S&P Global Ratings

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CEZ a.s.

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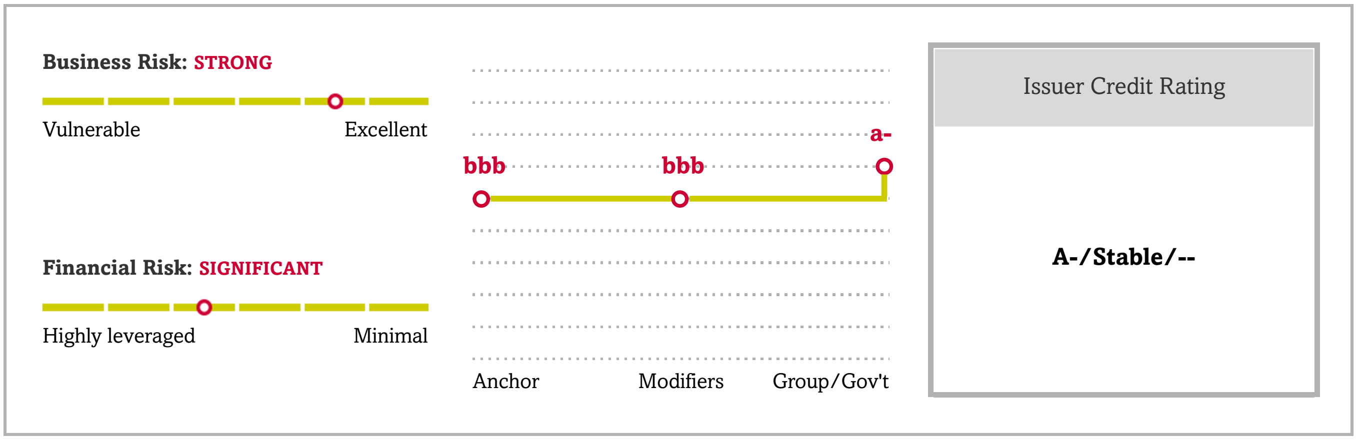


Credit Highlights

Overview

Key Strengths	Key Risks
Dominant position in the Czech Republic.	Persistent, large exposure to wholesale power, carbon prices, and carbon dioxide (CO_2) allowances.
Diversified and low-cost generation fleet.	Sizable portion of future sales hedged at below-market prices.
Sizable contribution from domestic regulated activities.	Limited geographic diversification with 90% of EBITDA generated domestically.
Potential for extraordinary government support given the company's importance in implementing state policies and strong link to the government.	Uncertain role in the new nuclear power plants.
	Material refinancing needs over the next three years.

CEZ a.s. has an unrivaled position in the Czech Republic, stemming from its vertical integration in the national power market. S&P Global Ratings believes CEZ continues to benefit from its incomparable position in the Czech Republic as a vertically integrated utility with approximately 70% and 30% domestic market shares for its generation and supply segments, respectively.

The company has a undefined role in the state's new nuclear power plants. We understand CEZ may be involved over the coming decade in the development of at least one new nuclear power plant under the state energy policy. At this stage, however, the details of the contract, the potential investments, and the role of CEZ have not been specified.

The company's relatively diversified and low-cost generation fleet, benefits from the ability to generate power from nuclear sources domestically. CEZ benefits from its diverse and relatively fuel- and emission-efficient generation fleet along the load curve, spread across lignite and hard coal, nuclear power, hydro and renewables, and combined cycle gas turbines

The company has a sizable and stable cash flow contribution from domestic regulated activities through the ownership of the largest Czech distribution network. CEZ derived 40% of its EBITDA in 2018 (35% in 2017) from its regulated activities, predominantly power distribution networks in the Czech Republic. The regulation provides the group with a favorable remuneration scheme, high stability of earnings, and minimal exposure to volume and inflation risk.

We believe there is a moderately high likelihood of extraordinary government support. In our view, CEZ benefits from a moderately high likelihood of potential extraordinary support from the Czech government. We base our opinion on the company's importance in the implementation of state policies and its strong link to government, which currently owns 70% of the company. CEZ is the dominant Czech power generator and the power distributor.

The company has ongoing, material exposure to competitive power markets, volatile wholesale power prices, and carbon prices. CEZ's generation fleet is predominantly fixed-cost and contributes substantially to the group EBITDA, which exposes consolidated EBITDA to market conditions. The company is mitigating this exposure through gradual hedges on generation over the next two-to-three years.

A large share of future sales are hedged at below-market prices, limiting any significant upside potential for credit metrics over the next two years. CEZ secures short-term hedges for the majority of its production. Prices in 2018-2019 are affected by market conditions in 2016 and 2017, with power prices well below current conditions. Eighty-four percent of CEZ's 2019 production is hedged at €35.8 per megawatt hour (/MWh), well below market conditions. Seventy-three percent of production in 2020 is hedged at €42.3 /MWh, which is 18% above the 2019 level.

The company has material refinancing needs over the next three years. CEZ will need to refinance approximately 45% of its current financing from 2020-2022.

