S&P Global
Ratings

RatingsDirect®

Research Update:

Uniper SE 'BBB-' Rating Affirmed As Stronger SACP Offsets Declining Need For German Government Support; Outlook Stable

March 8, 2024

Rating Action Overview

- Uniper SE's financial recovery has been faster than we previously expected, partly due to exceptionally strong operating results in 2023 with EBITDA reaching €7.2 billion. We improved our view on the company's financial risk profile to significant from aggressive due to more visibility regarding Uniper's future earnings profile and the cash the company will have to return to the German government under the terms of the support package approved by the European Commission in 2022. We now expect credit ratios will remain very robust over 2024 and 2025 despite our forecast that EBITDA will normalize at €1.5 billion-€2.0 billion in 2024.
- We believe management's decision to restructure Uniper's gas portfolio by diversifying gas procurement sources and shortening contract tenors has reduced operational risk and earnings volatility, and that a rebalanced trading strategy will result in a lower risk of sudden and abrupt margin collateral needs. We therefore reassessed Uniper's business risk profile upward to fair from weak.
- As a result of the improvement in Uniper's business and financial risk profiles, we revised the stand-alone credit profile (SACP) to 'bb' from 'b'.
- We reassessed our view of the likelihood that the government provides extraordinary support to Uniper to high, from very high. We believe the reduced risks related to Uniper's trading activities and Germany finding alternative sources of gas reduce the likelihood that Uniper could pose a systemic risk for the German energy market. Simultaneously, Uniper's rapid financial recovery could accelerate its privatization process of ahead of 2028, when the German government must reduce its ownership to 25% plus one share, according to the support package approved for Uniper by the European Commission.
- We affirmed Uniper's long-term issuer credit rating at 'BBB-'.
- The stable outlook reflects our view that if further improvement to Uniper's SACP occurs as the company continues its path to financial recovery and executes on a strategic plan that improves its long-term business prospects, this would likely be offset by a lower degree of government support. We expect Uniper will operate profitably over 2024 and 2025 and that it

PRIMARY CREDIT ANALYST

Gerardo Leal
Frankfurt
+ 49 69 33 999 191
gerardo.leal
@spglobal.com

SECONDARY CONTACTS

Per Karlsson
Stockholm
+ 46 84 40 5927
per.karlsson
@spglobal.com

Emmanuel Dubois-Pelerin
Paris
+ 33 14 420 6673
emmanuel.dubois-pelerin
@spglobal.com

Beatrice de Taisne, CFA
London
+ 44 20 7176 3938
beatrice.de.taisne
@spglobal.com

will gradually replace the share of merchant activities in its EBITDA by lower-risk contracted cash flows. The stable outlook also reflects expected financial discipline and tighter risk management, which we believe have reduced the risk associated with the group's trading activities; and we interpret the company's financial policy as being commensurate with a funds from operations (FFO) to debt sustainably above 45%.

Rating Action Rationale

We believe Uniper's gas supply business and trading activities are significantly less risky than three years ago, leading us to reassess its business risk profile to fair from weak. Uniper has reduced its gas exposure to around 200 Terawatt hour (TWh) over the medium-term from about 370TWh annual procurement before the crisis. We believe this is positive from a risk perspective, because it has shifted Uniper's position from being a net gas seller (i.e. having a net short position) to a net buyer (a long position) on margin channels. Uniper has also reduced its long-term volume exposure by only entering into new short-to-medium term contracts, which allows it to hedge its sales on back-to-back basis.

Despite the fact that this will likely result in a lower earnings upside compared to the old contract structure, which operated with a share of open gas volumes, we see it as credit supportive because it means that Uniper better matches the customer time horizon and volumes as the transaction closes, locking in a margin on the sale and limiting volume and price risk. An additional supportive factor is that Uniper keeps a customer portfolio dominated (more than 50% of volumes) by municipal utilities (Stadtwerke). These are typically loyal customers, which offer an opportunity for Uniper to bundle power and gas offerings.

