

Ellomay Capital Ltd.

Monitoring | August 2021

This credit rating report is a translation of a report that was written in Hebrew. The binding version is the Hebrew version.

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Ellomay Capital Ltd.

Issuer rating	Baa1.il	Outlook: Stable
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Midroog leaves unchanged its Baa1.il issuer rating for Ellomay Capital Ltd. (hereinafter: "the Company" or "Ellomay Capital"). Rating outlook is Stable.

Summary of rating rationale

The rating takes into account, *inter alia*, the following considerations: (1) The Company primarily operates in the renewable energy electricity generation sector, in Israel and world-wide, which is estimated by Midroog to carry medium risk. The risk is primarily due to exposure to regulation in the generation segment and exposure to market prices, in countries in which the Company operates; (2) Acquisitions strategy and project-based financing structure (typically by non-recourse debt), providing fixed rates in long-term agreements, which on the one hand is supportive of the certainty associated with the Company's cash flow, but on the other hand results in slow coverage ratios due to long-term project debt; (3) Barriers to entry into the power generation industry using renewable energy are low in comparison to the power generation industry using fossil power plants, which typically has higher barriers to entry due, *inter alia*, to significant capital investments as well as technology and engineering complexity; (4) The regulatory environment in countries in which the Company operates, alongside long-term agreements for sale of energy with strong end customers, create relative certainty with regard to stability of the anticipated cash flow over the long term; (5) Growth trend typical of the renewable energy sector in Israel and overseas, supported by setting of targets for promotion of renewable energy; (6) The Company's market share and size are small by comparison to the peer group, but we should note that it has grown significantly upon launch of commercial operation of the Talasol project (hereinafter: "**Talasol**"), and is expected to continue to grow over the short to medium term, with commercial operation of other projects in Spain and Italy by end of 2023, along with additional growth potential from material backlog of other PV projects; (7) The Company has relatively low operating margins due, *inter alia*, to the large component of development expenses; (8) Exposure to financial markets, to interest rates and to credit risk of the countries in which the Company operates (Italy, Spain, Netherlands and Israel), as well as exposure to exchange rates, which is partially mitigated by hedging transactions; (9) As of the report date, the Company's operating cash flow is primarily due to Talasol and to PV projects owned by the Company in Spain and in Israel, and the bio-gas projects in the Netherlands. Over the short to medium term, Company operations in the PV sector are expected to continue to grow, with completion of construction of other projects in Spain and in Italy. The completion of Talasol significantly increased the concentration of operations and cash flow from Spain, until the expected completion of a material new project portfolio in Italy; (10) Good revenue generation capacity, due to commercial operation of Talasol, as well as expected improvement upon completion of projects under construction; (11) The Company has a significant multi-year investment program, primarily consisting of construction of the pumped storage project at the Manara Cliff (hereinafter: "**Manara Project**") and another PV project in Spain, which are under construction, and a new project portfolio in Italy. According to the Company forecast, CapEx in 2021-2023 should amount to approximately EUR 500 million, including project financing at project level; (12) The Company's balance sheet leverage as of end of March 2021 was reasonable, but is expected to increase over the short to medium term due to construction of the Manara Project and development of other projects. However, we assume that the Company would balance its leverage by raising capital in conformity with its current needs, as progress is made on its investment plan; (13) Financial policy with regard to holding liquid balances is supportive of the rating, whereby as of March 31, 2021, liquid balances amounted to approximately EUR 105 million, and over the short to medium term, the Company is expected to maintain minimum cash of at least EUR 30-40 million; (14) The Company has good financial flexibility, reflected, *inter alia*, in accessibility to banks and to the capital market; (15) The Company has inferior structure

and cash flow compared to its senior debt for projects owned by the Company.

According to Midroog's baseline scenario, the Company would focus, over the short term, on completion of projects in Spain and Italy, with commercial operation scheduled for 2021-2023, while concurrently making progress on construction of other projects in Israel, Spain and Italy. Based on these assumptions, adjusted EBITDA in 2021 should amount to approximately EUR 20 million, primarily due to commercial operation of Talasol, and in 2022-2023, after commercial operation of other projects in Spain and Italy, this parameter should range between EUR 25-40 million. Moreover, funds from operations (FFO) in these years should range between EUR 15-25 million. Concurrently, the Company's coverage ratios in the coming years are expected to be slow for the rating level, even after operation of Talasol and the other projects on the investment plan due, *inter alia*, to inclusion of project debt to be assumed for the Manara Project. We also assumed that the Company's leverage, as reflected by the ratio of equity to total assets would increase and would range between 21%-25%. Moreover, in accordance with certification by Company management, we assumed that the Company would not distribute dividends to shareholders in years when an extensive investment plan is under way.

