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Summary:
Gaz Metro Inc.
Gaz Metro L.P.

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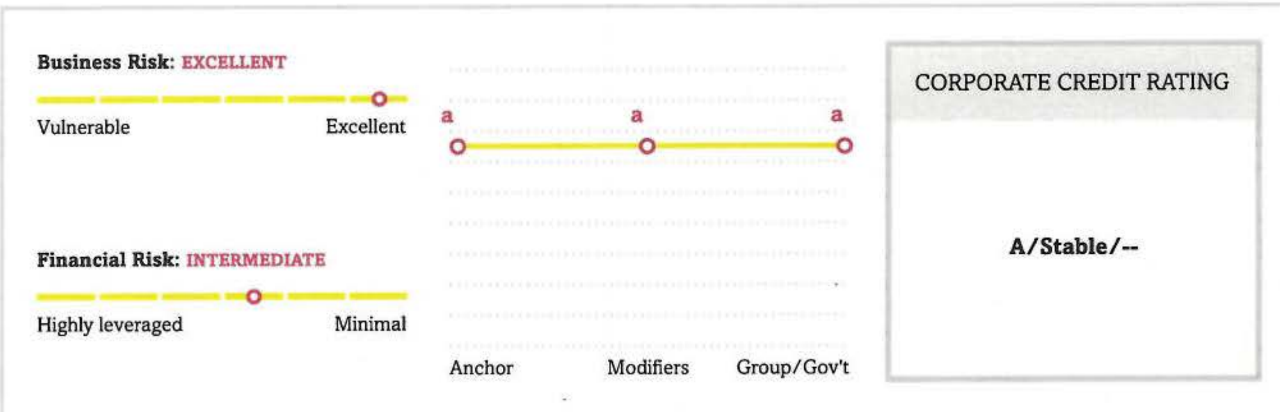

Rationale

Business Risk: Excellent	Financial Risk: Intermediate
• Supportive regulatory environment in Quebec and diversity of regulated operations provide stable cash flows • Dependence on industrial consumption in the province introduces higher volume variability than predominantly residential distributors	• Financial metrics reflect the regulated capital structure as well as additional debt at the L.P. level • Stable cash flows and financial metrics are in line with a "intermediate" financial risk profile during the two-year outlook period; however, the company has limited cushion to the rating triggers

Outlook: Stable

The stable outlook reflects Standard & Poor's expectation that on a consolidated basis Gaz Metro Inc. (GMI) will continue generating stable and predictable cash flow from its low-risk regulated operations in Quebec and Vermont during our outlook horizon. The outlook also reflects our expectation that management will continue to focus on its core regulated business and that the company will not experience any adverse regulatory decisions during our outlook horizon.

Upside scenario

We could take a positive rating action if the company demonstrates long-term commitment to improve its credit metrics resulting in sustained adjusted funds from operations (AFFO)-to-debt of 23% or better. However, we do not expect this to happen during our outlook period, given the company's current capital plan.

Downside scenario

We could take a negative rating action on GMI if the company's credit metrics deteriorate, with AFFO-to-debt falling to and staying below 16%, at the low end of the "intermediate" financial risk profile. This could happen as a result of adverse regulatory decision or a material debt-financed acquisition.

Standard & Poor's Base-Case Scenario

Assumptions

- GMI will continue to focus on regulated utility operations with unregulated energy-related activities and non-energy-related activities less than 10% of its total unconsolidated assets
- The company will not experience any adverse and material regulatory decisions and that the regulatory regime in Quebec and Vermont will remain stable and transparent

Key Metrics

	2015A	2016E	2017E
AFFO/debt	16.2x	16%-18%	16%–18%
Debt/EBITDA	5.7x	5.0x-6.0x	5.0x–6.0x

AFFO--Adjusted funds from operations. A--Actual. E--Estimate.

Business Risk: Excellent

In our view, GMI's business risk profile is "excellent." The company continues to benefit from its stable, low-risk, regulated utilities operations. Tariff structures are generally supportive, allowing recovery of prudently incurred operational and capital expenses in a timely manner that supports the stable cash flow. Furthermore, GMI's exposure to commodity input price is limited as electricity and natural gas input costs remain a pass-through to rate-payers, which we view as a credit strength.