Furthermore, on the trading side, we understand management has taken steps to reduce the risk of contingent collateral liabilities, and to better manage liquidity and counterparty risks. Before and during the energy crisis, Uniper was short both gas and electricity on margin channels, so it had to post additional margining collateral to hold its positions on both to the extent those commodities prices increased. Net margining collateral postings burdened Uniper's liquidity needs during the energy crisis, peaking at about €9 billion as of Sept. 30, 2022.

We expect Uniper's rebalanced position--after becoming a net buyer of gas and a net seller in electricity on margin channels--to be an offsetting position in terms of margining requirements, since both commodities are heavily correlated, particularly in Germany. Uniper's trading positions held at the exchange and under bilateral credit support annexes (CSAs) have significantly declined. This further reduces the risk of sudden, unlimited, and mostly one-sided margin calls, like the company experienced during the energy crisis in 2022.

We expect Uniper's business mix will show a higher share of non-merchant activities going forward. Uniper is prioritizing projects aimed at improving its business position, allowing for synergies and commercial feasibility. These projects include converting the site where coal power plants operate to gas-fired power plants (CCGTs or open cycle turbines) under the German Kraftwerkstrategie, which could benefit from stable capacity payments (although the approval of a specific remuneration mechanism is still pending); increasing renewable power generation (low-to-mid single-digit GW-scale by 2030); operating under power purchase agreements (PPA) contracts, feed-in tariffs, or contracts for difference (CfDs); and exploring green gas opportunities. Uniper is also de-risking its Nordic outright power generation portfolio, signing PPAs at more attractive conditions (11 and 15 years). Uniper is targeting a business mix that, over time, will reduce its merchant exposure (volume and price risk).

Today, merchant power generation and trading represent about 70%-75% of Uniper's total EBITDA. We expect EBITDA derived from merchant activities will decline as gas and power prices ease over the next two years and the company's coal capacity is shut down and converted to gas-fired power plants (CCGTs or open cycle turbines), which could be subject to capacity payments for security of supply (i.e. nonmerchant).

However, we see a risk that Uniper's relevance in the German energy market could decline as the country phases away from coal power generation and gas consumption gradually declines. The company historically has derived most of its earnings from segments dependent on these energy sources. Uniper's long-term competitive position will depend on the company successfully decarbonizing its asset mix while meeting the evolving needs of its customers, notably on the industrial segment. We see Uniper preserving its competitive position in a decarbonized energy mix as the company's key challenge, and we believe that the strategic plan could fall short of those ambitions because we see relevant execution risks, such as the reliance on the favorable evolution of a regulatory framework for market capacity payments, the ramping up of a green gas economy and sector-wide permitting issues and increasing pricing competition for new renewable capacity. In addition, Uniper lacks the capital to accelerate investments at the pace of leading European peers. Therefore, Uniper's ability to identify and execute projects that are credit quality accretive for its business is critical.

Our improved view of Uniper's financial risk profile reflects the company's strong operating results in 2023, increased visibility regarding future financial performance, and the clarification of the equity clawback mechanism. Uniper achieved exceptionally strong operating results in 2023, with S&P Global Ratings-adjusted EBITDA of about €7.2 billion. This was partly due to the gas volumes sold before Gazprom interrupted the gas supply, which Uniper was able to procure at lower prices during 2023, and to very strong thermal power generation earnings. We expect strong metrics will extend into 2024 and to a lesser extent in 2025. We treat Uniper's equity clawback payment obligation of €2.2 billion to the government as debt because it is a liability with no future operating benefits for Uniper.

Strong credit metrics and clarity on the clawback mechanism have led us to reassess our view of Uniper's financial risk profile to significant from aggressive. This also acknowledges management's efforts to increase financial discipline, which we believe have reduced the risk of uncapped contingent collateral needs at the group's trading activities. We interpret the company's financial policy targets commensurate with FFO to debt sustainably above 45%. Our assessment captures that over 60% of earnings remain volatile because they structurally depend on power and gas volume and price fluctuations, and as the hedged positions roll-over in 2025 and beyond at lower prices. Based on our estimates, we think this will lead to normalized EBITDA at significantly lower levels than 2023, at around €1 billion- €1.5 billion by 2025 and beyond. Given elevated capital expenditures, above €1 billion annually, we expect negative free operating cash flows (FOCF), potentially weakening credit metrics.