Outlook: Stable

The stable outlook on CEZ reflects our view that the company will be able to retain its strong market position in the Czech Republic and maintain adequate credit metrics, as earnings pressure will likely abate in the foreseeable future on the back of improving power prices. We consider a ratio of S&P Global Ratings-adjusted funds from operations (FFO) to debt above 25% and positive discretionary cash flow (DCF) as being commensurate with CEZ's stand-alone credit profile (SACP), which we currently assess at 'bbb'.

The outlook also reflects our unchanged view of a moderately high likelihood of extraordinary support from the Czech Republic. At this stage, our base case does not factor in the future decision of the Czech government regarding the financing of the planned nuclear project. Once this decision is announced, we could place the ratings on CreditWatch while we assess the implications for CEZ's future business perimeter and balance-sheet quality.

Downside scenario

We could lower the ratings on CEZ if its SACP falls by one notch or more. This could stem from:

- Markedly weaker power prices and coal spreads than we currently anticipate, or generated output markedly reducing due to unplanned outages, eventually leading to the adjusted FFO-to-debt ratio falling below 25% for a prolonged period.
- Signs of increased political risk--for example, policies that aim to extract cash from power utilities in the Czech Republic, either through increased dividends or windfall taxes--having adverse implications for CEZ's financial metrics and leading, for example, to a negative DCF-to-debt ratio. This would also stem from the Czech government's decision to use CEZ to fund the new nuclear project.

Increased political uncertainty and evidence of detrimental government intervention could also undermine our current assessment of the likelihood of extraordinary support to CEZ from the Czech government, which could prompt us to downgrade CEZ.

Furthermore, we could downgrade CEZ if we were to lower the local currency rating on the Czech Republic.

Upside scenario

Absent a potential favorable outcome regarding the government's reorganization of the company--not incorporated in our base case at this stage--we currently see the upside potential for the ratings as limited. This would require either a substantial, two-notch upward revision of CEZ's SACP, a higher assessment of the likelihood of extraordinary government support, or an upgrade of the Czech Republic.

Our Base-Case Scenario

Recent developments

CEZ had strong performance in first-half 2019, underpinned by:

- EBITDA increasing by 19% to Czech koruna (CZK) 32.1 billion in first-half 2019 versus CZK26.9 billion in first-half 2018 (see table 1). This growth stems mainly from:
- --Higher realization prices of generated electricity in Czechia, including the effect of hedges and commodity trading (+CZK2.9 billion);
- --the specific effect of growth in commodity prices in first-half 2018 (+CZK1.6 billion), including CZK1.2 billion from the revaluation of hedges for electricity generation in Czechia with delivery in second-half 2018 and CZK0.4 billion due to commercial procurement of allowances for 2018;
- --Greater output from traditional generating facilities in Czechia (+CZK0.6 billion); and
- --Higher expenses on emission allowances for generation in Czechia (-CZK0.8 billion) due to increased market prices and the lower allocation of free allowances.
- A 12% increase in reported net debt to CZK143.2 billion in first-half 2019, versus the CZK128.2 billion in first-half 2018.
- The agreed sale of CEZ Group's assets in Bulgaria to Eurohold for €335 million (about CZK8.6 billion).
- Purchased wind turbine projects in France, with an installed capacity of up to 119 megawatts (MW).

Table 1

CEZ a.s. Reported Stronger EBITDA Performance In H1 2019 Than In H1 2018

EBITDA	H1 2018 (Mil. CZK)	H1 2019 (Mil. CZK)	Growth (%)
Generation - Traditional energy	9,560	14,106	48
Generation - Net energy	1,980	2,273	15
Distribution	10,061	10,398	3
Sales	2,134	1,933	(9)
Mining	2,381	2,525	6
Support services	773	854	10
Adjustments	4	3	(25)
Consolidated	26,893	32,092	19

H1--First half. CZK--Czech koruna.

New CEZ Group's strategy, approved in June, envisages the gradual sale of assets in Bulgaria, Romania, Turkey, and Poland, excluding energy services companies (ESCOs). In addition, CEZ has recently announced a revision of its dividend policy, anticipating a payout ratio of 80%-100%. The guidance has been 60%-80% since 2015, although it was temporarily increased to 60%-100% in 2017.

Nuclear power projects

CEZ's Dukovany nuclear power plant is expected to shut down its four reactors (510 MW gross capacity each) between 2035 and 2037. As part of its future national energy policy, the Czech government is seeking long-term solution to secure supply of electricity and energy self-sufficiency in the Czech Republic after Dukovany's closure.

Under the current preferred solution, CEZ would develop a new nuclear reactor against a contract concluded between CEZ and the government. Details of the contract are not clear yet. The construction, which would not begin until 2029, would be entirely financed by CEZ with the support of loan guarantees. Preliminary estimates suggest the investment required to fund the construction of one nuclear power plant could be approximately CZK150 billion, which is similar to the fiscal 2018 consolidated reported debt.

At this stage, the information available is fairly limited and the main risks remains unclear. In addition, we expect negotiations to take several years. We will monitor how the evolution of CEZ's exposure to the project, which may be credit negative if the company were to finance the new plants on its own.

The current envisaged timeline would be:

- 2019: Business model selection;
- 2024-2025: Engineering, procurement, and construction contractor selection;
- 2029-2032: Construction permit and final notice to proceed; and
- 2037-2040: New nuclear unit put into operation.

