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Q3 2024 VATTENFALL AB EARNINGS CALL

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- **Anna Borg** Vattenfall AB - President, Chief Executive Officer
- **Kerstin Ahlfont** Vattenfall AB - Chief Financial Officer, Senior Vice President

PRESENTATION

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Good morning, and welcome to Vattenfall's Q3 reporting webcast, where we'll go through the main events and the financial performance of the first nine months of 2024. As always, I'm your host, Andreas Regnell. And with me in the studio, I have our CEO, Anna Borg.

Anna Borg Vattenfall AB - President, Chief Executive Officer

Nice to be here.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

And of course, our CFO, Kerstin Ahlfont.

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Good morning.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Before we jump into the financial performance and the highlights of the year, let's take a look at some of the main events of the last quarter.

(video starts)

Hello, and welcome to the Q3 report from Vattenfall. This quarter's highlights are related to wind and an important industrial collaboration.

Vattenfall has decided to pause all further development of the offshore wind power project, Swedish Kriegers Flak, until further notice. The reasoning is a combination of several factors, namely low electricity prices, inflation, and lack of connection to the national grid.

Danish offshore wind farms Vesterhav Nord and Syd were officially inaugurated by Danish Minister of Environment, Magnus Heunicke; Vattenfall's Head of Wind, Helene Biström; and Country Manager for Vattenfall Denmark, Anne Mette Traberg. These two almost identical wind farms are located entirely in Danish waters.

Vattenfall and the industrial cooperation Industrikraft have signed an agreement to identify and evaluate the conditions for co-investment in new fossil-free power generation in Sweden. Sweden is expected to need a doubling of fossil-free electricity generation in the coming decades to meet the increased demand for electricity from industry and society to cope with the transition. This applies mainly to indirect electrification of industry, direct industrial electrification, and transport.

Vattenfall and the steel producer Salzgitter are pushing ahead with their joint goal of decarbonizing industrial production processes. A new power purchase agreement, PPA, provides for fossil-free electricity from the Nordlicht 1 offshore wind farm to be available for steel production from 2028. 75 megawatts of connected load from the Nordlicht 1 offshore wind farm outside the island of Borkum will be made available to the Salzgitter Group over a period of 15 years.

(video ends)

Anna Borg Vattenfall AB - President, Chief Executive Officer

Quite a lot of interesting examples, right?

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Yes. And of all the things we heard about, which one stands out the most to you?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Probably that we finalized the Vesterhav project because that adds even more fossil-free electricity generation to our portfolio. It will be an important contribution to energy independence for Denmark, and it's also -- well, it's also benefiting the local community. So I think that would be a good example.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Great to hear. And Kerstin, now that we've seen some of the things that happened during the last quarter and the year, how have we performed financially during the first nine months of 2024?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Well, the overall results for the first nine months of 2024 remain consistent with the trends that we have seen so far this year. We have a slight increase in the underlying EBIT that amounted to SEK19.3 billion compared to SEK15.6 billion last year. And this growth, much like in Q2, is largely driven by efficient Nordic hedges that led to higher achieved prices. But we also have higher generation volumes, both from wind, nuclear, and hydro, and this is offsetting the falling electricity prices we have seen this quarter.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

And all that is regarding Vattenfall's underlying performance, but if we instead take a look at the profit for the period, how has that developed?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Well, we see an improvement in the profit for the period and quite a significant one. In fact, it increased by SEK23.6 billion to SEK28.3 billion. And to understand this increase, it's important to take a couple of parameters into account.

The underlying EBIT has, of course, a positive effect on the net profit. But the two main factors are positive market value changes of the energy derivatives, but also the value creation we have in the wind business, which is resulting in capital gains earlier in 2024. And then the increases, of course, relative also to the results in 2023, and those results were heavily impacted by provisions and impairments we did in the second quarter last year.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

So we continue to improve the bottom line. However, the lion's share of improvements seem to be related to one-off and temporary effects. Isn't that the case?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Yeah, that's correct.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Okay. And how has the financial development during this period impacted our financial targets?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Well, the increased EBIT has a positive impact on our profitability metrics, which is measured by the rolling 12 months return on capital employed, and that amounted to 13.3%, up from 11.5% in the second quarter. So we have an improvement here, and we are, in this quarter, above our minimum target for return on capital employed, which is at 8%. But if we look at the underlying return on capital employed, we are slightly below the 8% target, being at 7.9%, which really emphasizes our effort and needs to focus on profitability also going forward.

