

Research Update:

Alliander 'A/A-1' Ratings Affirmed On Plan To Acquire Grid Operator Endinet; Outlook Stable

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Overview

- Dutch electricity and gas network company Alliander N.V. has signed a non-binding agreement to acquire Dutch grid operator Endinet B.V.
- We are affirming our 'A/A-1' ratings and outlook on Alliander.
- The stable outlook reflects our expectations that Alliander will accommodate the proposed acquisition within its current financial profile.

Rating Action

On Dec. 16, 2009, Standard & Poor's Ratings Services affirmed its 'A/A-1' ratings on Dutch electricity and gas network company Alliander N.V. The outlook is stable.

At the same time, we affirmed our debt ratings on related entity Alliander Finance B.V.

Rationale

On Dec. 11, Alliander signed a non-binding agreement to acquire Netherlands-based grid operator Endinet B.V. (not rated), a Dutch network company operating three separate electricity and gas networks in The Netherlands. The cash offer requires approval from both companies' shareholders and the Dutch Ministry of Economic Affairs. Furthermore, the final terms of the transaction will be subject to a due diligence process expected to be conducted in early 2010.

On the basis of currently available information, we expect the proposed acquisition to be moderately positive for Alliander's business risk profile, which we assess as "excellent". The proposed acquisition of Endinet by much-larger Alliander would offer operating and investment synergies as two of Endinet's networks are located within or near by Alliander's current service areas.

We view the proposed acquisition as marginally dilutive to Alliander's financial risk profile, which we currently assess as "intermediate". We expect Alliander to finance the proposed acquisition by using a large part of its existing on-balance sheet cash. Due to timing effects in the consolidation of Endinet (expected as of mid-2010) and an increase in operating expenditures, we expect Alliander to post funds from operations to debt below 20% in 2010. Over the two following years, however, this ratio should again reach above 20%, which is in line with our expectations for the current 'A' rating.

The ratings on Alliander continue to reflect the credit quality of its regulated electricity and gas distribution network business, including its stable and predictable operating cash flow, its high quality network assets, and adequate operating performance. The ratings are constrained by an expected near- to medium-term increase in capital spending, a significant part of which may not be fully recovered through tariffs; exposure to incentive-based regulation; and counterparty and liquidity risks related to remaining cross-border lease agreements on the company's network assets.

Short-term credit factors

The short term rating is 'A-1'. As at June 30, 2009, Alliander reported adequate liquidity with available cash and equivalents of €337 million. In addition, Alliander had access to an undrawn €875 million committed credit facility, maturing in November 2011, with significant covenant headroom as of June 30, 2009. This compares with €130 million in maturing short-term debt at the same date. Alliander's liquidity position has strengthened since, following the sale of the company's high-voltage grid to Dutch electricity transmission operator TenneT (not rated), rendering cash receipts of €368 million. On a stand-alone basis, Alliander is expected to post positive free operating cash flow in 2010. However, the level will ultimately depend on development in discretionary capital spending related to investments in smart metering.

We expect Alliander to finance the proposed acquisition by using existing on-balance sheet cash without the need to draw on its €875 million credit facility, which mainly serves as a back-up to the company's €1.5 billion euro commercial paper program (unused as of Nov. 30, 2009). Upon completion of the acquisition, Alliander is expected to terminate existing loan facilities at Endinet to avoid potential structural subordination following consolidation of Endinet's three networks into the Alliander group.

Outlook

The stable outlook reflects our expectations that Alliander will continue to post stable and predictable cash flows from its regulated business, while performing adequately within the incentive-based Dutch regulatory framework.

The acquisition of Endinet would effectively exploit all headroom within the current rating. A negative rating action could follow should Alliander not sufficiently offset the negative impact from the proposed acquisition of Endinet on its financial profile. The ratings could come under pressure following adverse regulatory actions, higher than expected operating expenditures, or an increase in capital expenditure. An upgrade is unlikely over the near to medium term.

Related Research

Principles Of Corporate And Government Ratings, June 26, 2007

Ratings List

Ratings Affirmed

Alliander N.V.

Corporate Credit Rating

A/Stable/A-1

Alliander Finance B.V.

Senior Unsecured*

A

*Guaranteed by Alliander N.V.

NB: This does not include all ratings affected

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