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 14/12/2017 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. In December 2017 Viva Servizi S.p.A. (formerly Multiservizi S.p.A.) entered into E.S.TR.A's share capital with a 10% stake.

Key rating factors

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

The E.S.TR.A. Group organizes its business model in Strategic Business Units (SBU): 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. In 2017 the SBU sale of gas and electricity represented 60% of the consolidated revenues and 67% of the EBITDA. The clientele is diversified and comprises domestic, business, wholesalers and Public Administrations. The SBU distribution of natural gas accounted for 9% of the consolidated revenues and 30% of the EBITDA. In 2017 E.S.TR.A. was one of 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 weight of the gas distribution business will increase after Atem Foggia 1 Nord and Bari 2 Sud lots have been awarded to the Group. Implementation of the strategic pillars defined in 2017 continues, geared to organic and M&A growth, the development of networks (gas distribution network and optic fibre infrastructure) and preservation of market positioning supported by innovative projects.

- ***Key financial results***

The consolidated revenues for 2017 amounted to 1.0 billion euro, in line with the previous year. The EBITDA adj (net of the provision releases, bad debts and the derivatives MTM changes) was equal to 75.9 million euro (70.5 million euro in 2016) with an EBITDA margin adj increasing from 6.8% in 2016 to 7.5% in 2017, due to the improvement of the SBU sale of gas and EE gross margin and to the reduction of bad debt write offs. The net income in 2017 amounted to 16.1 million euro (+6.7% compared to 2016). As at 31/12/2017 the Net Debt was 216.1 million euro (203.5 million euro as at 31/12/2016) with the Net Debt/EBITDA adj and the Net Debt/Equity adj (net of derivatives reserves) ratios of 2.68x (2.69x in 2016) and 0.61x (0.59x in 2016) respectively. No significant changes in the Net Debt are expected at the end of 2018. In 2018 the application of the new IFRS 15 will result in a significant revenues reduction, mainly regarding the SBU Trading, despite the volumes growth in the period. The increase of the gas prices in 2018 had a negative impact on the results of the first semester. However in 2018 EBITDA is expected in line with 2017, due to the positive performance of SBU sales of gas and EE in the second semester, driven by the changes in the client mix and the impact of physical hedging.

- ***Liquidity***

In 2017 the Net Operating Cash Flow was around 100 million euro, a significant improvement compared to the previous year, mainly attributable to working capital optimisation. This dynamic also resulted in a positive Free Cash Flow, with the same trend expected in 2018.

Key risk factors

- **Market risk**

The Group is exposed to price volatility of the energy commodities. The risk is partially mitigated via the adoption of physical and financial hedging and continuous business diversification. 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 from the M&A operations already carried out in previous years, applying best practices.

- **Financial risk**

The liquidity risk is managed by maintaining an available liquidity buffer (229.8 million euro at 31/12/2017) 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 adequate 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

- Revenues increase for the sales of gas and EE, distribution and corporate SBUs
- Consolidated EBITDA margin adj exceeding 8.0% in the 2018-2019 period
- Positive Net Operating Cash Flow and Free Cash Flow in 2018
- No significant Net Debt changes at 31/12/2018
- Free Cash Flow stressed in 2019 following payment of the consideration of 42 million euro (subject to adjustments) for the gas distribution business awarded for Atem Foggia 1 Nord and Bari 2 Sud

Rating sensitivities

- A significant increase in net debt, failure to achieve expected profitability levels and a considerable worsening in the net operating cash flows could entail a negative rating action.
- The Group results aligned with the rating assumptions 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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