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## Research Update:

# German Utility RWE AG Hybrid Equity Content Revised To Intermediate; 'BBB/A-2' Ratings Affirmed; Outlook Negative

### Primary Credit Analyst:

Vittoria Ferraris, Milan (39) 02-72111-207; vittoria.ferraris@standardandpoors.com

### Secondary Contact:

Tobias Buechler, CFA, Frankfurt +49 (0)69-33 999-136; tobias.buechler@standardandpoors.com

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## Research Update:

# German Utility RWE AG Hybrid Equity Content Revised To Intermediate; 'BBB/A-2' Ratings Affirmed; Outlook Negative

## Overview

- RWE AG has announced that it is waiving a certain call option right in its hybrid security documentation.
- As a result, we have revised our assessment of the equity content of RWE's hybrid instruments to intermediate from minimal.
- We are affirming our 'BBB/A-2' corporate credit ratings on RWE AG and our 'BB+' ratings on RWE's hybrid debt.
- The negative outlook reflects adverse market fundamentals and the development of the nuclear debate in Germany.

## Rating Action

On Dec. 18, 2015, Standard & Poor's Ratings Services affirmed its 'BBB/A-2' long- and short-term corporate credit ratings on German utility RWE AG. The outlook remains negative.

We also affirmed our 'BBB' issue rating on RWE's senior debt and our 'BB+' issue rating on the three hybrid instruments issued by RWE AG in 2015: ISIN XS1219498141 (€700,000,000), ISIN XS1219499032 (€550,000,000), and ISIN XS1254119750 (\$500,000,000).

## Rationale

The affirmation follows the revision of our assessment of the equity content of RWE's hybrid capital to intermediate from minimal after RWE's announcement that it has, by a legally binding waiver, unconditionally and irrevocably waived a certain call option on the three aforementioned hybrid instruments, related to an "Equity Credit Rating Downgrade" clause in the instruments' documentation. The call option gives RWE the right to call the hybrid instruments if the equity content reduces as a result of a change in the rating on RWE. As we explained when we announced our revision of equity content on various issuances to minimal, this type of clause weakens our expectation that the issuance will remain a permanent part of the issuer's capital structure (see "Standard & Poor's Affirms Various Ratings Following Review Of Corporate Hybrid Equity," published on Oct. 27, 2015, on RatingsDirect)

In line with the appendix we have added to "Criteria Clarification On Hybrid

Capital Step-Ups, Call Options, And Replacement Provisions," published Oct. 22, 2012, to address several frequently asked questions, we considered the terms of the waiver of rights, its public nature, the circumstances under which it could be modified, the likelihood of its breach, and whether the other features of the hybrids are consistent with intermediate equity content (see "S&P Explains Treatment Of Step-Ups, Deeds, And Waivers For Certain Hybrids," published Nov. 13, 2015, for more details).

We have concluded that RWE's waiver of the call option sufficiently mitigates the risks of a call, and we have accordingly reassessed the equity content of RWE's hybrid instruments as intermediate rather than minimal. As a consequence, we now regard the hybrid securities as 50% equity when calculating RWE's credit ratios. The revised credit ratios support our ratings on RWE and, accordingly, none of the ratings are affected by the revision of equity content to intermediate.

The negative outlook reflects adverse market fundamentals and the development of the nuclear debate in Germany.

## **Ratings Score Snapshot**

Corporate Credit Rating BBB/Negative/A-2

Business risk: Strong

- Country risk: Very low
- Industry risk: Intermediate
- Competitive position: Strong

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: bbb

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Strong (no impact)
- Management and governance: Strong (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb

## **Related Criteria And Research**

## Related Criteria

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Key Credit Factors For The Unregulated Power And Gas Industry, March 28, 2014
- Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Methodology And Assumptions: Assigning Equity Content To Corporate Entity And North American Insurance Holding Company Hybrid Capital Instruments, April 1, 2013
- Criteria Clarification On Hybrid Capital Step-Ups, Call Options, And Replacement Provisions, Oct. 22, 2012
- Methodology: Hybrid Capital Issue Features: Update On Dividend Stoppers, Look-Backs, And Pushers, Feb. 10, 2010
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Hybrid Capital Handbook: September 2008 Edition, Sept. 15, 2008
- 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

## Related Research

- S&P Explains Treatment Of Step-Ups, Deeds, And Waivers For Certain Hybrids , Nov. 13, 2015
- Standard & Poor's Affirms Various Ratings Following Review Of Corporate Hybrid Equity, Oct. 27, 2015

## Ratings List

Ratings Affirmed

RWE AG

Essent Nederland B.V.

Essent N.V.

Corporate Credit Rating

BBB/Negative/A-2

RWE AG

Senior Unsecured

BBB

Junior Subordinated

BB+

Commercial Paper

A-2

RWE Finance B.V.

Senior Unsecured\*

BBB

\*Guarantor: RWE AG.

**Additional Contact:**

Industrial Ratings Europe; Corporate\_Admin\_London@standardandpoors.com

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