Axpo Holding AG
Swiss Confederation, Utilities

S-1

Key metrics

			Scope estimates	
Scope credit ratios	**FY 2021**	**FY 2022**	**FY 2023E**	**FY 2024E**
Scope-adjusted EBITDA/interest cover	4.2x	3.1x	14.2x	5.6x
Scope-adjusted debt/EBITDA	2.9x	7.5x	1.1x	0.8x
Scope-adjusted free operating cash flow/debt	0%	-55%	6%	94%
Liquidity	425%	292%	226%	305%

Note: Axpo's financial year (FY) starts on 1 October (t) and ends on 30 September (t+1)

Rating rationale

The affirmation of the S-1 short-term debt rating reflects the still strong credit quality of the issuers, supported by the good business risk and financial risk profiles of Axpo Holding paired with the group's status as a government-related entity, which guarantees strong and extensive public support amid potential liquidity needs. The affirmed rating is also based on a solid liquidity profile of the issuer, signalled by robust expected liquidity and good access to external funding from banks, the capital market and other funding channels.

Axpo Holding AG provides an unconditional and irrevocable guarantee to the Negotiable EUropean Commercial Paper (NEU CP) Program of Axpo International SA, started in December 2022 and promoted by Banque de France.

Rating history

Date	Rating action	Rating
4 Dec 2023	Affirmation	S-1
8 Dec 2022	New Rating	S-1

Ratings & Outlook

Short-term debt S-1

Analyst

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Related Methodologies

General Corporate Rating Methodology; Oct 2023

European Utilities Rating Methodology, March 2023

Government Related Entities Rating Methodology, Jul 2023

Related Research

ESG considerations for the credit ratings of utilities; April 2021

European utilities: continued electricity price hedging promises producer gain, consumer pain, Apr 2023

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Bloomberg: RESP SCOP

[1] The credit rating(s) and outlook(s) provided in this document may not be shared with any unauthorised third party.

Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Overall solid financial risk profile, with good cash availability and leverage (Scope-adjusted debt/EBITDA) expected at around 1.0x • Vertically integrated business model with leadership in Switzerland for power generation (both in general and from renewables) • Solid competitive position in domestic market for energy supply and good presence throughout Europe (one of the main European players in energy trading, among others) • GRE status: wide public support both from Swiss government and cantons (only in case of need), due to its role as a 'systemically-relevant' utility in Switzerland • Adequate historical profitability, mostly sustained by power generation business • One of the main European players in the field of renewable energy, with a comparatively low CO_2 footprint of the power generation fleet and a strong position in the merit order (ESG factor)	• Blended industry risk profile, mainly constrained by non-regulated power generation (especially nuclear and hydropower) due to industry-inherent volatility of achievable power prices • Limited growth opportunities in the domestic market for power generation (nuclear phase out and saturation of hydropower) and retail (competition with two players) • Deterioration of profitability and leverage in FY 2022, but deemed temporary (due to energy prices trend) • Limited geographical diversification outside Switzerland (despite increasing contribution from Italian market in FY 2023) • Comparatively weak (yet strengthened) debt protection, due to higher interest paid on rising financial debt • Exposure to power generation from nuclear assets poses some regulatory, environmental and political risks (ESG factor) considering the future phasing out of such technology in Switzerland and the EU

Positive rating-change drivers	Negative rating-change drivers
• Leverage (Scope-adjusted debt/EBITDA) remaining well below 2.0x on a sustained basis	• Reversion of the Outlook to Stable: leverage returning to significantly above 2.0x on a sustained basis • Rating pressure as expressed through a Negative Outlook or even downgrade (albeit deemed remote currently): strong deterioration in leverage and cash flow, i.e. if Scope-adjusted debt/EBITDA increased to above 4.0x paired with negative FOCF for a prolonged period • Any change affecting current public support framework (GRE status)

Corporate profile

Founded in 1914 as Nordostschweizerische Kraftwerke AG by Northeastern cantons of Switzerland, Axpo has become Switzerland's largest producer of renewable energy, as well as an international leader in energy trading and the marketing of solar and wind power. Axpo Group is defined as an integrated utility engaged in several activities within the energy value chain (i.e. electricity production, electricity distribution, trading with electricity, natural gas, other commodities, certificates and energy-based financial products, as well as electricity sales and services). In particular, the company operates through three business segments: i) Generation & Distribution operates and expands the Axpo power plant portfolio in Switzerland and abroad; ii) Trading & Sales encompasses energy trading, risk and portfolio management, customer service and the deployment of the power plant portfolio; iii) CKW is a subsidiary that supplies energy to Central Switzerland and ensures optimal use of hydro power in this region through existing exchange agreements.

