

Research Update:

Stockholm Exergi Downgraded To 'BBB' After Bioenergy Carbon Capture And Storage Investment Decision; Outlook Stable

March 31, 2025

Rating Action Overview

- On March 27, 2025, Swedish district heating operator Stockholm Exergi Holding AB announced that it had taken the final investment decision on the construction of a bioenergy carbon capture and storage (BECCS) facility at its combined heat and power plant in Värtahamnen, Stockholm. The investment is expected to cost around Swedish krona (SEK)13 billion and begin operations in late 2028, with a capacity to capture 800,000 tons of carbon dioxide (CO2) per year.
- We revised our assessment of the company's business risk, to reflect our view that the carbon capture-related activities have higher risk than its district heating operations. Additionally, we have observed increased volatility and reduced profitability in the district heating segment over the last few years due to elevated fuel prices.
- At the same time, we believe BECCS represents a key pillar in the City of Stockholm's decarbonization strategy and is essential for the city to meet its emissions targets. We therefore now consider the likelihood of extraordinary support from the city, which owns 50% of Stockholm Exergi, as moderately high, from moderate previously.
- We lowered our long-term issuer credit rating on Stockholm Exergi to 'BBB' from 'BBB+', as well as the Nordic regional scale rating to 'K-2' from 'K-1'. We affirmed the short-term issuer credit rating at 'A-2'.
- The stable outlook on the long-term issuer credit rating reflects our expectation that Stockholm Exergi's district heating operations will continue to support its operating cash flow and material investments in the BECCS project, and that funds from operations (FFO) to debt will remain around 13% over the coming years.

Rating Action Rationale

We believe the BECCS project increases Stockholm Exergi's importance for Stockholm but exposes the company to an unregulated and immature market. The BECCS business model

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remains largely untested in the European market at this scale. Compared with Stockholm Exergi's current operations, the SEK13 billion investment exposes the company to several new risks, such as the technological feasibility of the project at the planned scale and efficiency at full capacity, and increased counterparty risk from voluntary carbon market contracts, which we understand will continue to be signed throughout the construction period. Additionally, over the past few years, the profitability of district heating has declined due to increasing biofuel prices and the timely recovery of associated costs via tariff adjustments, leading to a marginally weaker business risk profile even before factoring in the BECCS investment. That said, we believe that Stockholm Exergi can benefit materially from the fact that the BECCS operations complement its existing business strategy. When commissioned, it will strengthen profitability, particularly due to the coclaiming process during the first 15 years, which provides subsidies through the reverse auction from which Stockholm Exergi has been granted SEK20 billion, and we understand the BECCS operations will have a high share of contracted revenue through long-term voluntary carbon market contracts. We revised down our assessment of the company's stand-alone credit profile (SACP) by two notches to 'bb+' to reflect our view of its weaker business risk profile and the deteriorating credit ratios.

We believe that Stockholm Exergi plays an important role for Stockholm's district heating and electricity provision to about 800,000 people and BECCS will strengthen this role for the city's decarbonization strategy including being fossil-fuel free by 2030 and climate neutral by 2040. We have therefore revised our view of the likelihood of support from the city toward Stockholm Exergi to moderately high from moderate, resulting in a two-notch uplift from the company's SACP and a long-term rating of 'BBB'.

The SEK13 billion investment pressures Stockholm Exergi's financial metrics, and the rating is sensitive to delays and cost overruns. The financial impact from the annual investment of more than SEK4 billion from 2025 will be material--an entire year of EBITDA--versus the about SEK2 billion in 2024. This will weaken Stockholm Exergi's ability to withstand adverse financial events and cost overruns. It could result in rating downside if FFO to debt sank materially outside the 12%-14% range we expect over 2025-2026, trending towards 11%. However, we expect dividends during the construction phase to reduce to around SEK400 million-SEK450 million annually in 2025-2027, compared with SEK850 in 2023. This will somewhat reduce the pressure on FFO to debt, but we see the headroom under the current rating as limited and sensitive to any increases in debt or reductions in cash flow, which could, for example, stem from higher fuel prices, higher dividends, or BECCS cost overruns. Any delays in the commissioning of the facility could markedly affect Stockholm Exergi's financial profile, as capital expenditure (capex) accumulates but new EBITDA doesn't materialize. Nevertheless, we expect Stockholm Exergi's district heating operations, which historically generated about 85% of total revenue, to continue contributing a large share of stable earnings during the construction of BECCS.

Outlook

The stable outlook reflects our expectation that Stockholm Exergi's stable district heating operations will continue to support its operating cash flow and material investments through the construction of the BECCS project. We forecast Stockholm Exergi's FFO to debt at around 13% and believe that its credit metrics will remain vulnerable to further fuel price increases and any inability to fully pass on the increased costs to consumers. Despite the execution risk, we expect that Stockholm Exergi's district heating activities will be unaffected by the development of the BECCS project and remain a stable profit contributor.

Downside scenario

We could lower the rating if we revised down our assessment of Stockholm Exergi's SACP, for instance if FFO to debt weakens toward 11%. This may be due to cost overruns on the BECCS investment, continued cost pressure from biomass prices, or higher-than-expected dividends. A change in our assessment of the likelihood of extraordinary government support from the City of Stockholm would also lead to a downgrade, all else remaining equal.

Upside scenario

While unlikely before the project is mostly complete, we could upgrade the company if it is able to prove the feasibility of BECCS at a larger scale and is able to complete the construction on time and on budget while consistently posting FFO to debt above 15%. We could also upgrade the company if the SACP remains 'bb+' and if we revised the likelihood of support to high, which we see as very unlikely over the next two years.