Factors which may result in a rating upgrade:

- Significant improvement in leverage and coverage ratios
- Increased diversification of cash flows across high-quality underlying assets

Factors which may result in a rating downgrade:

- Changes to the sector risk profile, including deterioration in the supporting regulatory environment
- Significant deterioration in leverage ratios, financial resilience and debt coverage ratios, compared to Midroog's baseline scenario

Ellomay Capital Ltd. – Key financial data, EUR in thousands

	March 31, 2021	March 31, 2020	December 31, 2020	December 31, 2019	December 31, 2018
Revenues	7,200	1,943	9,645	18,988	18,117
Adjusted EBITDA ¹	2,948	(1,208)	(378)	7,291	8,267
Cash and cash equivalents ²	105,020	66,429	76,719	53,197	39,014
Shareholders equity	123,820	132,919	125,026	107,756	76,957
Gross financial debt ³	334,851	193,198	296,469	178,906	116,035
Total balance sheet	491,647	376,142	460,172	310,172	211,160
Equity to balance sheet	25.2%	35.3%	27.2%	34.7%	36.4%
FFO ⁴	2,351	(1,404)	(1,117)	4,476	7,908

¹ Excludes dividend from Dorad, includes cash flow adjustment with respect to Talmei Yosef financial asset.

² Includes securities and short-term deposits.

³ Excludes reserves for debt service in projects.

⁴ Includes dividend from Dorad, normalized over the years, and cash flow adjustment with respect to Talmei Yosef financial asset.

Detailed main rating considerations

The operating risk profile is medium, benefiting from supportive regulation including renewable energy generation targets and tariff regulation

The Company operates in the renewable energy electricity generation sector in Europe and in Israel, through projects owned by the Company and mostly financed by senior non-recourse debt at project level. Company operations mostly rely on supporting regulation, with a commitment by local electricity / transmission companies and/or by another external party to purchase most or all of the electricity generated by the relevant projects (off-taker) for an extended period, backed by PPA agreements. Consequently, Midroog estimates that the renewable energy electricity generation sector carries medium risk, primarily due to high exposure to regulation in the generation segment and exposure to market prices, in countries in which the Company operates. Furthermore, it appears that regulators (in Israel and in some world markets) are promoting transition to new regulation to promote stronger competition in this segment, with a reduction of infant entity protection provisions. Factors which mitigate this risk are the existence of supportive regulation, accompanied by renewable energy generation plans and targets for the short to medium term, which creates cash flow certainty and transparency, which are appropriate for the rating.

Supportive regulatory framework in areas of operation, based on long-term agreements for sale of energy to high-quality end customers

The Company's core operations involve power generation using renewable and conventional energy in various countries, each with its own regulatory framework for this industry. Energy generation plants constitute vital infrastructure and a key pillar of the energy market, mostly backed by PPA agreements with the local system administrator and, in our opinion, contribute significantly to stability of the Company's cash flow. Most of the Company's revenues are derived from its PV and bio-gas facilities. Revenues from these facilities are based, *inter alia*, on payments from Governmental and private entities, and an impact to the financial robustness of such entities may, directly or indirectly, impact revenues from such operations. In Israel, the renewable energy power industry is defined and fixed over the term of the license, whereas fossil-based power plants are exposed to changes to the generation component. In Spain, revenues from facilities subject to arranged tariff are set for each facility upon connecting it to the power grid, consisting of three components: Operation, investment and Spot prices. In the Netherlands, Company revenues are composed of multiple components, both for gas production as part of the process and for power generation, payment from the supplier for removal of "waste", offset by the price paid to the supplier for sludge removal, and green certificates for production of gas and electricity, which are realized upon sale.