Assumptions

- Real GDP growth in the Czech Republic of 2.6% in 2019 and 2.5% in 2020.
- Moderate growth in electricity consumption in the Czech Republic.
- Profit margins strengthening in the long run, due to CEZ's increasing ability to produce electricity from more cost-efficient sources (nuclear and renewables), and a likely recovery of power prices. Share of production hedged: 84% in 2019 (€35.8/MWh), 73% in 2020 (€42.3/MWh), 42% in 2021 (€43.6/MWh).
- No significant changes to the regulatory framework for distribution companies, although the current Czech regulatory period ends in 2020.
- EBITDA margins recovering toward 30% from 2020, up from 27% in 2018.
- Annual investments averaging €33 billion-€35 billion over 2019-2021.
- Dividend payout ratio averaging 70%-100% over our forecast horizon.
- No large, debt-financed acquisitions.
- Sale of the Bulgarian assets in June 2019 for €335 million. The settlement is subject to anti-monopoly approval and the payment of the purchase price and is assumed to take place by first-quarter 2020 at the latest.

Key Metrics

	2018A	2019F	2020F	2021F
EBITDA (bil. CZK)	48.9	57.0-60.0	63.0-66.0	61.0-64.0
Debt (bil. CZK)	202.6	200.0-203.0	195.0-200.0	197.0-202.0
Dividends (bil. CZK)	17.6	12.0-14.0	15.0-17.0	19.0-21.0
Capex (bil. CZK)	26.0	33.0-36.0	32.0-35.0	33.0-36.0
FFO/debt (%)	19.5	23.5-24.5	26.5-27.5	25.5-26.5
Debt/EBITDA (x)	4.2	3.4-3.6	3.0-3.2	3.1-3.3

Note: All figures are adjusted by S&P Global Ratings. FFO--Funds from operations. CZK--Czech koruna. A--Actual. F--Forecast.

Company Description

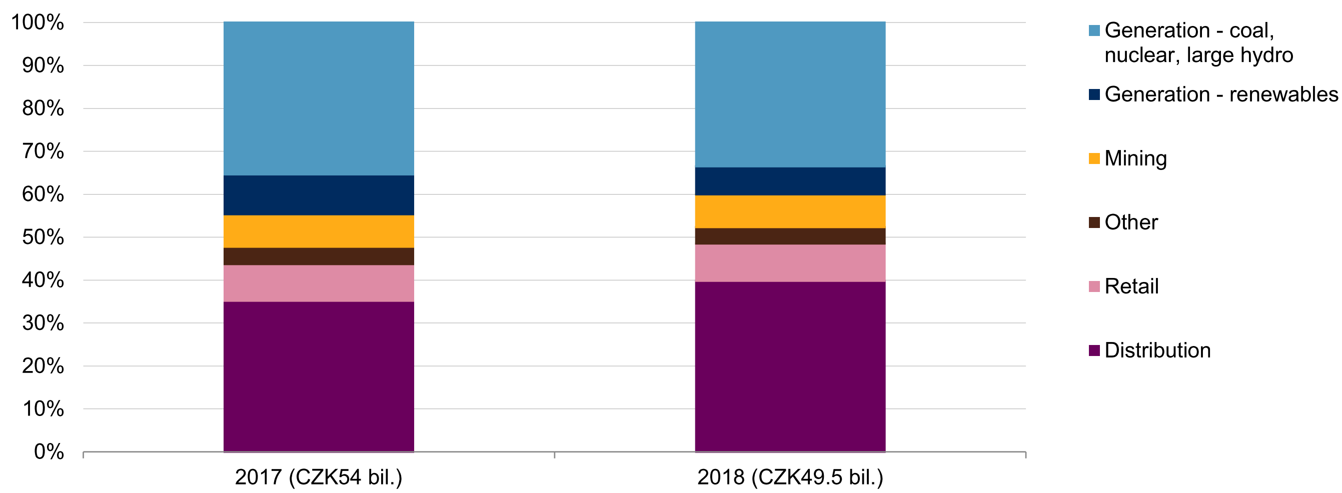
CEZ a.s. is an integrated energy company present in a wide range of electricity-related businesses: Generation, distribution, supply, mining, and energy trading. The utility benefits from an unrivaled position in the Czech electricity market and a small presence in Central and Eastern European countries, mainly Romania, Bulgaria, and Poland.

CEZ has a market share of about 67% of the generation segment in the Czech Republic, with a total capacity in 2018 of 14.9 gigawatts (GW) (out of which 13.05 GW is located in the Czech Republic) and a total production of 63.1 terawatt hours (TWh) (of which 58.8 TWh was generated in the Czech Republic). The generation mix comprises mostly nuclear and lignite/hard coal (91%). The latter is supported by its ownership of the Czech Republic's largest mining company, which provides 71% of CEZ's lignite needs. CEZ sold externally about 28% of the coal extracted. Coal-fired power plants represented 46% of capacity and 44% of generation volume in 2018, and their revenues are less than 20% of the group's total. The utility also has an overall market share of 28% in the competitive Czech supply market and supplied 17.5 TWh of electricity to its end customers in 2018.