We define Axpo as a GRE in line with our Government Related Entity Rating Methodology. This is based on its fully public ownership (cantons like Zurich and Aargau, along with canton utilities) and the essential public services provided in Switzerland by the group, which can also be underpinned by the classification as a systemically-relevant utility.

Financial overview

				Scope estimates		
Scope credit ratios	**FY 2020**	**FY 2021**	**FY 2022**	**FY 2023E**	**FY 2024E**	**FY 2025E**
Scope-adjusted EBITDA/interest cover	6.8x	4.2x	3.1x	14.2x	5.6x	5.6x
Scope-adjusted debt/EBITDA	2.8x	2.9x	7.5x	1.1x	0.8x	0.8x
Scope-adjusted free operating cash flow/debt	3%	0%	-55%	6%	94%	7%
Liquidity	334%	425%	292%	226%	305%	311%
Scope-adjusted EBITDA in CHF m						
EBITDA	1,168	1,126	(579)	4,760	1,786	1,793
Operating lease payments	-	-	-	-	-	-
Management adjustments (for one-off items)	-	(247)	1,343	(1,792)	-	-
Disposal proceeds fixed assets	17	(157)	(166)	-	-	-
Share of result of partner plants and other associates	(70)	(74)	(103)	(84)	(67)	(65)
Associate dividends received	62	47	79	84	67	65
Scope-adjusted EBITDA	**1,177**	**696**	**574**	**2,968**	**1,786**	**1,793**
Free operating cash flow in CHF m						
Funds from operations	960	403	140	2,003	1,292	1,270
Change in working capital	(352)	(2,748)	(7,894)	7,543	841	(317)
Non-operating cash flow	(187)	2,820	5,796	(9,218)	(65)	37
less: capital expenditure (net)	(304)	(448)	(397)	(103)	(629)	(867)
less: lease amortisation	(19)	(19)	(19)	(19)	(19)	(19)
Free operating cash flow	**98**	**7**	**(2,374)**	**205**	**1,420**	**104**
Net cash interest paid in CHF m						
Net cash interest per cash flow statement	91	84	100	126	235	237
Interest expense pensions	-	0	(0)	0	0	0
Interest component operating leases	-	-	-	-	-	-
Interests attributable to asset retirement obligations	81	82	83	83	83	83
Net cash interest paid	**172**	**167**	**183**	**210**	**319**	**321**
Scope-adjusted debt in CHF m						
Reported gross financial debt	5,029	4,492	7,745	7,980	9,234	4,734
less: cash and cash equivalents	(2,216)	(2,559)	(3,917)	(5,271)	(8,206)	(3,705)
add: asset retirement obligation (net)	399	59	478	478	478	478
add: pension adjustment	67	-	-	-	-	-
add: operating lease obligations	-	-	-	-	-	-
Other items (contingencies)	52	21	9	9	9	9
Scope-adjusted debt	**3,330**	**2,013**	**4,314**	**3,195**	**1,514**	**1,515**

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Environmental, social and governance (ESG) profile[2]

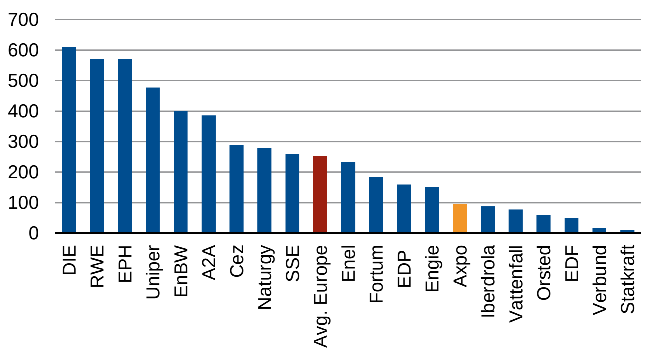
Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend
Green leaf (ESG factor: credit positive)
Red leaf (ESG factor: credit negative)
Grey leaf (ESG factor: credit neutral)

