Transcription

Fortum Q1 2022 / Interim report

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PRESENTATION

Ingela Ulfves

Good morning, everyone, and welcome to Fortum's webcast and news conference on our first quarter results for this year. My name is Ingela Ulfves and I'm the Head of IR at Fortum. This event is being recorded and we will post a replay of the call after this event on our website. With me here in the studio is our CEO, Markus Rauramo, and our CFO, Bernhard Günther who then together will present Fortum's first quarter 2022 figures and the Group's performance. Markus will also comment on the Russian situation.

After the presentation, we will open up for questions in the Q&A session over the teleconference. There will also be an opportunity to ask questions on the chat. So with this, I will now hand over to Markus to start.

Markus Rauramo

Thank you very much, Ingela. Today I will start with our Q1 performance and our key developments. As the war continues in Ukraine, I will give you an update on our perspective on our Russian businesses, we will briefly touch the disruption in global energy markets and close with our contribution to secure reliable and affordable energy by engaging with governments, customers and suppliers. Bernhard will walk you through the numbers in more detail.

I start with setting the frame looking at the Q1 headline KPIs. Last time on this stage, I was pleased to present outstanding operational 2021 results across the Group following the very volatile market fundamentals with unprecedented commodity price levels. Since then, following Russia's attack on Ukraine, the developments in the operating environment have been even more dramatic, and it seems at first glance that we have not been able to maintain our high earnings level, but that we have had to take a substantial hit on our results. But before you jump to conclusions on our Q1 performance, let me address the main reason for the negative earnings in the first quarter.

First, as a reminder, last year's Uniper related Q1 earnings included the extraordinary positive effects from the cold spell in North America, which did not reoccur this year. Additionally, some of the gas margins shifted from Q1 2022 into Q4 2021 because of Uniper's operational measures to secure liquidity. This was highlighted and included in Uniper's Q1 guidance in February. Therefore, it was already anticipated that Q1 2022 was going to be generally below prior year level.

Second, as Uniper announced in its profit warning some weeks ago, approximately €750 million of the normal earnings in Uniper's gas midstream business shifted to subsequent quarters of 2022. In March, Uniper seized the provided market opportunities and decided to shift earnings in order to create additional value. So what happened is that less gas was withdrawn from storage facilities in the first quarter than had been sold to our customers. Instead, the volumes were brought back from the market at higher market prices, hitting the Q1 result. This was done so that the gas in storage could be sold forward at a premium. These gains will materialise later this year.

What we see is normal optimisation activity at Uniper, but at current price levels, the magnitude of such a swing is substantial. However, this is not affecting the full year results and Uniper confirm their result guidance for 2022 and could also keep more gas in storage in Q1. What comes to the operating cash flow, the figures are in line with the earnings development for the first quarter and reflect the liquidity measures taken in Q4 2021, which now reversed in Q1. Our leverage is well below our target ratio of 2x financial net debt to comparable EBITDA. Please note that the sale of our 50% stake in Fortum Oslo Varme for roughly €1 billion that we disclosed in the end of March is not yet included. Similarly, Fortum's dividend was paid in April during Q2 2022. Bernhard will give more insights to this in his section.

Now, let me update you on our thinking on the Russian businesses. The ongoing brutal war in Ukraine continues to shock and outrage us all at Fortum, and our compassion is with the people who have been displaced or hurt by the senseless violence. As a company, we are exposed to the direct and indirect implications of Russia's invasion. There are several angles to be considered, but since the early days of the war, it has been clear, and we have said that we will not continue to operate in Russia as before.

So what have we done to manage and reduce our exposure to Russia? In addition to the previously announced investment and financing freeze in our Russian subsidiaries, we are preparing for a controlled exit from the Russian market with potential divestments as the preferred path. Also, Uniper has been preparing a possible divestment of its separately listed subsidiary, Unipro, and said that the process will be resumed as soon as possible.

Exiting Russia may take some time, and under the current Russian law, any transaction would require an approval from the Russian government. So far, our heat and power activities in Russia have continued to run efficiently. However, due to existing sanctions imposed by Russia, our operations are subject to significant foreign exchange transfer restrictions, which limit the ability to transfer funds, including potential dividend distributions out of Russia.

You have also seen that we have recorded pre-tax impairments of approximately €2.1 billion related to the Group's Russian assets. This includes Uniper loan to Nord Stream 2 and ownership in our assets in Russia. This is what we are doing with our operations in Russia and reflects how they are now valued. The other challenge is Uniper's commodities business, especially for gas. Uniper will not renew its coal import contracts after this year and will end the use and import of Russian coal in line with the EU sanctions in August.

And when it comes to Uniper's existing long-term contracts for Russian gas, this will not be prolonged, but we will have to import natural gas from Russia also in the future, as this is a substantial building block for Europe's, and especially Germany's, security of supply. Any major interruption of this flow will have severe consequences for end customers and industrial production in Germany. I will come back momentarily to how we are supporting Germany's efforts to reduce the dependence.

Having said that, I will move over to the market slide. After an extraordinary autumn and winter in 2021, the war and concerns over supply curtailments caused an upheaval in all commodity markets. The effects are most pronounced in natural gas with the European Front Month gas prices spiking above €200 per megawatt hour in Q1. High gas prices have also clearly increased both demand and prices of other commodities, coal, oil and power.

The Nordic system price has strongly increased in the wake of continental, European and UK power. Despite this increase, the spread to German power prices has grown both in delivery, but especially on the forward curves. German forwards continue to be set by the gas short run margin on costs, which are impacted by significant volatility and uncertainty. Nordic spot prices still more than Central European, exposed to low prices in case of wet and windy weather periods, which is reflected in the forward curve. Strong wind buildout, internal transmission net and interconnector restrictions and bottlenecks also affect the Nordic German spread.