And if we look at the closing of Q3, then we see that we do have a solid capital structure, which we measure with the FFO over adjusted net debt, also that on the rolling 12 months basis. And that increased from 40.9% in the second quarter to 46.7% in this quarter, and this increase is largely driven by lower adjusted net debt.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. And before we jump into the development of our operating segments, you mentioned the lower electricity prices this quarter. Anna, could you elaborate a little bit on what has happened there?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Sure. The prices have been lower in all our markets, actually both continental and Europe, approximately 30% compared to last year, both if you look at the nine months and the quarter. In continental Europe, we do see lower gas prices and coal prices, that has an impact, but we've also seen more renewable production, which also has a dampening effect on the prices.

That also then translates into lower prices in the south of Sweden, and in the north of Sweden, we had quite a lot of hydro power. So it's these things in combination that has caused the low prices.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Yes. So the prices have really come down to the levels we saw during 2022. How has that impacted our operating segments?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Well, it does have an impact, and we see this effect in business segments Wind, Customers & Solutions, and in the Power Generation segment. And if you start with the Wind segment, here, we report an underlying EBIT of SEK3.7 billion, which is a decrease of SEK0.6 billion. And this is mainly due to the lower electricity prices that Anna just talked about. But we have also higher generated volumes, both from the Hollandse Kust Zuid wind farm in the Netherlands, as well as the Vesterhav projects in Denmark that we saw in the film earlier, and that has a slight offsetting effect.

And if you look at Customers & Solutions, there, the lower electricity prices have had a negative impact, mainly on the heat and condensing business in the Netherlands. So there, we have a decrease in underlying EBIT, and it amounts to SEK5.7 billion and

come down then from SEK7.6 billion last year.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. And Anna, how was the development in the Power Generation segment?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, naturally, the low prices had quite an impact on our generation assets. So that has a clear negative effect, of course, but we have also done quite a lot of hedges. So sold our production in advance and to good prices, so that has an offsetting effect here.

And then, as Kerstin mentioned, we also have increased volumes in our nuclear production, but we also have more wind volumes due to more assets being up and spinning compared to last year. So all in all, you can say -- or you cannot say -- it is the fact that our underlying EBIT is up by SEK3.8 billion to SEK6.8 billion.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. And if we look at the distribution business, what is development there?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Well, there, we have a positive contribution. The underlying EBIT is up from SEK1.5 billion last year to SEK1.8 billion this year. And that is partly due to increased revenues, but also due to the fact that we last year did a temporary reduction of the electricity grid tariffs in the second half of 2023.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you, Kerstin and Anna, for that. So overall, we have improved our bottom line and we are meeting our financial targets. At the same time, we do see some challenges going forward because of the lower electricity prices. Isn't that the case?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

That's right. And that is why it is so crucial for us to continue to safeguard our profitability so that we can continue to meet our financial targets also in the future.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

And speaking of profitability, or rather lack thereof, was one of the main reasons for our decision to pause the Swedish Kriegers Flak offshore project. Anna, could you elaborate a bit more on why?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Yeah, for sure. And I think we have been quite clear on the challenges there for quite some time when it comes to Swedish Kriegers Flak, which is offshore wind then. And now, we were at a decision point where we could see that this is an unviable investment at this point in time under the current conditions.

It has to do with three factors, which we always look at when we look at these projects. One is, of course, price in the market. But then you need to understand that we look at the prices long term, not only momentarily here and now.

We look at the costs, of course, in relation to what kind of offers we can get from the suppliers. And both these we are quite used to managing in these kind of projects.

And then the third aspect is a grid connection at the reasonable point in sea to a grid. And that is also what is differentiating in the Swedish market compared to other markets where we see offshore coming live. So that's the sort of main reason why we didn't make this investment decision at this point in time.

And I think that there is an increasing concern in general about profitability in the energy transition. And we've seen a lot of discussion around that in media and also a lot of examples being delayed.

And I think it's important to reflect around, first of all, that these kind of major transformations are never straightforward. There will be ups and downs, and timing will be extremely important. So when in time is there a demand for the products and services that you are going to develop and you have to adjust to that pace?

So I think the direction is very, very clear. In order to be competitive in the future, you need to be sustainable and profitable, of course. But the pace is the question mark right now.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Yes. And if we elaborate a bit on that, profitability concerns, both the level of profitability, but maybe also uncertainty about the level of profitability is something that pauses projects or delays targets, et cetera. And ideally, we would like to have very clear policies and requirements for investment.