CEZ controls about 65% of the Czech Republic's electricity distribution, owning the largest distribution company in the country. Regulated operations contributed about 35% and 40% of EBITDA in 2017 and 2018, respectively. The Czech Republic is CEZ's largest shareholder, with a stake of nearly 70% in the company's share capital and voting rights. The remaining 30% is publicly listed.

Chart 1

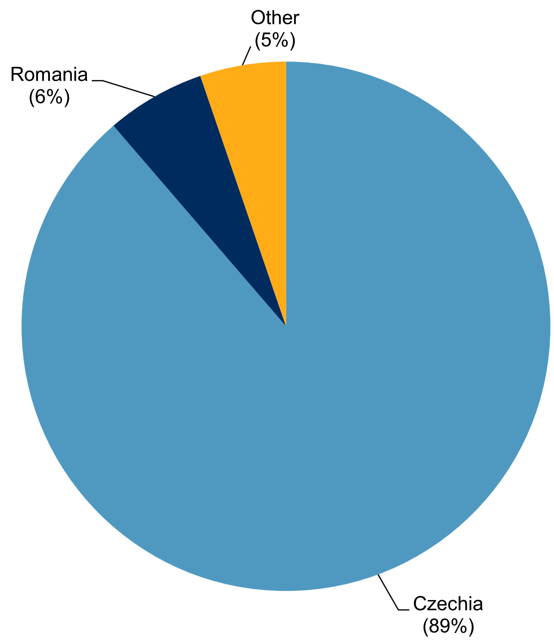
CEZ EBITDA Generation By Activity



CZK--Czech koruna. Source: Company data.

Chart 2

CEZ's 2018 EBITDA (CZK49.5 Billion) By Country Of Operation



Source: Company data.

Business Risk: Strong

We assess CEZ's business risk profile as strong. Our assessment is underpinned by:

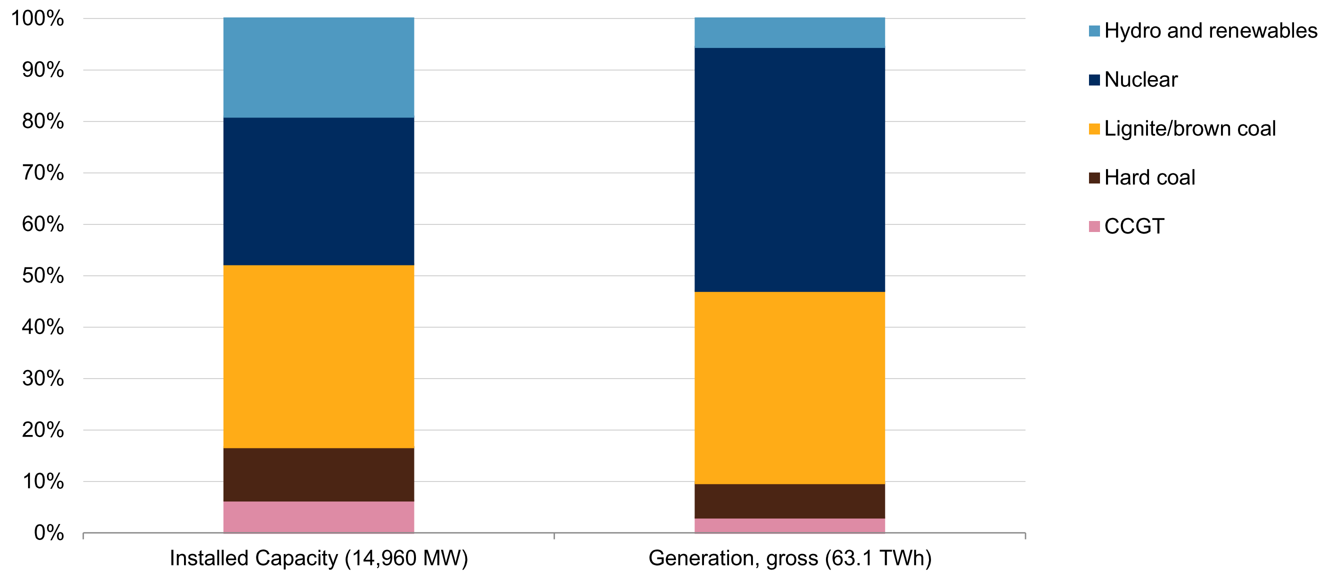
- CEZ's unrivaled position in the Czech power market;
- Its diversified and low-cost electricity generation fleet, despite the significant exposure of its unregulated activities to volatile power prices; and
- The large contribution of stable cash flows from regulated activities.

A diversified and low-cost electricity generation fleet exposed to power prices

In our view, CEZ benefits from its diverse and relatively fuel- and emission-efficient generation fleet along the load curve, spread across lignite and hard coal, nuclear power, hydro and renewables, and combined cycle gas turbines.

Chart 3

CEZ's 2018 Installed Capacity And Generation



MW--Megawatts. TWH--Terawatt-hour. Source: Company data.

In addition, the predominantly low-cost structure of CEZ's power generation fleet--with more than 80% of its generated output sourced from nuclear and recently redesigned lignite plants--also allows the company to benefit from increased power prices. CEZ's generation fleet currently operates with a low fuel cost base; nuclear fuel costs (including an approximate €2/MWh contribution to the state's nuclear account) amount to approximately €8/MWh, while lignite costs amount to €30/MWh-€32/MWh with a current CO_2 price of about €26/ton. The relatively low variable cost on the latter is partly the result of the internal sourcing of 72% of the company's needs, along with the geographic proximity of the mines from which the company sources its lignite.

