RATING COMMUNICATION

Cerved Rating Agency S.p.A. downgrades

E.S.TR.A. S.p.A. public rating

to **B1.1**

Prato (PO) – Via Ugo Panziera, 16

Cerved Rating Agency on 05 June 2020 has downgraded E.S.TR.A. S.p.A. rating from A3.1 to B1.1

Date of first issuance of the rating: 24 December 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

The rating review reflects the physiological impacts related to the Covid-19 emergency on the core business (Gas and EE Sales) in FY20. The Agency estimates that in FY20 the Group's economic and financial performance lower than management's assumptions, in terms of volumes, margins and working capital requirements, will affect the Group's ability to reduce debt exposure.

Business diversification focused on new investments in gas distribution and waste management – During FY19, management continued the growth path of the Group, through consolidation of core segments (Gas and Electricity Sales and Gas Distribution), and the further development of secondary, although strategic, businesses such as energy efficiency services, renewables and waste management. In this respect it should be noted the investments carried out during the year, i.e. the acquisition of Murgia Reti Gas S.r.l., which comprises 544 km of distribution network and 66,000 PdR and the acquisition of Ecolat S.r.l., involved in the integrated cycle of waste through plants and collection centers, in order to achieve know-how and skills in a relatively new area for the Group, with expansion perspectives in the coming years.

Significant increase in revenues in FY19, with broadly stable operating margin levels – The growing incidence of business customers, especially in the Gas segment, and the rise in sales on PSV led to an important boost of delivered volumes during the year, driving the increase in Group revenues to 985.8 million euros in FY19 (+ 17.8% YoY), despite a reduction of Gas household and a drop in market prices. At the same time, SBU Gas Distribution, in spite of a growth in revenues arising from the gas carriage tariff, reported a slight decrease overall (-6.3 million euros) deriving from lower income for TEE trading, whereas the smaller business units (TLC, Services, Renewable Energies, Waste management) contributed albeit marginally to the year-end result, with an increase of 11.4 million euro, attributable to the consolidation of Ecolat and the development of energy efficiency activities. With regard to operating profitability, although the growing business volumes have determined a greater absorption of fixed costs, EBITDA margin adjusted was equal to 7.6%, roughly in line with the previous year (7.1% in the FY18), negatively affected by a reduction in the gross margin of SBU Gas e EE Sales and by the higher bad debt provision accruals.

Capex exceeding operating cash flows resulting in financial requirements growth – In the FY19 the Group generated higher operating cash flows for 54.1 million euros (51.9 million euros in the FY18), which however have only partly funded the significant capex of 91.3 million euros. The resulted financial requirement has been covered through the huge liquidity held by the Group, determining an increase of the Net Debt at 316,6 million euros at 31/12/2019 (259,7 million euros at 31/12/2018), which also includes new lease debts (IFRS 16) and payables to shareholders for dividends. Net Debt/Equity and Net Debt/EBITDA ratios remain however sustainable at 0.98x and 4.24x respectively (0.80x and 4.34x at 31/12/2018).

FY20 forecast affected by Covid-19 impact – Cerved Rating Agency estimates a reduction in revenues and margins at the Group level in FY20 due to: (i) a bearish trend of EE and Gas market price; (ii) a negative Gas heating effect (January and February 2020); (iii) a decrease in consumptions of both retail and business customers in the period March – May 2020 as a consequence of the lockdown imposed by the Government, partly offset by an increase in household consumptions; (iv) a likely increase in credit losses/depreciation. From a financial perspective the Agency estimates higher financial requirements deriving from working capital needs due to higher cash in delays, partly offset by a recourse to factoring, with a consequent increase of Net Debt at year-end.

Rating sensitivities

- The public rating of E.S.TR.A. S.p.A. could be upgraded in light of: (i) improvement of operating margins; (ii) efficient working capital management in spite of the expected higher requirements; (iii) significant decrease of current Net Debt, resulting in an improvement of main debt coverage ratios.
- The public rating of E.S.TR.A. S.p.A. could be downgraded in light of: (i) significant worsening of the profitability and economic results; (ii) negative operating cash flows; (iii) further growth of Net Debt with a consequent burdening of capital and financial structure.

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

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