What we are experiencing in Europe today is a severe energy crisis with deep uncertainty about supplies and further rising prices. It is therefore no surprise that energy is fast becoming the most important policy area for our economies. The factors at play simultaneously range from security of supply to geopolitics, inflation and climate objectives, triggering short- as well as long-term energy considerations.

With markets, political developments, and additional sanctions continuously in flux this has created unprecedented short-term challenges for the entire sector in Europe, as well as far-reaching implications for the longer-term energy system and transition. In this situation, utilities will continue to play a crucial part in diversifying supply to the EU, investing in domestic clean production and in developing critical infrastructure to increase the system's resilience. Let me now move to how Fortum group is positioned in this context.

The EU is tackling the need for short- and long-term transformation with the Repower EU plan. Policymakers demand an acceleration of the energy transition and have the ambition for energy independence. This is pursued while electrifying Europe, gas supply diversification, and transforming industry. Our strategy supports these goals, in particular through our strong position in CO_2-free power generation, security of supply, and gas. Security of supply in power generation is key, especially in our market in Germany and the UK. We are ready to extend the use of coal-fired generation into coming winters to bolster energy security, but we will only do this if it is requested by the respective governments, as we do not want to compromise on our decarbonisation ambitions.

In addition, we are ramping up our CO_2-free power generation. This year, we will get the addition of Olkiluoto 3's generation with our share of 400 MW. We have also applied for a lifetime extension of our fully-owned Loviisa nuclear plant until 2050. At the same time, we are proceeding with our investment in renewable growth, which includes the launch of our first Fortum Uniper wind and solar team project. The Pjelax-Böle and Kristinestad Norr Wind Parks with 380 MW capacity will be built in cooperation with Helen, the Helsinki city-owned utility.

In addition to clean power, Europe will continue to need gaseous fuels. However, Europe's indigenous natural gas production is declining and there are limited pipeline import opportunities as the production from the UK and the Netherlands is structurally trending down; hence, demand will need to be managed down and LNG imports need to rise sharply. European gas prices are high enough to attract substantial LNG volumes to Europe and visibly erode demand. But the phasing out of Russian gas is likely to be a multi-year effort. Consequently, Uniper will build and operate Germany's first LNG terminal in Wilhelmshaven to diversify the country's natural gas supply sources. Uniper is supporting this project with its on-site projects in the short term and in the medium and long term in the form of the Green Wilhelmshaven project.

Decarbonisation of gas will be key. Therefore, the plan is to provide additional unloading and handling facilities for green gases – for example, ammonia – in order to be able to utilise the full potential of this new infrastructure project. The green ammonia is either transported directly by rail or converted back into hydrogen on-site and can meet more than 10% of German hydrogen demand in 2030. But hydrogen will also have to be stored. Uniper has put the natural gas storage facility Krummhörn to the test for storing hydrogen as a large volume hydrogen storage facility is essential for the energy transition and the development of a hydrogen economy. Additionally, Uniper lately signed another agreement to produce blue hydrogen at that site in Killingholme in the UK in large scale. We are also participating in projects that are most obvious to support the energy transition, the use of waste energy.

In March, Fortum and Microsoft announced a unique collaboration project whereby Fortum will capture the excess heat generated by Microsoft's new datacentre region to be built in the Helsinki metropolitan area in Finland. The datacentres will use 100% emission-free electricity, and Fortum will transfer the clean heat from the server cooling process to homes, services and business premises that are connected to its district heating system. The waste heat recycling concept from the datacentre region will be the largest of its kind in the world.

And with this, I will now hand over to you, Bernhard.

Bernhard Günther

Thank you, Markus, and a warm welcome also from my side. As usual, I will start with an overview of our key financials. As exceptional market price movements continue, I will again run you through some reconciliations how the market volatility has impacted our P&L balance sheet and cash flow. As Uniper is the main driver of the year-on-year delta and most of you will have followed their disclosure and investor call in previous weeks, I will comment the segments only on an aggregated level today and close with the outlook session.

I want to start with our financial overview summarising the key comparable indicators. Q1 comparable operating profit was predominantly affected by a significant €750 million earnings shift in Uniper's gas business, which turned Q1 earnings into a loss. However, as this is only a shift of earnings between quarters, it is consequently not affecting full-year earnings. As Uniper confirmed in their profit warning, the full year results guidance remains intact.

Also, net cash from operating activities turned negative, which is in line with the earnings development, but also a consequence of liquidity measures taken by Uniper at the end of last year. This was to manage the liquidity situation that is now reverting to a certain extent. Please remember that cash conversion from comparable EBITDA to OCF has been above 130% in 2021. Therefore, this reversal should not come as a surprise.

Our financial position reversed accordingly with financial net debt to comparable EBITDA at 1.0x at the end of Q1; however, still well below our target of below 2x. The 0.2x at year end was also driven by the aforementioned liquidity measures taken by Uniper and the Group. The strong increase in commodity prices has naturally impacted P&L, balance sheet, and liquidity. But before diving into these details, let's have a brief look on the segment overview.

Looking at the Q1 earnings figures, we see a substantial decrease in comparable operating profit. Nearly all business segments are down year on year due to various reasons, but obviously the largest deviation is related to Uniper. Let me start with generation. Comparable operating profit increased by €13 million with another strong first quarter. This is due to almost €7/MW higher achieved power prices. And these numbers show strong physical optimisation, despite lower hydropower volumes due to lower inflow and lower reservoir levels at the beginning of the quarter.

