FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms EDF's IDR at 'BBB+'; Removes RWN; Outlook Negative

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Fitch Ratings - Milan - 02 Mar 2022: Fitch Ratings has affirmed Electricite de France's (EDF) Issuer Default Rating (IDR) at 'BBB+', and removed the Rating Watch Negative (RWN). The Outlook on the IDR is Negative. A full list of rating actions is available below.

The rating affirmation mainly reflects EDF's commitment to restore a reported net debt/EBITDA at about 3.0x by 2023. This is consistent with Fitch's revised funds from operations (FFO) net leverage sensitivity for a 'bbb' Standalone Credit Profile (SCP) at 4.0x. We expect performance to normalise in 2023, since our base case assumes no further state intervention and no necessity to buy back electricity. We have taken a cautious approach on prices and production (305TWh) for 2023, and we see further outages as the key risks for our base case, driving the Negative Outlook.

The IDR factors in a one-notch uplift for state support and links with the state. The recent statements about France's ambitions for new nuclear reactors underpin the company's strategic relevance, despite EDF receiving less capital injection from the state than our previous expectations. The uplift also considers that the state would support the company to reach the target leverage in 2023, in case of unexpected events.

KEY RATING DRIVERS

Mixed Picture from Remedial Measures: The measures announced by EDF to deal with the extraordinary situation of 2022 mainly include a capital increase of about EUR2.5 billion and asset disposals of about EUR3 billion across 2022-2024. The state is also committed to a scrip dividend for 2022-2023. This is lower than our expectations in presence of Fitch-projected negative free cash flow (FCF; pre-measures) of about EUR12 billion.

However, the clear commitment to bring reported leverage back to 3x in 2023 (about 4.0x in terms of our FFO net leverage) indicates that further actions will be taken if things turn out to be different from the current management's expectation. This is a key consideration for the rating affirmation.

Operational Risk Is Key Threat: The state of the fleet is the key risk for EDF's future, in our view. Currently, five reactors - among the newest of the fleet - are undergoing outages to repair corrosion close to the welds on the pipes of the safety injection system (a back-up system needed to cool the reactor in case of emergency). Six further reactors will be investigated, while no public statement has been made about the remaining reactors.

The company has revised the French nuclear production expected for 2022 (295TWh-315TWh) and 2023 (300TWh-330TWh); however, a material downside risk remains, and we cannot rule out that similar problems could re-emerge in the future in other parts of the plants.

Uplift Confirmed: The rating continues to incorporate a one-notch uplift for state support. The capital increase of EUR2.5 billion, coupled with the commitment to scrip dividends, is lower than our expectations, but the recent developments have enhanced EDF's strategic importance. President Macron's announcement in February 2022 that France would develop up to 14 new nuclear reactors with huge public investments over the coming decades makes EDF pivotal for the country's energy transition. It has been made clear that the new nuclear plants would not be funded through EDF's balance sheet. The uplift also considers our expectation that the state would further intervene to preserve EDF's financial health, if needed.

Back to Normal in 2023: Our forecasts for 2023 foresee a production of 305TWh (lower end of the communicated range), no repeated state intervention and no necessity to buy back electricity on the market. We also consider the hedging policy of the group and mitigate the current forward prices for the open position. This leads to a Fitch-defined EBITDA of about EUR16 billion, in line with the results of 2020-2021. We assume net investments of about EUR17 billion and the execution of the remedial actions, with a resulting FFO net leverage of 4.0x.

We expect some EBITDA recovery in 2024, mainly due to a production assumption of about 340TWh, while assuming much lower prices than current forwards. However, the expected FCF is negative, with Fitch-adjusted net debt rising to EUR67 billion (from EUR49 billion at end-2021) and a flat net leverage of 4.0x. In our view, the key risk of underperforming the rating case is related to additional outages not factored in at the moment.

Nuclear Reform Remains Important: We believe that recent market and political events have confirmed the very high importance of the nuclear reform. The current exposure to price volatility can be detrimental for EDF, even when the market environment is theoretically favourable, as in 2022. We expect France's dialogue with the EU to resume after the presidential elections. An agreement granting good price visibility would be positive for the company's debt capacity.

Nuclear Plants Burdens Balance Sheet: Based on our estimate, more than half of EDF's FY21 reported net debt is related to the new nuclear plants of Flamanville and Hinkley Point C (HPC), both burdened by massive delays and extra costs. Flamanville should start its production within the rating horizon (full-year contribution would be about 12TWh), while HPC should be commissioned in the second half of the decade. The commissioning of these assets would give a fairer picture of the company's financial structure.

Positive Results in 2021: EDF posted solid results in FY21, with reported EBITDA increasing by 11% to EUR18 billion. This was mainly driven by higher volumes for French regulated activities and the contribution of the trading activity. French generation and supply remained broadly flat, due to high energy buy-back costs in 4Q21 fully offsetting the benefit from higher nuclear generation (up by 25.3TWh yoy) and production taxes. Fitch-defined net debt increased by about EUR2 billion, while FFO net leverage remained broadly stable at 3.6x.