Company Description

Stockholm Exergi is the largest provider of district heating in the greater Stockholm region, with production capacity of about 4,000 megawatts. More than 90% of its district heating system is based on renewable or recycled energy. It has about an 80% market share in its operating area, and reported EBITDA of SEK2.511 billion in 2024. Stockholm Exergi provides heating for over 800,000 people in and around Stockholm, and the district heating network is made up of 3,000 kilometers of underground pipes. Of its 10,400 customers, about 8,000 are apartment building associations and real estate companies. Stockholm Exergi also provides cooling to about 400 customers.

The company is 50% owned by the city of Stockholm (AAA/Stable/A-1+) and 50% by Ankhiale, a consortium of mainly pension funds, including APG, Keva, Alecta, PGGM, and AXA. Ankhiale acquired its 50% stake from Fortum in 2021.

Our Base-Case Scenario

Assumptions

- Sweden's GDP growth of 1.8% in 2025, and 2.8% in 2026.
- EBITDA margin of 33% in 2025 as biofuel prices normalize and increased costs are passed onto customers through the new pricing mechanism. From there we expect the EBITDA margin to reach 38%-45% gradually.
- Combined capex of SEK22 billion over 2025–2029, largely to fund the BECCS project but also general maintenance and development of the district heating network.
- Limited working capital outflows of less than SEK200 million annually, and with a generally neutral effect.
- We assume dividend payout in the range of SEK400 million-SEK450 million annually over 2025-2027.
- Debt will increase significantly as investments in BECCS accelerate in coming years, resulting in debt around SEK22 billion in 2027.

Key metrics

Period ending	Dec-31-2023	Dec-31-2024	Dec-31-2025	Dec-31-2026	Dec-31-2027
(Mil. SEK)	2023a	2024p	2025e	2026f	2027f
EBITDA	2,142	2,511	2,900-3,100	3,400-3,600	4,000-4,200
Funds from operations (FFO)	1,541	1,767	1,900-2,100	2,300-2,500	2,700-2,900
Capital expenditure (capex)	1,627	2,134	~3,000	~4,000	~7,000
Dividends	850	-	400-450	400-450	400-450
Debt	14,810	14,823	15,700-15,900	17,700-17,900	21,800-22,900
Adjusted ratios					
Debt/EBITDA (x)	6.9	5.9	5-5.5	4.9-5.3	5.2-5.5
FFO/debt (%)	10.4	11.9	12-13	13-14	12-13

Liquidity

We view Stockholm Exergi's liquidity as adequate, reflecting our view that upcoming BECCS-related investment will erode the excess liquidity in the coming year. We expect available liquidity sources to cover 3.5x our forecast of near-term cash outflows, but much of the new financing is designed to fund BECCS capex. We also expect that sources will exceed uses even if EBITDA declines by 15%. We believe that the company has sound relationships with banks, and a high standing in the credit markets. This is evident from the continued participation Stockholm Exergi has in fixed-income markets.

Principal liquidity sources

- FFO of about SEK2 billion;
- Unrestricted and cash equivalents of SEK873 million;
- Working capital inflows of SEK450 million
- Undrawn bank lines and capex facilities of SEK18 billion (SEK3 billion maturing in 2028).

Principal liquidity uses

- Upcoming debt maturities of SEK2.7 billion;
- Capex of SEK3 billion, most of which relates to BECCS and;
- Dividends of about SEK400-450 million

Environmental, Social, And Governance

Environmental factors are a moderately negative consideration in our credit rating analysis of Stockholm Exergi, reflecting its large district heating operations (80% of current EBITDA). That said, the company was able to phase out coal from its district heating system two years ahead of schedule and ahead of many peers, and now only uses nonfossil fuels such as biomass. The sustainability of bioenergy is part of an ongoing discussion about the EU Taxonomy. We view

positively the BECCS project which will enable the company to shift from reducing CO2 emissions to zero.

The utilities industry, which includes district heating providers, faces short- and long-term risks from environmental factors. It also faces societal issues in terms of pollution laws and governance risk arising from political decisions affecting the industry; for example, targets for CO2 emissions.

Rating Component Scores

Rating Component Scores

Rating Component Scores	
Component	
Foreign currency issuer credit rating	BBB/Stable/A-2
Local currency issuer credit rating	BBB/Stable/A-2
Business risk	Satisfactory
Country risk	Very Low Risk
Industry risk	Low Risk
Competitive position	Satisfactory
Financial risk	Significant
Cash flow/leverage	Significant
Anchor	bb+
Diversification/portfolio effect	Neutral/Undiversified
Capital structure	Neutral
Financial policy	Neutral
Liquidity	Adequate
Management and governance	Neutral
Comparable rating analysis	Neutral
Stand-alone credit profile	bb+

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015

- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Related Research

- How Rising Fuel Costs Could Stress Swedish District Heating Companies' Creditworthiness, Feb. 12, 2024
- Stockholm Exergi Holding AB Outlook Revised To Negative On Cost Pressure; 'BBB+' Ratings Affirmed, April 26, 2023

Ratings List

Ratings list

Downgraded; Outlook Action

	To	From
Stockholm Exergi Holding AB (publ)		
Issuer Credit Rating	BBB/Stable/A-2	BBB+/Negative/A-2

Downgraded

	To	From
Stockholm Exergi Holding AB (publ)		
Issuer Credit Rating		
Nordic Regional Scale	--/--/K-2	--/--/K-1
Senior Unsecured	BBB	BBB+

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