Russia. There, comparable operating profit was down €39 million following the expiry of the CSA payments for Nyagan 1, the lower Russian rouble exchange rate and the lapse of €17 million sales gain in 2021.

Then, City Solutions comparable operating profit was down 38 million, mainly due to structural changes, including the sale of the Baltic District heating business and solar plants in India in 2021. The Q1 2022 result is also negatively affected by significantly higher fuel prices. Consumer Solutions was almost flat, despite a very challenging market environment for retailers.

And finally, and as mentioned before, Uniper. Here we see a massive decrease of €1.5 billion year on year. The decline in earnings is mainly attributable to Uniper's global commodities gas midstream business, in particular, the already mentioned gas storage optimisation. In view of the current market environment, Uniper reduced its anticipated gas storage withdrawals in the first quarter to the benefit of future quarters. This resulted in a significant earnings shift of 750 million from the first quarter into the remaining quarters of 2022. Additionally, Q1 2021 took profit from one-offs like the cold spell in North America, which did not reoccur. For further details, may I refer to Uniper publications. And now over to the P&L.

What you see here is the reconciliation between comparable and reported figures. In essence, there are three things I would like to highlight that are all linked to the situation in Russia and the development of commodity prices. First, the items affecting comparability. Operating profit for the period was impacted by nearly €2 billion of items affecting comparability. One component is changes in fair values of non-hedge accounting derivatives. They amounted to €1.1 billion and are almost entirely related to the Uniper segment as Uniper has the strongest exposure to commodities.

As commodity prices surged, these hedges decreased significantly in value. However, the corresponding value of underlying assets, like power plants or inventories is not reflected here as their book values are kept at historic cost under IFRS. The mismatch is only temporary and will resolve over time as the products go into delivery and the position settle. Therefore, this will revert. Additionally, the items affecting comparability include impairments of 830 million and in Q1 we booked 275 million related to fixed assets and goodwill for Fortum's Russia segment and 555 million of impairments for the fixed assets from Uniper's Russian segment, Unipro.

The second effect we see in P&L is in the share of profits or losses from associates and joint ventures. They turned negative, as it includes now €150 million impairments related to Fortum's ownership in Russian TGC-1 and 22 million of impairments for the renewables joint ventures in Russia.

Thirds, in finance cost, you'll see a strong decrease of €956 million. The change in finance cost net, mainly relates to the 1 billion impairment of Uniper's financial loan receivable, including accrued interest for the Nord Stream 2 pipeline project. The receivable was fully written down. Consequently, the corresponding 100 million of interest income will no more be recorded going forward. Now over to the balance sheet.

The substantial increase in fair value of our financial derivatives further increased the balance sheet. The increase in commodity prices had a significant impact on the derivative financial instruments, especially in the Uniper segment. Please note that those are booked on a gross basis to the balance sheet, so all the yields increase the balance sheets, even though maybe the same product has been sold back and forth and several times in the same period.

One focus area in the last month has been to reduce the exposure to collateral and margin requirements as a major part of our hedges have been placed at traded markets. Therefore, Uniper increased the share of OTC deals that have limited or no margin requirements. This has been proven right as commodity prices further increase substantially, especially on the outer end of the curve, while margin receivables decreased. We are working closely together with Uniper, their business, as well as their financing partners to make sure that the margin calls and the resulting liquidity risks are properly managed. Liquid funds decreased by 1.2 billion following the repayment of debt, but are still at a very healthy level.

Now over to the cash flow statement. The cash flow statement confirms what we have seen on the balance sheet. The net cash delta of the change in margin in receivables and liabilities is synchronised with the financing. The net cash from operating activities turned negative in Q1. This was, on the one hand, driven by the very low cash effective EBITDA in the context of gas storage optimisation where we shifted earnings to the later quarters, but also due to the reversion of the operational liquidity measures, mainly payments for CO2 allowances and gas that were undertaken by Uniper in Q4 to manage the higher margin requirements following the extremely high commodity prices and volatility.

The cash flow from investing activities for the last 12 months is clearly driven by the divestments and margin receivables. In order to achieve high liquidity in the most cost-efficient way, Fortum and Uniper used a broad set of financing tools, including commercial papers, bank loans, intra-group loans, and ultimately also operational measures within the commodities portfolio.

The next slide shows net debt and our maturities profile. As the graph shows, our financial net debt is up following the negative Q1 operating cash flow. Consequently, our leverage KPI of financial net debt to comparable EBITDA reverted from the extremely low level of 0.2x to 1x which is still comfortably below our target of below 2x. We currently have $13.8 billion of gross debt and an average interest rate of 1.0% for the whole loan portfolio.

Looking at the loan maturity profile, this might appear a bit front loaded, but please note that the increase in short-term liability is linked to our cash reserves as we wanted to increase and secure sufficient financial flexibility in these extreme commodity market situations. At the same time, our liquidity position is very solid with liquid funds of approximately €6.4 billion. In addition, we have committed undrawn financing of close to €6 billion. So overall, our liquidity position is solid.

Regarding our BBB flat rating. Due to the constantly developing external circumstances and increased uncertainties, we are in continuous dialogue with our rating agencies. In March, S&P put both Fortum's and Uniper's rating on CreditWatch negative while Fitch kept Fortum at stable outlook. Our discussion continues with rating agencies, and we await S&P to resolve the CreditWatch negative in due course.

Let me finally now come to the outlook. Fortum's successful hedging has continued to create predictability and visibility. The hedge prices for our generation segment have increased for this year, and also the 2023 hedges are up. Regarding Uniper's hedges, it is important to note that Uniper's hedge prices have changed in Q1 because they made some changes to the hedge price reporting. It is also good to note that the hedge prices shown here are only for outright volumes, meaning hydro and nuclear volumes. So, gas or coal volumes are not included. The same also applies for Uniper.