We are revising the likelihood of support we embed in Uniper's rating to high from very high, leading to a two-notch support from the SACP. We believe a financial distress scenario at Uniper translating into a systemic risk for the German energy market has become less likely. There now exist alternative sources of gas to replace Russian piped volumes, and Uniper has reduced its trading risks.

The assessment of the likelihood of extraordinary support by the German government incorporates our view of a gradual, declining transition in Uniper's link to the government, based on our opinion that Uniper's rapid financial and business recovery will likely accelerate the gradual divestment of the government's stake ahead of the 2028 deadline. We expect this process will gradually increase the representation of private capital in Uniper's supervisory board and management, thereby somewhat diluting the link between both entities. This also represents some medium- to long-term uncertainty of Uniper's strategy and financial policy that we will continue to monitor.

This said, we currently believe Uniper remains an important asset of the government because it owns about one-quarter of Germany's gas storage capacity and national supply. We also anticipate the government may keep a 25% plus one share stake in Uniper even beyond 2028, which would highlight the company's relevance for the country's long-term energy objectives.

Outlook

The stable outlook reflects our view that if further improvement to Uniper's SACP occurs as the company continues its path to financial recovery and executes on a strategic plan that improves its long-term business prospects this would likely be offset by a lower degree of government support.

It also reflects our expectation that Uniper's financial headroom will progressively decline as positions hedged at favorable conditions during 2023 at its gas supply and power generation segments gradually roll over, but that Uniper will continue operating profitably on these segments going forward.

It also reflects that Uniper will gradually replace the share of merchant activities in its EBITDA by lower risk contracted cash flows as it executes on its strategic plan. Our stable outlook on Uniper takes into account management's efforts on financial discipline, which we believe have reduced the risk of uncapped contingent collateral needs at the group's trading activities and Uniper's target of FFO to debt sustainably above 45%.

Downside scenario

We expect Uniper's rating will be less resilient to a sudden deterioration in its stand-alone credit profile as the government support we incorporate in the rating progressively declines.

For instance, we could downgrade Uniper if the company were to post an FFO to debt below 30% without any prospects of recovery. Extreme volatility abruptly increasing liquidity needs at Uniper's trading activities would put immediate downside pressure on the rating because it would mean that the remedies introduced by the management to mitigate such risk were insufficient.

Upside scenario

Ratings upside will remain limited over the next two years because we expect German government support will decline if and as Uniper's own credit quality improves.

The ratings upside on Uniper's SACP depends on whether the company can build a track record delivering stable and reliable earnings from its restructured gas portfolio. If Uniper demonstrates it can grow profitably from new investments, this would also contribute to an upside. We view broadly neutral FOCF without sacrificing growth and while preserving FFO to debt above 45% as a necessary but insufficient condition for SACP upside.

We see a risk that Uniper's relevance in the German energy market declines as Germany phases away from coal power generation and as gas consumption declines, since the company historically has derived most of its earnings from segments dependent on these energy sources. Therefore, upside to the SACP hinges on Uniper demonstrating that its strategic plan can preserve the company's competitive position in a decarbonized energy mix.

Company Description

Uniper is an international, diversified energy company that operates in more than 40 countries. Its operations include power generation in Europe, energy trading, and a broad gas portfolio, including long-term gas procurement, sale, and storage. Its core markets are Germany, the U.K., Sweden, the Netherlands, and North America.

As of end-2023, the company owned and operated a well-diversified power generation portfolio in Europe totaling about 22.4 gigawatts (GW), including facilities running on fossil fuels such as gas (8.5 GW), coal (6.2 GW), hydroelectric (3.6 GW), Swedish nuclear (1.4 GW), and other (2.8 GW). On Dec. 20, 2022, the European Commission approved a support package that allowed Germany to take over 99% of Uniper's share capital, after injecting equity in the company and purchasing all of Fortum's shares. The approved package requires Uniper to divest its Russian operations by 2026 (about 9 GW of power generation capacity at Unipro, currently under Russian state administration), its European gas pipeline infrastructure, several thermal power plants, and its North American power business, among other assets. We believe this will reduce its scale of operations initially, but that the proceeds will ultimately be reinvested in the business.

