MOODY'S
INVESTORS SERVICE

CREDIT OPINION
12 April 2017

Update

Rate this Research

RATINGS

Alliander N.V.

Domicile	Netherlands
Long Term Rating	Aa2
Type	LT Issuer Rating
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Analyst Contacts

Stefanie Voelz 44-20-7772-5555
Senior Credit Officer
stefanie.voelz@moodys.com

Velina Karadzhova 44-20-7772-5478
Analyst
velina.karadzhova@moodys.com

Adeline Poireau 44-20-7772-8704
Associate Analyst
adeline.poireau@moodys.com

Neil Griffiths-Lambeth 44-20-7772-5543
Associate Managing Director
neil.griffiths-lambeth@moodys.com

Alliander N.V.

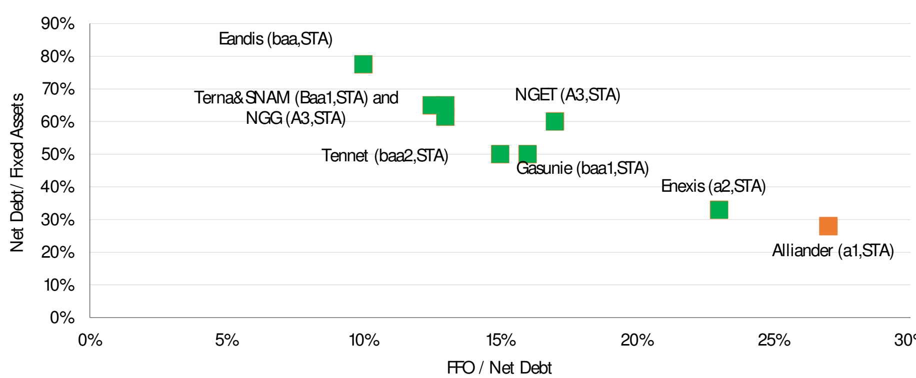
Update following rating affirmation

Summary Rating Rationale

The Aa2 long-term issuer rating of Alliander N.V. (Alliander) is underpinned by a combination of (1) the low-risk business profile of Alliander's domestic electricity and gas distribution network operations; (2) the well-defined and transparent Dutch regulatory framework; and (3) the company's balanced financial profile, with relatively modest leverage for the sector and solid liquidity position.

Despite decreasing allowed returns in the current regulatory period to 2021, we expect Alliander to maintain a strong financial profile over the medium term, supported by (1) a moderate distribution policy; (2) a €359 million compensation payment received from Enexis Holding N.V. (Enexis, Aa3 stable) under an asset swap agreement; and (3) manageable investment requirements.

Exhibit 1
Modest leverage compared to European peers supports strong stand-alone credit quality



Note 1: Financial metrics used represent middle point of Moody's forward view estimates as published in latest credit opinions and ratings shown represent stand-alone credit quality (expressed as assigned final rating or baseline credit assessment where applicable); Note 2: NGET - National Grid Electricity Transmission plc and NGG - National Grid Gas plc
Source: Moody's forward view

The Aa2 rating also incorporates a two-notch rating uplift reflecting the potential extraordinary support from Alliander's owners, the largest of which is the Province of Gelderland with a 45% shareholding, if such were ever needed.

The report was republished on 18 April 2017 to correct the source quoted in Exhibit 4.

Credit Strengths

» Low business risk profile supported by predictable cash flows due to predominantly regulated activities

» Stable and transparent regulatory regime

» Moderate investment requirements and balanced distribution policy underpin strong financial profile going forward

» Two notches of rating uplift reflecting potential support from local government shareholders

Credit Challenges

» Falling regulatory returns in the current low interest-rate environment reduce financial flexibility

Rating Outlook

The stable outlook for Alliander reflects our expectation that the company will maintain focus on its regulated business and continue to follow its balanced financial policy, thus, allowing it to maintain a financial profile in line with the guidance for the current rating.