DERIVATION SUMMARY

We estimate regulated and contracted EBITDA at 40%-45% of EDF's total - well below that of peers Engie S.A. (A-/Stable), Enel S.p.A. (BBB+/Stable) and Iberdrola, S.A.

(BBB+/Stable). EDF's weaker business profile (also due to higher operational risk entailed in its investment plan and asset base) and the large negative FCF expected across its business plan drive its lower debt capacity versus peers'. The FFO net leverage threshold between 'BBB+' and 'BBB' is 4.9x for Enel, Iberdrola and Engie (nuclear-adjusted) versus 3.0x for EDF (on an SCP basis).

As a consequence, EDF's SCP is weaker than the ratings of Engie, Enel and Iberdrola. EDF's IDR benefits from a one-notch uplift, due to the application of Fitch's *Government-Related Entities Rating Criteria*.

The ratings of EDF's subsidiaries in the UK reflect the application of Fitch's *Parent and Subsidiary Linkage Rating Criteria* and Fitch's view of their strong links with EDF.

KEY ASSUMPTIONS

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

-Absence of further state intervention on ARENH

-French nuclear output at 303TWh for 2022, 305TWh for 2023, 340TWh for 2024; French hydro output at 40TWh for 2022-2024

-100% hedging for a given year in December of the previous year; for the unhedged position we assumed market prices in the range of EUR65-EUR100/MWh in 2023-2024, much lower than current curves

-No regulatory allocations to dedicated assets across the period

-Annual net investments of about EUR17 billion for 2023-2024

-Cumulative disposals of about EUR3 billion in 2022-2024

-Scrip dividends for the state for 2022-2023

-Capital increase of EUR2.5 billion in 2022

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

-The rating may be affirmed with the assignment of a Stable Outlook if the company reduces FFO net leverage to about 4.0x from 2023, in absence of further problems on the fleet

Factors that could, individually or collectively, lead to negative rating action/downgrade:

-Change in the state's attitude towards EDF, lack of support to reach the target leverage in 2023 (with further supporting actions, if needed) and reiteration of the measures taken in 2022 would result in a removal of the rating uplift

-Lack of visibility on deleveraging towards FFO net leverage of 4.0x by 2023

-Long-term reduction of available generation capacity from the existing fleet in France and weaker assessment of EDF's asset base

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

LIQUIDITY AND DEBT STRUCTURE

Moderate Liquidity: At 31 December 2021, EDF had readily available cash comprising cash and cash equivalents of EUR9.7 billion, (Fitch-defined) liquid assets of EUR11.1 billion and committed undrawn facilities of EUR13 billion, including EUR1.7 billion that is maturing within a year. This means that EDF can cover scheduled debt maturities of EUR13.6 billion for 2022, and expected negative Fitch-defined FCF of about EUR11.7 billion for the same year without resorting to additional debt issuance.

ISSUER PROFILE

EDF is a leading electricity company and global leader for low-carbon energy production. It is particularly well established in Europe, especially in France, the UK, Italy and Belgium, as well as North and South America. It covers all businesses spanning the electricity value chain - from generation to distribution - including energy trading activities. It has 37 million customer accounts and is particularly exposed to generation from nuclear sources.

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.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This 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. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT	RATING		PRIOR
EDF Energy Limited	LT IDR	BBB- Rating Outlook Negative Affirmed	BBB- Rating Watch Negative
EDF Energy Customers Limited	LT IDR	BBB- Rating Outlook Negative Affirmed	BBB- Rating Watch Negative
Electricite de France (EDF)	LT IDR	BBB+ Rating Outlook Negative Affirmed	BBB+ Rating Watch Negative

	ST IDR F2 Affirmed		F2 Rating Watch Negative
senior unsecured	LT BBB+ Rating Outlook Negative Affirmed		BBB+ Rating Watch Negative
subordinated	LT BBB- Rating Outlook Negative Affirmed		BBB- Rating Watch Negative
EDF Energy Nuclear Generation Limited	LT IDR BBB Rating Outlook Negative Affirmed		BBB Rating Watch Negative
EDF Energy Holdings Limited	LT IDR BBB Rating Outlook Negative Affirmed		BBB Rating Watch Negative

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Government-Related Entities Rating Criteria (pub. 30 Sep 2020)

Corporate Hybrids Treatment and Notching Criteria (pub. 12 Nov 2020)

Corporates Recovery Ratings and Instrument Ratings Criteria (pub. 09 Apr 2021) (including rating assumption sensitivity)

Corporate Rating Criteria (pub. 15 Oct 2021) (including rating assumption sensitivity)

Sector Navigators - Addendum to the Corporate Rating Criteria (pub. 15 Oct 2021)

Parent and Subsidiary Linkage Rating Criteria (pub. 01 Dec 2021)

APPLICABLE MODELS

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

Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

EDF Energy Customers Limited	EU Issued, UK Endorsed
EDF Energy Holdings Limited	EU Issued, UK Endorsed
EDF Energy Limited	EU Issued, UK Endorsed
EDF Energy Nuclear Generation Limited	EU Issued, UK Endorsed
Electricite de France (EDF)	EU Issued, UK Endorsed

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