Credit-supportive leadership in renewables and comparatively low CO_2 footprint

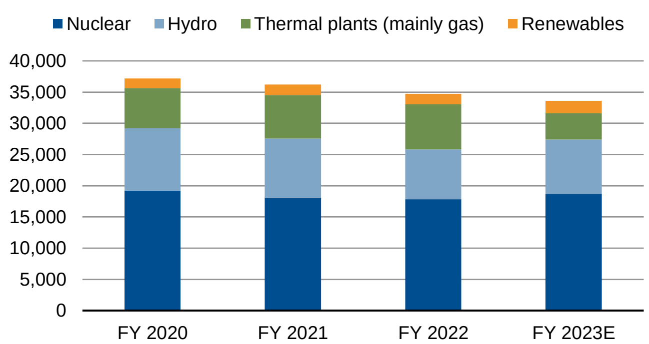
Axpo is leader in power generation from renewables in Switzerland, especially thanks to its experience and expertise in hydropower technology. Even at the European level, Axpo is one of the main energy companies engaged in renewables and one of the leaders for low carbon footprint among power generators, thanks to its high share of low-carbon electricity production (nuclear and hydro). Axpo reported around 95 gCO_2e/kWh in FY 2022, one of the lowest levels among main European power generators and widely below the average (251 gCO_2e/kWh), positioning itself as a leader in energy transition and showing a credit-supportive aspect from a ESG perspective.

Figure 1: Carbon footprint of power generators in Europe (gCO_2e/kWh, 2022)



Sources: public information, Scope

Figure 2: Electricity generation breakdown by type (GWh)



Sources: Axpo, Scope

[2] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Potential ESG risk arising from large exposure to nuclear

At the same time, the group's large exposure to nuclear power generation (around 50% of total production) poses some regulatory, environmental and political risks. In the long term, the potential phasing out of such technology could represent a risk for the company (especially social, as highlighted in the table above) and a big challenge as Axpo aspires to shift its business model towards decarbonised power generation.

Supportive investment strategy to enable the energy transition

Axpo is highly committed to ESG goals, as demonstrated by the results achieved so far. Especially in relation to the environmental factor, Axpo is currently facing the challenge of energy transition, with strong planned investments on renewables – especially wind and solar – and new clean technologies (i.e. hydrogen, batteries). We expect these investments to total about CHF 3.0bn by 2028.

Business risk profile

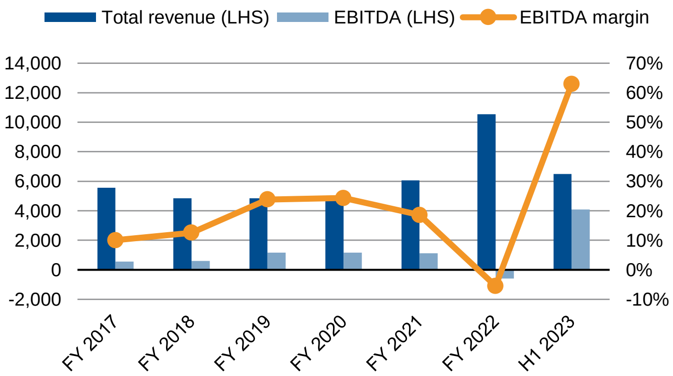
Blended industry risk profile

Given Axpo's exposure to several utility segments, which are driven by different fundamentals (i.e. regulated versus unregulated and upstream versus downstream operations), our industry assessment reflects a blended industry risk. We apply a normalised segment split of 50% for non-regulated power generation, 40% for retail, and 5% each for trading and regulated power generation, based on historical EBITDA contributions. This assessment is constrained by Axpo's major exposure to nuclear power generation (non-regulated activity as well as a technology envisaged to be phased out in the medium-to-long term), even though increasing contribution from highly profitable and regulated power generation from renewables will likely sustain a stronger industry risk profile in the coming years.