CEZ continues to receive part of its CO_2 emission allowances for free, as decided in early 2013 by the European Commission. The group will be allocated a total of about 70 million free allowances for electricity production between 2013 and 2020, in exchange for a commitment to make investments of at least the amount of the allocated allowances. We understand that the value of free CO_2 allowances has been invested in the modernization and upgrade of infrastructure and in clean technologies. Furthermore, we note that, unlike some other EU countries, the Czech Republic has an energy policy that is somewhat supportive of nuclear power and coal, owing to the relatively limited natural potential for wind and solar generation in the country.

Stable cash flows from regulated activities

CEZ derives the rest of its EBITDA (40% in 2018) from its regulated activities, predominantly power distribution networks in the Czech Republic (about 35% of total EBITDA). We assess the Czech regulatory framework as strong, supported by an independent regulator with a relatively established track record, sufficient clarity on key inputs, and good predictability under the three-year regulatory period (2016-2018) extended to 2020. The regulator is also fairly supportive of new investments. This has helped to enhance the stability and predictability of earnings that CEZ derives from its regulated activities, and will underpin the group's business risk profile overall.

The remaining regulated network activities are located in Romania (see table 2), after the company announced the sale of its assets in Bulgaria in February 2019. Nevertheless, we view this exposure as slightly weakening CEZ's business risk profile, given that we assess the regulatory frameworks in Romania as less supportive than that in the Czech Republic.

Table 2

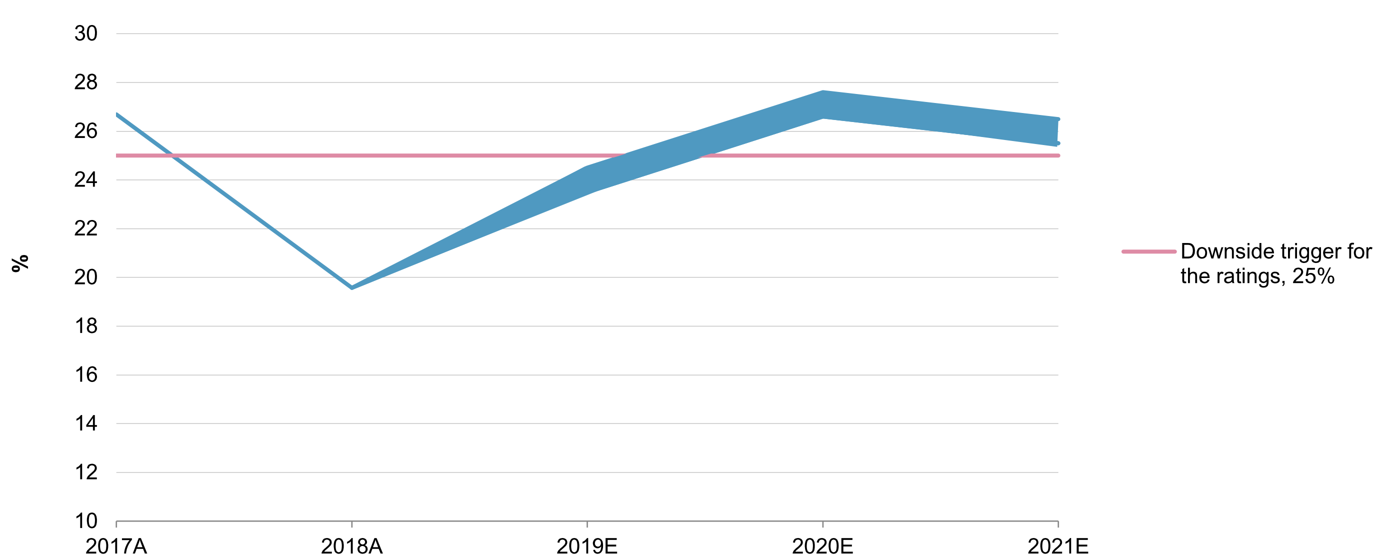
CEZ a.s.--Regulated Networks Breakdown

	Czech Republic	Romania	Bulgaria*
RAB (bil. CZK)	101,580	2,278	588
RAB (mil. €)	3,952	462	300
WACC (pretax) (%)	7.951% (nominal)	6.9% base (+ 1% pt. bonus for certain assets) (real)	6.67% (nominal)
Current regulatory period	2016-2020	2019-2023	2018-2021
2018 EBITDA (bil. CZK)	17.2	1.6	1.0

*SPA signed in June 2019. Settlement subject to the antimonopoly approval and payment of the purchase price. CZK--Czech koruna.

Chart 4

Evolution Of Adjusted Funds From Operations To Debt For CEZ, Upper And Lower Bounds



Note: As adjusted by S&P Global Ratings. A--Actual. E--Estimate. Source: S&P Global Ratings.