But if that's not possible, then, of course, Vattenfall needs to learn how to navigate these uncertain times. And how would you say we do that in our day-to-day business?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, we can de-risk in several ways, I would say. One example is the long-term agreement with Salzgitter that we refer to. So to sign long-term corporate power purchase agreements is, of course, a way of offloading the merchant risk and also know what you will get paid for the production in an asset that you are about to build. The contract we signed with Salzgitter in Q3 this year is a 15-year contract, and it is connected to the Nordlicht wind farm that we will build in Germany, but that we haven't started yet.

You can also do partnerships in different ways. We already have the partnership with BASF doing joint investments. And as we heard in the introduction, we now also signed a cooperation agreement with Industrikraft. So the group of Swedish and international companies that we are working with in order to see if there are possibilities to jointly invest into more fossil-free electricity generation in Sweden in that sense.

Then, we also have to support our customers navigating in this transformation by providing products and solutions that enable their decarbonization and sustainability long term. So I would say that the technology is there; it's in place.

We have proven that, for example, when it comes to fossil-free steel and the pilot plant in HYBRIT, where we know the technology is working, the production is up and running, the volumes are already sold. And the next step is, of course, the first step of the transformation of LKAB, who is one of the partners in HYBRIT, that they will do in Malmberget in Sweden. And then we now know that there are uncertainties about the timing for the next step.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. And speaking about mitigating risks and risk sharing, the report for risk sharing when it comes to Swedish nuclear was released by the government in August. What are the conclusions from that you see?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, we really welcome that proposal. It's good because it's needed to have a risk sharing model for new nuclear. And I think there would be some major benefits for Sweden as a country to build new nuclear.

But it is also very, very difficult, if not impossible, to do that on a commercial balance sheet. And that's also what you've seen in the projects built around the world. So therefore, we're very happy about this report now being finalized and the proposal being here. And we look forward to both the dialogue around that, but also the sort of final, more comprehensive proposal that the government will put on the table because they're doing a number of different investigations here. And I have good hopes that that will make it possible for us and others to invest in new nuclear.

We cannot forget, however, that we will need more electricity production also short and midterm. And that's also why we have to continue to build projects like the Vesterhav in Denmark to meet the demand in that time perspective.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. And now when we're through most of the main information sharing, before we conclude, I'd like to ask both of you, what are your main takeaways so far during 2024? And let's start with you, Anna.

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, I think it's the pace of the transition that is very challenging, as we said before. I mean, the direction is very clear. If you're going to be competitive in the future, as an energy company or as an industry, you have to make sure that you are sustainable and you have to find your sort of business models in order to do that in a good way. So the direction is clear, and we also hear that from many companies.

But the pace is the challenge here. So it's about focusing and really capturing the opportunities which are the best ones and be good in timing that. And for us, it is a lot about increasing the supply of fossil-free electricity in a profitable way. So that would be my focus right now. And then it is a bit of a cold season as well, right?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

And I agree. And I think safeguarding profitability is also essential to enable fossil freedom. And if I just take the example of the underlying return on capital employed, where we are not still really meeting the 8% target that we have, that really means that it is crucial to continue to focus on operational excellence as well within the company and increase our efficiency and being very prudent with expenses as well.

Anna Borg Vattenfall AB - President, Chief Executive Officer

I absolutely agree. We need to build an even more robust and an even more competitive Vattenfall.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

A perfect final comment. So on that note, we will wrap up this part of the webcast. And as always, the material is available on our website. And now, we will turn into the Q&A session. And please do not forget to state your name and organization. See you in a few seconds.

QUESTIONS AND ANSWERS

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Welcome back. And let's see what we have as questions here. From Andrew Moulder, welcome. You spoke about PPA, but yesterday, Fortum said it was seeing very little demand for pay-as-produced renewable PPAs. Is that what you're seeing? And what percentage of your PPAs are pay-as-produced?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, I think in general there is quite a good demand for PPAs. The discussion is usually around the pricing and the time, the duration of them, where there is a natural sort of two perspectives, I think, on that, depending on if you're a buyer or a seller.

It's a good question connected to pay-as-produced, because since the renewable assets are volatile in their production, that of course causes risk. So the question is basically who is taking that risk. And I think you can solve that in different ways.

