

Tear Sheet:

# Vattenfall AB

December 5, 2024

**In our view, Vattenfall should be able to maintain its strong credit ratios on the back of divestments, and further supported by our expectation of higher achieved power prices.** We now expect the ratio of funds from operations (FFO) to debt to increase to about 35%-40% in 2024, from 26% in 2023 and that FFO to debt will also remain above 35% in 2025 and 2026.

**Divestments in 2024 related to the Norfolk Offshore Wind Zone in the U.K. and Nordlicht 1 and 2 and heat activities in Berlin, totaling around SEK36 billion.** These have strengthened Vattenfall's financial ratios in 2024, after a temporary weakening in 2023.

The divestments do not have a material effect on Vattenfall's capital expenditure (capex) in 2024, when we expect capex to reach about SEK30 billion. The divested projects will lead to lower capex in the coming years, by about SEK25 billion-SEK30 billion.

Furthermore, we expect the company's price realization to be higher in 2024; during the first nine months of 2024, achieved power prices stood at €42/MWh compared with €35/MWh in the same period in 2023. The improvement in achieved prices, compared to last year, was mainly driven by hedge effects, and lower price differences in between zones.

For 2025, the group has hedged 52% of expected output at €48/MWh, which supports our view of continued robust cash flow from its generation segment. That said, Nordic system prices have softened remarkably in 2024, with the average NordPool system price at about €31/MWh. Price volatility has increased. Given more wind generation in the asset mix in the Nordics, we expect price volatility to remain high.

**Capex will shape credit ratios in 2025-2027.** Despite the temporary decline in investments in 2024, we view Vattenfall's investment program as ambitious and likely to be the main driver of its credit ratios in 2025-2027. The strategy for 2024-2025 points to SEK65 billion of investment, already a historical high. In the coming period, we expect investments will increase further such that FFO to debt approaches the group's financial policy range of 22%-27%. We believe the wind segment will remain the largest focus area--Vattenfall has guided about 45% of growth capex for 2024-2025--followed by investment in distribution assets (16%). As the largest nuclear operator in Sweden, we view Vattenfall as particularly well positioned to participate in the Swedish government's ambitions to have two new large nuclear plants constructed by 2035. Realistically, a financial investment decision is a few years away and therefore is not part of our current base case. However, even if Vattenfall takes only a minority stake in such a mega project, its capex needs would increase significantly.

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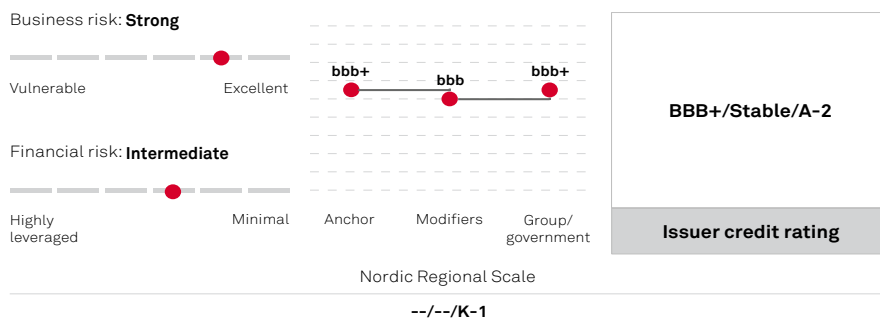
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**Margin call movement continues to create volatility in credit ratios.** Vattenfall received about SEK20 billion in margin calls during the first nine months of 2024 as a consequence of increasing prices on natural gas, mainly used in its German and Netherlands operations. We expect that fluctuations will continue over the winter because of high seasonal gas price movements. These large margin call movements stem from power and gas hedging and trading, and result in fluctuations in reported and S&P Global Ratings-adjusted debt. Volatility in the price of underlying commodities, such as natural gas, creates short-term volatility for Vattenfall’s debt and liquidity ratios. That said, in our analysis we assume that margin calls will be neutralized over time as Vattenfall takes delivery of the gas it has purchased.

