MOODY'S
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Credit Opinion: Avinor AS

Global Credit Research - 08 Feb 2016

Norway

Ratings

Category	Moody's Rating
Outlook	Stable
Issuer Rating -Dom Curr	A1
Senior Unsecured	A1

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Key Indicators

[1]**Avinor AS**

	12/31/2014	12/31/2013	12/31/2012	12/31/2011
(FFO + Cash Interest Expense) / (Cash Interest Expense)	**4.8x**	**4.5x**	**4.7x**	**5.0x**
FFO / Debt	**13.7%**	**15.4%**	**15.3%**	**16.9%**
Moody's Debt Service Coverage Ratio	**4.0x**	**4.4x**	**4.1x**	**4.4x**
RCF / Debt	**11.3%**	**12.4%**	**12.5%**	**13.0%**

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Source: Moody's Financial Metrics

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

- Monopolistic position and modest transmodal competition

- Supportive strategic framework

- Relatively robust traffic growth underpinned by strong passenger volume increases at Oslo Airport and across the Large Airports division

- Significant capital expenditure programme

- Expected increase in leverage

- Likelihood of support from the Kingdom of Norway, should it become necessary

Corporate Profile

Avinor AS (Avinor) is a company that owns and operates a network of airports in Norway, and is the sole provider of air navigation services within Norwegian airspace.

Avinor benefits from a near monopoly position in Norway, accounting for over 90% of Norwegian passenger traffic in 2015. It is currently 100% owned by the Kingdom of Norway.

SUMMARY RATING RATIONALE

Avinor's A1 rating reflects the groups fundamental credit quality, which is represented by (1) a baseline credit assessment (BCA) of a3; and (2) a two-notch rating uplift for the likelihood of extraordinary support being provided by the Kingdom of Norway (Aaa stable) in the event that this were ever to be required to avoid a default, as assessed in accordance with Moody's Government-Related Issuers rating methodology, published in October 2014.

The BCA of a3 reflects (1) the strong business profile of Avinor, on account of its near monopoly position and modest transmodal competition for medium-long distance travel within Norway; (2) a supportive strategic framework established by the State which reflects the importance of Avinor's operations to achieve societal objectives; (3) relatively robust traffic growth underpinned by strong passenger volume increases recorded by the Oslo Airport and Large Airports divisions, which is expected to continue albeit at somewhat lower levels (4) the significant capital expenditure programme which entails investment of approximately NOK20 billion during the period 2013-2017; and (5) an expected move to relatively high leverage.

After a corporate reorganization, Oslo Lufthavn AS was merged into Avinor on 11 January 2016, decreasing the proportion of the Avinor Group debt that is structurally subordinated to indebtedness at its subsidiaries' level from c. 30% to less than 10%. Prior to this reorganisation we did not lower the rating of Avinor to take account of this potential structural subordination because over 75% of the subsidiary indebtedness was provided by the State, the ultimate owner of Avinor and we considered it unlikely that the State, as lender, would seek to benefit from its structural position to the detriment of lenders at the Avinor level. Given the low percentage of group debt provided to Avinor's other operating subsidiaries, we do not adjust Avinor's rating to reflect structural subordination despite the fact that all the remaining debt is from commercial lenders.

DETAILED RATING CONSIDERATIONS

MONOPOLISTIC POSITION AND MODEST TRANSMODAL COMPETITION

Avinor is a limited liability company subject to normal laws, albeit 100% owned by the Kingdom of Norway. It is classified in Norway as a category 4 company on the scale of State-owned enterprises, and is thus viewed as an important entity by the State, on the basis that it fulfils `national sectoral political' objectives. Avinor owns and operates 46 airports in Norway, and its management controls all key aviation infrastructure.

Avinor is the sole provider of air navigation services within Norwegian airspace and has a virtual monopoly of air travel originating and ending in Norway capturing approximately 98% of domestic passengers and approximately 88% of international passengers. International airports in other Scandinavian countries are not readily accessible to the Norwegian population. Whilst other forms of transport are used in the south of Norway, the topography of the country and the large distances between population centres means that air travel is by far the most efficient mode of travel. Fast rail connections are limited to the Oslo region and cover a relatively short distance. The location of Norway on the periphery of Europe means that air travel is largely required when travelling internationally.