Peer comparison

Table 3

CEZ a.s.--Peer Comparison

Industry Sector: Energy

	CEZ a.s.	Vattenfall AB	Verbund AG	Energie AG Oberoesterreich
Ratings as of Sept. 26, 2019	A-/Stable/(A-2)	BBB+/Stable/A-2	A-/Stable/--	A/Stable/--
(Mil. €)	**--Fiscal year ended Dec. 31, 2018--**			**--Fiscal year ended Sep. 30, 2018--**
Revenue	6,828.5	15,413.1	2,847.9	1,686.1
EBITDA	1,889.6	3,357.5	902.1	311.8
Funds from operations (FFO)	1,541.1	2,677.8	746.7	255.0
Interest expense	257.0	404.3	129.7	27.2
Cash interest paid	219.1	316.3	73.8	21.9
Cash flow from operations	1,376.8	4,097.8	678.5	262.5
Capital expenditure	1,001.0	2,143.3	292.4	200.2
Free operating cash flow (FOCF)	375.8	1,954.5	386.1	62.3
Discretionary cash flow (DCF)	(308.7)	1,597.2	208.0	7.2
Cash and short-term investments	282.8	3,938.3	29.3	262.6
Debt	7,874.5	10,715.7	2,599.4	486.8
Equity	9,298.7	11,156.4	5,941.0	1,381.4
Adjusted ratios				
EBITDA margin (%)	27.7	21.8	31.7	18.5
Return on capital (%)	3.9	8.0	8.6	9.8
EBITDA interest coverage (x)	7.4	8.3	7.0	11.4
FFO cash interest coverage (x)	8.0	9.5	11.1	12.6
Debt/EBITDA (x)	4.2	3.2	2.9	1.6
FFO/debt (%)	19.6	25.0	28.7	52.4
Cash flow from operations/debt (%)	17.5	38.2	26.1	53.9
FOCF/debt (%)	4.8	18.2	14.9	12.8
DCF/debt (%)	(3.9)	14.9	8.0	1.5

Financial Risk: Significant

We expect the positive power price developments over the past two years will result in a gradual improvement of the company's operating performance. As part of its hedging strategy, CEZ sells a sizable portion of its future power production to the Czech power market at a pre-agreed price. This means that positions hedged at lower prices in the past will gradually reach maturity and the company will take advantage of the past price increases on future hedges. We understand that pre-sold volumes accounted for 84% at a pre-agreed price of €35.8/MWh for 2019, 73% (€42.3/MWh) for 2020, and 42% at €43.6/MWh for 2021. This is higher than the approximate €31/MWh price in 2017-2018. We therefore estimate the company's sensitivity to adverse power prices or generated output to be relatively moderate.

We believe that cash flow visibility is bolstered by the material contribution of regulated activities (35% in 2017 and

40% in 2018)--predominantly power distribution networks in the Czech Republic--to the company's earnings. We assess the Czech regulatory framework as strong, supported by an independent regulator with a relatively established track record, sufficient clarity on key inputs, good predictability under the five-year regulatory period (2016-2020), and a 7.951% allowed nominal return. We also consider the regulator to be fairly supportive of new investments. This has helped enhance the stability and predictability of earnings that CEZ derives from its regulated activities, and will support the company's overall business risk profile. As power prices recover and EBITDA from power generation increases, the relative contribution from network activities will reduce. We see a normalized level of contribution from network activities under the supportive Czech regulatory framework of 25%-30%. As such, we benchmark CEZ's credit metrics with the standard volatility table.

We also believe that contained capital expenditure (capex) intensity will support cash flow generation flexibility over the coming two years. This is because CEZ has invested heavily in recent years in the renovation and upgrade of its coal generation fleet, and capex outlays will now be predominantly geared toward maintenance expenditure, averaging CZK32 billion-CZK33 billion per year over 2018-2022.

That said, we believe that CEZ's ability to reduce its debt will be hindered by continuous, sizable dividend distributions at the request of its majority shareholder, the Czech government. We expect these distributions will average about CZK15 billion per year over 2018-2020, and payout ratios will remain relatively high (90%-100%) over this period.

Financial summary

Table 4

CEZ a.s.--Financial Summary

Industry Sector: Energy					
	--Fiscal year ended Dec. 31--				
(Mil. CZK)	**2018**	**2017**	**2016**	**2015**	**2014**
Revenue	175,717.0	200,156.0	205,887.0	210,729.0	205,092.0
EBITDA	48,624.0	59,848.0	65,756.0	73,468.0	78,109.0
Funds from operations (FFO)	39,657.9	48,943.0	50,510.0	62,548.0	62,838.0
Interest expense	6,612.6	6,168.0	6,630.6	7,472.0	8,910.0
Cash interest paid	5,639.1	6,698.0	8,557.0	6,351.0	7,733.0
Cash flow from operations	35,427.9	44,204.0	45,964.0	68,956.0	66,864.0
Capital expenditure	25,758.0	29,080.0	32,564.0	28,286.0	31,742.0
Free operating cash flow (FOCF)	9,669.9	15,124.0	13,400.0	40,670.0	35,122.0
Discretionary cash flow (DCF)	(7,943.1)	(2,735)	(7,933)	19,357.0	13,802.0
Cash and short-term investments	7,278.0	21,428.0	48,460.0	13,482.0	35,474.0
Gross available cash	9,434.0	16,312.0	16,572.0	25,012.0	35,474.0
Debt	202,631.5	183,375.5	190,626.1	169,920.1	185,450.4
Equity	239,281.0	254,322.0	261,360.0	272,155.0	265,851.0
Adjusted ratios					
EBITDA margin (%)	27.7	29.9	31.9	34.9	38.1
Return on capital (%)	3.9	5.9	7.1	7.2	8.5
EBITDA interest coverage (x)	7.4	9.7	9.9	9.8	8.8
FFO cash interest coverage (x)	8.0	8.3	6.9	10.8	9.1

Table 4

CEZ a.s.--Financial Summary (cont.)