## Ratings Score Snapshot



## Recent Research

- Sweden , Oct. 28, 2024
- Vattenfall , July 4, 2024

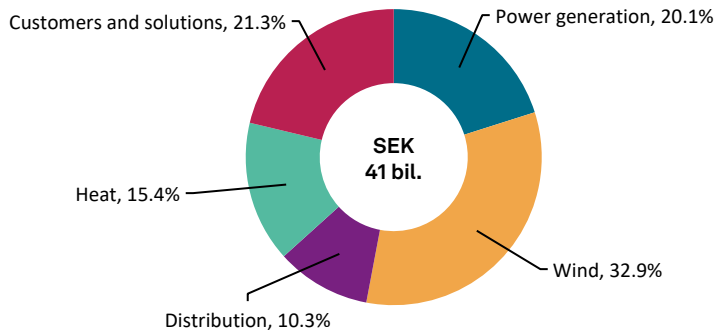
## Company Description

Vattenfall is one of the largest electricity and heat producers in Europe. The company is fully owned by the Swedish government. The majority of its earnings are derived from hydro, nuclear and wind electricity generation, but other activities include regulated DSO and heat activities, and customer solutions including retail.

The Sweden-based company generated about 100.9 TWh of electricity and sold about 13.5 TWh of heat in 2023. At year-end 2023, the company reported sales of about SEK290 billion, up from SEK240 billion in 2022, and adjusted underlying EBITDA of about SEK41 billion.

## The majority of Vattenfall's earnings is from electricity generation

Underlying EBITDA breakup by operating segment for 2023



Vattenfall's hedging related to electricity generation is accounted in power generation. Source: S&P Global Ratings. Copyright © 2024 by Standard & Poor's Financial Services LLC. All rights reserved.

## Outlook

The stable outlook reflects our assumption that Vattenfall's share of EBITDA from regulated operations will be at least 15%-20% over 2024-2026, excluding subsidized wind. If the share of regulated earnings is diluted further, we believe that this risk to increase earnings volatility. At the same time, Vattenfall's generation fleet is expected to produce almost 100TWh annually. We forecast FFO to debt to increase to about 35%-40% in 2024, from 26% in 2023, and FFO to debt to also remain above 30% in 2025 and 2026.

We also expect continuity in the company's relationship with its owner the Swedish government.

### Downside scenario

We believe downside risk is currently remote. We could lower the rating if we believe Vattenfall's position in the power generation business is weakening; for example, if realized power prices are lower than expected or if the expansion into renewables weakens the group's profitability. These factors could have negative financial consequences for the company and, unless countermeasures are implemented, lead to weaker credit measures, such as prolonged FFO to debt of about 25%.

We could also downgrade Vattenfall if government support weakens, for example if the government privatizes a significant part of its stake. However, we consider this unlikely over the next few years.

Aggressive investments in nuclear power, without tangible support or risk-sharing by the Swedish government, could also exert downside pressure. Although discussions about nuclear power generation have increased, and the government has stated its intention to implement strong incentives, we believe any tangible investment is unlikely within the next few years.

### Upside scenario

We could upgrade Vattenfall by one notch if we conclude that:

## Vattenfall AB

- The company's financial risk profile has sustainably strengthened, with FFO to debt of about 30% and sufficient visibility on the long-term debt trajectory; and
- Management has a clear commitment to keep a strong financial risk profile. This could occur if the current headroom is not consumed by additional capex as expected, potentially due to a lack of meaningful and profitable projects to invest in.

We could also raise the rating by one notch if the relationship with the government strengthens, potentially through changes to Vattenfall's ownership directive.

