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Q1 2023 Vattenfall AB Earnings Call

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CORPORATE PARTICIPANTS

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Anna Borg *Vattenfall AB (publ) - CEO & President*

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PRESENTATION

Andreas Regnell *Vattenfall AB (publ) - Senior VP & Head of Strategic Development*

Welcome to Vattenfall and this Q1 reporting webcast. I'm Andreas Regnell and by my side, I have, as usual, our CEO, Anna Borg, and our CFO, Kerstin Ahlfont. We will today go through the main events and the financial performance of the last quarter. After the initial discussion, we will open up for questions on the phone and online. And as usual, our customary financial reporting material is available on the web. Let's begin.

Anna, I think it's fair to say that this quarter has been slightly less dramatic than the previous ones. Is that correct?

Anna Borg *Vattenfall AB (publ) - CEO & President*

Yes, you are right. We see that the prices are a bit lower, and we also see that the volatility is lower than it was last year. So that's good. It sort of calmed down the market a bit. But fundamentally, nothing has changed. So I would say that the uncertainty is just as high as ever.

Andreas Regnell *Vattenfall AB (publ) - Senior VP & Head of Strategic Development*

And what has it meant for us?

Anna Borg *Vattenfall AB (publ) - CEO & President*

Well, it has meant that we didn't have to spend as much time managing urgent market movements and situations, so we could fully focus on delivering our strategy, which means keep investing in new fossil-free electricity production, but also in upgrading our grids and taking care of our customers. So that's good. We can also see that we have a stable financial performance. That's also good because this high investment pace needs to be kept.

Andreas Regnell *Vattenfall AB (publ) - Senior VP & Head of Strategic Development*

It certainly needs to be. And Kerstin, how would you summarize the financial performance this quarter?

Kerstin Ahlfont *Vattenfall AB (publ) - Senior VP & CFO*

I would say it is a stable development with a bit of a mixed picture between the different operating segments. It's a good contribution from our heat operations, which is offset by a lower result from our wind business due to the lower prices on the continent we have seen.

Andreas Regnell *Vattenfall AB (publ) - Senior VP & Head of Strategic Development*

Understood. Then we will dig much deeper into that later on. Anna, you previously mentioned the continued high level of uncertainty. Can you expand a bit?

Anna Borg *Vattenfall AB (publ) - CEO & President*

Well, we still have a war in Europe. So that is, of course, impacting. That has not changed, and we can see that that will have an impact on the European energy market for the foreseeable future, I would say. The customers are still struggling. We saw a decrease in demand during last year, but the prices are still high, if you look at the sort of historic comparison. Then we had a mild winter, which eased the situation a bit, but the weather is always uncertain, of course. It also means that the gas storages are relatively well filled in Europe, and that is also helping to ease the situation a bit. But again, the uncertainty is high. So it's not over from that perspective.

In addition, there is a discussion around the market regulation on EU level. That's good, because there probably need to be some adjustments, but we also need to make sure that there is a stable long-term framework in order to make it attractive to invest in Europe.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Yes, handling and living with uncertainty is clearly something we need to live with. And on the subject of delivering our strategy. Are there things to mention there?

Anna Borg Vattenfall AB (publ) - CEO & President

Yes, a couple of things happened during the first quarter. We made the decision to move on with the onshore wind farm Bruzaholm, in Sweden, that's 139 megawatts. Then we have a project, which is fairly large scale regarding solar in Germany, which is actually combined with sustainable agriculture. So it's a fairly interesting project from an innovation perspective. Then we also continue the strategic review regarding our heat business in Berlin. We see a very high interest in the business, which I understand. It's a good business. And as we said before, we are planning to make a decision on how to move forward there during the year.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

And on the subject of district heating, we've also acquired a district heating network in Bristol. Haven't we?

Anna Borg Vattenfall AB (publ) - CEO & President

That's correct. The city of Bristol actually have ambitious targets and have set out to be net zero by 2030. We are now going to manage the district heating system, and we're going to use a lot of residual heat, waste heat in order to be able to phase out the fossil fuels. And I think another piece of positive news is that Ringhals 4 is back and up and running fully again, and that's really good. And I would like to come back to the topic of nuclear later.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Yes. So clearly, some progress on the strategy front also this quarter?