The total population of Norway is 5.1 million (as per Statistics Norway). This represents approximately 1% of the total EEA population and ranks as 21st in relative population size. Norway has a very prosperous economy, generating a GDP per capita which is generally ranked within the top 5 countries in the world. The economy is mixed but is heavily dependent on natural resources, most significantly oil and gas but also hydroelectric power and fishing. Approximately 60% of Norway's exports relate to crude petroleum or petroleum gases.

SUPPORTIVE STRATEGIC FRAMEWORK

The Kingdom of Norway, via the Norwegian Ministry of Transport and Communications ("MoTC"), controls 100 percent of the share capital of Avinor. As owner, the State has established that Avinor should operate in such a way as to support the population of Norway in providing a vital form of transport, rather than as a profit maximizer. Nevertheless the State requires Avinor to operate as a commercial entity with management and a Board that comprise experienced commercial professionals, rather than civil servants.

The State also has a role in aeronautical rate-setting, albeit this is governed by a relatively informal process rather than through formal price review and determination processes that operate in other European jurisdictions. The process operates by Avinor management proposing charges in an annual plan which reflects the financial objectives that are outlined in the Ownership Report and the proposed capital investment plans. These charges proposals are then reviewed, presented at a public hearing and ultimately approved by MoTC.

The State requires Avinor to establish a uniform set of aviation charges across its network, which effectively leads to a cross-subsidisation of the marginal rural airports by the more commercially viable larger airports including Oslo, Stavanger, Bergen and Trondheim. From a competitive perspective, management and MoTC also endeavour to set charges at levels that will encourage airlines to develop their route strategies in Norway rather than in nearby competitor countries such as Denmark and Sweden. The State aims to ensure its companies make a fair return on capital employed, although this is not the primary objective of Avinor. Generally, aviation charges have been rising in line with CPI and the recent Ownership Report makes reference to a similar approach for the next four year period.

Although Norway is not an EU member state, the government has transposed the EU's Airport Charges directive. The directive sets out minimum requirements in terms of transparency, consultation with airlines and non-discrimination of charges, and mandates the setting up of an independent supervisory authority. Although the implementation of the directive has introduced some formal changes to the rate setting mechanism, we do not expect it will introduce major changes to the level of charges implied in the Ownership Report.

Strategic objectives are outlined in the Ten-Year Transportation Plan, with specific operational and financial requirements set out in the Avinor Ownership Report. These documents are effectively government policy documents, rather than a formal charter. They set out that the focus for Avinor should be on quality improvements for, and financial returns from, the airport network and air navigation system in Norway. International expansion is limited to developments in air navigation services under the North European Functional Airspace Block.

RELATIVELY ROBUST TRAFFIC GROWTH UNDERPINNED BY STRONG PASSENGER VOLUME INCREASES AT OSLO AIRPORT AND ACROSS THE LARGE AIRPORTS DIVISION

Avinor is regarded as an O&D airport system. Avinor`s proportion of O&D traffic has been above 80% for the last decade. The current proportion of O&D traffic is approximately 83%, which reflects a strong core of traffic and provides for more resilient revenues when compared to transfer traffic.

Over the last decade passenger growth rate has averaged 4.2% per annum across the 46-airport network, whilst growth at the top 4 airports (Oslo, Bergen, Stavanger and Trondheim) has been slightly higher at 4.5% per annum on average.

In addition, compared to most other airports rated by Moody's, Avinor has experienced relatively low volatility of passenger traffic in the last ten years. The standard deviation of the growth rate between 2006 and 2015 was 4.5%.

