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Ratings

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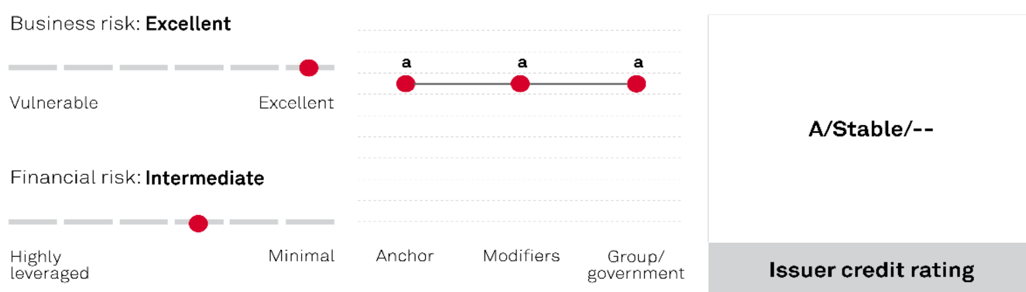
Energir Inc.

January 6, 2023

Ratings Score Snapshot



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Credit Highlights

Overview

Key strengths	Key risks
Low-risk, regulated natural gas and electricity distribution utility operations with limited commodity exposure.	Some exposure to nonutility operations that are susceptible to cash flow volatility.
Geographic and regulatory diversity with operations in multiple service territories, primarily in Quebec and Vermont.	Negative discretionary cash flow indicates external funding needs.
Effective management of regulatory risk under generally supportive tariff structures and use of various regulatory mechanisms, including decoupling.	Commodity price pressures might require effective management of regulatory risk.

The rating reflects the credit-supportive regulatory frameworks in Quebec and Vermont. The company generates the majority of its cash flow from its low-risk, regulated utility operations in Quebec and Vermont, which we view as credit-supportive jurisdictions. Energir's use of regulatory mechanisms, including decoupling and multi-year rate plans, enable it to recover its incurred operational and capital expenses in a timely manner, which underpins the stability of its cash flows.

We expect the company's financial measures will be above our downgrade trigger with some, albeit limited, cushion. We forecast Energir's funds from operations (FFO) to debt will be in the 15.0%-17.5% range through our forecast period. This is due to an about C$60 million increase in its rates approved by the Régie de l'énergie (Régie) for 2023 and incorporates our expectation for annual increases. However, we anticipate the company's financial measures will be pressured by its robust capital expenditure.

Rising natural gas prices could pressure the company's financial measures. While Energir is able to pass-through increases in its commodity costs, rising commodity prices could require it to effectively manage its regulatory risk, such as by deferring expenses.

We are monitoring the multi-year rate plan (MYRP) of its subsidiary Green Mountain Power (GMP). In August 2022, the Vermont Public Utility Commission (VPUC) approved a 2.18% base rate increase effective Oct. 1, 2022, and a new MYRP that will govern **GMP's** rates for four years. The increase in its base rates for 2023 was approved using a traditional cost-of-service rate regulatory review. The subsidiary will make subsequent base-rate filings each year and include expected base-rate adjustments based on certain annual adjustments and the application of a rate-smoothing adjustment**.** The initial rate-smoothing mechanism will be set in the 2023 filing, which establishes an annual amount that is either added to or subtracted from the revenue requirement for 2024-2026. Any adjustments will be deferred and recovered or refunded in the subsequent year. Depreciation expense will be fixed, and controllable operations and maintenance (O&M) costs will either be fixed or adjusted for inflation.

Outlook

The stable outlook reflects our expectation that Energir will continue to generate stable and predictable consolidated cash flows from its low-risk and regulated utility operations throughout our two-year outlook horizon. The outlook also reflects our expectation that management will continue to focus on its core regulated business and the company will not experience any adverse regulatory decisions over the same time period.

Downside scenario

We could lower our rating on Energir over the next 12-24 months if:

- The company's credit metrics deteriorate, including its S&P Global Ratings-adjusted FFO to debt falling below 14% and remaining at that level with no prospects for improvement. This could occur because of an adverse regulatory decision, a material debt-financed acquisition, or if it encounters significant operating challenges; or
- The company's business risk weakens substantially. This could occur if it materially increases its unregulated or generation operations.

Upside scenario

We could raise our rating on Energir over the next 12-24 months if it demonstrates long-term, sustainable, and low-risk growth or improved financial measures, including S&P Global Ratings-adjusted FFO to debt of consistently near or above 20%.