Factors that Could Lead to an Upgrade

Funds from operations (FFO)/net debt comfortably above the mid-thirties and retained cash flow (RCF) permanently in the high-twenties in percentage terms may put upward pressure on the ratings, provided that such metrics are combined with a still conservative approach to the business, with continuing focus on the core regulated activities, and a prudent financial and dividend policy.

Factors that Could Lead to a Downgrade

The rating could be considered for downgrade if Alliander failed to maintain the following minimum credit metrics: funds from operations (FFO)/net debt above 25% on a sustainable basis and net debt/fixed assets below the low forties in percentage terms. Downward rating pressure could also arise if the potential support from Alliander's local government shareholders were to be seen less likely to be obtained or if their credit strength were to weaken.

Key Indicators

Exhibit 2
Alliander exhibits strong financial metrics

	12/31/2016	12/31/2015	12/31/2014	12/31/2013	12/31/2012
FFO Interest Coverage	8.4x	7.7x	7.5x	7.6x	6.3x
Net Debt / Fixed Assets	27.9%	29.2%	28.1%	33.7%	35.8%
FFO / Net Debt	25.1%	26.3%	31.9%	30.7%	28.3%
RCF / Net Debt	20.1%	19.4%	24.4%	26.6%	22.5%

Note: All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Source: Moody's Financial Metrics TM

Detailed Rating Considerations

Low business risk profile supported by predictable cash flows from predominantly regulated activities

Regulated activities (i.e., the operation of energy distribution networks) contribute around 85-90% of Alliander's revenues, providing relatively stable and predictable cash flows under a transparent regulatory regime, and medium term visibility over investment requirements.

Alliander's unregulated activities represent less than 15% of revenues and comprise network service, maintenance and operations for regulated monopolies (through Liandon) and are strongly linked to Alliander's core business.

Stable and transparent regulatory regime but allowed returns continue to decline

The Dutch framework applied since 2000 and 2001 for electricity and gas networks, respectively, allows the country's distribution companies to earn a return on their regulated asset base (RAB), adjusted for consumer price index (CPI) inflation. The regulation incorporates incentives based on a "yardstick" mechanism, which defines the efficiency and quality factors based on industry averages and encourages network companies to improve profitability by outperforming the sector. This approach is typical of peer regulatory regimes in Europe and we consider that the application by the Dutch regulator, the Authority for Consumers and Markets (ACM), has been transparent and consistent to date.

The current price control period for both electricity and gas runs from January 2017 to December 2021. In September 2016, ACM published its final determination for the period and this includes a further gradual reduction in the allowed return to 3.0% (pre-tax, real) by 2021 from 4.0% at the start of the current regulatory period in 2017 (see also Moody's sector-in-depth comment on the draft regulatory proposal 'Dutch Regulated Energy Networks: Lower allowed return poses fresh challenge', published in May 2016).