Solid competitive position in domestic market, constrained by low growth opportunities

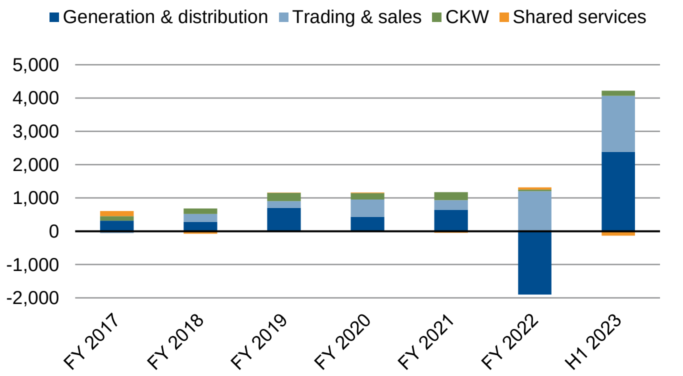
Axpo's business risk profile is based on its solid competitive position, especially in Switzerland, where the group is the largest overall producer of electricity accounting for roughly 40% of generated power as well as the leader in hydropower (roughly 30%) and in overall renewable energy. We expect business volumes to be stable in the coming years, given limited domestic growth opportunities due to the saturation of the retail market and power generation technologies like nuclear and hydro, as well as intense competition from established utilities across Europe. Business development abroad is also subordinated to the shareholders' (political) strategic decisions.

Figure 3: Reported revenue and EBITDA (CHF m) versus EBITDA margin reported



Sources: Axpo, Scope

Figure 4: EBITDA breakdown by business segment (CHF m)



Sources: Axpo, Scope estimates

Fully diversified business model reducing cash flow volatility

Axpo is fully integrated as it covers almost all parts of a power utility value chain from generation to distribution and B2C retail. As seen in our assessment of industry risks for the different utility sub-segments (non-regulated generation: BB; retail: BBB; trading: BB and regulated generation: AA), the underlying business fundamentals of the different segments are not fully correlated. The company's diversification across these segments is credit-supportive.

Significant dependency on nuclear despite the growth of renewables

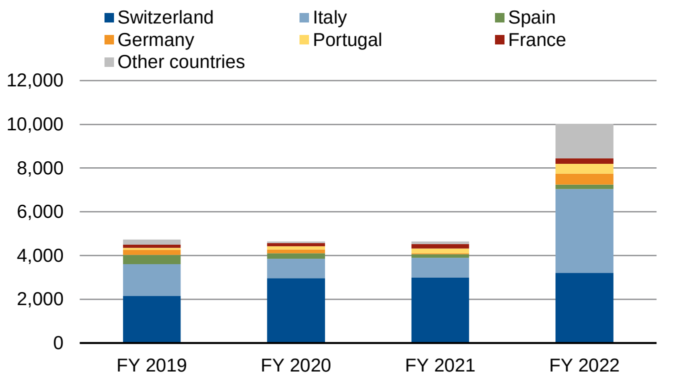
In FY 2023, Axpo is expected to generate about 55% of electricity from its nuclear power plants in Switzerland and abroad. Hydropower remains an important part of its energy production, albeit less predictable as it is affected by weather conditions. Overall, new renewables (i.e. solar, wind) are growing but still show a negligible contribution (roughly 6% of total production). The group is therefore significantly dependent on one major energy source, which comes with ESG-related risks and is already intended to be phased out in the medium term.

Wide and diversified customer base with relatively large outreach

In relation to end-customer markets (B2B and B2C), Axpo directly supplies large companies, SMEs and energy resellers, as well as private households and agricultural businesses in

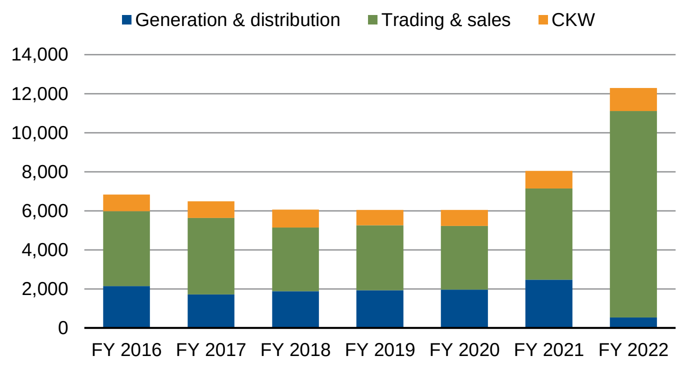
Switzerland. The diversification of the group's customer base is credit-supportive.

