

05 DEC 2023

## Fitch Affirms Energa at 'BBB+'; Outlook Stable

Fitch Ratings - Warsaw - 05 Dec 2023: Fitch Ratings has affirmed Energa S.A.'s Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) at 'BBB+' with Stable Outlook. A full list of rating actions is below.

The affirmation reflects Fitch's unchanged view on the company under Fitch's Parent and Subsidiary Linkage (PSL) Rating Criteria, under which Fitch equalises Energa's rating with that of parent ORLEN S.A.

Energa's Standalone Credit Profile (SCP) remains at 'bbb-' and is supported by a solid business profile, with a focus on its predictable regulated electricity distribution business, and strong operational record. Its large capex plan will increase Energa's net leverage, which after peaking in 2025, should return to within our sensitivities in 2026 when its new generation units start contributing to EBITDA.

### Key Rating Drivers

**Distribution Supports Credit Profile:** The ratings reflect a high share of regulated electricity distribution in Energa's EBITDA (on average 83% in 2021-2022 and 60% in 2023-2027), which indicates lower business risk and greater cash flow predictability than merchant power generation.

The higher weighted-average cost of capital (WACC) at 8.5% in 2023, up from 5.8% in 2022, is a primary driver of solid results in distribution in 2023, despite a decrease in the volume of distributed energy. We assume WACC to average 8.5% over the forecast period. We expect a large investment plan in the distribution grid to build up a regulated asset base, which, combined with increased WACC, will further strengthen EBITDA in this segment over the next four years.

**Supply Driven by Regulations:** Based on Fitch's projections, Energa is likely to post PLN1.2 billion of EBITDA in the supply segment in 2023, contrary to negative EBITDA last year. This is because in 2023 Energa has been gradually releasing a PLN1,068 million provision established in 2022 for a cap on energy prices for households, SME, local governments and utilities after receiving compensation from the state mechanism for the supply price cap.

However, we expect an adverse, uncompensated impact of around PLN320 million following further regulatory changes implemented in September 2023, which reduced bills for households (by PLN125 per household).

**No Price Caps Assumed from 2024:** Fitch assumes no price caps from 2024 under our rating case, and final settlements under the current compensation mechanism in the first months of 2024 to only temporarily increase working capital in 2023. However, if price caps are implemented in 2024 we assume a compensation mechanism will be put in place. Over 2023 there have been no delays in

payments of compensation due to a monthly settlement mechanism.

During 9M23 Energa recognised extra costs related to contributions paid by the generation segment to the Price Difference Payment Fund of PLN924 million, and PLN3.2 billion of revenue from compensation for the electricity price freeze, relating mainly to the sales (85%) and distribution segments (15%).

**Generation EBITDA to Normalise:** Under Fitch's rating case we project Energa's EBITDA in the generation segment to reach PLN350 million in 2023, after an exceptionally strong EBITDA of PLN843 million in 2022. Weaker performance expected this year results from extra costs relating to the price cap for generators, higher coal prices in conventional generation and declining trend in generation volumes. We view the substantial share of quasi-regulated income from capacity payments and additional support for renewable assets as a factor driving the segment's profitability.

**Conventional Generation Under Pressure:** Over the long term, we expect deterioration in the profitability of coal-fired assets due to declining electricity prices and increasing CO<sub>2</sub> costs, which will put clean dark spread under pressure. Under the rating case, Fitch assumes revenue from the capacity market will partly compensate worsened margins on electricity sales. We view conventional coal-fired assets as a burden on Energa's generation profitability until its two new combined heat and power units (CCGT) units in Ostroleka and Grudziadz are commissioned in 2026.

**New CCGT to Boost Profits:** We expect the new CCGT units to increase Energa's capacity by nearly 1.3 GWe in 2026. Both projects have signed 17-year capacity payments agreements, which will significantly improve the segment's result from 2026 and mitigate the plants' cash flow exposure to gas and CO<sub>2</sub> prices.

**Capex-Driven Leverage:** Fitch projects Energa's funds from operations (FFO) net leverage to peak at 6.0x in 2025 following high capex and leading to a sharp increase of net debt. Capex plan includes investments in distribution and on strategic projects, including the construction of new CCGTs in Ostroleka and Grudziadz. The new CCGTs should contribute to EBITDA growth from 2026, leading to gradual reduction in Energa's leverage to about 4.1x in 2026-2027.

**Hybrids Lose Equity Credit:** Energa redeemed tranche A of its EUR125 million hybrid bonds in September 2023 under the first call option without refinancing it with a similar equity-like instrument. Fitch is revising its equity credit to zero from 50% for the remaining EUR125 million hybrid debt with a first call option in 2027, as we do not have sufficient assurance that hybrids will remain in the capital structure.