Our Base-Case Scenario

S&P Global Ratings assumptions

- German outright generation hedges: 80% hedged at about €20 per megawatt-hour (/MWh) for 2024 and 70% hedged at €128/MWh for 2025; unhedged generation sold at €75 per MWh in 2024 and €70 per MWh in 2025.
- Swedish outright generation hedges: 65% hedged at about €44/MWh for 2024 and 30% hedged at €42/MWh for 2025; unhedged generation sold at €55 per MWh in 2024 and €50 per MWh in 2025.
- Around 60%-70% of Uniper's earnings remaining exposed to merchant risk, at least until 2025.
- Cash outflow to fulfill public claim from the equity clawback enforced under the support package approved by the EU Comission of about €2.2 billion in 2025, based on Uniper's 2023 provision, although we note that the final amount will depend on 2024 financial performance. We account for the provision as a debt-like obligation until then.
- Declining load factors at Uniper's coal generation coupled with the retirement of Heyden in 2024, the divestment of Datteln IV before end of 2026, and the mothballing of Ratcliffe coal plant in the UK lead to a marked decline of coal-fired generation EBITDA by 2025.
- We expect higher load factors for Uniper's CCGT plants as coal capacity is retired in the country, and the share of renewables increase. However, we expect them to operate at lower prices than in 2022-2023.
- Our base case accounts for limited net margin collateral posted, ranging between +/- €1 billion as gas and power positions roughly even out.
- Divestment of Gonyü in 2024, and Uniper continuing its divestment plan enforceable by the

support package approved by the EU Commission until the end of 2026. Our base case assumes less than half a billion euro for asset divestments spread until that point.

- Capital expenditures of €1 billion in 2024, €1.2 billion in 2025, and €1.7 billion in 2026, of which, we expect investments in green generation (primarily renewable generation), flexible generation and greener gases to be evenly split.
- No dividend distributions.
- Uniper having continuous access to KfW liquidity lines.

Key metrics based on S&P Global Ratings assumptions

Table 1

Uniper SE--Forecast summary*

Industry sector: Energy

	--Fiscal year ended Dec. 31--					
(Mil. €)	**2020a**	**2021a**	**2022a**	**2023a**	**2024e**	**2025f**
EBITDA (reported)	1,685	(4,165)	(10,837)	9,070	1,500-2,000	1,000-1,500
Plus/(less): Other	237	6,662	(292)	(1,809)	0-100	0-100
EBITDA	1,922	2,497	(11,129)	7,261	1,550-2,050	1,000-1,550
Less: Cash interest paid	(123)	(82)	(403)	(451)	(170-220)	(130-180)
Less: Cash taxes paid	(91)	(215)	(345)	(362)	(500-600)	(50-150)
Funds from operations (FFO)	1,708	2,200	(11,877)	6,448	1,000-1,500	750-1,250
Debt (reported)	982	8,230	10,885	922	800	800
Plus/(less): Other	1,944	1,162	(57)	4,656	4,800	2,300
Less: Accessible cash and liquid Investments	(388)	(3,077)	(4,729)	(4,362)	(5,400-5,900)	(2,300-2,800)
Debt	2,538	6,315	6,099	1,216	--	380
Cash and short-term investments (reported)	384	2,966	4,634	4,257	5,400-5,900	2,300-2,800
Adjusted ratios						
Debt/EBITDA (x)	1.3	2.5	(0.5)	0.2	--	0.1-0.5
FFO/debt (%)	67.3	34.8	(194.7)	530.1	NM	>250
FOCF/debt (%)	20.3	46.1	(265.0)	492.1	NM	Negative

All figures are adjusted by S&P Global Ratings, unless stated as reported. *2023 adjusted figures are still work in progress. a--Actual. e--Estimate. f--Forecast.