Regarding CapEx for 2022, we reiterate our CapEx guidance of approximately 1.5 billion, of which maintenance is expected to be around 800 million. For the year 2022, maintenance CapEx is accordingly at the upper end of the range as normal maintenance CapEx would be rather in the ballpark of 750 million.

With this I conclude our presentation and we are now ready to start the Q&A session. Ingela, over to you.

Ingela Ulfves

Thank you, Bernhard, and thank you also, Markus, for the presentation. So, as said, we're now ready to take your questions. Please state your name and company before you ask the question. And we would also ask you now to limit yourself to maximum two questions each. As I said, there is also the possibility to ask questions on the chat. However, if there are many questions on the telco, we will prioritise those first and therefore ask you to also leave your contact details when posting a question on the chat so that we can come back to you later from the IR team.

But with this, let's begin the Q&A session. Moderator, please start.

Q&A

Operator

Thank you. Just as a reminder, if you wish to ask a question, please dial 01 on your telephone keypads now to enter the queue. Once your name is announced, you can ask your question. If you find your question has been answered before it's your turn to speak, you can dial 02 to cancel.

And our first question comes from the line of Sam Arie at UBS. Please go ahead. Your line is open.

Sam Arie

Thank you very much. And good morning, everybody. Thank you for the presentation. It's a complicated set of results, but you did a great job by walking us through all the detail. If you forgive me, Markus, I'd just like to jump in with a question on a topic you didn't really talk about, which is the German energy security law, which, if I'm right, is going through German parliament at the moment. And my question is, if you have seen a draught of that law, and if I'm right in thinking that what it currently says is that if Germany goes to the next level up in the gas framework – so that's kind of like the next level of security risk from where we are today – then gas suppliers like Uniper would no longer be required to honour contract prices, and customers could choose to take gas at market prices or not to take it. If so, I think that would be an extremely sensible set of measures for the Government to be implementing. But of course, it would be very helpful news for Uniper as well. So really, it would be helpful if you can talk us through what's going on there and if my understanding is correct.

And then secondly, if I'm allowed a second one, just a short one for Bernhard. And perhaps Bernhard, I could just ask you if you can confirm, please, if your shareholding in Uniper has changed at all since full year? Those are my two questions. Thank you very much.

Markus Rauramo

Again, good morning, everybody, and thank you, Sam, for the question and compliment on working through this. Yes, this is roughly our understanding of what will be handled now by the German government and parliament. My key takeaway is that in case there would be gas curtailment, then the gas suppliers would be allowed to procure gas from the market and pass on the cost to the customers, and customers would have a possibility then to not take. For me, this resembles the third level of the current Energy Security Act.

But what I would say here is that this is one part of tackling the energy crisis that we have at hand. Because of the Ukraine war, we have extreme conditions in the market. High prices, demand/supply uncertainty, and uncertainty on how the market is supposed to work in different conditions. And this is something that the governments truly have to address, between governments within the EU and then between governments and companies. And whilst I agree on a high level that this is what you described and what I am seeing, then the details of how this would actually then happen, that remains still to be seen. But what I see is that the German government and other governments, they are taking actions to have a controlled situation or transition when Europe is then decreasing its dependency on Russian energy. So this is part of that that transition path, as I see it.

Bernhard Günther

Shall I take the second question, Markus? Sam, on your question about our shareholding, it's important to see that we have a change in our reporting practise starting in 2022. So, unlike hitherto where we reported, including in 2021, share purchase of Uniper under investing activities, we have now revised this reporting and to bring it more in line with IFRS 7 requirements, and it's now shown under financing cash flow because in terms of IFRS consolidation, we also consolidate 100% of Uniper and therefore, basically, the search you had to do in former quarters in the investment cash flow is now to be done in the financing cash flow.

Sam Arie

Okay. Thank you for the pointer, but you're not going to comment what's your overall percent ownership today and has that changed since full year?

Bernhard Günther

No, unfortunately not.

Sam Arie

I'm going to have to try and figure it out. Okay. Thank you very much. And thanks, Markus, for your answer too. That seems like very positive development on the German side.

Bernhard Günther

Okay. Operator I guess we're waiting for the next question.

Ingela Ulfves

There's some technical issues here now with the line. Meanwhile, we can take a question from the chat. So there's a question from Ingo Becker from Kepler Cheuvreux: Good morning. Could you comment on your view on the risk of a clawback in Finland and Sweden respectively? In particular after the recent comments in Austria concerning Verbund, like Fortum, an outright power producer.

Markus Rauramo

I haven't seen any such discussion taking place actually in Finland. The discussion is focussing on how we reduce the dependency on Russian energy and how we expedite the energy transition. So, this is where the focus of the discussion has been.

Ingela Ulfves

Thank you so much. And meanwhile, we're still waiting for the teleconference to get back on line. So, I will continue with a question from the chat again: What needs to happen to resolve the CreditWatch negative? What is the latest on the rouble payment to the Russian government on gas? This is a question from Deepa at Bernstein.

Markus Rauramo

Maybe I'll let Bernhard take the CreditWatch question and I'll take the roubles question.