Industry Sector: Energy

	--Fiscal year ended Dec. 31--				
(Mil. CZK)	**2018**	**2017**	**2016**	**2015**	**2014**
Debt/EBITDA (x)	4.2	3.1	2.9	2.3	2.4
FFO/debt (%)	19.6	26.7	26.5	36.8	33.9
Cash flow from operations/debt (%)	17.5	24.1	24.1	40.6	36.1
FOCF/debt (%)	4.8	8.2	7.0	23.9	18.9
DCF/debt (%)	(3.9)	(1.5)	(4.2)	11.4	7.4

Liquidity: Adequate

We believe CEZ has adequate liquidity, based on our expectation that available liquidity resources will cover expected cash outflows by more than 1.2x in the next 12 months.

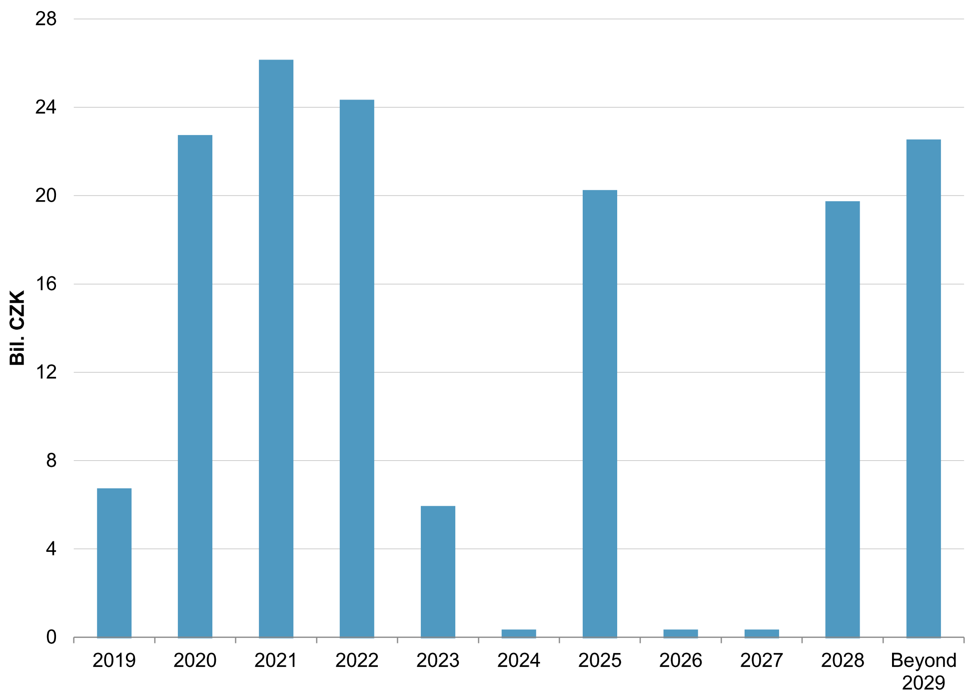
CEZ currently has a relatively lumpy debt maturity profile with approximately €750 million and €900 million coming due in 2020 and 2021, respectively, as part of previous Eurobond issuances.

Principal Liquidity Sources	Principal Liquidity Uses
We expect principal liquidity sources over the 12 months from March 31, 2019x will include: • Unrestricted cash and securities of CZK12.1 billion, according to management data; • Available headroom of about CZK11.8 billion under various committed back-up facilities maturing after 12 months; and • Cash FFO of about CZK53.8 billion.	We expect principal liquidity uses over the same period will include: • Debt maturities of about CZK6.5 billion; • Working Capital outflows of about CZK7.5 billion; • Annual capex of about CZK34.4 billion for 2019, as per the company's guidance; and • Dividends of about CZK 13.7 billion.

Debt maturities

Chart 5

CEZ's Debt Maturities As Of Dec. 31. 2018



CZK--Czech koruna.

Government Influence

We consider CEZ to be a government-related entity, and believe there is a moderately high likelihood that the Czech government would provide extraordinary support to CEZ in the event of financial distress. Ongoing political uncertainty surrounding the recent formation of the current Czech government, following the latest parliamentary elections in October 2017, does not affect our assessment. We consider CEZ's:

- Important role for the Czech government, as both a provider of an essential service and a key player in the implementation of state energy policies. The company produces about 70% of the domestic power output--sufficient to cover domestic consumption requirements--and distributes more than 65% of electricity in the Czech Republic; and
- Strong link with the Czech government, as the latter is actively involved in key strategic decisions through its representation on CEZ's supervisory board. The finance ministry owns about 70% of CEZ, and the remaining shares are publicly held. We anticipate that the state will retain its strategic control over CEZ and remain a supportive shareholder by avoiding negative interventions, such as significantly raising the dividend payout ratio or implementing windfall taxes on power companies.

