Industry Top Trends Update

Utilities

It's all about the energy transition

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What's changed?

Climate regulation is accelerating. European energy transition policies are taking the form of enhanced national renewable targets, higher carbon-reduction goals, government subsidies, and the implementation of a European taxonomy for sustainable activities. The energy transition is becoming more concrete, with clearer price signals and legal frameworks, which is positive for the sector.

Carbon prices are at historical highs. Anticipation of stricter trading volumes led carbon prices to surge above €50 per ton in 2021 from about €25 over 2019-2020. This is expediting fuel switching away from the most polluting energy sources.

Annual investments will rise about 30% over 2020-2023. The top-25 European utilities plan to up investment in more defensive renewables and networks, which will slowly strengthen their business risk profiles, but tighten balance sheets.

How is recovery taking shape?

High power prices support power generators' earnings. This is underpinned by higher carbon prices, tightening of supply from nuclear and thermal plant closures, and economic recovery. European power prices almost doubled in first-half 2021 compared with 2020 levels, and baseload producers will benefit the most.

Power demand offers brighter prospects. We see improved growth prospects in Europe, thanks to economic recovery and the electrification of economies to reduce carbon emissions, particularly for heavy industries and heating. Growth in power purchase agreements could substitute subsidy schemes.

Debt financing remains attractive. The cost of debt remains low and the sector's attractiveness for green financing further compresses yields. We anticipate utilities will continue seizing (re)financing opportunities, particularly on hybrids.

What are the key risks around the baseline?

Nuclear and gas remain in limbo. Uncertainties persist for European gas assets as growth prospects depend on EU taxonomy and technological progress on green gases. For nuclear, financing life extension and new projects remain complex.

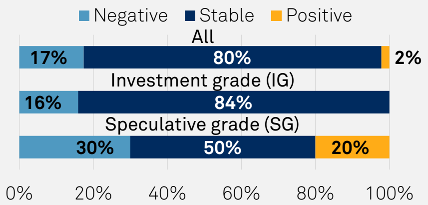
Lower profitability from renewables. Tougher competition for new renewable projects combined with more risk appetite could weaken returns further. That said, the growth of investment opportunities and competitive advantage for market leaders mitigate these risks at least over the coming three years.

A squeeze in network remuneration. Recent regulatory reviews have led to a decline in remuneration for power and gas networks, at a time of significant investment need, especially for power. Operators' ability to cut costs, grasp bonuses, and adapt shareholder remuneration are key for rating stability.

Latest Related Research

- The Hydrogen Economy: Storage Is Paramount For Utilities In The Long Term, April 22, 2021
- The Energy Transition And The Diverging Credit Path For European Utilities, Feb. 16, 2021
- The Energy Transition And What It Means For European Power Prices And Producers: January 2021 Update, Jan. 27, 2021

Outlook Distribution



Ratings Statistics*

	IG	SG	All
Ratings	82	10	92
Downgrades	1	1	2
Upgrades	5	1	6

Ratings data as of end-June 2021. * Year to date.

COVID-19 Heat Map

Utilities	
Estimated recovery to 2019 credit metrics	2022
Potential negative long-term industry disruption	No

2020 Versus 2019		
Revenue decline	EBITDA decline	Incremental borrowings
0%-5%	0%-10%	<5%

2021 Estimates Versus 2019	
Revenue decline	EBITDA decline
0%-10%	0%-10%