



## Rating Action: **Moody's affirms Elering's A2 rating, outlook stable**

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19 Feb 2024

Frankfurt am Main, February 19, 2024 – Moody's Investors Service (Moody's) has today affirmed the A2 long-term issuer rating and the a3 Baseline Credit Assessment (BCA) of Elering AS (Elering). The outlook remains stable.

### RATINGS RATIONALE

Today's rating action reflects that Elering's A2 rating remains underpinned by the low business risk profile of its regulated transmission network activities in Estonia, which operate under a flexible and generally supportive regulatory framework. Moody's expects Elering to gradually grow cash flow generation, mainly on account of an increase in return rates for electricity and gas transmission assets to 6.22% and 6.25% respectively (up from 4.51% for electricity and 4.58% for gas previously) due to higher risk free rates. Moreover, the introduction of a 10% capacity component and 4.5% connection point component for electricity transmission tariffs applicable since January 2024 reduces volume risks, a credit positive. Moody's expects that future tariff decisions will continue to bolster Elering's financial profile, despite lower cash flow visibility due to potential annual tariff changes under Estonia's regulatory framework as opposed to other European frameworks.

At the same time, the rating affirmation reflects that Elering's rating remains constrained by (1) the company's small size; and (2) execution risks associated with elevated levels of capital spending in the near term. Investments remain dominated by the Baltic Synchronisation project alongside investments designed to increase capacity for the integration of renewables and new cross-border projects. Moody's expects capex to peak in 2024, but free cash flow generation to remain negative until 2025, when the Baltic Synchronisation project is targeted to be completed. Moody's notes that investment risk is mitigated as projects are co-financed with a mix of non-refundable grants, congestion income and EU funding.

The rating affirmation further factors in the solid financial profile of Elering, which exhibited funds from operations (FFO)/net debt of 159% in 2022. Moody's notes, however, that this ratio is boosted by the accumulation of congestion income stemming from the transmission of power between different price zones. By law, such congestion income will have to be returned to consumers eventually; Moody's therefore views their impact on Elering's credit metrics as temporary only and thus credit neutral. The rating affirmation nonetheless reflects Moody's expectation that Elering's underlying credit metrics will remain in line with the applicable guidelines for the current rating.

Given its 100% ownership by the Government of Estonia (A1 stable), Elering falls under Moody's Government-Related Issuers (GRI) methodology. Accordingly, Elering's A2 rating incorporates one notch of uplift from its BCA of a3. This reflects the combination of the credit quality of the Government of Estonia, Moody's assessment of a high

probability of government support for the company in the event of financial distress, as well as Moody's view of very high default dependence between the Government of Estonia and Elering.

## RATIONALE FOR THE STABLE OUTLOOK

The outlook on Elering's rating is stable, reflecting Moody's expectation that the company will maintain a financial profile commensurate with the guidelines for the current rating and continue to manage its liquidity prudently.

## FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

For a rating upgrade, Moody's would expect Elering to consistently maintain FFO/net debt of at least 25%, underpinned by the absence of any significant adverse changes in the regulatory framework.

The rating could come under downward pressure if Elering's FFO/net debt were to decline below the high teens in percentage terms for a sustained period. Downward pressure could also be exerted on the rating as a result of a deterioration in the credit quality of the Government of Estonia; a reduction in the government support assumptions currently incorporated into Moody's assessment; or a significantly unfavourable change in the regulatory framework, leading to a significant increase in the company's business risk.

## PRINCIPAL METHODOLOGIES

The methodologies used in these ratings were Regulated Electric and Gas Networks published in April 2022 and available at <https://ratings.moodys.com/rmc-documents/386754>, and Government-Related Issuers methodology published in January 2024 and available at <https://ratings.moodys.com/rmc-documents/406502>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of these methodologies.

Headquartered in Tallinn, Elering AS is the monopoly transmission system operator for electricity and gas in Estonia. Elering is 100% owned by the Government of Estonia. Elering reported revenues of EUR244.7 million and EBITDA of EUR81.8 million for the 12-month period that ended 31 December 2023 according to unaudited interim results.

## REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

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