But I agree that the demand for pay-as-produced PPAs are slightly smaller than the demand for PPAs of a different structure. But I think we have a good dialogue around that with all our customers that we have signed PPAs with and that we're discussing with now as well.

I actually don't remember up front exactly how big the share of renewable PPAs that are pay-as-produced that we will have to come back to, unless Kerstin has that on top of mind.

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

No, I don't think that is a number that we are disclosing. But I think our ambition is to close pay-as-produced or potentially pay-as-forecasted. But the baseload PPA is difficult, of course, when it comes to renewables.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

And I think it's fair to say that the demand differs a bit from where you are geographically because I think Sweden is a different market from continental Europe there.

Next question, Camilla Naschert from S&P. Are you seeing significant demand growth from the data center sector in Sweden? Fortum this week laid out the potential for long-term nuclear PPAs with data center operators leveraging lifetime extensions. Do you see similar potential in Sweden?

Anna Borg Vattenfall AB - President, Chief Executive Officer

I think we already see that that market is there. And we also have several of the big data centers located in Sweden already. So I would say that, yes, the demand is definitely there and we see it being big also going forward.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Then we get to Philip Akoto from Energate. Could you give us an update on negotiations surrounding the sale of GASAG? Do you think this will happen?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, we don't give any updates on negotiations for natural reasons, I would say. But it's something that we are discussing. And I think we also communicated that we had an option for the city of Berlin to buy GASAG. But we'll see.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. Second question for Philip. You already talked about Kriegers Flak. What are the financial consequences of stopping this project for Vattenfall? Have there already been PPAs? Is there a realistic chance of relaunching the project?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, maybe on a more general note, and then Kerstin can ask about the exact impact in the books, but we hadn't signed any PPAs for Swedish Kriegers Flak yet. But we had quite a lot of dialogue around possible PPAs for Swedish Kriegers Flak.

And normally, you also make them dependent on the fact that you make a final investment decision. So even if they would have been signed, they would have not come into effect unless we actually make the investment decision. But there was a fairly big interest for that.

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

And when it comes to the financial impacts, we have an impairment in the Q3 closing of SEK345 million related to Swedish Kriegers Flak.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. Maz Plechinger from EnergyWatch, two questions on offshore wind. As Anna mentions, difficulties getting grid connection is what sets the Swedish market apart from others, which seems to have been the case for quite some years. But would you go as far as to say it's futile to develop any offshore wind in Sweden at this moment?

Anna Borg Vattenfall AB - President, Chief Executive Officer

I think that the prerequisites are different from market to market. So I think that maybe it's also natural that the conditions differ a lot. But I think it will be difficult for most offshore wind projects to see a good enough profitability without a grid at sea. And we can also see that where offshore wind has been built is in countries where there is a solution to that.

So basically, I think if you want a lot of energy production at sea, you also need the infrastructure, i.e., the transmission grid. There could be a few products that can do without that. But in general, that's what's needed.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. And now, the second question from Maz, can you share your thoughts on the current Danish offshore wind auction?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Yeah, the prerequisites are changing a bit. So we are looking into the possibility of doing good projects and being profitable at the same time. So we know that the rules are changing a bit, and we're actually looking into what that means for our projects. The ones we've built so far have been in the old regime.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. Next question from Bernd Radowitz from Recharge. You say you halted Kriegers Flak on grid link concerns. Does the Swedish government do enough to provide offshore grid links by 2029-32 through Svenska Kraftnät as it has promised?

Anna Borg Vattenfall AB - President, Chief Executive Officer

Well, I think the dialogue between the government and the TSO, they will have to answer. What we can conclude is that there is no outlook right now for us to have a transmission grid at sea for offshore wind. And that is what determines our sort of investment decision.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

Thank you. Another question from Andrew Moulder, you mentioned that the final decision from the Energy Market Inspectorate for 2020 to 2023. What does that mean for Vattenfall?

Kerstin Ahlfont Vattenfall AB - Chief Financial Officer, Senior Vice President

Well, we got a decision now and we got that the WACC, the weighted average cost of capital, was 3.39% for the regulatory period of 2020 to 2023.

Andreas Regnell Vattenfall AB - Senior Vice President, Head of Strategic Development

That's the answer. Good. Okay. No more questions in the chat.

Thank you so much for joining us today, and welcome back for our full-year Q4 report, if you want, next year. See you then, and bye -bye.

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