STANDARD & POOR'S
RATINGS SERVICES

RatingsDirect®

Summary:
Fingrid Oyj

Primary Credit Analyst:
Alf Stenqvist, Stockholm (46) 8-440-5925; alf_stenqvist@standardandpoors.com

Secondary Contact:
John D Lindstrom, Stockholm +46 8 4405 927; john_lindstrom@standardandpoors.com

Table Of Contents

Summary:
Fingrid Oyj

Credit Rating:	AA-/Negative/A-1+

Rationale

The ratings on Finnish transmission system operator (TSO) Fingrid Oyj reflect the company's stand-alone credit profile (SACP), which Standard & Poor's Ratings Services assesses at 'a'. Our view of Fingrid's SACP is based on its excellent business risk profile and significant financial risk profile. The ratings also reflect our opinion that there is a "high" likelihood that the Republic of Finland (AAA/Negative/A-1+) would provide timely and sufficient extraordinary support to Fingrid in the event of financial distress.

Fingrid's business risk profile is underpinned by its strategic position as the electricity TSO in Finland. It further reflects Fingrid's strong record of network efficiency, Finland's favorable cost-plus regulatory regime, and the company's clear strategic focus on the national electricity transmission network and enhancement of the Nordic electricity market. Relative weaknesses, in our view, are modest exposure to short-term volume risk and low returns on capital across the industry. Fingrid's financial risk profile is constrained by relatively high leverage and low debt-service coverage ratios. These weaknesses are partly mitigated by the company's access to a diverse funding base and an extensive hedging policy.

The long-term ratings receive two notches of uplift, in accordance with our criteria for government-related entities (GREs). Our view that there is a "high" likelihood of extraordinary government support is based on our assessment of Fingrid's "very important" role for and "strong" link with the Finnish government, reflecting the Finnish state's majority ownership.

S&P base-case operating scenario

Fingrid increased its tariffs by an average of 30% at the beginning of 2012, the start of a new four-year regulatory period. This increase, coupled with additional, albeit smaller, tariff increases in the coming years, should bring Fingrid's annual return on capital closer to the return allowed by the regulatory framework. In the previous regulatory period (2008-2011), Fingrid undercharged its customers by about €250 million compared with what was allowed under the regulatory framework. This deficit resulted from Fingrid's previous ownership structure prior to April 2011, since its largest owners were also its largest customers.

In our base-case operating scenario, we predict that the current regulatory framework, in place since 2005, will not undergo major changes. This should add stability and predictability to the company's underlying earnings, in our view. However, we note that in 2011, revenues from the sale of imbalance power--used to cover periods of peak demand--decreased as a result of lower electricity prices during these periods. Fingrid is responsible for managing Finland's imbalance power, and therefore collects revenues through the sale and purchase of imbalance power. This can also lead to short-term fluctuations in revenues, as evidenced in the first nine months of 2012. In addition, there was a decrease on the cross-border income between Finland and Russia during this period, although this was partly offset by an increase in congestion income between Finland and Sweden. Fingrid is, however, allowed to adjust its tariff for these fluctuations.

S&P base-case cash flow and capital-structure scenario

Fingrid initiated an ambitious €1.7 billion investment plan for the period 2011-2022, which includes enhancement of the transmission grid, strengthening of cross-border connections, and investments in reserve power. In the 12 months to Sept. 30, 2012, its capital expenditure was about €176 million. Noteworthy projects were the completion of the Fennoskan 2 interconnector to Sweden and the initiation of the Estlink 2 interconnector to Estonia. We believe that Fingrid's investments will remain high over 2012 and 2013, but will gradually decline thereafter.

We believe that Fingrid's funds from operations (FFO) will increase in 2012 and beyond as a result of tariff increases. This should mitigate the cost of its sizable investment program and likely increasing dividends in light of the ownership change in 2011. We therefore estimate that discretionary cash flows (cash flows after investments and dividends) will be slightly negative in the coming years. We anticipate that Fingrid will fund part of its investments with additional debt, which will likely add slightly to the €1.25 billion debt the company had outstanding at the end of September 2012. However, as a result of increasing FFO, but only slightly increasing debt, we expect the FFO-to-adjusted-debt ratio to improve gradually to 13%-15% over the next few years, a level we consider commensurate with the current SACP. This compares with about 10% in 2011. We adjust Fingrid's reported debt for operating lease commitments of about €20 million, and for surplus cash, which was €230 million at the end of September 2012, after excluding €15 million from the company's reported cash and equivalents.

Liquidity

The short-term rating is 'A-1+'. We view Fingrid's liquidity position as "adequate" under our criteria and calculate that liquidity sources will comfortably exceed liquidity uses by more than 1.2x over the next 12 months.

As of Sept. 30, 2012, we estimate Fingrid's liquidity sources at above €600 million including:

- Cash and marketable securities of €245 million;
- Access to an undrawn committed revolving credit facility of €250 million expiring in April 2017; and
- FFO in 2012 likely in excess of the €108 million in 2011.

We estimate Fingrid's liquidity needs over the next 12 months to be above €400 million, comprising:

- Debt maturities of €194 million
- Investments in excess of €200 million; and
- Dividends in excess of the €11 million for 2011, paid out in 2012.

The existing credit agreements do not contain financial covenants or material adverse-change clauses, to our knowledge.

We will continue to closely monitor Fingrid's liquidity policies and funding plans in light of the large investment program. At the current rating level, we assume Fingrid will maintain a prudent approach to liquidity management and prefunding of capital expenditures. We expect that Fingrid will continue to enjoy good access to the capital markets and fund most of its investments with longer-dated bonds.

Outlook

The negative outlook on Fingrid reflects that on Finland, indicating that we could lower the ratings on Fingrid by one notch if the ratings on Finland were lowered by one notch. These potential actions are in accordance with our rating methodology for GREs. A revision of the outlook on Finland to stable would likely lead to a similar rating action on Fingrid.

We anticipate that Fingrid will remain strategically important to the Finnish government as Finland's monopoly TSO and that there will be no material changes in ownership in the near to medium term. For the current SACP, we anticipate the ratio of FFO to debt remaining higher than 10% in the near term, improving toward 12% in 2013, and to 13%-15% from 2014 and thereafter.

We could raise the ratings if we saw a higher likelihood of government support for Fingrid, for example if the link between Fingrid and the Finnish government were to strengthen. Conversely, we could lower the ratings if we perceived a weakening of the likelihood of extraordinary state support, for example in the event of an unexpected dilution of the government's ownership stake.

In line with our methodology for GREs, we could take a negative rating action if Fingrid's SACP weakened to 'bbb+' or lower. Although unlikely at this stage, this could result from a major regulatory overhaul, a change in the group's financial policies, an unexpected shortfall in liquidity, or a significant deterioration of Fingrid's credit measures and financial risk profile.

We believe that ratings upside is very limited over the medium term, as it would require an improvement of Fingrid's SACP to 'aa-', all else being equal. We consider such a scenario unlikely, owing to the group's significant investment program and relatively high financial leverage.