Exhibit 3

Allowed return for Dutch network operators shows declining trend

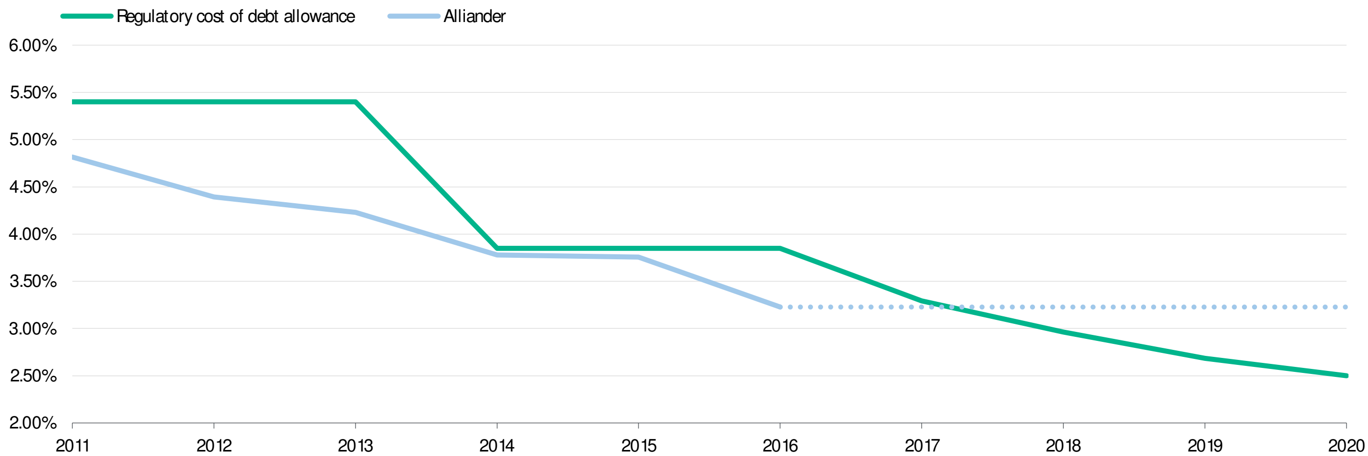
WACC - Dutch DSOs	2008-2010	2011-2013	2014-2016	2017	2018	2019	2020	2021
risk free rate	4.00%	3.95%	2.50%	2.20%	1.90%	1.67%	1.50%	1.33%
risk premium	0.80%	1.50%	1.20%	0.95%	0.91%	0.87%	0.86%	0.81%
transaction costs	0.00%	0.00%	0.15%	0.15%	0.15%	0.15%	0.15%	0.15%
Nominal Cost of Debt	**4.80%**	**5.45%**	**3.85%**	**3.29%**	**2.96%**	**2.68%**	**2.50%**	**2.29%**
nominal risk free rate for CoE	4.00%	3.95%	2.50%	1.28%	1.28%	1.28%	1.28%	1.28%
market risk premium	5.00%	5.00%	5.00%	5.05%	5.05%	5.05%	5.05%	5.05%
asset beta	0.41	0.42	0.35	0.42	0.42	0.42	0.42	0.42
equity beta	0.86	0.81	0.61	0.74	0.74	0.74	0.74	0.74
Nominal Cost of Equity	**8.30%**	**8.00%**	**5.55%**	**5.02%**	**5.02%**	**5.02%**	**5.02%**	**5.02%**
gearing assumption	60%	55%	50%	50%	50%	50%	50%	50%
tax rate	25.5%	25.5%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
Nominal WACC pre-tax	**7.3%**	**7.8%**	**5.6%**	**5.0%**	**4.8%**	**4.7%**	**4.6%**	**4.5%**
inflation	1.75%	1.55%	2.00%	0.90%	1.03%	1.16%	1.29%	1.42%
Real WACC pre-tax	**5.5%**	**6.2%**	**3.6%**	**4.1%**	**3.8%**	**3.5%**	**3.3%**	**3.0%**

Source: ACM, Moody's calculations

The reduction in allowed returns is less material than in the previous regulatory period where it fell from 6.2% to 3.6% (both pre-tax, real) in gradual steps over 2014-16. Alliander has demonstrated its ability to fund comfortably around the cost of debt embedded in the return allowance, and benefits from recent issuance at favourable terms, such as the €300 million 0.875% 10-year notes in April 2016.

Reflecting the 2016 issuance and taking into account the company's hybrid, Alliander's average cost of debt is just over 3.0% (nominal), broadly in line with the regulatory cost of debt assumptions into 2018. Further decline could be possible depending on rates obtained for funding Alliander's increased investments and the re-financing of the debt maturity in 2019.

