RATING COMMUNICATION

Cerved Rating Agency S.p.A. affirms at

A3.1

the public rating assigned to **E.S.TR.A. S.p.A.**

Prato (PO) – Via Ugo Panziera, 16 – Italy

Cerved Rating Agency on 23/12/2017 has affirmed E.S.TR.A. S.p.A. rating at A3.1

Date of first issuance of the rating: 24/12/2013

E.S.TR.A. S.p.A. Energia Servizi Territorio Ambiente (E.S.TR.A., The Group) was founded in 2010 following a process of aggregation of three public energy services companies with a long-standing presence in gas distribution in Tuscany: Consiag S.p.A. of Prato, Intesa S.p.A. of Siena and Coingas S.p.A. of Arezzo. These firms are owned entirely by 97 municipalities located in the provinces of Arezzo, Florence, Grosseto, Pistoia, Prato and Siena. In the two-year period 2016-2017 numerous M&A deals and extraordinary operations were carried out aimed at rationalization and simplification of the Group structure. Entry of the strategic partner Multiservizi S.p.A. into the share capital, scheduled to take place by the end of 2017, is an important milestone in the positioning of E.S.TR.A., also in view of its listing on the Italian Stock Exchange expected in 2018.

Key rating factors

- ***Business model and market positioning***

The E.S.TR.A. Group organizes its business model in Strategic Business Areas (SBA): sale of gas and electricity (EE), gas trading, distribution of natural gas, production of electricity from renewable sources, energy management related services, distribution of LPG and telecommunications. The SBA sale of gas and electricity in 2016 represented 61% of the consolidated revenues and 66% of the EBITDA. The Group targets a diversified clientele comprising domestic, business, wholesalers and Public Administrations. The SBA distribution of natural gas and LPG in 2016 accounted for 9% of the consolidated revenues and 28% of the EBITDA. In 2016 E.S.TR.A. was among the top ten players operating in the distribution of natural gas in Italy and among the top fifteen (on the basis of volumes handled) in the sale of gas to the end market. The Group's strategic pillars are geared to organic growth, achieved by the implementation of new commercial policies, and growth through acquisitions, in addition to the development of networks (gas distribution network and optic fibre infrastructure) and preservation of market positioning supported by innovative projects.

- ***Key financial results***

As from the financial year ended 31st December 2016, the E.S.TR.A. Group has adopted the International Financial Reporting Standards (IFRS). The consolidated revenues for 2016 amounted to 1,007.1 million euro, a growth of 19.2% compared to 2015; this expansion trend is due mainly to the organic growth in volumes and customers of the SBA sale of gas and EE, impact of consolidation of the companies Prometeo, Coopgas and Gas Tronto, and increase in the gas trading activity. The EBITDA adj (net of the non-recurring items and bad debts) is 69.4 million euro (50.1 million euro in 2015) with an EBITDA margin of 6.7% in 2016 (5.8% in 2015). It should be noted that the EBITDA adj 2015 was adjusted for the net gain of 51.5 million euro from the sale of the gas distribution assets in the Municipality of Prato to Toscana Energie. The increase in the EBITDA margin is due both to the change in the customer mix, with reduction of sales to the wholesalers, and to the favourable trend of the commodity prices. The net income in 2016 amounted to 15.1 million euro.

At 31/12/2016 the Net Debt was 203.5 million euro, an increase with respect to the 166.4 million euro as at 31/12/2015 mainly due to financing of the M&A operations. The Net Debt/EBITDA ratio was 2.93x, whereas the Net Debt/Equity ratio was 0.63x in 2016. For 2017 is expected a Net Debt in line with 2016 levels, a slight decrease in turnover linked to the reduction in the trading activity and an EBITDA margin at the same levels as the last FYs, as confirmed by the interim results.

- ***Liquidity***

In 2016 the Net Operating Cash Flow was 35.5 million euro, an increase compared to the previous FY due to the greater contribution of the Gross Operating Cash Flow and improved dynamics of the net working capital. The investments made in the FY nevertheless resulted in a negative Free Cash Flow in 2016.

Key risk factors

- **Market risk**

The Group is exposed to price volatility of the energy commodities. The risk is partially mitigated via the use of hedging derivatives and diversification of the business. The sector is further significantly influenced by the complexity and evolution of the regulatory reference framework.

- **Operational risk**

The operational risks are partly limited by the internal procedures involving control instruments and investments in advanced IT systems. The risk connected with integration of the acquired companies is moderate as the Group has built up experience, applying best practices, from the M&A operations already carried out in previous years.

- **Financial risk**

The liquidity risk is managed by maintaining an available liquidity buffer (264.2 million euro at 31/12/2016) and by the cash flows generated from the operating activities. E.S.TR.A., having a considerable long-term loans amount, partially mitigates the interest rate risk via a balanced portfolio of loans and debt instruments at fixed and variable interest rates and by means of suitable derivatives. The credit risk is monitored by the company, by selecting its commercial partners on the basis of their credit standing and by prompt accruals of the relative bad debt provision.

Rating assumptions

- Organic and M&A driven revenue growth, with an EBITDA margin level around 7.0%
- Net operating cash flow positive in 2017 and 2018
- Net debt in line with FY 2016

Rating sensitivities

- A significant increase in net debt, failure to achieve expected profitability levels and a significant worsening in the net operating cash flows could entail a negative rating action.
- Achievement of the results forecast by the Business Plan would allow the rating class attributed to be maintained.

The applied methodology is published on Cerved Rating Agency's website: www.ratingagency.cerved.com

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