Bernhard Günther

Okay. So, yes. Hi, Deepa. What needs to happen, I think it's part of the business model of rating agencies that they usually don't give you precise what-if instructions. So if you do this, then exactly that will happen. But I think in all the discussions we had over the last couple of weeks, it became clear that the issues around potential gas curtailment scenarios are the main ones currently driving the discussion, like also on the equity capital markets side. And we have demonstrated, I think quite convincingly that we manage to de-risk significantly our positions in terms of liquidity swings triggered by commodity price volatility, as I mentioned before, and as you can also see in our balance sheet. And on the curtailment, of course, there are now these initiatives going on that Sam asked in his question on *Energiesicherungsgesetz* in Germany and others.

Markus Rauramo

With regards to the payments, the big question is about the security of supply, and especially in case of Germany on the natural gas supply to Germany. So we are working on then substituting the Russian volume, Russian energy volumes, for example, with additional LNG re-gas bookings, LNG terminal into Wilhelmshaven. So, looking for additional supply. Then when it comes to how the transition for the pipeline gas should be managed, we are in very close cooperation with the German government to find a solution for this transition to happen. We have, and we will, comply with all EU sanctions and we have, and we will, continue to pay in euro. And then for the solution, how will that happen going forward? I trust that we will find a sanction compliant solution together with the German government and Gazprom.

Operator

Thank you. Our next question comes from the line of Wanda Serwinowska of Credit Suisse. Please go ahead. Your line is open.

Wanda Serwinowska

Hi. Good morning. Wanda Serwinowska, Credit Suisse. Two questions from me. The first one is on Russia. Even if you sell the power and heat assets in Russia, Uniper still has a long-term contract with Gazprom, which also creates some exposure to Russia. Is there any way you can terminate it before 2035, 2036? And the second question is on Finland's prime minister's statement that Finnish companies should leave Russia soon. If I read your report this morning, there is no real hard commitment and there is no date. So has there been any development in the legislation? What is the thinking of your largest shareholdings as of the timing of exiting Russia? And would also the government consider the LTC of Uniper as a kind of asset in Russia? Thanks a lot.

Markus Rauramo

Yes, indeed. We said already in the previous quarter that we will not do new financing or new investment decisions in Russia. We have stopped the purchases of coal and biomass. And now we then told that we are targeting a controlled exit from Russia, and that includes our Russian assets. And that process will take some time. But the target is to have potentially a transaction for an exit. That also requires government approvals from the Russian government. These transactions take the time they take, and we will work determinedly towards that target.

With regards to the Gazprom contract. Yes, indeed, we have very long-term contracts that are in place, and then we have to then work out, like I said earlier, to reduce the dependency on Russian energy together with the governments, between the governments, between governments and companies. How does this transition happen in a way which then takes into account the security of supply and energy security of Europe. And that is something, for example, that the German government and parliament are addressing now this week.

Wanda Serwinowska

Thank you very much. A quick follow up. So, in my understanding, you are not basically able to terminate the LTC with Gazprom at the moment. And then when you said that any transaction in Russia would need to be approved by the government, was it the case always? I mean, if you find a buyer can you choose any buyer you want, or does it need to be a utility? Is there any restriction there? Thanks a lot.

Markus Rauramo

There's a valid long-term contract with Gazprom with a take-or-pay obligation and delivery obligation by Gazprom. So that continues to be in place. And like I said, there has to be an agreement between the governments, between governments and companies how to make this happen. When it comes to our controlled exit from Russia and a potential transaction, then we will see during the process what kind of interest for these assets there is. But it is indeed so that Russian government approval is needed for a potential transaction.

Wanda Serwinowska

Thank you very much.

Operator

Thank you. Next question comes from the line of Lueder Schumacher of Société Générale. Please go ahead. Your line is open.

Lueder Schumacher

Yes. Good morning. Lueder here. Two questions on my side. The first one is coming back to the energy security law. Just to confirm as it's a rather important point. Is it your understanding that in the case of any curtailment in gas volumes, all suppliers would be free of their contractual delivery obligations? Just double checking there. Also, is that part new? I.e., was that not covered in the 1975 version of the law? And also, are there any other relevant changes to the law that is being discussed at the moment? I mean, you will be as close to this as very few other people, so your views will be very interesting there.

The second question is on hedging. Given the high level of spot prices and the cost of hedging in terms of variation margins, etc., have you or are you planning to change your hedging strategy towards hedging less, i.e., sell a lot more spot than you used to do? The reason for asking is a) it would seem to be an obvious decision to be making, given that spot prices are very high, the forward curve is ridiculously low compared to spot prices, and we have recently seen other players, other generators such as Vattenfall announced that they are adopting a new price hedging strategy. What is your view on that?

Markus Rauramo

With regard to the energy security law, from my point of view, this is an addition to what was already in place. This goes one step further in clarifying that in case of a severe or full disruption, then the government is ready to go for additional measures to ensure the continuity in the market. I think this is my important takeaway. Then how that will happen in practise, the details, at least for me, they still remain to be clarified. How will the volumes be? How will they be allocated? Because there's not a physical matching, of course, in the market even today. So, there are details that remain open. But I think the intention, from my point of view, from an energy security and continuity of the market point of view is very important.

Then, for the hedging, especially with our Nordic outright position. We continue to be exposed to weather conditions to, for example, hydrology levels, temperatures and so on. So, what we are targeting with the hedging is the predictability and stability of the cash flows. And we have not changed our approach there.

Bernhard Günther

Maybe just adding that on the gas side, without going into any details, those long-term gas contracts, as you probably know, Lueder, have a certain element of indexation. So you're basically tracking the gas prices as they evolve. There you have even higher economic reason for hedging, because you know that on the one side, you're basically following exactly the same index that you can be selling it without going into further detail.

Lueder Schumacher

Okay. So you see no reason for changing your hedging strategy, irrespective of this huge disconnect between spot prices, forward curves and other big parties in the market changing. I mean, I can't really see where the value is, but obviously you still seem to be keen on hedging. So that's fine. Thank you.

