



## **Rating Action: Moody's Ratings affirms PGE's Baa1 rating; stable outlook**

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28 Aug 2024

Paris, August 28, 2024 -- Moody's Ratings (Moody's) has today affirmed the Baa1 long-term issuer rating of PGE Polska Grupa Energetyczna S.A. (PGE). Concurrently, we have affirmed the baa2 Baseline Credit Assessment (BCA) of PGE, as well as the Baa1 backed senior unsecured rating and the (P)Baa1 backed senior unsecured EMTN program rating of PGE Sweden AB (publ). The outlook on both issuers remains stable.

### **RATINGS RATIONALE**

The rating affirmation reflects (1) the company's leading position as the largest utility group in Poland; (2) its strategy of focusing on renewables and network operations, which underpins cash flow visibility; (3) its historically low financial leverage and; (4) our expectation of strong support from the Polish government, given its 60.86% ownership.

At the same time, the Baa1 long-term issuer rating is constrained by (1) uncertainties surrounding the implementation of the former Polish government's plan to take over PGE's coal and lignite assets; (2) the group's high exposure to commodity price volatility and; (3) a substantial capital spending programme, which absorbs operating cash flow and carries some execution risk, and which will weaken credit metrics over the next two years.

In April 2021, the Polish government presented a road map for nationalising the coal and lignite assets of state-owned domestic utilities. In July 2023, it announced its intention to create the National Agency for Energy Security for this purpose. However, the law was subsequently discontinued in the new term of the Parliament after the parliamentary election, which took place in the middle of October 2023. As a result of the elections and a change of government in Poland, the future of the coal spinoff — including what form it may take — is currently highly uncertain and it is unlikely that the spinoff will materialise within the parameters outlined by the previous government. On the other hand, we also acknowledge that, so far, there has been no broad political opposition to a coal carve-out. Thus, a spinoff could still materialise, however, the

process is now currently clouded with uncertainty and we do not expect a coal spinoff to occur until 2025 at the earliest.

In the coming years, we expect PGE to need incremental funding in view of its large forecasted capital expenditures. PGE has over a number of years displayed a very strong financial risk profile, however, we expect credit metrics to weaken in tandem with increased capital expenditures. As part of its 2030 strategy, PGE has announced a PLN75 billion investment programme mainly directed towards renewables and networks, which will enable the company to address the changing energy mix because of the energy transition. While no final investment decision has yet been taken, we expect that PGE will soon start deploying funds to the construction of the Baltica 2 offshore wind park. Further investments will also be directed towards power storage, onshore wind and photovoltaic capacity, whereas PGE currently also is commissioning several combined cycle gas turbine (CCGT) plants with the Rybnik plant expected by the end of 2026. As the energy transition accelerates, we also expect that there will be increasing funding needs in the network segment. As such, an eventual spinoff of the coal assets would enhance the company's business risk profile because it would increase earnings from contracted and regulated activities and enable the company to access additional liquidity from coal-averse investors. Should the coal spinoff fail to materialise at all, we expect PGE to obtain some form of support from the Polish government, which is likely to remain the majority shareholder, so that PGE can implement its transition to a low-carbon business mix as planned in its corporate strategy as of October 2020.

PGE falls under Moody's Government-Related Issuers methodology due to its 60.86% ownership by the Government of Poland (A2 stable). The Baa1 issuer rating incorporates one notch of uplift from PGE's current BCA of baa2, reflecting the combination of very high default dependence given the company's strategic importance to the domestic economy and strong likelihood of extraordinary support being provided by the Polish government in case of financial distress.

The affirmation of the provisional long-term senior unsecured rating of (P)Baa1 on the €2 billion euro medium-term note programme and the Baa1 senior unsecured rating of PGE Sweden AB (publ) reflect the unconditional and irrevocable guarantee that PGE provides under the programme, and the absence of structural and contractual subordination of the eurobond creditors to the claims of other PGE group lenders.

## RATIONALE FOR THE STABLE OUTLOOK

The stable rating outlook reflects our expectation that the Polish government will take measures to protect PGE against the risks arising from its currently high carbon exposure. The outlook also reflects our expectation that PGE will maintain solid credit metrics, expressed as funds from operations (FFO)/net debt above 30%.

## FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Upward pressure on the ratings is unlikely over the short to medium term, given the dynamic evolution of the energy market in Poland and the lack of clarity around the final design of an eventual spinoff of the coal assets; and PGE's planned sizeable capital investment programme, which we expect to weaken the company's credit metrics over time.

PGE's Baa1 rating could be downgraded if its FFO/net debt were to decline below 30% for a sustained period, or if there were significant adverse changes in the Polish regulatory or market framework.

A significant deterioration in the credit quality of the Polish government or a reduction in the support assumptions incorporated into our assessment, or both, would also likely strain PGE's rating.

The ratio guidance could be reviewed once there is more clarity on PGE's credit profile following the potential spinoff of the coal assets or other measures to protect the company from carbon transition risks.

The methodologies used in these ratings were Unregulated Utilities and Unregulated Power Companies published in December 2023 and available at <https://ratings.moodys.com/rmc-documents/412151>, and Government-Related Issuers methodology published in January 2024 and available at <https://ratings.moodys.com/rmc-documents/406502>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of these methodologies.

Headquartered in Warsaw, PGE is the largest integrated electric utility group in Poland. PGE is majority-owned by the Government of Poland and reported an EBITDA of PLN10 billion in 2023.

## REGULATORY DISCLOSURES

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