Exhibit 4
Regulatory allowance for cost of debt 2017-2021 and Alliander's average cost of debt (Moody's estimate)



Note: Moody's estimates exclude Alliander's refinancing needs in 2019 and ongoing investment needs
Source: ACM, Alliander annual reports and Moody's estimate

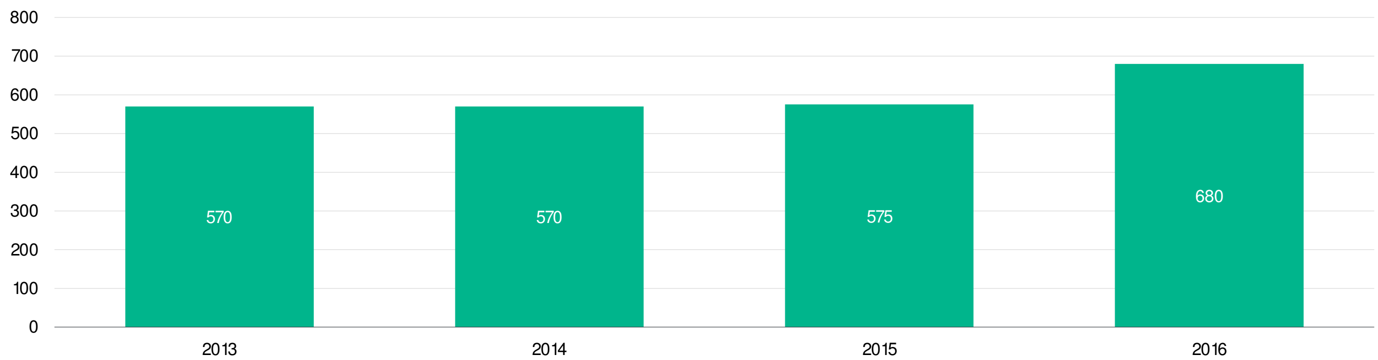
The regulator also imposes a series of cost efficiency targets on the networks, which combined with the allowed return determine the so-called `X-factor', currently set at 1.90% for electricity and 1.42% for gas annually for Alliander (previously around 4% and 7% respectively). This results in an incremental decline in the element of revenue funding of operating costs. While base costs are reset on the basis of average costs in the period 2013-2015, resulting in an increase in the overall revenue allowance for 2017-21, and the X-factor also incorporates the decrease in the allowed returns, operating efficiency targets may still prove challenging.

Limited investment requirements and conservative financial policy support strong financial profile

The technical operating performance of the Dutch networks is excellent when compared to other European peers, demonstrated by the networks' high reliability and lower unplanned interruptions time. The generally good condition of the Dutch energy network assets reduces necessary maintenance requirements. Total capital expenditure was stable around €500-600 million (gross of customer contributions) in the past, but we expect an increase over the next five years with the smart meter roll-out that started in 2015. This is the biggest single investment project for Alliander and will see total annual capex closer to €750-800 million (gross of contributions). Investment needs to accommodate decentralised energy generation as well as integration of renewable generation are somewhat mitigated by ongoing technology updates to the existing network.

Exhibit 5

Increasing, but manageable investments due to smart meter roll-out



Source: Alliander Annual Reports

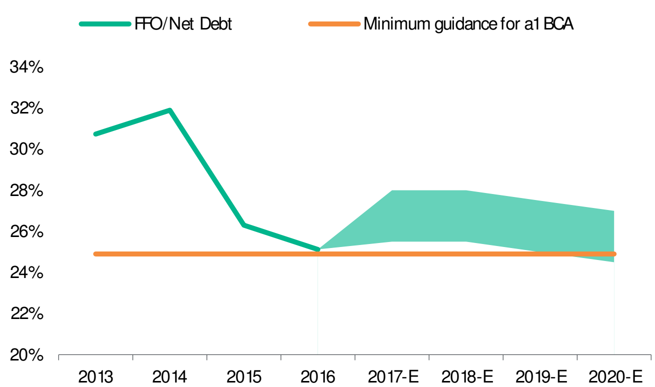
The modest investment requirements, particularly when compared with transmission network operators, underpin our expectation of a continuously strong financial profile. In addition, management maintains a conservative dividend policy, with distributions around 45% of net income.