In addition, GMI operates in multiple service territories primarily in Quebec and Vermont, through its wholly owned subsidiary Green Mountain Power Corp., providing regulatory, geographic, and market diversification.

Further supporting the business risk profile is GMI's exposure to a diverse customer base primarily consisting of residential and small-to-medium commercial customers that are less affected by economic cycles, although in Quebec, GMI has a relatively large industrial user base. However, these users' gas consumption is largely dependent on the price of natural gas. Given that natural gas is relatively cheap compared to other fuel costs, the fuel switching seen historically is now at a minimum.

GMI also owns and operates a renewable energy wind farm, an unregulated business, but its cash flow contribution to GMI is minimal and is immaterial to our rating on the company.

Financial Risk: Intermediate

We assess GMI's financial risk as "intermediate." The company has a large capital program and relies on the combination of internal generated funds and external debt to fund these capital investments. This places downward pressure on the company's credit metrics, especially the AFFO-to-debt ratio. Nevertheless, we expect GMI will maintain its AFFO-to-debt above the downside trigger at about 16%-18% during our outlook period in 2016-2017. However, we note this leaves the company very little cushion to their downside trigger of 16%. When evaluating GMI's cash flows, we used the low-volatility table to reflect the generally supportive regulatory regime that underpins the stability and predictability of the cash flow stream and that vast majority of GMI's operating cash flows are from the low end of the utility risk spectrum. We expect the company to maintain its balance sheet, in line with the regulator's deemed capital structure.

We exclude the C$892.8 million of non-common equity financing from Noverco Inc. provided to GMI from our leverage and coverage calculations as per our criteria, "The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities," published April 29, 2014, on RatingsDirect. The notes have more than 10 years of remaining life, and we believe that the company intends to extend the maturity date to at least 30 days after all other debt matures. If there is less than 10 years of remaining life, or, while unlikely, we no longer believe GMI intends to extend the maturity, we might include the notes in our leverage and coverage calculations.

The "excellent" business risk and "intermediate" financial risk profiles produce a split anchor scores of 'a+/a'. We have chosen the lower of the two anchor scores to reflect the weaker business risk profile relative to that of other regulated utility operators. GMI has a relatively large industrial user base in Quebec, whose natural gas consumption is more variable, with a meaningful contributing to the company's cash flows compared to those of other regulated peers with more stable residential customers.

Liquidity: Adequate

Our view on GMI's liquidity is "adequate." We expect liquidity sources will be adequate to cover uses more than 1.1x in the next 12 months. We expect that in the event of a 10% EBITDA decline, the company's sources of funds would still exceed its uses. In our view, GMI has sound relationships with its banks and generally prudent financial risk management. In the event of an unexpected financial stress situation, we believe the utility would scale back on its capital expenditures and has the flexibility to suspend dividend payments to preserve credit metrics.

Principal Liquidity Sources	Principal Liquidity Uses
• Cash FFO of about C$670 million in the next 12 months • Committed credit facilities availability of about C$670 million as of Sept. 30, 2015, maturing in 2020 • Equity issuance of about C$120 million from Sept. 30	• Capital expenditure of C$460 million-C$500 million in the next 12 months • Dividends of C$120 million-C$130 million over the next 12 months

Other Credit Considerations

All modifiers had no effect on the rating, so the 'A' corporate credit rating is the same as the 'a' initial anchor score.

Ratings Score Snapshot

Corporate Credit Rating

A/Stable/--

Business risk: Excellent

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

Financial risk: Intermediate

- **Cash flow/Leverage:** Intermediate

Anchor: a

Modifiers

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

Recovery Analysis

GMI has secured utility bonds (first mortgage bonds [FMBs]) outstanding with maturities of 2016-2045. These FMBs are secured under trust deeds that contains a hypothec on all of Gaz Metro's assets. A first immovable hypothec on Gaz Metro L.P.'s pipelines and gas distribution system also covers creditors. We estimate that the regulated capital value at GMI is greater than 1.5x the secured utility bonds outstanding. This results in a '1+' recovery rating, and an 'A+' rating on the FMBs.

Related Criteria And Research

Related Criteria

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities, April 29, 2014
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Collateral Coverage And Issue Notching Rules For '1+' And '1' Recovery Ratings On Senior Bonds Secured By Utility Real Property, Feb. 14, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Business And Financial Risk Matrix

	Financial Risk Profile					
Business 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-