Figure 5: Revenue breakdown by country (CHF m)



Sources: Axpo, Scope

Figure 6: Revenues breakdown by business segment – aggregated figures (CHF m)



Sources: Axpo, Scope

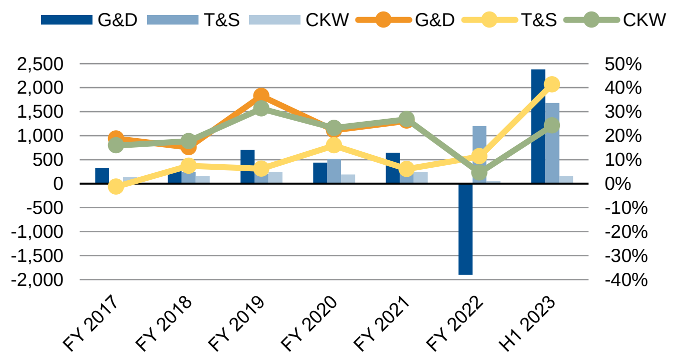
Limited geographical diversification outside Switzerland despite good penetration of certain markets

Axpo operates in 32 countries and more than 40 markets, mainly in Europe. Nevertheless, the domestic market and Italy remain preeminent, representing more than 70% of revenue. In FY 2022, Italy was the main country with CHF 3.8bn of revenue (38% of total), significantly boosted by higher energy prices in the end-customer business, while Switzerland generated CHF 3.2bn, contributing 32% of total revenue. However, the group reports a good penetration even in other main countries, especially in southern Europe and the Nordics, actively developing its business in France and Germany. Activities in other continents (primarily US and Asia) are negligible. Overall, despite a good penetration of certain European markets, the concentration in two primary markets is a moderate constraint in terms of geographical diversification.

Profitability expected to stabilise in the coming years after some volatility

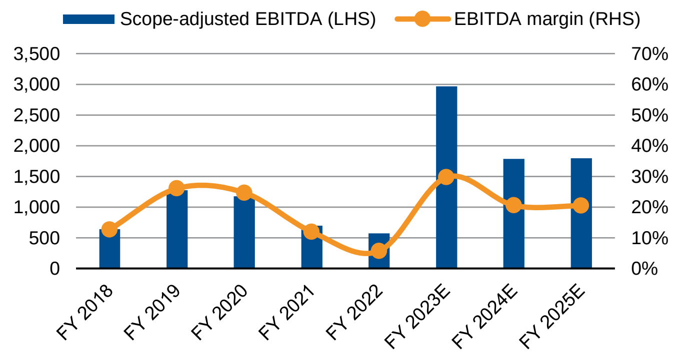
In recent years, Axpo has experienced some volatility in profitability, mainly due to the unprecedented turmoil in the energy sector. After the declining trend in FY 2021 and FY 2022, mainly driven by an accounting mismatch on Swiss production and by lower electricity generation volumes, the Scope-adjusted EBITDA margin will likely be exceptionally high in FY 2023 (estimated at around 30% versus 6% in FY 2022), boosted by significant gains in trading activity and increasing production from nuclear and hydro power plants. In the next few years, given the gradual normalisation of market conditions (i.e. reduced volatility), profitability is expected to return to historical levels of around 20%, still sustained by high prices paired with an effective hedging strategy.