Traffic declined by 0.25% (or c. 0.1 million passengers) in 2015. Passenger growth started to decline in September 2014, coinciding with a sudden and unexpected fall in crude oil prices, which particularly impacted cities exposed to the oil industry, such as Stavanger, home to Statoil, the largest oil and gas operator in the Norwegian continental shelf, and Bergen. Travel by helicopter to and from oil and gas offshore platforms has been hit by lower levels of activity. Unemployment has also recently climbed to 4.6% of the workforce, a level that is modest by international standards but that represents a 10-year high in Norway and has curtailed discretionary demand for travel. Finally, the anticipated fall in oil revenues for the country triggered a depreciation of the Norwegian Krone, which has lost 28% of its value against the Dollar and 14% against the Euro since September 2014. As the depreciation increases the cost of holidaying abroad, leisure travel has also been impacted. As a consequence, the network sawsome modest year on year traffic declines in the first few months of 2015 with traffic in the first 6 months of the year down 1.5% compared with the same period in 2014. Whilst traffic started to grow again in the second half of the year (+0.9% compared with the same period in 2014) and some of that momentum should continue in 2016, particularly at Oslo where airlines are increasing seat capacity, the outlook for 2016 remains uncertain given that oil prices remain depressed and a previously unexpected NOK80 tax on every departing passenger is to be introduced from 1 April.

Avinor's long term growth strategy focuses on supporting international travel by incentivising the development of new direct routes and thus capture some of the more lucrative intercontinental passenger traffic that would otherwise be routed via hubs outside of Avinor's network. The success of this strategy will largely depend on Norwegian Airlines' success with its recently introduced low-cost, long haul product.

SIGNIFICANT CAPITAL EXPENDITURE PROGRAMME

As outlined in the Ten Year National Transportation Plan, Avinor intends to pursue an extensive capital programme during the period to 2023 with approximately NOK24 billion planned for the period 2014-19.

The terminal 2 extension at Oslo airport is by far the most significant and challenging of the individual projects within Avinor's capital programme. The airport is said to be currently operating close to capacity and so expansion works are intended to create an additional 50% in passenger capacity. The works must take place within an operational airport environment which creates additional complexity and a requirement for the works to be carefully phased. In addition, Avinor's Board of Directors approved in March 2014 the NOK 4.2 billion terminal expansion project at Bergen airport, which will almost double the airport's terminal capacity by 2017. Both projects are on track to be delivered on time and within budget.

The other capital projects in the programme are more modest in scope, although in aggregate do represent a sizeable projected expenditure. A number of these are scheduled to commence in future years and so could be deferred by management if the business rationale no longer justified them.

EXPECTED INCREASE IN LEVERAGE

Management has indicated that it intends to pursue a relatively conservative financial strategy, in the context of the requirement to finance the major capital programme. Current debt facility from the EIB contains financial covenants requiring an Equity Ratio (defined as Equity : Equity + Net interest bearing debt) of in excess of 30% and places constraints on Avinor's ability to enter into additional indebtedness. However, Avinor is expected to move to relatively high leverage with its credit metrics (particularly FFO / Debt) experiencing a temporary downward pressure until 2016-17 as they reflect the impact of the increased capital expenditure and lower than expected traffic levels in 2015.

The increase in indebtedness and leverage will be mitigated, however, by the decision to cap dividend payments to NOK500 million, which will allow the company to retain the majority of the proceeds from the planned disposals of non-core assets, such as the recent sale for NOK1.58 billion of a hotel located near Oslo airport, to part fund planned investments.

In addition, there is scope to postpone some of the projects, which are due to start in 2017 and beyond to better align the increase in indebtedness and the company's cash generation.

LIKELIHOOD OF SUPPORT FROM THE KINGDOM OF NORWAY, SHOULD IT BECOME NECESSARY

Moody's categorises Avinor as a Government-Related Issuer ("GRI") as a result of it being wholly owned by the Kingdom of Norway. Moody's therefore applies its Government-Related Issuers rating methodology, published in October 2014. The A1 rating incorporates: (i) our baseline credit assessment of a3 for Avinor, (ii) our sovereign rating of Norway (Aaa stable); (iii) our assessment of default dependence being Moderate (i.e. 50%); and (iv) our assessment of the likelihood of extraordinary support being Strong (i.e. within a range of 51%-70%).

We have assigned two notches of rating uplift from the baseline credit assessment, reflecting the strategic importance of the asset and the recent examples of extraordinary State support including a payment holiday on the State loan provided to Avinor's subsidies, a relaxation of dividend payments in 2009 and 2010 and the recent decision to lower dividend payments to finance capital investments (although we note that Avinor does not receive direct, ongoing State subsidies in contrast to certain other State-owned companies).