Anna Borg Vattenfall AB (publ) - CEO & President

Yes.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Financial reports, Kerstin.

Kerstin Ahlfont Vattenfall AB (publ) - Senior VP & CFO

Yes. And as I said earlier, we see a bit of a mixed picture between the different operating segments, which again then shows the benefit of being an integrated and diversified company. But if you look at the combined financial development that is stable and the underlining operating profit is flat between the years. And if you look at net profit, that is going up with SEK 5.8 billion, mainly due to a good contribution from the nuclear waste fund, where we saw a negative development last year. And we also have a positive outcome from the changes in fair values of energy derivatives and inventories. And you might remember that we in the fourth quarter last year had a significant negative impact from fair values. But this quarter, we've seen our positive impact as contracts go into realization.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Yes. So large temporary effects as usual. This is something we spent quite some time on the last quarterly reports. Maybe you want to kind of mention a bit more on that.

Kerstin Ahlfont Vattenfall AB (publ) - Senior VP & CFO

Yes, sure. These are temporary accounting effects, and they have been unusually large and visible these last 18 months due to this very volatile energy market that we have seen. But it's important to say that it's not reflecting the performance of the business, it's rather sort of affected by the market development.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Okay. Thank you. And what can you say about the financial targets?

Kerstin Ahlfont Vattenfall AB (publ) - Senior VP & CFO

Well, the balance sheet is strong. We have an FFO over adjusted net debt at 39.6%, and return on capital employed is at 5.4%. That is below our target of 8%, but that is also a rolling 12-month number. So in that number, we have the significant negative impact from fair values in the fourth quarter last year. So what you really need to pay attention to here is the underlying level. And here, the ratio is at 12.5%.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

In the beginning, you mentioned that there were mixed contributions from our different operating segments. Tell us a bit more.

Kerstin Ahlfont Vattenfall AB (publ) - Senior VP & CFO

Well, I think most striking is the fluctuation we see in the Customers & Solutions segment. There we see a reduction in the number of gas customers both in the Netherlands and in Germany, which in combination with lower average gas consumption is impacting the results negatively. We have actually seen that the gas consumption from our customers on the continent has decreased with 9%, and the electricity consumption from our Nordic retail customers have come down with 13%.

So our customers have really paid a lot of attention to and made a real effort to save energy, which has had a good contribution when it comes to the stabilization of the energy market and has lowered the prices, I would say.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Thank you. And a very interesting observation. Let's move to wind. Another area that has been impacted by extraordinary effects. Anna, why don't you take that?

Anna Borg Vattenfall AB (publ) - CEO & President

Yes, here, we see several impacts. First of all, the lower prices this quarter compared to the same period last year. And as I said earlier, that's mainly due to the warmer weather. That has an impact on parts of our wind portfolio. We have also seen that wind speeds have been a bit lower this quarter compared to the same one last year, which means less volume in our wind production.

On the other hand, we have more capacity up and running because we are building constantly. And we now have a part of Hollandse Kust Zuid up and running, and the remaining part will be finalized during the year. When it's done, it will be the world's largest offshore wind farm. And we, of course, see the impact of this new production in the numbers as well.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

And talking wind. I mean, the reporting is primarily the assets we have already spinning, but we also have a significant portfolio that is before FID. And I think it's important to observe that the investments in renewable has actually gone down in Europe and particularly in the offshore segment, many actors along the supply chain are struggling and turbine orders are actually steeply down. What's your take on that, Anna?

Anna Borg Vattenfall AB (publ) - CEO & President

No, but that is true. And I think it's due to several things. First of all, we have the geopolitical situation that creates challenges when it comes to raw materials and components, but we also see inflation and increased interest rates. So this is sort of pressuring the profitability in all ends, you can say. And you're right, we see a slowdown in investment decisions. During 2022, we saw slightly more than 12 gigawatts of decided new capacity. It actually needs to be 30 gigawatts a year in order to reach the targets set out in EU. So I think that it's really important what these market design proposals will look like and how the market development is as well. But it's important to make Europe attractive for investments again.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Yes. And this is clearly something we probably come back to many times going forward. The difference between the actual speed of investment and the required speed of investments.

And let's look at Heat and Distribution, Kerstin.