Liquidity

We view liquidity as adequate as of Dec. 30, 2023, though the company's liquidity needs significantly diminished as power and gas price ease. This led to available sources significantly exceeding expected uses over the next 12 months, well above 2x. However, our assessment is muted by the company's trading activities that still remain exposed to margin collateral, which can prompt liquidity needs unexpectedly. In addition, we believe the company has yet to regain its status in the capital markets, and the company is actively working to diversify its funding sources. Currently, Uniper's committed credit facilities are mostly granted by the German promotional bank KfW. The below liquidity sources and uses assumptions are for the 12 months starting Dec. 30, 2023.

Principal liquidity sources

- €4.38 billion of cash and liquid investments as of Dec. 31, 2023.
- €11.2 billion available credit lines maturing beyond the next 12 months, which correspond to KfW financing and a €1.7 billion syndicated loan.
- Our forecast of cash FFO of about €1 billion.

Principal liquidity uses

- Debt maturities of €617 million over next 12 months.
- Uniper's trading activities remaining exposed to sudden margin collateral needs.
- Capital expenditures of about €1 billion.

We forecast Uniper will have to repay €2.2 billion to the German government during the first quarter of 2025, related to the equity clawback enforced by the support package approved by the EU Commission, which can still vary depending on 2024 financial results.

Covenants

Uniper trading activities are subject to contingent collateral margin calls in the event of a rating downgrade. These have nevertheless significantly declined since 2022.

Environmental, Social, And Governance

We are revising our view of Uniper's management and governance to neutral from moderately negative before. This is because of our opinion that Uniper's updated risk management policies reduce the risk of sudden liquidity needs, and that a diversified gas procurement strategy coupled with shorter contract tenors protects the company against long-term volume and price risks.

Environmental factors remain a moderately negative consideration in our analysis of Uniper. We believe Uniper's business will have to be transformed to ensure its long-term competitiveness, since it currently relies heavily on gas supply and thermal power generation (coal and gas), but Germany intends to phase out gas consumption by 2045 and retire all coal power generation by 2038 at the latest. Uniper's power generation portfolio is very carbon intensive, with 355 gCO_2 per KWh generated in 2023, above the European average of about 250 gCO_2 per KWh, and significantly above the industry leaders with average gCO_2 per KWh below 100. As of 2023, about 60% of Uniper's power generation was derived by coal and gas power plants.

Uniper's strategy is focused on decarbonizing its asset mix by taking opportunities amid the European energy transition, such as participating in tenders for hydrogen-ready gas-fired power plants (OCGT or CCGTs) under the German Kraftwerkstrategie and CCGT plants with CCS in the UK. It also entails the deployment of renewable generation of up to low-to-mid single digit GW scale by

2030. However, we believe that Uniper's strategy carries execution risks and depends to a large extent on the evolution of public policies that remunerate back-up capacity to guarantee security of supply. Also, Uniper lags the sector significantly in the deployment of new renewable capacity. While its pipeline consists of solar PV and shore wind, which are less risky than, for instance, offshore wind, we believe that Uniper will have to accept less attractive conditions as the market saturates from new renewable capacity.

Ratings Score Snapshot

Issuer Credit Rating	BBB-/Stable/--
Business risk:	Fair
Country risk	Low Risk
Industry risk	Moderately High Risk
Competitive position	Fair
Financial risk:	Significant
Cash flow/leverage	Significant
Anchor	bb
Modifiers:	
Diversification/Portfolio effect	Neutral
Capital structure	Neutral
Financial policy	Neutral
Liquidity	Adequate
Management and governance	Neutral
Comparable rating analysis	Neutral
Stand-alone credit profile:	bb
Related government rating	AAA
Likelihood of government support	High (+2 notches)

Related Criteria

- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- 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
- 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: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Ratings List

Ratings Affirmed	
Uniper SE	
Issuer Credit Rating	BBB-/Stable/--
Senior Unsecured	BBB-