Bernhard Günther

I think it's fair to say we are looking at it. It's not that we dogmatically stick to that. And for example, as soon as we would come to the conviction that there is a structural backwardation in the market, as you suggested, yeah, in terms of the relation between [inaudible 00:47:27] depending on what you assume for the underlying fundamentals. And then, of course, these are element which drive our specific decisions. But his is nothing we have announced in public.

Lueder Schumacher

Okay. Thank you very much.

Operator

Our next question comes from the line of Vincent Ayral of JP Morgan. Please go ahead. Your line is open.

Vincent Ayral

Hi. Good morning, everyone. So I had a question regarding the Russian asset sale. So it's been through already the question, so what I'll ask is regarding this: Will you keep consolidating these activities? I mean, the question I think is fair on whether you really have control in these operations. So far, we can see that both Uniper and Fortum keep consolidating these P&Ls from Russia. So what would make you change your mind going forward? Will we see these Russian assets [inaudible] at some stage in the next 12 months? So that would be question number one.

And then question number two, given it's a forced asset sale, you do not, and understandably, put any timeline in order to relieve a bit of pressure and hopefully be able to do that in better conditions later. But if the political pressure were to keep forcing on there, there is the risk that actually these assets could be seized as a compensation for long-term contracts, gas purchase commitments, if we had to get like a one-sided Europe in the ban on Russian gas, which is not a base case, but we're working here on crazy scenarios, as you understand. Thank you.

Markus Rauramo

Yeah. With regards to the thinking behind the asset sales. I would first look at how our business is doing, and actually the performance of the assets is very good. They are efficient. The availability is best-in-class and we are operating them safely. It is a question of the operating environment and our investment appetite in Russia, while we are now then targeting the full exit and as a part of that potential sale transaction of the assets. And then we will see how that process goes. I'll let Bernhard answer the consolidation question, which then has its normal triggers.

With regards to the whole question about political pressure and various scenarios. So, this is actually, the scenario work is something we do and that leads into the consideration. So, not only Russian assets but about other assets as well. We look at operating environment. We look at our possibilities to add value. Where do we best place our capital? And in this case, of course, for quite natural and very, very sad and unfortunate reasons, the war in Ukraine and the resulting view that we have on our ability to work in Russia, we have come to the conclusion that we will take a controlled exit from there. But it's a controlled exit, and our assets are performing well at the moment.

Bernhard Günther

Yes. On the consolidation question. It is obviously a very dynamic situation, so we are watching it by the day, by the week. And end of Q1, we concluded that we still had control of our Russian assets as shareholders, both Fortum and Uniper, for their respective assets. But of course, there can be circumstances also developing rather soon where we would come to the conclusion that we no longer have this control, so that we can no longer exert our shareholder rights. This is not an exact science, but this is a discussion we need to have both within the company and with our auditors, and then come to a judgement at the end of the quarter on how to treat it.

Vincent Ayral

Thank you. Just to be a bit more precise, what type of— If we see Board changes on these assets which are mandated and we started to see a few, could that be a trigger? So basically, I'm saying actually we don't have any more control on these assets.

Bernhard Günther

Yeah. For example, if we could no longer determine, or exercise our shareholder rights by appointing Board members. If we had no way of communicating with these assets or whatever, we would receive no data anymore. So I think these are all indicators that for a loss of control. Of course, there are very clear scenarios mentioned also about nationalisation or so, where it is quite obvious. But there are also other scenarios where it's about how you interpret different shades of grey and what conclusions you draw from it. Again, it's not an exact science and we are keenly watching it and attentively watching it every day.

Vincent Ayral

Thank you very much.

Operator

Thank you. Our next question comes from the line of James Brand at Deutsche Bank. Please go ahead. Your line is open.

James Brand

Hi. Thank you for taking my questions. I'm actually going to ask exactly the same questions that Vincent asked, so I'll ask a couple of different ones. The first one, just maybe following on from the topics that he was raising, can you get cash out of Russia? Because as I've heard, no one can, but maybe you can. And then secondly, on the SE2 region and the issues there, are there any reasons to think that that could improve at any point or maybe even deteriorate? If you have any thoughts on what the likely evolution is going to be there, that would be really useful. Thank you very much.

Markus Rauramo

Okay. I can start with the SE2 question, and then the cash out of Russia, maybe Bernhard wants to answer that one. But I see actually the long-term potential of clean energy for the Nordics, especially for the areas in Finland and Sweden and along the coastlines where you have very good wind conditions, great logistics, port infrastructure, road infrastructure. And this is attractive for new renewables development and therefore also energy intensive industries who will, going forward, need huge amounts of clean electricity and also increasingly clean gases.

And we see different kind of initiatives from companies who want to decarbonise their activities in the industries of steel, chemicals, manufacturing and so on, who are making today pledges. So, I do see that a dynamic building also around the recent announcements of building the Bay of Bothnia, Gulf of Bothnia, potential future hydrogen infrastructure. So yes, I see a very good potential there for the dynamic to develop positively and actually building on these good conditions which are now, of course, they are impacting now the SE2 prices because there is congestion on transmission capacity. But in the longer term, this will be a good investment signal for industries that are looking for stable countries to invest in and affordable, clean energy.

Bernhard Günther

With regards to getting cash out of Russia, our Russian division has never been, or has always been from a cash perspective, an entity of its own. So we did have dividend payments, or the like, happening but obviously not on a monthly, let alone weekly basis. So we have not tried it recently, but our assumption would be that currently it would not be possible to move the cash out of Russia.