Kerstin Ahlfont Vattenfall AB (publ) - Senior VP & CFO

Yes. The contribution from Heat improved due to higher prices for heat, mainly in Berlin. We have had higher prices from the fuel, gas, last year, and that is compensated in the heat price, but that comes with a time delay, and that is what we see the impact from now. We have seen also, when it comes to heat, the slight decline in heat sales, so also the heat customers have made a great effort of actually saving energy this quarter.

And if you look at the Distribution segment, there we see an improvement between the years. And that is mainly due to that we had extraordinary high cost for the transmission grid last year. And that is cost that we, as an operator, need to pay to the TSO, the Transmission System Operator.

But having a robust electricity grid is a prerequisite for this energy transition that you talked about. And we see lots of requests coming in when they want to connect to our electricity grids, not the least from customers who want to install solar panels.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Yes, tremendous growth in that area. And then we also have the Power Generation segment.

Anna Borg Vattenfall AB (publ) - CEO & President

Yes. And here, we see an increased result. And it's a number of things that happened. We have a good trading result. We see less price area differences in Sweden, and we see a higher achieved price for the electricity that we sell, although the prices are lower compared to the same quarter last year. And the reason for this is several. First of all is these price area differences that hit us really hard last year since the prices were much lower in the Nordics where we have a lot of hydro power. So now it's more equal.

But it's also because we are doing hedging. So we sell part of our production at forehand in order to even out these fluctuations. And we have decreased our hedge ratio a bit. We have communicated that before, which is now impacting in a way that we have a lower hedge ratio where the price is set at forehand and slightly more volume that is exposed to the market prices. So it's a combination that makes this achieved price higher.

Then we've also had a lower availability in our nuclear this first quarter compared to the same last year. That is due to Ringhals 4. That was not up and running. It is now, fully, very happy for that. We have continued the feasibility study regarding small modular reactors at the Ringhals site. So right now we're working with some of the investigations needed in order to be able to submit an application at all. We're also talking to the suppliers to see what kind of technology they can offer, when and at what cost.

And then maybe say something about the happenings yesterday where there was a disruption in the grid in Sweden, just north of Stockholm, which has had an impact on 2 of our nuclear plants. So Forsmark 1 and Forsmark 2 went down immediately, they are supposed to. So everything worked the way it's supposed to. And now we're phasing up Forsmark 1 again today, and we are expecting to phase in Forsmark 2 again yesterday.

But I would like to say that even though this was a quite big disturbance in the grid, it could actually be felt in the area of Stockholm, where we could see the lights flickering, et cetera. Immediately there was other power compensating in order to keep the stability in the grid. And here, hydro power is one of the reasons why that was possible, which brings me to something that we announced after the end of the quarter, which is investments in upgrading our existing hydro power. We haven't made the investment decisions yet, but we see projects that could actually add up to 720 megawatts of capacity. So investing in our existing assets and upgrading them is also important on top of growing.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Yes, it certainly is. So if we summarize across the operating segments, a bit of a mixed bag, but overall a stable development.

Yesterday, we had the Annual General Meeting. Any reflections from that?

Anna Borg Vattenfall AB (publ) - CEO & President

It was a good one. We received appreciation from the owner for a good result in 2022 despite a very volatile market. The Board of Directors had proposed a dividend of SEK 4 billion, which was also approved by the owner at the Annual General Meeting. That reflects the strong underlying performance in the business during last year, of course. And then there were 3 new directors elected to the Board of Directors, and we are very happy about that. We welcome them and look forward to work together. There's a lot of important things to do.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Indeed we do. Thank you. This was the end of the initial discussion. And now we open up for questions.

QUESTIONS AND ANSWERS

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Still waiting for questions. Maybe there is someone on the phone. So please raise your hand in that case, so we clearly can -- raise your hand, yes. make yourself known so that we can -- so that we notice you. No question yet. No one on the phone either.

Anna Borg Vattenfall AB (publ) - CEO & President

Crystal clear, apparently.

Andreas Regnell Vattenfall AB (publ) - Senior VP & Head of Strategic Development

Less dramatic quarter led to no questions. We give you another 10 seconds. Still no questions.

That means that I thank you for listening in on this Q1 reporting webcast and welcome you back to the Q2 report. Thank you.

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