Liquidity Profile

In line with other major airport companies, Avinor generates strong operating cash flow throughout the year, albeit with some seasonality because the northern hemisphere summer season generates more cash flow than the winter season. Avinor's projected cash balances and available bank facilities should be sufficient to meet its cash requirements for the next 12 months, and we expect Avinor to maintain good liquidity.

Avinor benefits from a sound liquidity position by virtue of its positive operating cash flows and sizeable undrawn banking lines. The company's current financing strategy is to pursue diversity in terms of sources of credit and to achieve a spread of maturities.

As at 31 December 2015, Avinor had an NOK1.667billion of cash and cash equivalents and NOK4.8 billion of undrawn banking lines. The largest undrawn line of NOK4bn is revolving and subject to utilization conditions and is due to mature in June 2020; additionally a fully available NOK0.8billion revolving credit line due November 2017 is in place. Avinor has around NOK1 billion of borrowings (excluding commercial paper issuance) due within 12 months. Moody's expect capital expenditure in 2016 to be around NOK4.4 billion.

Rating Outlook

The stable outlook assigned to the rating reflects the near monopoly position of Avinor and the strategic importance of Avinor's airport and air navigation operations to Norway.

What Could Change the Rating - Up

Upward rating pressure could develop if (i) material projects within the capital investment programme are successfully completed, particularly at Oslo Airport; and (ii) Avinor's Cash Interest Coverage Ratio was consistently higher than 5.0x and FFO / Debt trending towards 20%.

What Could Change the Rating - Down

The rating could come under downward pressure if (i) the capital investment programme were to experience delay and/or overruns; or (ii) Avinor's Cash Interest Coverage Ratio fell below 4.0x and FFO / Debt ratio declined to below the low teens in percentage terms on a sustained basis. Furthermore, any downwards move in the Kingdom of Norway's credit rating could put downward pressure on Avinor's rating.

Rating Factors

Avinor AS

Privately Managed Airports and Related Issuers Industry Grid [1][2]	**Latest Financial Year ended 31/12/2014**		[3]**Moody's 12-18 Month Forward ViewAs of 2/8/2016**	
Factor 1: Concession and Regulatory Frameworks (15%)	**Measure**	**Score**	**Measure**	**Score**
a) Ability to Increase Tariffs	Baa	Baa	Baa	Baa
b) Nature of Ownership / Control	Aaa	Aaa	Aaa	Aaa
Factor 2: Market Position (15%)				
a) Size of Service Area	Aa	Aa	Aa	Aa
b) Economic Strength & Diversity of Service Area	Aa	Aa	Aa	Aa
c) Competition for Travel	Aaa	Aaa	Aaa	Aaa
Factor 3: Service Offering (15%)				
a) Passenger Mix	Aa	Aa	Aa	Aa
b) Stability of traffic performance	A	A	A	A
c) Carrier Base	A	A	A	A
Factor 4: Capacity and Capital (5%)				
a) Ability to accommodate expected traffic growth	Baa	Baa	Baa	Baa
Factor 5: Financial Policy (10%)				
a) Financial Policy	A	A	A	A
Factor 6: Leverage and Coverage (40%)				
a) (FFO + Cash Interest Expense) / (Cash Interest Expense)	4.9x	A	4x - 4.6x	Baa
b) FFO / Debt	14.0%	Baa	12% - 14%	Baa
c) Moody's Debt Service Coverage Ratio	4.1x	Baa	3.6x - 4x	Baa
d) RCF / Debt	11.5%	A	9% - 11%	A
Rating:				
Indicated Rating from Grid Factors 1-6		A2		A3
Rating Lift	0.0	0.0	0	0.0
a) Indicated Rating from Grid		A2		A3
b) Actual Baseline Credit Assessment				a3

Assigned					

Government-Related Issuer	Factor
a) Baseline Credit Assessment	a3
b) Government Local Currency Rating	Aaa, Stable
c) Default Dependence	Moderate
d) Support	Strong
e) Final Rating Outcome	A1, Stable

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] As of 12/31/2014; Source: Moody's Financial Metrics [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on http://www.moodys.com for the most updated credit rating action information and rating history.

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