James Brand

Thank you.

Operator

Our next question comes from the line of Iiris Theman of Carnegie. Please go ahead. Your line is open.

Iiris Theman

Yes. Hello, this is Iiris from Carnegie. My first question is related to your net debt. How would you expect your net debt to develop during the rest of the year? And my second question is related to this electricity price difference in Sweden. I understand that Sweden is talking about higher crazy investments in the future to solve this bottleneck between north and south. What is your understanding of these future investments and what kind of lead times one should expect? Thank you.

Markus Rauramo

I can start that with the second question, and I'll let Bernard take the first one. But I see two alternatives, two basic alternatives. Either the society invests heavily in debottlenecking, in Sweden especially, in debottlenecking the north-south direction. They should also do it east-west in South Sweden, but then enable the electricity to be transported into South Sweden or then, and maybe combined with some debottlenecking, actually create good infrastructure and grid connections in the SE2 area and Northern Sweden in general, not so much to transport the electricity.

There's a lot of potential. We talk about huge potential for wind in the northern parts and central parts of Sweden and Finland but actually attract, if we have a situation of really high competitiveness for clean energy production, then the question is, do you want to transport the energy or do you actually want to take the energy intensive industries there and have short-term transport distance. Whichever the case, actually investment in infrastructure will be needed. So, the SVK cannot forego investing. Either it is used to locally and you build some tens of hundreds of kilometres of high-voltage grid or then you build even more and take the energy south and eventually even to Europe.

I'm pretty convinced that we will actually see energy-intensive industries locate themselves to the areas where there will be, in the long term, clean electricity and clean gas surplus. And in Europe, that would mean the north and the very south. North for wind-based clean energy, and in the south, solar-based clean energy. And then the continental, much denser inhabited areas they may serve part of the need locally, but still a lot has to be imported. And then the question is, will that happen in the long-run in electricity or in gaseous forms?

Bernhard Günther

On the much more profane question of net debt guidance. You know that we don't guide net debt as we generally don't guide for the full year on the Fortum side at all. I can just maybe recall some of the big drivers and then leave it to your imagination on how you combine them. So we have obviously these intra-year movements of gas volumes which affected both the earnings side in Q1, but will also affect, or have also affected, the cash flow in Q1 and are bound to revert in the later quarters of this year. So this will be a positive effect.

Then we have obviously the transaction on Fortum Oslo Varme where we expect the proceeds to arrive in the second quarter. But we will also pay a dividend, Fortum dividend – or we have paid in Q2 and it's not in the reported numbers yet. So, these are maybe some of the big moving parts there, but it's very clear that the Q1 cash flow and its effect on net debt should not be linearly extrapolated to the full year.

Iiris Theman

Thank you. And regarding these grid investments in Sweden, what kind of lead times one should expect?

Markus Rauramo

They are long because of the permitting, the regulation, acceptance issues. So, we talk about years of development. And there has to be, first of all, there has to be conviction that this could be done. You're touching a very important point. So this is one of the things that continental Europe and Germany are really struggling with. So, permitting either new renewables or permitting energy transmission lines takes too long. It can take up to ten years. And that's not that does not facilitate the energy transition. This is why we're raising this point continuously. And our peer companies are doing that as well, both in the Nordics and as well as on the continent.

Iiris Theman

Thank you.

Operator

Our next question comes from the line of Piotr Dzieciolowski of Citi Bank. Please go ahead. Your line is open.

Piotr Dzieciolowski

Hi. Two questions from me. Thank you for your presentation. First one, I wanted to ask about the dividend policy. Is this crisis and what's going on with your financials changing anyhow your outlook on your dividend policy? You are about to pay the dividend now from last year profits. But I mean, just thinking about going forward, does this create any constraint or you are strongly still committed to the dividend as it is?

And second question, I wanted to ask you about your expectations towards the Russian assets, their operational performance. Clearly, first quarter doesn't show the picture. What do you see going on now in terms of the economic activity in the country and the impact of the assets? I remember last time in 2014 actually we've seen a significant impact also on the load factors, prices and so on. So what is your expectations with regards to this?

Markus Rauramo

With regards the dividend policy. Our policy is, and remains to be, that we want to pay a stable, sustainable over-time increasing dividend. And it's a combination of this. So we look at our dividend, we look at the balance sheet and we look at the CapEx and then we evaluate over time how these three are balanced. And of course, we listen closely to our stakeholders, investors look at the possibilities, how we can reinvest the money into growth. But I would say that what underpins all of this is that we believe that we have good competencies. We are in the right places, and we can grow our business and generate new revenues and new operating profit from our businesses.

And then we have to look at all this in the prevailing situation. We shall see how this year develops and where are we next spring. And then our Board will make the evaluation then. But my objective is that we use our competencies to invest in growth and deliver more results and run our assets efficiently and safely, which is a good bridge to the second question, with regards to the Russian economy.

There are various forecasts on how big is the impact on Russian economy of the war in Ukraine and the sanctions and its implications. It will be a heavy impact. What comes to our assets then? The key thing is that we continue. We keep up the good availability, the efficiency and safety of our operations. We take good care of the assets. So, we want to preserve the value in all circumstances. If we sell the assets, we want to sell them in a good shape and at the same time keeping the assets running efficiently. And our earnings are based on the spread we can earn over the fuel costs and the CSA or CCS payments. So there's the spread element and then the regulated part. And both of these have continued to perform as expected.

Piotr Dzieciolowski

Thank you very much.

Operator

Currently, we have one further question in the queue. That's from the line of Louis Boujard of Oddo BHF. Please go ahead. Your line is open.