Over the next five years, we expect Alliander to continue to exhibit strong financial metrics, although operational cash flows will decline due to the reduction in allowed returns and the composition of the asset swap with Enexis. We forecast Alliander to maintain FFO/net debt above 25%, and RCF/net debt in excess of 20% over the medium term, creating a slightly stronger stand-alone financial profile than exhibited by its peer Enexis, recognised in a one-notch higher rating.

Exhibit 6

Moody's forecast declining cash flows due to lower returns...

FFO/Net Debt against guidance



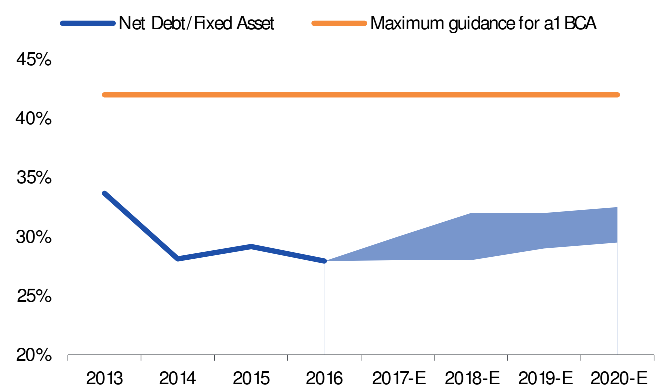
Note: [1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations; [2] As of 12/31/2016; [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.

Source: Moody's Financial Metrics TM,

Exhibit 7

... but also lower gearing due to asset swap compensation payment

Net Debt/Fixed Assets against guidance



Asset swap with Enexis resulted in deleveraging during 2016, but one-off effect

On 1 January 2016, Alliander and Enexis concluded an asset sale and purchase agreement to swap certain assets within their areas. The transaction saw Enexis transfer its networks in the Friesland province and the Noordoostpolder area, in exchange for Alliander's network in the Eindhoven and southeast Brabant region (operated by Endinet). This is part of the Dutch government's wider policy to arrange network operations along provincial borders.

Alliander's Endinet business serves a larger number of customers (108,000 electricity and 398,000 gas connections) than the Enexis assets to be transferred (combined 79,000 electricity and 223,000 gas connections). Therefore, Enexis made a €359 million compensation payment to Alliander for the larger revenue generation capability of the latter's assets to be transferred. While, as a consequence, Enexis's financial metrics weakened marginally, Alliander's leverage metrics improved, albeit recognising lower operational cash flows going forward.

Liquidity Analysis

Alliander continues to maintain a strong liquidity position, supported by large committed liquidity facilities and solid cash flow generation, although we expect operating cash flows to decline over the current regulatory period. As at 31 December 2016, the company had €48 million of cash (plus €15 million of short-term deposits) and a €600 million revolving credit facility - fully undrawn and available until July 2021. In addition, Alliander is an active issuer of commercial papers (CP) under its established €1.5 billion ECP programme.

The next significant bond maturity is €300 million due in 2019. Liquidity in place is sufficient to cover in excess of 12 months' scheduled cash requirements.

Alliander has exposure to contingent liabilities represented by three cross-border leasing (CBL) arrangements. In the case of an unscheduled early termination of all of these CBLs at the same time this could give rise to a total exposure (maximum strip risk) of US $194 million as of 31 December 2016. According to the conditions of some of the CBLs, the company would need to post additional letters of credit if its ratings were to drop below certain minimum levels. We note that the company can access its €600 million revolving credit facility to cover potential financing needs stemming from the CBLs.

Profile

Alliander N.V. owns and manages low and medium voltage electricity and gas distribution networks in the Dutch provinces of Gelderland, Noord-Holland, Flevoland and large parts of, Friesland and Zuid-Holland. The company is the largest electricity and gas network operator in the Netherlands with approximately 3.1 million electricity and 2.5 million gas connections and it has a combined market share of 35% in the Netherlands.