## Key Metrics

Period ending	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025	Dec-31-2026
(Mil. SEK)	2022a	2023a	2024e	2025f	2026f
Revenue	239,644	290,168	180,000-200,000	215,000-235,000	210,000-230,000
EBITDA	48,107	40,857	43,000-48,000	51,000-56,000	50,000-55,000
Funds from operations (FFO)	40,293	31,894	29,000-34,000	35,000-40,000	35,000-40,000
Interest expense	5,236	564	4,000-5,000	4,000-5,000	4,000-5,000
Capital expenditure (capex)	24,765	40,695	25,000-35,000	35,000-45,000	20,000-30,000
Debt	75,154	121,251	85,000-95,000	95,000-105,000	90,000-100,000
<b>Adjusted ratios</b>					
Debt/EBITDA (x)	1.6	3.0	1.8-2.2	1.7-2.1	1.6-2.0
FFO/debt (%)	53.6	26.3	35-40	35-40	35-45

## Peer Comparison

### Vattenfall AB--Peer Comparisons

	Vattenfall AB	Fortum Oyj	CEZ a.s.	Statkraft AS	Orsted A/S
Foreign currency issuer credit rating	BBB+/Stable/A-2	BBB+/Stable/A-2	A-/Stable/--	A/Stable/A-1	BBB/Stable/A-2
Local currency issuer credit rating	BBB+/Stable/A-2	BBB+/Stable/A-2	A-/Stable/--	A/Stable/A-1	BBB/Stable/A-2
Period	Annual	Annual	Annual	Annual	Annual
Period ending	2023-12-31	2023-12-31	2023-12-31	2023-12-31	2023-12-31
Mil.	SEK	SEK	SEK	SEK	SEK
Revenue	290,168	74,598	151,374	102,776	118,200
EBITDA	40,857	21,276	57,662	42,982	19,565
Funds from operations (FFO)	31,894	13,695	27,573	16,559	9,108
Interest	564	3,913	4,459	2,050	7,130
Cash interest paid	4,267	2,534	2,948	1,210	6,405
Operating cash flow (OCF)	(24,411)	19,008	61,691	8,717	42,173
Capital expenditure	40,695	6,403	19,942	8,966	56,975
Free operating cash flow (FOCF)	(65,106)	12,605	41,749	(250)	(14,802)
Discretionary cash flow (DCF)	(70,035)	3,524	6,903	(17,321)	(24,286)

**Vattenfall AB--Peer Comparisons**

Cash and short-term investments	48,704	46,497	7,897	44,718	59,008
Gross available cash	48,704	46,497	7,897	44,718	59,008
Debt	121,251	19,401	117,422	13,972	102,611
Equity	149,923	94,473	110,521	143,387	101,771
EBITDA margin (%)	14.1	28.5	38.1	41.8	16.6
Return on capital (%)	9.9	16.0	18.9	28.8	3.5
EBITDA interest coverage (x)	72.4	5.4	12.9	21.0	2.7
FFO cash interest coverage (x)	8.5	6.4	10.4	14.7	2.4
Debt/EBITDA (x)	3.0	0.9	2.0	0.3	5.2
FFO/debt (%)	26.3	70.6	23.5	118.5	8.9
OCF/debt (%)	(20.1)	98.0	52.5	62.4	41.1
FOCF/debt (%)	(53.7)	65.0	35.6	(1.8)	(14.4)
DCF/debt (%)	(57.8)	18.2	5.9	(124.0)	(23.7)

**Rating Component Scores**

<b>Foreign currency issuer credit rating</b>	<b>BBB+/Stable/A-2</b>
<b>Local currency issuer credit rating</b>	<b>BBB+/Stable/A-2</b>
<b>Business risk</b>	<b>Strong</b>
Country risk	Very Low
Industry risk	Moderately High
Competitive position	Excellent
<b>Financial risk</b>	<b>Intermediate</b>
Cash flow/leverage	Intermediate
<b>Anchor</b>	<b>bbb+</b>
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Negative (-1 notch)
Liquidity	Adequate (no impact)
Management and governance	Neutral (no impact)
Comparable rating analysis	Neutral (no impact)
<b>Stand-alone credit profile</b>	<b>bbb</b>
Related government rating	AAA
Likelihood of government support	Moderate (+1 notch from SACP)

**Related Criteria**

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019

## Vattenfall AB

- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Unregulated Power And Gas Industry, March 28, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

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