Louis Boujard

Thank you very much. Good morning, everyone. Maybe two questions from my side. The first one, coming back on the Russian impairments. Just wondering, considering that most of them still consider intact [inaudible] as a share that is directly linked to Fortum is still relatively limited, in the question, considering that there is a lot of risk still notably in these values, how could you consider that the number and the figures that are currently proposed here are a fair value in case of exchange, in case of disposal? Do you have any support on this assumption that you have provided here for the €2.1 billion impairment? Or do you see that it could eventually be some risk on these assumptions and eventually further impairments that could be expected down the road on these assets' fair value?

Second question would be on the CapEx, the 1.5 billion CapEx that are considered for 2022, what share could be considered to be earmarked for actual renewable developments and energy transition developments? And what share is more related to traditional business? Thank you very much.

Markus Rauramo

Maybe I'll make a general remark for the impairments and let Bernhard elaborate. The assets are performing well. So basically, the cash flows are such the forecast has not changed. So, this is about scenarios and risk elements and risk premiums. And this is then a judgement we have to make, and I'll let you elaborate on that. We do open up in the report also how we have addressed this, so you will find guidance there.

On the CapEx side, renewables form a big part of it. And then it is the investments in grid services, grid stability – Grain, Killingholme, Irsching, Scholven. Then the investments into Pjelax-Böle and Kristinestad, and our other RES projects. So, the very big part is going into renewables and grid services.

Bernhard Günther

Maybe just to add only a bit to what Markus said, because he already, I think, has mentioned the big moving parts in the impairment. Technically, it is now obviously prescribed by our auditors both at Uniper and at Fortum, that you reflect a situation like the one we have in Russia by considering different risk scenarios. So, you assume different potential ways forward. And this, of course, is again like what we discussed on the full consolidation question, a very dynamic situation. So, it evolves as we speak, and we all don't know what the future will bring. So yes, of course, there is the possibility that in next quarter or in any quarter thereafter, we might come to a different view on how certain risks and scenarios might evolve in Russia, and therefore the impairment or the asset values would be accordingly adapted.

Louis Boujard

Thank you.

Operator

Thank you. Once again, if there are any further questions from the phones, please dial 01 on your telephone keypads now.

Ingela Ulfves

In the meanwhile, we could actually take some questions from the chat. There's a question from James Sparrow at BNP Paribas. How much more confident do you feel about your liquidity position and derivative exposure compared to what you presented at the full-year results? Despite the increase in derivative exposure during Q1, your margin exposure has gone down. Can you give more colour on how you have achieved this?

Bernhard Günther

I think I already mentioned on an earlier question that we have achieved a significant de-risking with regards to margins at risk or collateral at risk and the i.e. the liquidity swings that can be caused by commodity price movements. And this is very significant compared to the position we were in Q4 last year. So from that perspective, I feel much more comfortable and confident given the overall geopolitical situation and scenarios. Of course, it feels a bit odd to use the word comfortable, generally, but we are clearly much better positioned than we were some five or six months ago.

What have we done in the meantime? We have, basically, allocated our hedging activities much more, always a very different balance between exchange-traded channels and other channels, be they CSA or non-CSA in order to achieve a position where the overall exposure against commodity price shifts, especially on the gas side, is now drastically reduced. So, this is something we have been working on very hard since basically it all started end of Q3 last year, but now have reached a position, I think, there where that position at least generally I do feel comfortable, yes.

Ingela Ulfves

Thank you. And then we have a few more minutes until we need to end the call. There's one question, partly has been touched upon already, from Helsingin Sanomat, Laura Kukkonen: Uniper has long gas contracts with Gazprom. Would it be possible for Uniper to stop buying Russian gas controllably before these contracts end? And if so, how and when?

Markus Rauramo

This is a question about how do we handle the energy crisis. How do we take care of the security of supply and energy security of Europe? And it is an issue, like I said before, it's an issue that has to be dealt between the governments together, and together between governments and companies. We need to develop a pathway how to make the decrease on dependency on Russian energy. How do we make that happen? And we are actually making that happen by providing more supplies to the market, for example, in the form of booking more capacity at Gate LNG Terminal for more supplies into Europe. We are now building the first LNG floating re-gas storage terminal in Wilhelmshaven. This, together with the other LNG terminals will actually take care of a very substantial part of the supplies of Russian pipeline gas into Germany.

When it comes to the contracts themselves, they are contracts that have many years of length and there needs to be an agreement how they would be then modified. But currently, these contracts continue to be valid. But the key question is the security of supply, energy security of Europe, and how do we handle that? How do we make the transition in this situation?

Ingela Ulfves

And one last question from Ingo Becker at Kepler Cheuvreux: Could you comment on how your strategic ambitions with Uniper have changed with recent developments beyond the decisions you have taken for Russian operations?

Markus Rauramo

Our strategy actually remains the same. We are targeting to help with the energy transition to happen. Climate change is one of the biggest threats, if not the biggest threat we are facing. The energy transition needs to happen to a reliable, affordable, clean energy system.

So we are investing, and we will invest in growing in CO_2-free power, increasingly clean gas and infrastructure. And if anything, the current events, the current war, the terrible war in Ukraine and the resulting crisis, the resulting high prices, these just highlight the importance of the energy transition to happen. We are well placed for that. We have good competences, we have technology, we have capability, as we have shown just recently of working in all of these areas. And the recent announcements just highlight this point.

Ingela Ulfves

Thank you so much, Markus. Thank you, Bernhard. And thank you to the whole audience for participating here today. On behalf of Fortum, we now wish you a very nice rest of the day and end the call here.

Markus Rauramo

Thank you very much, everybody.