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Summary:
Alliander N.V.

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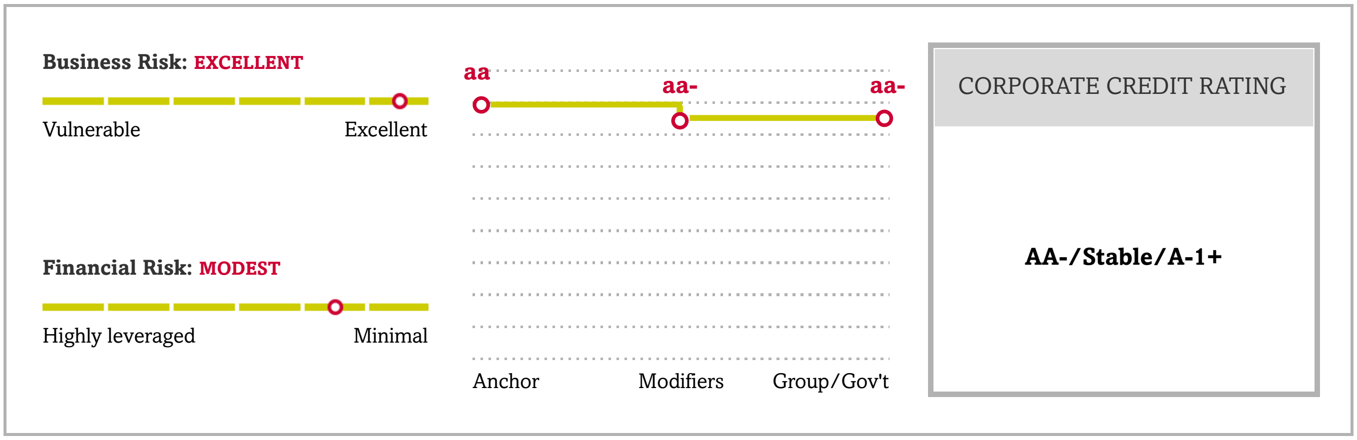

Rationale

Business Risk: Excellent	Financial Risk: Modest
• More than 95% of operating profit derived from stable, regulated revenues. • Natural monopoly position in service areas. • Strong operational performance of networks. • Regulatory reset risk every three years.	• Stable and predictable operating cash flows within regulatory periods. • Conservative financial policy and strong debt coverage ratios. • Risk associated with remaining cross-border leases.

Outlook: Stable

The stable outlook reflects our opinion that Dutch electricity and gas distribution network operator, Alliander N.V., will be able to sustain adjusted funds from operations (FFO) to debt of about 25%. Underpinning this opinion are our assumptions that Alliander will partially offset the impact of lower tariffs in the current regulatory period by reducing its operating costs and dividend distributions.

Downside scenario

We could lower the ratings if we believe that the company is likely to recapitalize its balance sheet to maintain its publicly stated minimum requirement of FFO to debt of 20%. In our view, this could occur either through further sector consolidation in The Netherlands or an extraordinary dividend distribution. We could also lower the ratings if the company's credit ratios were to weaken sustainably below our guidance of 25% FFO-to-debt, for example as a result of operational issues or negative regulatory intervention.

Upside scenario

We consider an upgrade as unlikely in light of the relatively predictable tariffs set by the regulator to end-2016, and the company's capital expenditure (capex) plan and dividend policy. This said, we would consider an upgrade if Alliander were able to sustain an adjusted FFO-to-debt ratio of more than 35%, assuming an unchanged business risk profile.

Standard & Poor's Base-Case Scenario

We have developed our own base-case forecast based on our assumptions and Standard & Poor's methodologies.

Assumptions

- Revenues and FFO decrease in 2014 due to a reduction in tariffs in the current regulatory period starting 2014. We expect a slight recovery from this level in 2015 and 2016.
- Moderately negative discretionary cash flows after capex and dividends result in gradually rising debt levels.
- Solid operating margins support strong interest cover ratios.

Key Metrics

	2013A	2014F	2015F
EBITDA Margin (%)*	44.3	35-45	35-45
Debt/EBTIDA (x)*	2.4	2.5-3.5	2.5-3.5
FFO/Debt (%)*	33.4	23-28	23-28
FFO cash interest coverage (%)*	9.3	7-9	7-9

*Standard & Poor's adjusted figures. A—Actual. F--Forecast. FFO--Funds from operations.

Business Risk: Excellent

Alliander's "excellent" business risk profile primarily reflects the very low risk associated with its regulated electricity and gas distribution network businesses, the company's natural monopoly status in its license areas, and the high quality network assets.