Our Base-Case Scenario

Assumptions

- Energir continues to use the regulatory mechanisms provided by the authorities in both Quebec and Vermont, as well as under the Federal Energy Regulatory Commission (FERC);
- Capital expenditure of about C$500 million-C$600 million throughout the outlook horizon; and
- Dividends payout at 100% of net income.

Key metrics

Energir Inc.--Key Metrics*

	2022a	2023e	2024f
FFO to debt (%)	15.5	15.5-17.5	15-17
Debt to EBITDA (x)	5.0	4.5-5.0	4.5-5.0

*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast. FFO--Funds from operations.

Company Description

Energir provides electricity and natural gas energy services in Canada and the U.S. The company mainly holds an ownership stake of about 71% in Energir L.P. (ELP), the General Partner and a financing vehicle. ELP is a diversified energy infrastructure and services company with more than C$8 billion in assets serving over 520,000 customers. ELP's core operations are the distribution of natural gas in Quebec and Vermont and regulated electric transmission and distribution in Vermont. ELP also operates in the energy production and energy services and storage sectors.

Business Risk

Our assessment of Energir's business risk profile largely reflects its low-risk, regulated natural gas and electricity distribution utility operations, its management of its regulatory risk through the use of various regulatory mechanisms, including decoupling and MYRPs, and its geographic and regulatory diversity due to its operations in multiple territories. The company operates under generally supportive tariff structures that allow for the recovery of prudently incurred operational and capital expenses in a timely manner, which provide stability to its cash flows. We expect Energir will continue to benefit from the supportive regulatory frameworks in both Quebec and Vermont, as well as under the FERC. Additionally, the company has a limited exposure to commodity input prices because it passes through its electricity and natural gas input costs to its ratepayers, which we view as supportive of its credit quality. Moreover, the company is not exposed to cast iron or bare steel in its pipeline infrastructure gas network, which mitigates the potential for gas leaks and explosions.

Energir's business strengths are partially offset by its investments in generation assets and its nonutility operations, which entail higher business risk. We also believe the company's obligation to supply natural gas could lead to potential sourcing and operational risks.

Financial Risk

We assess Energir's financial risk profile using our low-volatility financial benchmarks, which reflect its lower-risk, regulated electric and gas distribution operations and effective management of regulatory risk. Our base-case scenario assumes its continued use of regulatory mechanisms, capital spending of about C$500 million-C600 million throughout the outlook horizon, and a target dividend payout of 100% of net income during the forecast period. We expect the company's financial measures will remain in the lower end of our benchmark range for the intermediate category, with FFO to debt of about 15.0%-17.5% throughout our outlook horizon. This level of FFO to debt provides it with a limited cushion relative to our 14% downgrade threshold at the current rating.

Liquidity

In our assessment, Energir's liquidity is adequate. We expect the company's sources of liquidity will be more than 1.1x its uses over the next 12 months and anticipate its net sources would remain positive even if its EBITDA declined by 10%. In our view, Energir has sound relationships with its banks and a generally satisfactory standing in the credit markets. In the unlikely event of liquidity distress, we expect the company would scale back its capital spending and cash distributions to preserve its liquidity position.

Principal liquidity sources

- Balance sheet cash of about C$75 million as of Sept. 30, 2022;
- Credit facility availability of about C$800 million; and
- Cash FFO of about C$700 million.

Principal liquidity uses

- Debt maturities of about C$40 million;
- Capital expenditure of about C$550 million; and
- Cash distributions (including dividends) of about C$200 million.

Environmental, Social, And Governance

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicator Definitions And Applications," published Oct. 13, 2021.

ESG factors have no material influence on our credit rating analysis of Energir Inc.

Issue Ratings--Recovery Analysis

Key analytical factors

Energir has outstanding secured utility bonds (first-mortgage bonds [FMBs]). These FMBs are secured under trust deeds that contain a hypothec on Energir's assets. A first immovable hypothec on ELP's pipelines and gas distribution system also covers its creditors. We estimate the regulated capital value at Energir is 1.0x-1.5x of the secured utility bonds outstanding. This corresponds to a '1' recovery rating and an 'A' issue-level rating on the FMBs, which is the same level as our issuer credit rating on Energir.

Rating Component Scores

Foreign currency issuer credit rating	**A/Stable/--**
Local currency issuer 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**
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)
Stand-alone credit profile	**a**

Related Criteria

- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities, April 29, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- ARCHIVE | Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- ARCHIVE | General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | Utilities: Collateral Coverage And Issue Notching Rules For '1+' And '1' Recovery Ratings On Senior Bonds Secured By Utility Real Property, Feb. 14, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009