A relatively small portfolio with diversified energy sources and with geographic diversification, with expected continued growth in total MW over the short term

The Company develops, constructs and owns facilities for generating electricity from renewable energy sources. The business model is based on investment in project development and construction, to be repaid out of revenues from sale of electricity to the grid and/or realization of assets owned by the Company, through sale of Company's interest in such facilities. The projects are financed by a combination of equity and debt, provided by bank financing (at project level) and/or public financing (at solo level). The Company has appropriate experience in project financing in Israel and overseas, in co-operation with local and international banking corporations and institutional investors. Currently, the Company is focused on development, financing, construction and operation stages of the projects. In the Israeli market, the Company acquired a 9.4% interest in Dorad power plant, as well as the PV facility at Talmei Yosef. In the Manara Project, the Company operates across the entire value chain of project development, construction, and licensing. In the international market, in 2017 the Company acquired interest in the Talasol project and started development and construction of this project. Total MW generated by

the Talasol project account for over 50% of the Company's total share of its projects. We should note that this percentage is expected to decrease over the short term. Moreover, the Company is currently promoting the development of multiple PV projects in Spain and Italy, some of which are scheduled for commercial operation in 2022-2023, with construction expected to start over the short to medium term.

Relatively small market share, along with diversification of customers with strong financial robustness and large exposure to a single project over the short to medium term

The Company's market share is relatively limited compared to the peer group, with the Company owns Talmei Yosef project, at 9 MW⁵. The Company also owns PV projects of approximately 7.9 MW in Spain, bio-gas projects of approximately 19 MW in the Netherlands and the Talasol project in Spain at 300 MW. As of the report date, Company customers include Israel Electric Company Ltd. (hereinafter: "IEC") as well as local electric authorities in Spain and in the Netherlands, that purchase electricity and gas from Company-owned PV and bio-gas facilities, respectively. In December 2020, the Talasol project started commercial operation, and the Company also signed a hedging transaction for the price of electricity with a leading international energy company operating in more than 40 countries. The hedging transaction covers 80% of total electricity generation of this project, to be sold at a pre-agreed price for a 10-year term, with electricity generated by this project expected to be sold at market price upon the sale date. The hedging agreement stipulates that should the market price drop below the price agreed in the electricity sale agreement, the hedging provider shall pay to Talasol the difference between the market price and the agreed price. Should the market price be higher than the agreed price, Talasol would pay to the hedging provider the difference between the market price and the agreed price. The agreement is expected to hedge most of the risk associated with volatility of electricity prices on the market, by allowing Talasol to ensure fixed revenues for generation of electricity covered by the agreement. This project is expected to account for 40%-65% of EBITDA in the coming years. We believe that the hedging transaction significantly mitigates the large exposure to significant revenues from this significant operating asset.

Significant increase in Company revenues over the short term due to commercial operation of Talasol and over the long term – mitigated cash flow exposure to the Talasol project as other projects are put into operation in Spain and Italy

The Company has been growing in recent years, due to its operating strategy and accelerated project acquisition and development including, *inter alia*, acquisition of bio-gas facilities in the Netherlands and the PV facility at Talmei Yosef and development of additional PV projects in Italy and Spain. In 2020, Company revenues amounted to approximately EUR 10 million, compared to approximately EUR 19 million in 2019 and to approximately EUR 18 million in 2018. Following start of commercial operation of Talasol in late 2020, as well as other projects in Spain and Italy, accounting revenues are expected to increase and in 2021-2023 should range between EUR 40-66 million.

The Company has low operating margins by comparison to the peer group

The Company's operating margin has been eroded in recent years due, *inter alia*, to material project development expenses at Manara, Talasol and the new project backlog in Italy and Spain, and due to low profitability rates at its bio-gas operations in the Netherlands. In 2021-2023, we expect to see material improvement in operating margins due, *inter alia*, to start of commercial operation of the Talasol project, improved operation of the bio-gas projects and reduction in development expenses.

Upward trend in balance sheet leverage in coming years, due to significant project development

The Company operates by holding project companies, whose typical debt structure includes significant leverage between 60%-80%. The Company's balance sheet leverage ratio has been growing in recent years, as reflected by

⁵ As well as a small holding stake of approximately 9.4% of Dorad project (approximately 80 MW).

the ratio of equity to total assets, from 56% at end of 2016 to 25% as of March 31, 2021. This growth trend in leverage is primarily due to acquisition of projects (acquisition of another bio-gas project in the Netherlands) and to new project development (mostly Talasol and the pumped storage project in Manara), which involved material development expenses and increased total debt on a consolidated basis. Under Midroog's baseline scenario, the ratio of equity to total assets in the coming years is expected to range between 21%-25%.