Additionally, our assessment is underpinned by the strong competitive position supported by a strong regulatory advantage. The majority of Alliander's activities, including its electricity and gas tariffs, are regulated by the Dutch Ministry of Economic Affairs and the Dutch regulator, Authority for Consumers & Markets (ACM). The regulatory framework is well established, supportive, mature and relatively stable through a regulatory period, having started in 2001. It allows companies to recover its costs and earn a return on their regulated asset base (RAB), adjusted for CPI and an efficiency incentive, the x-factor (CPI-X adjustment of revenues). We consider that the tariff decision for the current three-year regulatory period which started on Jan. 1, 2014, will be challenging for the Dutch distribution network operators since it will result in substantial tariff level reductions over the 2014-2016 period. The decision indicates that the ACM will lower the tariffs, mainly through a step-by-step reduction of the real pretax weighted-average cost of capital to 3.6% from 6.2%, which we calculate would reduce Alliander's revenues by about €50 million in 2014. However, we believe that Alliander's efforts to reduce costs and its prudent prefunding of upcoming debt maturities at a lower cost, as well as the fact that dividends are likely to reduce with lower net profit, could mitigate the lower tariffs.

These strengths are partly offset by 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 Alliander will take an active part. However, it is possible that consolidation will take the form of asset swaps or bolt-on acquisitions, with limited financial outlay on behalf of Alliander.

Financial Risk: Modest

Alliander's "modest" financial risk profile is based on its continued ability to report solid earnings and cash flow coverage of debt measures. Adjusted FFO-to-debt and debt-to-EBITDA stood at about 33% and 2.4x, respectively, at the end of the last regulatory period that ended in December 2013. We anticipate a weakening in these ratios from 2014, due to lower tariffs in the current regulatory period, and we also note that the rising capex will result in moderately negative discretionary cash flows. However, we expect that the ratios will remain commensurate with the modest financial risk profile. In our opinion, Alliander has a conservative financial policy with specific minimum ratio thresholds that also support the company's strong liquidity position.

Liquidity: Strong

The short-term rating is 'A-1+'. We assess Alliander's liquidity position as "strong" as defined in our criteria, supported by our view that Alliander's liquidity sources will exceed its funding needs by more than 1.5x over the next 12 months. Alliander's well-established and solid relationships with banks, generally high standing in the credit markets, and typically very prudent risk management further support our opinion of liquidity as strong.

As of Dec. 31, 2013, we estimate that Alliander's liquidity sources over the next 12 months will be close to €1.5 billion while uses will be around €900 million under our base-case scenario.

Principal Liquidity Sources	Principal Liquidity Uses
• Unrestricted cash and short-term marketable securities of about €390 million. • Access to an undrawn €600 million committed credit facility expiring in July 2018. The credit facility contains no financial covenants. • Annual FFO of about €515 million.	• Capex of about €520 million. • Debt repayments of €280 million. • Dividend payments of about €125 million.

Other Modifiers

We modify the stand-alone credit profile (SACP) on Alliander down by one notch based on our "comparable rating analysis" to reflect Alliander's ratios will be at the low end of the "modest" financial risk profile during the current regulatory period. In addition to our forecast that FFO-to-debt will be about 25%, we anticipate that Alliander will post negative discretionary cash flows and that the supplementary payback ratios of free operating cash flow/debt and discretionary cash flow/debt will be in the "significant" range.

Government Support

The 'AA-' long-term rating on Alliander is based on the company's SACP, which we assess at 'aa-', 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 (GREs), our view of a "moderate" likelihood of extraordinary ownership support is based on our assessment of Alliander's:

"Important" role, given its strategic importance to the provinces 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. Nevertheless, most of the smaller shareholders, primarily municipalities, have historically been connected to the provinces, which are the larger shareholders, in terms of geography and administration.

Ratings Score Snapshot

Corporate Credit Rating

AA-/Stable/A-1+

Business risk: Excellent

- **Country risk:** Low
- **Industry risk:** Very low
- **Competitive position:** Excellent

Financial risk: Modest

- **Cash flow/Leverage:** Modest

Anchor: aa

Modifiers

- **Diversification/Portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Liquidity:** Strong (no impact)
- **Financial policy:** Neutral (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Negative (-1 notch)

Stand-alone credit profile : aa-

- **Likelihood of government support:** Moderate (no impact)

Related Criteria And Research

Related Criteria

- Corporate Methodology, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Jan. 2, 2014
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013
- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria Clarification On Hybrid Capital Step-Ups, Call Options, And Replacement Provisions, Oct. 22, 2012
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008
- Corporate Criteria: Rating Each Issue, April 15, 2008

Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	**Modest**	Intermediate	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	**aa**	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

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