Figure 7: EBITDA (columns, CHF m) versus EBITDA margin (lines, %) by business segment



G&D: Generation & Distribution
T&S: Trading & Sales
Sources: Axpo, Scope

Figure 8: Group Scope-adjusted EBITDA (CHF m) and EBITDA margin



Sources: Axpo, Scope estimates

Financial risk profile

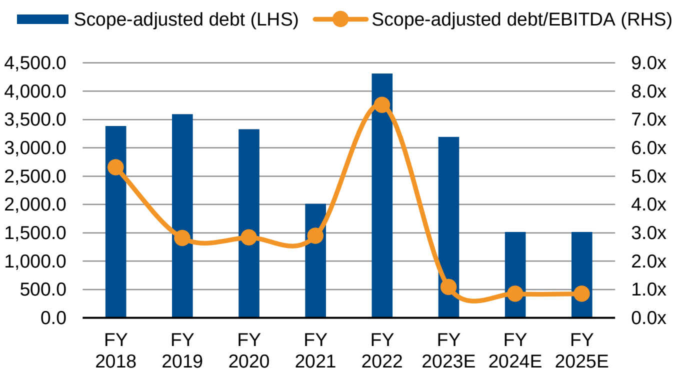
FOCF returning positive in FY 2023 after a temporary deterioration in FY 2022

FOCF considerably deteriorated in FY 2022 (-CHF 2.4bn), strongly affected by the weakening of margins and the large outflows for cash collateral. In FY 2023, the group will likely return to a positive and solid FOCF, mainly sustained by the robust Scope-adjusted EBITDA and a significant release of previously posted cash collateral. Furthermore, FY 2023 capex (around CHF 0.5bn) should not represent a burden for FOCF, as it will be almost entirely offset by the disposal of non-strategic assets for a total amount of CHF 0.4bn.

Solid internal financing capacity in the next two years

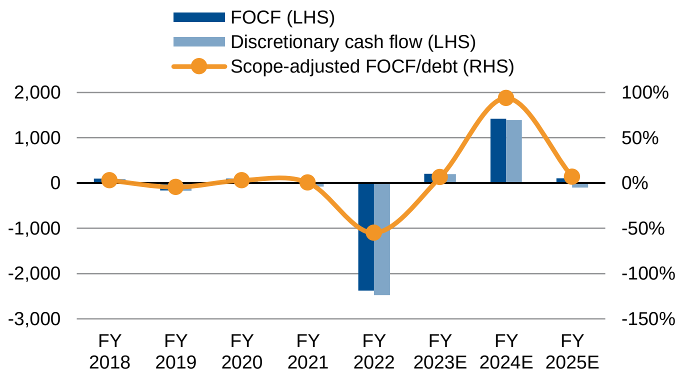
For FY 2024 and FY 2025, FOCF is expected to remain positive and robust, benefitting from still solid funds from operations and a further release of cash collateral, capable of covering the increasing net capex planned by the group and even reduce financial indebtedness. This trend, along with historical positive FOCF (except for FY 2022), confirms the group’s good capacity to generate sufficient cash flow to finance its capex needs internally.

Figure 9: Scope-adjusted debt (CHF m) versus Scope-adjusted debt/EBITDA



Sources: Axpo, Scope estimates

Figure 10: FOCF and discretionary cash flow (CHF m) versus Scope-adjusted FOCF/debt



Sources: Axpo, Scope estimates

Strong improvement of leverage in FY 2023, after the trough in September 2022

As of September 2022 (FY 2022 closing date), Scope-adjusted debt more than doubled to CHF 4.3bn (versus CHF 2.0bn at FYE 2021), due to the very sharp increase in collateral payments, leading to leverage (Scope-adjusted debt/EBITDA) peaking at 7.5x (versus 2.9x at FYE 2021). This deterioration was temporary and entirely attributable to the unprecedented turmoil on European energy markets. Indeed, in FY 2023 Scope-adjusted debt should decrease to CHF 3.2bn (down by CHF 1.1bn YoY), given solid cash flow. This trend, coupled with exceptional margins (Scope-adjusted EBITDA estimated at CHF 3.0bn versus CHF 0.6bn in FY 2022), should then lead to a considerable decline in leverage (1.1x versus 7.5x at FYE 2022).