Expected negative free cash flow over the short term, due to material investments in new project construction in Spain, Italy and the Manara Project

In recent years, operating cash flow (CFO) ranged from a negative cash flow amounting to approximately EUR 5.8 million in 2020, to a positive cash flow amounting to approximately EUR 6.5 million in 2018 due, *inter alia*, to changes in working capital and in financing expenses. Upon commercial launch of Talasol, along with other projects in Spain and in Italy, in 2021-2022, current operating cash flow is expected to range between EUR 10-13 million. In 2021-2023, total CapEx of the Company should range between EUR 100-230 million, due to construction of the pumped storage project in Manara and new projects in Italy and Spain. We regard the construction period of large-scale projects in these years to be a risk factor for the Company rating. Delays in commercial operation or increase in project construction budgets may impact the Company rating. Free cash flow (FCF) would be materially impacted in 2021-2023 by construction of the pumped storage project in Manara and other projects in Spain and in Italy, and is expected to be negative in 2021-2023, ranging between EUR 90-200 million. We should note that in 2017-2021 no dividends were distributed and as certified by Company management, no dividend distributions to Company shareholders are expected in the coming years, while the Company is in the midst of a massive investment plan.

Slow coverage ratios for the rating

The Company's coverage ratios deteriorated significantly in 2019-2020 and currently are not appropriate for the rating. This deterioration is due, *inter alia*, to full consolidation of project debt of the Talasol project, which is 51% owned by the Company, to low profitability of bio-gas projects compared to financial debt assumed with respect to these projects and to material development expenses. Moreover, sale of the PV portfolio in Italy in late 2019 resulted in a significant decrease in operating cash flow and in coverage ratios. This is reflected, *inter alia*, in the ratio of debt to FFO, which in 2017-2018 ranged between 17.5-20.8 and was materially weakened in 2019-2020, in light of negligible FFO generated. In 2021-2023, this ratio should decrease to between 23.0-25.0, which is still weak for the rating. We should note that the Company's rapid growth, through development and financing of new projects, significantly slows down its debt coverage ratios, but we expect that as project currently under planning and construction go into commercial operation in the coming years, the coverage ratios should improve significantly.

Policy of holding high liquid balances and appropriate financial flexibility

Throughout its years of operation, the Company has maintained high liquid balances compared to total assets. This reflects the Company policy with regard to maintaining sufficient liquid balances. Currently, it is Company policy to maintain minimum liquid balances of EUR 30-40 million on a consolidated basis, which should reflect principal and interest payments to holders of Company debentures for at least 18-24 months over the coming years. We should note that in conformity with Midroog's baseline scenario, in 2023 the liquidity balance on consolidated basis should be low for the Company's liquidity policy, but in line with policy in recent years, we expect the Company would maintain sufficient liquidity for its operations, which require high liquidity for investments. We believe that the Company's financial flexibility is good, as reflected, *inter alia*, in accessibility to capital and debt markets, as reflected by the capital raised in the first half of 2020 (approximately EUR 22 million), expansion of debentures (Series C) in October 2020 (by approximately EUR 38 million), expansion of debentures (Series C) by approximately EUR 25 million and issuance of convertible debentures (Series D) in February 2021 (amounting to approximately EUR 15 million). The Company is also compliant with the financial covenants to

holders of its debenture series, with large margins. The Company also has low leverage at Company solo level, and the Company should present a ratio of sources to uses ranging between 1.2-1.8 in 2021-2022. However, the Company has exposure to foreign currency at solo level, due to debentures issued and redeemed in the local market in NIS, with material revenues in EUR, further to the strengthening of the NIS and general trend of weakness in EUR in recent years. This exposure should increase due to the effect of material cash flows from the Talasol project and other projects in Spain and Italy. We should note that this exposure is partially offset by hedging transactions.

Other rating considerations

The Company has a subordinated structure and cash flow compared to projects owned by the Company

The Company has a subordinated structure and cash flow, due to holding project companies mostly with senior debt, including significant concentration of expected cash flows from the Talasol project. The underlying assets in these companies, including the cash flows there from, are typically pledged by a first-ranked lien to senior debt lenders. Moreover, distribution of retained earnings from the project companies is subject to compliance with distribution conditions.

No dividend distributions over the short to medium term

According to the Company, it is not expecting to distribute dividends in the coming years, while the Company is in the midst of a massive investment plan. We believe that this certification by Company management reduces the uncertainty associated with sources for debt service and is supportive for the Company rating.

