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Summary:

SPI (Australia) Assets Pty Ltd.

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Summary:

SPI (Australia) Assets Pty Ltd.

Credit Rating: A-/Negative/--

Rationale

The 'A-' long-term corporate credit rating on Australian-based utility SPI (Australia) Assets Pty Ltd. (SPIAA) is underpinned by the support of the company's ultimate 100% shareholder Singapore Power Ltd. (SP; AA-/Negative/—). However, SPIAA's underlying rating is more consistent with a low-investment-grade rating and reflects the substantial cash-flow contributions from the company's stable regulated and contracted businesses in Australia, and reasonably good-quality assets. Offsetting these strengths are SPIAA's aggressive financial structure (which is distinguished by very weak financial metrics), a concentrated debt profile, and the company's moderate exposure and reliance on unregulated cash flow.

SPIAA is the holding company that owns a portfolio of Australian regulated and contracted utility assets, including those under Jemena Ltd. (A-/Negative/--) and the asset-management business of the former Alinta group. The group's fungible cash flow and the modest amount of A$645 million legacy debt means the credit risk of SPIAA is considered to be equivalent to Jemena. All future new and refinanced debt issuance will be undertaken at the SPIAA level.

Parent support for the 'A-' rating on SPIAA is considered substantial due to a combination of: SP's full operational and board control of SPIAA, the guaranteed syndicated facility, and SP's represented willingness to defer dividends from SPIAA until SPIAA's funds from operations (FFO) interest cover is above 2x. Furthermore, as SP has a substantial presence in the Australian market, we believe SP would support SPIAA well before any "stress event".

SPIAA's strong business profile is bolstered by stable and predictable revenue streams from a diverse asset portfolio. Regulated and contracted utility assets contribute about 85% of EBITDA, with the balance coming the Jemena Asset Management (JAM) business, which predominately provides asset-management services to in-house businesses. Overall, the assets benefit from creditworthy off-takers, with the underlying markets providing consistent incremental demand for throughput over recent years. Furthermore, the asset portfolio is characterized by good condition, wide-spread age, and reliable performance, reflecting in forecast modest demand for replacement capital expenditure in the medium term.

High debt levels and a subpar performance from the JAM business, relative to our expectations, is likely to result in continued weak credit metrics for SPIAA. Also, significant capital commitments until 2010 limit the prospects of any de-leveraging in the short term. SPIAA's debt-to-regulated asset base (RAB) ratio is likely to range 115%-120% over the medium term, incorporating a quasi RAB for the gas pipeline assets and no value contribution from JAM. Notwithstanding overall performance being in line with budget, FFO to debt and FFO interest cover are expected to remain weak at about 5% and 1.5x, respectively, for fiscal 2009. We consider that material improvement in the metrics is dependent on the performance of the JAM business, completion of some pipeline expansion works, and SPIAA's ability to control financing costs.

SPIAA's business strength is exposed to growth in the unregulated JAM businesses. The competitive exposure of

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JAM's contracts and restricted ability to pass-through cost increases to customers is offset to some extent by no material contract cessation before 2011 and JAM's scale and ability to leverage off SP's co-located businesses.

Liquidity

SPIAA's liquidity position is adequate. At the end of January 2009, SPIAA had undrawn bank lines of about A$250 million. To ensure rating stability, we expect SPIAA to be well progressed in managing both the September refinancing of the A$275 million Jemena notes and the renewal of its August 2009 A$150 million of bank lines before the end of April 2009. A review event for the SPIAA's A$3.4 billion syndicated facility will be triggered if the rating on SP falls below 'A'.

The 'AA-' rating on SPIAA's A$3.4 billion three-year unsecured syndicated facility benefits from an unconditional and irrevocable guarantee from SP. The guarantee ranks pari passu with SP's unsecured and unsubordinated debt. SPIAA's other unsecured obligations not covered by the guarantee will have the same credit risk as the 'A-' rating on SPIAA.

Outlook

The negative outlook reflects the negative outlook on the parent. A potential rating downgrade will depend on the circumstances that lead to the resolution of negative outlook on SP and the flow-on effect of the parent's attitude to its offshore subsidiaries. Despite SPIAA's strong business profile, the weakness of SPIAA's financial profile weighs on the company's creditworthiness. Accordingly, a sustained improvement in SPIAA's credit metrics over the medium term will be crucial to stabilizing SPIAA's underlying creditworthiness.

Notwithstanding parental support from SP, material deterioration in SPIAA's credit metrics, aggressive growth of the asset-management business, or any material change to the composition of SPIAA's portfolio could have negative ramifications for the rating. Any upward movement of the rating on SPIAA is unlikely in the near term, given the company's aggressive capital structure and limited upside to the rating on SP.

Please refer to research for Jemena Ltd. (formerly Alinta LGA) on RatingsDirect for a full analysis of the business and financial profiles of SPIAA's operations.

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