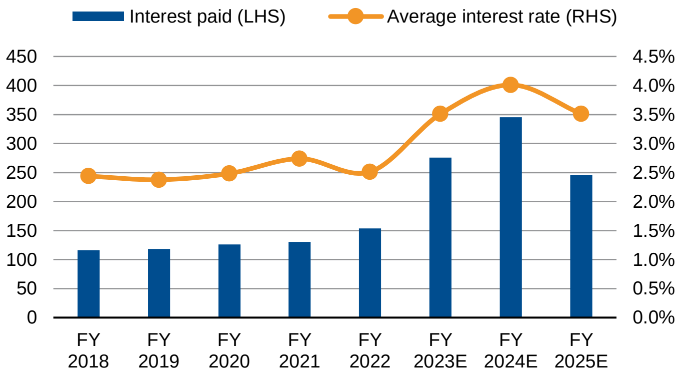
Leverage expected at around 1.0x over the next two years

As described above, the expected positive and robust FOCF mainly sustained by the solid operating results and further cash collateral release would allow a significant net debt reduction (Scope-adjusted debt estimated at around CHF 1.5n in FY 2024 and FY 2025). Leverage is likely to remain stable around 1.0x, despite expected lower margins.

Temporary strengthening of debt protection in FY 2023, expected to return to below 10x in FY 2024

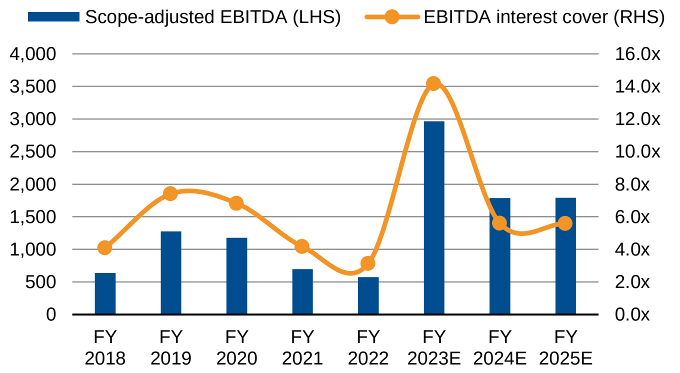
In FY 2023 the aforementioned boost of EBITDA should increase interest cover to above 10x (versus 3.1x in FY 2022), despite the slight growth of Scope-adjusted interest due to a higher average cost of debt (3.5% versus 2.5% in FY 2022). However, this performance is temporary as it has been positively impacted by the exceptional rebound of operating results in the same period. In light of the envisaged normalisation of margins, debt protection is expected to return to below 10x as early as FY 2024 (estimated at 5.6x), remaining around this level also in FY 2025, still penalised by high interest paid.

Figure 11: Interest paid (CHF m) versus average interest rate



Sources: Axpo, Scope estimates

Figure 12: Scope-adjusted EBITDA (CHF m) vs debt protection

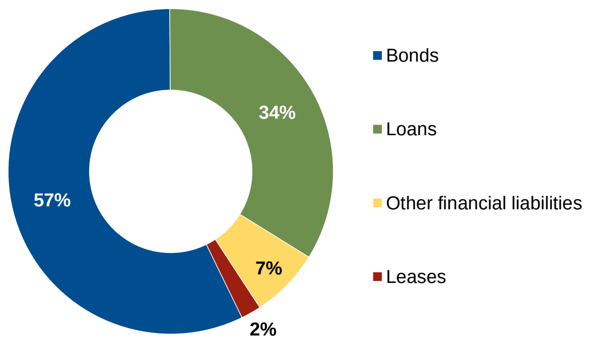


Sources: Axpo, Scope estimates

Solid liquidity profile supported by large cash availability

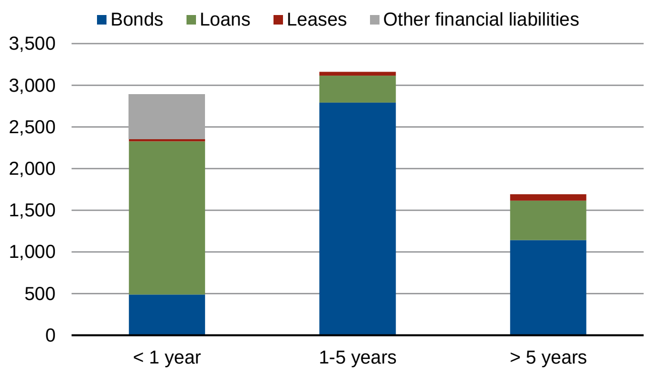
Axpo's internal liquidity ratio has always been considerably above 110%, reflecting low amounts of short-term and long-term debt maturing every year compared to the usual large cash availability of the group. In FY 2022, the liquidity ratio significantly decreased, standing at 23% (its first time below 200% over the period considered) due to the exceptionally high working capital absorption. We expect this ratio to once again exceed 110% in FY 2023 and predict comfortable levels even in the following years, supported by robust FOCF as well as available cash and cash equivalents constantly far greater than CHF 3.0bn. When considering a significant amount of committed unused bank facilities, Axpo's overall liquidity profile is even stronger, with liquidity ratios standing sharply above 200%.

