

April 27, 2009

**Research Update:**

# Eneco Holding N.V. Ratings Lowered To 'A-/A-2' To Reflect Negative Effect Of Regulatory Unbundling; Outlook Negative

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## Research Update:

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## Rationale

On April 27, 2009, Standard & Poor's Ratings Services lowered its long-term corporate credit ratings to 'A-' from 'A' and its short-term corporate credit ratings to 'A-2' from 'A-1' on Dutch utilities Eneco Holding N.V. and N.V. Eneco (collectively known as Eneco). The outlook is negative.

At the same time, Standard & Poor's removed all these ratings from CreditWatch, where they were placed with negative implications on July 18, 2008.

The rating actions factor in the upcoming unbundling by Jan. 1, 2011, at the latest, of Eneco's regulated electricity and gas distribution business (the network company; 64% of EBITDA) from the company's commercial generation, trading, and supply businesses (the energy company; 36%). We understand from management that Eneco intends to unbundle the company by spinning off the energy company and that after the unbundling, Eneco Holding N.V. would comprise the network company Stedin and the infrastructure business Joulez.

Eneco's business risk profile should become stronger after the unbundling in our view because the regulated distribution of electricity and gas would generate more than 90% of its earnings. At present, the strengths of the network business are offset by the energy business, which we consider as much weaker because of its exposure to competition and volatile wholesale power prices, given its short power supply position.

However, the downgrade reflects our understanding that the network company would likely target a financial profile in line with the minimum capital requirements and financial ratios proposed by the Dutch regulator, which are significantly more aggressive than Eneco's current credit metrics.

The regulator has proposed minimum capital requirements and financial ratios that the network companies would have to comply with on the unbundling date, including a ratio of 60% debt to 40% equity. These metrics are significantly more aggressive than Eneco's credit metrics at present. On Dec. 31, 2008, Eneco's adjusted debt to capital was 36%, adjusted funds from operations (FFO) to debt was 28%, and FFO interest coverage was 7.0x. Also, following the unbundling, the regulator proposes to allow the network companies to increase their leverage further if the increase would result from investments in the network.

We understand from Eneco that the network company would retain all the existing external debt (reported debt of €1.9 billion at year-end 2008) apart from debt related to sustainable production facilities in The Netherlands (about €120 million) and nonrecourse project financing, which will follow the generation and supply business. The revolving credit facility would be divided between the network and energy companies. We also understand that the network

company would likely increase leverage up to the allowed level upon unbundling and we believe that debt could increase further after unbundling given planned capital expenditures of €350 million per year through 2012.

### Short-term credit factors

Eneco's 'A-2' short-term rating reflects an adequate liquidity profile. Eneco currently has €1.11 billion of short-term debt, including a €400 million drawdown under its €1.5 billion revolving credit facility, and about €600 million outstanding under its €750 million commercial paper program. We understand from the company that it is close to refinancing the drawdown through German Schuldscheins and private placements in the U.S.

Following the unbundling, only €250 million of the €1.5 billion revolving credit facility, which matures in 2013, will be available for the network company. Given the likely increase in its leverage, we expect the network company to have put in place significant additional credit facilities and funding by the time of the unbundling.

Eneco's net exposure to the costs of early termination of cross-border leases charged to its network assets, amounting to \$652 million (€468 million) in 2009, is a negative credit factor. However, the current exposure is effectively covered by letters of credit (LOCs) totaling \$948 million (€680 million). That said, the proportion of costs that must be covered by LOCs depends on the corporate credit rating; a downgrade would require an increase of the drawing amounts of about \$75 million. The majority of the LOCs expire in 2010, but we understand from management that they would be extended comfortably ahead of maturity. Eneco uses its €1.5 billion credit facility as a backstop for the LOCs.

## Outlook

The negative outlook reflects our view that the network company could increase its leverage toward 70% after unbundling, compared with about 60% upon unbundling. We would likely lower the rating by one notch if Eneco increases its debt to the proposed maximum level of 70% after unbundling. Conversely, we could revise the outlook to stable if Eneco's financial policy becomes more conservative.

## Ratings List

Downgraded; CreditWatch/Outlook Action

|                         | To              | From            |
|-------------------------|-----------------|-----------------|
| Eneco Holding N.V.      |                 |                 |
| Corporate Credit Rating | A-/Negative/A-2 | A/Watch Neg/A-1 |
| Senior Unsecured        | A-              | A/Watch Neg     |
| Commercial Paper        | A-2             | A-1/Watch Neg   |
| N.V. Eneco              |                 |                 |
| Corporate Credit Rating | A-/Negative/A-2 | A/Watch Neg/A-1 |

*Research Update: Eneco Holding N.V. Ratings Lowered To 'A-/A-2' To Reflect Negative Effect Of Regulatory Unbundling; Outlook Negative*

Commercial Paper\*

A-2

A-1/Watch Neg

\*Guaranteed by Eneco Holding N.V.

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