Environmental, Social, And Governance

Over the past decade, CEZ has committed to generate carbon-neutral electricity before 2050 and has implemented several measures to reduce its CO2 emissions intensity (0.39 tons of CO2/MWh in 2018 versus 0.57 tons of CO2/MWh in 2010) by upgrading its lignite fleet and planning to close some of its least efficient lignite and hard coal plants. We believe CEZ remains significantly exposed to challenges from carbon price developments and EU decarbonization objectives in light of its carbon-intensive fleet (electricity generation from coal was approximately 43% of total output, or 27.0 TWh, in 2018). Additional risks lie in its sizable nuclear fleet (47% of output in 2018). The group recently mismanaged the documentation of welded joints on piping in nuclear power plants, causing significant outages and additional costs. Its end-of-cycle liabilities (of both decommissioning and nuclear waste storage) are also substantial and captured in our asset retirement obligation debt adjustment (approximately CZK64 billion in 2018).

From a social perspective, the Czech Republic's main political parties support both nuclear and coal, acknowledging nuclear generation's central role in preserving national energy independence. There are limited renewable ambitions, stemming from the country's limited natural and weather potential for wind and solar generation. CEZ's nuclear activities also pose several governance risks, as we believe uncertainty surrounding the government's decision on future nuclear reactor construction will continue to limit the long-term visibility of the group's overall structure and strategic directions.

Issue Ratings - Subordination Risk Analysis

CEZ issues most of its debt at its parent company CEZ a.s. hence there is no issue regarding on structural subordination.

Reconciliation

Table 5

Reconciliation Of CEZ a.s. Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. CZK)

	--Fiscal year ended Dec. 31, 2018--								
CEZ a.s. reported amounts									
	Debt	**Shareholders' equity**	**Revenue**	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**	**Cash flow from operations**	**Capital expenditure**
	160,966	234,721	181,318	49,664	19,759	5,177	48,624	35,351	26,018
S&P Global Ratings' adjustments									
Cash taxes paid	--	--	--	--	--	--	(3,327.00)	--	--
Cash taxes paid: Other	--	--	--	--	--	--	--	--	--

Table 5

Reconciliation Of CEZ a.s. Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. CZK) (cont.)

Cash interest paid	--	--	--	--	--	--	(5,091.00)	--	--
Operating leases	4,115.27	--	--	625.00	288.07	288.07	(288.07)	336.93	--
Accessible cash and liquid investments	(8,018.90)	--	--	--	--	--	--	--	--
Capitalized interest	--	--	--	--	--	260	(260)	(260)	(260)
Share-based compensation expense	--	--	--	33	--	--	--	--	--
Dividends received from equity investments	--	--	--	5	--	--	--	--	--
Asset retirement obligations	44,131.23	--	--	--	--	888	--	--	--
Nonoperating income (expense)	--	--	--	--	1,074	--	--	--	--
Noncontrolling interest/minority interest	--	4,560	--	--	--	--	--	--	--
Debt: Guarantees	2,853.00	--	--	--	--	--	--	--	--
Revenue: Other	--	--	(5,601)	(5,601)	(5,601)	--	--	--	--
EBITDA: Gain/(loss) on disposals of PP&E	--	--	--	(129)	(129)	--	--	--	--
EBITDA: Other	--	--	--	4,027	4,027	--	--	--	--
Depreciation and amortization: Impairment charges/(reversals)	--	--	--	--	1,766	--	--	--	--
Depreciation and amortization: Other	--	--	--	--	(4,027)	--	--	--	--
Total adjustments	43,080.60	4,560.00	(5,601.00)	(1,040.00)	(2,601.93)	1,435.57	(8,966.07)	76.93	(260.00)
S&P Global Ratings' adjusted amounts									
	Debt	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**	**Capital expenditure**
	204,046.60	239,281.00	175,717.00	48,624.00	17,157.07	6,612.57	39,657.93	35,427.93	25,758.00

Ratings Score Snapshot

Issuer Credit Rating

A-/Stable/--

Business risk: Strong

- **Country risk:** Intermediate
- **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
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Stand-alone credit profile : bbb

- **Related government rating:** AA
- **Likelihood of government support:** Moderately high (+2 notches from SACP)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- 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
- Criteria | Corporates | Industrials: Key Credit Factors For The Unregulated Power And Gas Industry, March 28, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Czech Republic 'AA-/A-1+' Foreign Currency And 'AA/A-1+' Local Currency Ratings Affirmed; Outlook Stable, July 19, 2019
- Czech Utility Company CEZ a.s. 'A-' Rating Affirmed; Outlook Stable, Nov. 23, 2018

Business And Financial Risk Matrix

	Financial Risk Profile					
Business Risk Profile	Minimal	Modest	Intermediate	**Significant**	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	**bbb**	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of September 27, 2019)*

CEZ a.s.	
Issuer Credit Rating	A-/Stable/--
Senior Unsecured	A-
Issuer Credit Ratings History	
02-Oct-2006	A-/Stable/--
31-May-2005	BBB+/Positive/--
12-Nov-2003	BBB+/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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