Figure 13: Debt composition as of September 2022



Sources: Axpo, Scope

Figure 14: Maturity profile as of September 2022 (CHF m)



Sources: Axpo, Scope

Balance in CHF m	FY 2022	FY 2023E	FY 2024E
Unrestricted cash (t-1)	2,559	3,917	5,271
Committed unused credit lines (t-1)	2,185*	2,400	2,400
Free operating cash flow (t)	(2,374)	205	1,420
Short-term debt (t-1)	812	2,890	2,978
Coverage	**292%**	**226%**	**305%**

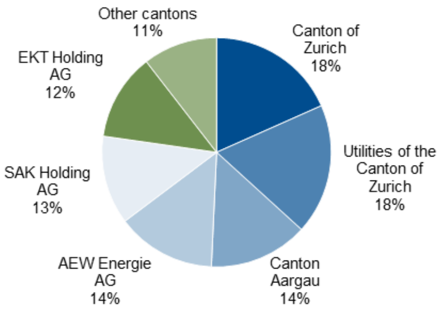
*Average unused headroom available at September 2021 (CHF 1,435m) and at March 2022 (assumed around CHF 1,500m)

Supplementary rating drivers: +2 notches

Credit-neutral financial policy

Management's 'risk appetite' for discretionary spending is low and reflects a prudent approach, as demonstrated by its dividend policy and its M&A activity. Apart from investment dedicated to the development of renewables assets, we do not expect other debt-funded business acquisitions. Furthermore, Axpo's management demonstrates its commitment to keeping credit metrics under control in order to maintain its investment grade profile. Based on these elements, financial policy is still credit-neutral, supporting our view that Axpo's future financial setup is likely to underpin the rating.

Two-notch uplift due to wide public support from Swiss authorities



Axpo is a government-related entity in accordance with our Government Related Entities Rating Methodology. This is based on the full public ownership by Swiss cantons and the essential public services provided by the company, signalled by its status as a systemically relevant utility. Given the positive differential between Axpo's standalone issuer rating of BBB on the one hand and the Swiss Confederation's sovereign credit rating and the Canton of Zurich's sub-sovereign rating of **AAA/Stable** on the other, the capacity to provide financial support is high. In light of Axpo's strategic role in the Swiss energy market as a critical power generator and electricity supplier with a strong public interest, we deem the willingness of Swiss authorities to provide support as high, as demonstrated by events in 2022 amid the energy crisis (i.e. CHF 4.0bn credit facilities granted by the Swiss Government). Based on the above, we have granted a two-notch uplift to the standalone rating.

Outlook and rating-change drivers for the underlying issuer rating

Outlook: Positive

The revision of the Outlook to Positive from Stable reflects our expectation that credit metrics will remain strong, with leverage – measured by Scope-adjusted debt/EBITDA – stable below 2.0x over the next few years, sustained by a still solid cash generation capacity despite normalising margins and mounting capex.

Positive rating-change driver

A rating upgrade would be considered if the company confirmed the improvement of its credit metrics, with Scope-adjusted debt/EBITDA remaining well below 2.0x on a sustained basis, paired with a still solid cash flow generation, despite the cooling down of commodity prices.

Negative rating-change driver

A negative rating action, such as a reversion of the rating Outlook to Stable, could be considered if our expectation of Scope-adjusted debt/EBITDA remaining well below 2.0x does not materialise.

Further ratings downside – albeit deemed remote currently – could be triggered by i) a strong deterioration in leverage and cash flow generation, i.e. if Scope-adjusted debt/EBITDA exceeded 4.0x accompanied by negative free operating cash flows, or ii) any change that negatively affects our view of the potential shareholder support from public authorities.

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