

Japan Credit Rating Agency, Ltd. (JCR) announces the following credit rating.

JCR's Rating Viewpoints on City Gas Companies

JCR has reviewed its ratings on city gas companies and announced the results. The following are JCR's main rating viewpoints on the review of them. Please refer to JCR's press release 17-D-0054 to 17-D-0059 for ratings of individual city gas companies.

Rating Viewpoints

- (1) JCR reviewed its ratings on 5 city gas companies (OSAKA GAS CO., LTD., TOHO GAS CO., LTD., HOKKAIDO GAS CO., LTD., HIROSHIMA GAS CO., LTD. and SAIBU GAS CO., LTD.) and affirmed all of their ratings with Stable outlook. JCR also assigned afresh a rating to TOKYO GAS CO., LTD.
- (2) JCR, in its rating for city gas companies and other public utilities, places emphasis on their stable business bases under the government's regulation and protection. As such, major attention is being focused continually on progress of gas system reform, and it is necessary to watch for the time being impact from full liberalization of retail city gas market that was implemented in April 2017. The trend of new entry to city gas' retail market significantly differs depending on regions, but there have been few new entrants due partly to a high barrier to entry as compared with electricity. However, it should be noted that major electric power companies, which are highly competitive in LNG procurement, will constitute major new entrants. In the field of already liberalized large-volume users, competition will intensify with deregulation of double construction of pipelines.
- (3) In city gas business after full liberalization of retail city gas market, a certain shift of existing customers to new entrants cannot be avoided mainly in areas where competition with those new entrants including major electric power companies is expected to advance, increasing the substantial downward pressure on gas rates for the time being. Given that the falling into price competition might impair the city gas companies' earnings bases, however, JCR will watch to what extent they can reduce the shift of existing customers to new entrants through measures including leveraging its strength of having contacts with customers, enhancement of set menus of electricity and gas, and offering value added services. Impact of slide time lag, which has been a factor for an increase of profit, was almost eliminated by rise of crude oil price, and this may turn into a factor for a decrease of profit. Under these circumstances, differences among city gas companies in business portfolio and growth strategies may lead to a wider gap among them in profits.
- (4) While the 3 major city gas companies have different stances on investments, it is highly likely that they all will make a high level of capital investment for the time being at least. JCR sees, however that the impact on financial structure will be limited in general thanks partly to an increase of equity capital through income accumulation. Meanwhile, large capital investments by city gas companies other than the 3 major companies are peaking out, but their initiatives for power generation business including projects under consideration need to be carefully watched. Following full liberalization of electricity and city gas retail markets, conversion into an integrated energy company is a challenge for all city gas companies in common, but there are differences among them in detailed policies on electricity retail and their own electric power developments. Many alliances across industries may be realized in the new competitive environment with less regulations. JCR will pay attention to measures to be taken by city gas companies.

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