Energa has access to cash-pooling within the ORLEN group together with intercompany loans from its parent as the company moves to centralised funding for most of its new debt. Removal of equity credit increases Energa's FFO net leverage only by 0.1x.

**Equalisation Rating Approach:** We view ORLEN's SCP as stronger than Energa's due to its larger-scale operations, stronger business diversification and lower leverage. Applying the stronger parent/weaker subsidiary approach under our PSL Criteria, we equalise the rating of Energa with that of ORLEN. This is

based on our reassessment of 'Medium' legal incentives, combined with 'High' strategic and operating incentives.

## **Derivation Summary**

Energa's close peer group comprises three other electricity-focused integrated utilities in Poland, PGE Polska Grupa Energetyczna S.A. (BBB+/Stable), ENEA S.A. (BBB/Stable) and TAURON Polska Energia S.A. (BBB-/Stable).

All peers are rated on a standalone basis. Energa's and Tauron's business profiles benefit from a large share of regulated distribution in EBITDA, which provides good cash flow visibility when conventional generation and mining are under pressure. Both companies' credit profiles are also supported by inflows from capacity payments that improve revenue visibility, although Tauron benefits from more significant amounts due to its larger coal-fired fleet.

We believe Energa has a more sustainable business profile, which is reflected in its higher debt capacity, with a negative rating sensitivity of 5.0x compared with Tauron's 4.5x.

PGE is the largest integrated utility in Poland and has the lowest leverage among the peer group. It derives most of its EBITDA from electricity generation and has a high share of lignite in the generation fuel mix, which provides the company with a cost advantage over hard coal-fired peers such as ENEA and Tauron. However, rising CO2 prices could diminish this cost advantage if not accompanied by high hard coal prices, given the higher carbon footprint of lignite than hard coal.

ENEA has a lower share of regulated distribution than Energa and Tauron and at the same time higher exposure to hard coal-fired generation, but controls a low-cost mining business.

## **Key Assumptions**

Fitch's Key Assumptions Within Our Rating Case for the Issuer:

- WACC in the distribution segment averaging 8.5% in 2023-2027
- Electricity prices on average at PLN607/MWh in 2023-2027
- CCGT Ostroleka operational from 2026, with 50% plus one share ownership by Energa
- Capex totaling about PLN18 billion in 2023-2025
- Continuation of a no-dividend policy

## **RATING SENSITIVITIES**

### **Factors That Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade**

- Positive rating action on ORLEN

- FFO net leverage below 4x on a sustained basis would be positive for the SCP

### **Factors That Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade**

- Negative rating action on ORLEN

- FFO net leverage above 5x on a sustained basis, for example due to a protracted economic downturn, higher-than-planned capex or reinstatement of dividends, which would be negative for the SCP

ORLEN's rating sensitivities from the most recent Rating Action Commentary on 9 November 2022 are:

#### Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

- Rating upside is currently limited unless the business profile strengthens significantly with larger scale of operations and geographical diversification combined with lower execution risk in shifting the business towards lower-emission technologies

- Net debt/EBITDA below 1.5x or FFO net leverage below 1.7x on a sustained basis

#### Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

- Net debt/EBITDA above 2.5x or FFO net leverage above 2.7x on a sustained basis

- Higher-than-expected variability of cash flow

- Aggressive financial policy with higher-than-expected dividend payments or debt-funded acquisitions

### **Liquidity and Debt Structure**

**Adequate Liquidity:** At end-September 2023, Energa had PLN88 million of unrestricted cash and equivalents, and PLN3.8 billion of committed unused credit lines. This compared with short-term maturities of PLN2.2 billion, and about PLN4 billion Fitch-projected negative free cash flow in the next 12 months from October 2023.

We expect that ORLEN will continue to address Energa's short-term financing needs through intra-group loans, cash pooling, and revolving credit lines accordingly to current needs. Our rating case assumes additional external financing for distribution capex to be finalised in 1Q24.

### **Issuer Profile**

Energa is an integrated utility operating in Poland. The main areas of operations are electricity distribution, generation and supply.

### **REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING**

The principal sources of information used in the analysis are described in the Applicable Criteria.

### **Public Ratings with Credit Linkage to other ratings**

Energa is credit-linked to ORLEN.

## ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

## Fitch Ratings Analysts

### Renata Dobrzynska, PhD

Director

Primary Rating Analyst

+48 22 103 3035

Fitch Ratings Ireland Limited spolka z ograniczona odpowiedzialnoscia oddzial w Polsce Marszalkowska 107, 00-110 Warsaw

### Katarzyna Sulek

Senior Analyst

Secondary Rating Analyst

+48 22 103 3032

### Arkadiusz Wicik, CFA

Senior Director

Committee Chairperson

+48 22 103 3016

## Media Contacts





### Isobel Burke

London

+44 20 3530 1499

[isobel.burke@thefitchgroup.com](mailto:isobel.burke@thefitchgroup.com)

## Rating Actions

ENTITY/DEBT	RATING		RECOVERY	PRIOR
Energa S.A.	LT IDR	BBB+ 	Affirmed	BBB+ 
	LC LT IDR	BBB+ 	Affirmed	BBB+ 

ENTITY/DEBT	RATING		RECOVERY	PRIOR
	Natl LT	AA+(pol) ●	Affirmed	AA+(pol) ●
• senior unsecured	LT	BBB+	Affirmed	BBB+
• subordinated		BBB-	Affirmed	BBB-
• senior unsecured	Natl LT	AA+(pol)	Affirmed	AA+(pol)
Energa Finance AB (publ)				
• senior unsecured	LT	BBB+	Affirmed	BBB+

#### RATINGS KEY OUTLOOK WATCH

POSITIVE	⊕	◊
NEGATIVE	⊖	◊
EVOLVING	◊	◆
STABLE	○	

#### Applicable Criteria

[Corporate Hybrids Treatment and Notching Criteria \(pub.12 Nov 2020\)](#)

[Corporate Rating Criteria \(pub.03 Nov 2023\) \(including rating assumption sensitivity\)](#)

[Corporates Recovery Ratings and Instrument Ratings Criteria \(pub.13 Oct 2023\) \(including rating assumption sensitivity\)](#)

[National Scale Rating Criteria \(pub.22 Dec 2020\)](#)

## Parent and Subsidiary Linkage Rating Criteria (pub.16 Jun 2023)

### Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

### Additional Disclosures

#### Solicitation Status

### Endorsement Status

Energa Finance AB (publ)      EU Issued, UK Endorsed

Energa S.A.                      EU Issued, UK Endorsed

### DISCLAIMER & DISCLOSURES

All Fitch Ratings (Fitch) credit ratings are subject to certain limitations and disclaimers. Please read these limitations and disclaimers by following this link: <https://www.fitchratings.com/understandingcreditratings>. In addition, the following <https://www.fitchratings.com/rating-definitions-document> details Fitch's rating definitions for each rating scale and rating categories, including definitions relating to default. ESMA and the FCA are required to publish historical default rates in a central repository in accordance with Articles 11(2) of Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 and The Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019 respectively.

Published ratings, criteria, and methodologies are available from this site at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance, and other relevant policies and procedures are also available from the Code of Conduct section of this site. Directors and shareholders' relevant interests are available at <https://www.fitchratings.com/site/regulatory>. Fitch may have provided another permissible or ancillary service to the rated entity or its related third parties. Details of permissible or ancillary service(s) for which the lead analyst is based in an ESMA- or FCA-registered Fitch Ratings company (or branch of such a company) can be found on the entity summary page for this issuer on the Fitch Ratings website.

In issuing and maintaining its ratings and in making other reports (including forecast information), Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings and reports should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating or a report will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings and its reports, Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings and forecasts of financial and other information are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings and forecasts can be affected by future events or conditions that were not anticipated at the time a rating or forecast was issued or affirmed.

The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. Sector-specific best- and worst-case scenario credit ratings are listed in more detail at <https://www.fitchratings.com/site/re/10238496>

The information in this report is provided "as is" without any representation or warranty of any kind, and Fitch does not represent or warrant that the report or any of its contents will meet any of the requirements of a recipient of the report. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion and reports made by Fitch are based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings and reports are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating or a report. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A



report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001. Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see <https://www.fitchratings.com/site/regulatory>), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

dv01, a Fitch Solutions company, and an affiliate of Fitch Ratings, may from time to time serve as loan data agent on certain structured finance transactions rated by Fitch Ratings.

Copyright © 2023 by Fitch Ratings, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved.

## **Endorsement policy**

Fitch's international credit ratings produced outside the EU or the UK, as the case may be, are endorsed for use by regulated entities within the EU or the UK, respectively, for regulatory purposes, pursuant to the terms of the EU CRA Regulation or the UK Credit Rating Agencies (Amendment etc.) (EU

Exit) Regulations 2019, as the case may be. Fitch's approach to endorsement in the EU and the UK can be found on Fitch's [Regulatory Affairs](#) page on Fitch's website. The endorsement status of international credit ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.