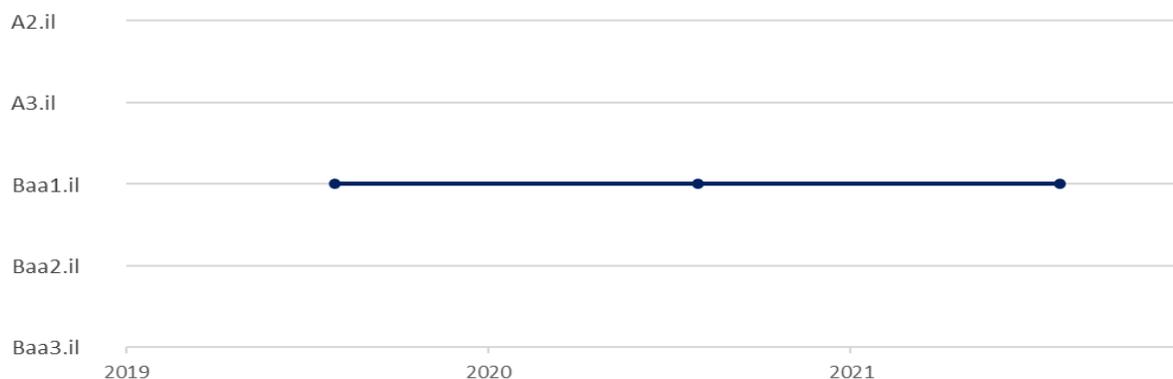
Company profile

Ellomay Capital Ltd. is engaged in development, construction, operation and holding of power generation plants using renewable energy and conventional technologies, in Israel and in Europe. Since 2009, the Company business is focused on energy and infrastructure. The Company was incorporated in 1987, its shares are traded on the stock exchange in New York (NYSE American) since 2011, and is also traded on the Tel Aviv Stock Exchange (TASE) since 2013. The Company's primary operations involve power generation from renewable energy sources – the Company owns power generating facilities using PV technology⁶, and this segment currently accounts for most of its revenues. As part of these operations, the Company owns PV facilities with a total capacity of 307.9 MW in Spain, including the Talasol project, a PV facility with a capacity of 300 MW in Telavan, Spain which, as of the report date, is 51% owned by the Company, and a 9 MW PV facility in Israel; the Company also owns 3 bio-gas facilities in the Netherlands with a capacity of approximately 18 million m³ gas (equivalent to approximately 19.0 MW); the Company also holds approximately 9.4% in Dorad Energy Ltd. (hereinafter: "**Dorad**"), one of the largest private power plants in Israel, with power generation capacity of 860 MW. The Company is also promoting a pumped storage facility at Manara Cliff, with a capacity of 156 MW, which is approximately 83.84% owned by the Company. Currently, the controlling shareholders of the Company are Shlomo Nehama, Chairman of the Company (27.95%⁷), Kanir Limited Partnership (20.3%), whose General Partner is controlled by Ran Fridrich, who also serves as CEO of the Company, and Ms. Anat Rafael and the estate of the Late Mr. Menachem Rafael (1.98%). These controlling shareholders hold approximately 50.2% of Company shares.

⁶ Photo-voltaic.

⁷ Through S. Nehama Investments (2008) Ltd. and directly.

Rating history



Related reports

[Ellomay Capital Limited – Related Reports](#)

[Methodology report for rating of electricity companies and providers operating in markets with no arranged tariff, July 2020](#)

[Rating of fossil power stations and renewable energy – Methodology Report, February 2018](#)

[Rating financing for construction and operation of projects and infrastructure – Methodology Report – February 2018](#)

[Adjustments to financial statements and presentation of key financial benchmarks for corporate ratings – Methodology Report, May 2020](#)

[Table of affinities and holdings](#)

[Midroog's rating scales and definitions](#)

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General information

Rating report date:	August 5, 2021
Most recent rating revision date:	August 3, 2020
Initial rating issue date:	August 29, 2019
Rating initiated by:	Ellomay Capital Ltd.
Rating paid for by:	Ellomay Capital Ltd.

Information from the issuer

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B.il	Issuers or issues rated B.il are those that, in Midroog judgment, have relatively very weak creditworthiness relative to other local issuers, and involve significant speculative characteristics.
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