The company is fully owned by Dutch provinces and municipalities, with the largest owners being the provinces of Gelderland (45%), Friesland (13%), Noord-Holland (9%), and the City of Amsterdam (9%). The remaining 24% share is owned by 52 small municipalities where Alliander provides its network services.

Rating Methodology and Scorecard Factors

The principal methodology used in assessing Alliander's stand-alone credit quality, i.e. prior to incorporating the benefit of its ownership structure, is Moody's rating methodology for regulated electric and gas networks, published in March 2017.

The indicated rating from the regulated networks methodology grid is Aa3, one notch higher than the assigned a1 baseline credit assessment (BCA), representing the company's stand-alone credit quality. Over the next 12-18 months, we expect Alliander to exhibit a financial profile broadly in line with historical metrics.

Exhibit 8

Alliander N.V. - Rating Grid

Regulated Electric and Gas Networks Industry Grid [1][2]	Current FY 12/31/2016		Moody's 12-18 Month Forward View as of April 2017 [3]	
Factor 1 : Regulatory Environment and Asset Ownership Model (40%)	Measure	Score	Measure	Score
a) Stability and Predictability of Regulatory Regime		Aa		Aa
b) Asset Ownership Model		Aa		Aa
c) Cost and Investment Recovery (Ability and Timeliness)		A		A
d) Revenue Risk		Aa		Aa
Factor 2 : Scale and Complexity of Capital Program (10%)				
a) Scale and Complexity of Capital Program		Baa		Baa
Factor 3 : Financial Policy (10%)				
a) Financial Policy		A		A
Factor 4 : Leverage and Coverage (40%)				
a) FFO Interest Coverage (3 Year Avg)	7.8x	Aaa	7x - 10x	Aaa
b) Net Debt / Fixed Assets (3 Year Avg)	28.4%	Aaa	28% - 30%	Aaa
c) FFO / Net Debt (3 Year Avg)	27.7%	Aa	25% - 29%	Aa
d) RCF / Net Debt (3 Year Avg)	21.2%	Aa	18% - 22%	A
Rating:				
Indicated Rating from Grid Factors 1-4		Aa3		Aa3
Rating Lift		0		0
a) Indicated Rating from Grid		Aa3		Aa3
b) Actual BCA Assigned				a1
Government-Related Issuer				**Factor**
a) Baseline Credit Assessment				a1
b) Government Local Currency Rating				n/a
c) Default Dependence				Very High
d) Support				Strong
e) Final Rating Outcome				Aa2

Note: [1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations; [2] As of 12/31/2016; [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.

Source: Moody's Financial Metrics TM

Given its 100% ownership by Dutch provinces and municipalities, Alliander falls within the scope of our rating methodology for government-related issuers (GRIs), published in October 2014.

Alliander's Aa2 rating incorporates a two-notch uplift from its stand-alone credit quality, expressed as a BCA of a1, reflecting a strong probability of extraordinary financial support being provided by its owners, if ever required, the largest of which is the Province of Gelderland with around 45% holding. Although ownership of Alliander is relatively fragmented among 56 provinces and municipalities, our assumption of strong support reflects (1) the importance of Alliander's network operations for the regional economy; (2) the fact the four largest provinces together hold 76% of the company's shares; and (3) the strong governance framework in the Netherlands with oversight by the national government.

Our assessment of very high default dependence reflects Alliander's significant exposure to the Dutch economy, as almost all of the company's revenues and cash flows are generated from domestic activities.

Ratings

Exhibit 9

Category	Moody's Rating
ALLIANDER N.V.	
Outlook	Stable
Issuer Rating	Aa2
Senior Unsecured -Dom Curr	Aa2
Jr Subordinate -Dom Curr	A2
ST Issuer Rating	P-1
ALLIANDER FINANCE B.V.	
Outlook	Stable
Bkd Senior Unsecured -Dom Curr	Aa2

Source: Moody's Investors Service

REPORT NUMBER 1064612

MOODY'S INVESTORS SERVICE