk. Given this monopolistic position, the company's lack of product and geographical diversification is not important for Scope's rating assessment. Operational efficiency is expected to improve, and remains an important rating factor. However, the overall group profitability expectations are mixed due to expectations of reduced regulated surplus income over the next few years. Successful implementation of a cost-cutting programme, including a reduction in the number of employees, is partially offsetting the decline in regulated surplus income.

Tensio's policy to distribute excess capital to its owners to reach its targeted financial leverage ratio of 5x is central to the financial risk assessment by Scope. Now, with the increased leverage, higher interest expenses and continued pressure on the company's FOCF, the company will move into a new phase from 2023 where it will need to focus on retaining its leverage ratio instead of increasing it. Tensio's high investment requirements result in negative free operating cash flow in the medium term. In the longer term, the company might increase capital expenditure even more to meet rising electricity demand in the region (strategic planning ongoing), but its financial leverage target remains firm.

Liquidity remains adequate, with the first debt maturity refinancing needs in Q3 2023. Scope projects some new funding needs as well, due to the negative discretionary cash flow, which should be manageable.

As regards supplementary rating drivers, Tensio's financial policy leads to no adjustment as it is already incorporated in Scope's financial risk profile assessment. Parent support continues to warrant a one-notch uplift on Tensio's standalone rating, based on the application of the agency's Government Related Entity (GRE) rating methodology, using a bottom-up approach. Scope's assessment of indirect majority municipal ownership of Tensio is based on potential parent support, determined not by the standalone performance or credit quality of TrønderEnergi and NTE, but by the capacity and willingness of their municipal owners to provide support if needed.

Outlook and rating-change drivers

The Stable Outlook reflects Scope's expectation that Tensio will continue to generate stable cash flow from monopolistic and regulated grid operations. The Outlook also assumes that the company will operate in line with its financial policy, which should result in leverage, of SaD/EBITDA around 5x. Scope also assumes that the company will remain indirectly majority-owned by Norwegian municipalities.

A positive rating action could be warranted if Tensio keeps the SaD/EBITDA multiple around 4x on a sustained basis and signalling its intention to have significant headroom to its leverage target, by generating positive free operating cash flow and reduced dividend distributions.

A negative rating action could be triggered by a financial policy change that significantly weakened Tensio's financial risk profile, with SaD/EBITDA moving towards 6x (or higher) on a sustained basis. A reduction in indirect municipal ownership to below 50% and the loss of GRE status could also trigger a downgrade.

Stress testing & cash flow analysis

No stress testing was performed. Scope Ratings performed its standard cash flow forecasting for the company.

Methodology

The methodologies used for this Credit Rating and/or Outlook, (General Corporate Rating Methodology, 15 July 2022; Government Related Entities Rating Methodology, 6 May 2022; European Utilities Rating Methodology, 17 March 2022), are available on https://scoperatings.com/governance-and-policies/rating-governance/methodologies.
Information on the meaning of each Credit Rating category, including definitions of default, recoveries, Outlooks and Under Review, can be viewed in 'Rating Definitions – Credit Ratings, Ancillary and Other Services', published on https://www.scoperatings.com/governance-and-policies/rating-governance/definitions-and-scales. Historical default rates of the entities rated by Scope Ratings can be viewed in the Credit Rating performance report at https://scoperatings.com/governance-and-policies/regulatory/eu-regulation. Also refer to the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope Ratings' definitions of default and Credit Rating notations can be found at https://www.scoperatings.com/governance-and-policies/rating-governance/definitions-and-scales. Guidance and information on how environmental, social or governance factors (ESG factors) are incorporated into the Credit Rating can be found in the respective sections of the methodologies or guidance documents provided on https://scoperatings.com/governance-and-policies/rating-governance/methodologies.
The Outlook indicates the most likely direction of the Credit Rating if the Credit Rating were to change within the next 12 to 18 months.

Solicitation, key sources and quality of information

The Rated Entity and/or its Related Third Parties participated in the Credit Rating process.
The following substantially material sources of information were used to prepare the Credit Rating: public domain, the Rated Entity and Scope Ratings' internal sources.
Scope Ratings considers the quality of information available to Scope Ratings on the Rated Entity or instrument to be satisfactory. The information and data supporting the Credit Rating originate from sources Scope Ratings considers to be reliable and accurate. Scope Ratings does not, however, independently verify the reliability and accuracy of the information and data.
Prior to the issuance of the Credit Rating action, the Rated Entity was given the opportunity to review the Credit Rating and/or Outlook and the principal grounds on which the Credit Rating and/or Outlook are based. Following that review, the Credit Rating was not amended before being issued.

Regulatory disclosures

This Credit Rating and/or Outlook is issued by Scope Ratings GmbH, Lennéstraße 5, D-10785 Berlin, Tel +49 30 27891-0. The Credit Rating and/or Outlook is UK-endorsed.

Lead analyst: Henrik Blymke, Managing Director

Person responsible for approval of the Credit Rating: Sebastian Zank, Managing Director

The Credit Rating/Outlook was first released by Scope Ratings on 25 November 2020. The Credit Rating/Outlook was last updated on 30 November 2021.

Potential conflicts

See www.scoperatings.com under Governance & Policies/EU Regulation/Disclosures for a list of potential conflicts of interest related to the issuance of Credit Ratings.

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With more than 250 employees operating from offices in Berlin, Frankfurt, Hamburg, London, Madrid, Milan, Oslo and Paris, Scope Group is the leading European provider of independent credit ratings, ESG and fund analysis. Based on forward-looking and innovative methodologies, Scope offers a European perspective that contributes to greater diversity of opinion for institutional investors worldwide. **Scope Ratings** is the largest European credit rating agency, registered in accordance with EU and UK rating agency regulation, offering opinion-driven and non-mechanistic credit risk analysis. **Scope ESG Analysis** provides tools for analysing and reporting on ESG impact and risk, as well as second-party opinions on green, social and sustainable bonds. **Scope Fund Analysis** rates more than 10,000 funds and asset managers across all major asset classes. The shareholders of Scope Group include CEO and founder Florian Schoeller and anchor shareholder Stefan Quandt, numerous senior personalities in European finance and industry as well as institutional investors from several European countries. More on www.scopegroup.com

Contact

Analyst	Henrik Blymke	h.blymke@scoperatings.com
Team leader	Olaf Tölke	o.toelke@scoperatings.com

Scope Ratings GmbH • Lennéstraße 5 • D-10785 Berlin • Phone: +49 30 27891-0 • Fax: +49 30 27891-0
www.scoperatings.com