urenco
The Energy to Succeed

50 YEARS

Annual report and accounts 2019

GROUP FINANCE REPORT

EBITDA[1] remaining broadly in line with last year, although revenue slightly down. Net income impacted by impairment charge on US assets and lower discount rates resulting in an increase in nuclear provisions.

Results for 2019

Revenue

Revenue for the year ended 31 December 2019 was €1,804.5 million, a decrease of 7.8% on the €1,957.7 million in 2018. Both SWU revenues and uranium-related sales were lower in 2019 by €53.5 million and €74.6 million respectively. For SWU revenues, volumes were slightly higher than the previous year but with lower average unit revenues. By contrast, uranium-related sales experienced significantly lower volumes but with higher realised unit prices. Other revenues decreased by €25.1 million compared to 2018, primarily as a result of lower sales at Urenco Nuclear Stewardship and losses associated with uranium-related commodity contracts.

EBITDA[1]

EBITDA for 2019 was €1,219.6 million, an increase of €19.2 million (1.6%) from €1,200.4 million in 2018. The change in EBITDA reflects the different mix in customer deliveries between the two years satisfied from in-year production and inventories[2].

In 2019 EBITDA also benefited from lower net costs of nuclear provisions (€19.4 million) and lower other operating and administrative expenses (€12.0 million).

The net costs of nuclear provisions (before exceptional items)[3] were €154.7 million in 2019 compared to €174.1 million in 2018, a decrease of €19.4 million.

The net costs for tails provisions in 2019 were €8.2 million higher than those for 2018. The higher costs of tails provisions created arose due to the higher volume of new tails generated during 2019 and uplifts in the unit deconversion cost estimates of tails for both the European and US enrichment operations. The increased release from the tails provisions relates to the optimisation of operations and the impact of the reduction in higher assay tails associated with enrichment services contracts.

Tails provision movement[3]

	2019 €m	2018 €m	increase/ (decrease)
Additional provisions in the year	212.5	144.7	**67.8**
Release from provisions in the year	(88.8)	(29.2)	**(59.6)**
Net costs for provisions in the year	**123.7**	**115.5**	**8.2**

The net costs for decommissioning provisions in 2019 decreased by €66.8 million primarily due to a lower charge for additional provisions, with 2018 reflecting the triennial review of nuclear liabilities, together with a slightly higher release of provisions in the year associated with cylinder assets.

Decommissioning provision movement[3]

	2019 €m	2018 €m	increase/ (decrease)
Additional provisions in the year	-	65.9	**(65.9)**
Release from provisions in the year	(9.7)	(8.8)	**(0.9)**
Net costs for provisions in the year	**(9.7)**	**57.1**	**(66.8)**

The net costs for other nuclear provisions in 2019 increased by €39.2 million primarily as a result of changes to the forecasts for future re-enrichment of low assay feed.

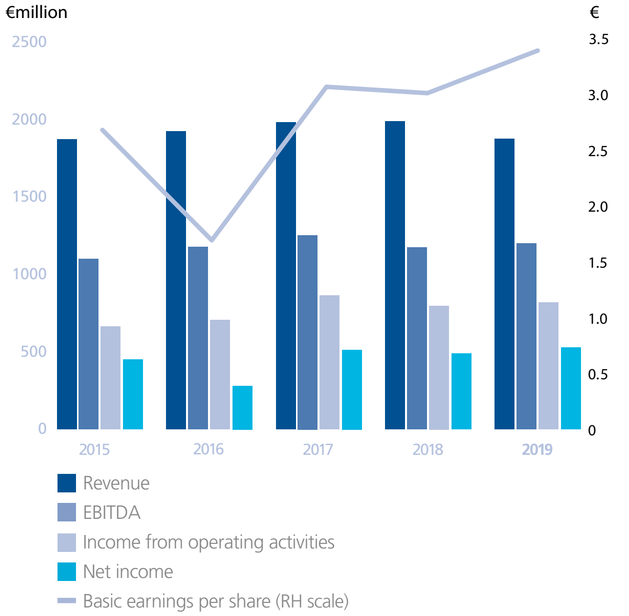
Other operating and administrative expenses[4] were €424.7 million in 2019 compared to €436.7 million in 2018, a reduction of €12.0 million. In the first half of 2019 the assets and liabilities of the Dutch-defined benefit pension scheme were transferred to Pensioenfonds Grafische Bedrijven ("PGB"), a multi-employer pension scheme, which resulted in a loss of €6.9 million to the income statement. In 2018 a provision of €17.3 million was made for a potential bad debt associated with a specific customer and this position remained unchanged at the end of 2019. Adjusting for these two items, other operating and administrative expenses for 2019 were broadly in line with the prior year.

The EBITDA margin for 2019 was 67.6% compared to 61.3% in 2018, with the EBITDA margin in 2018 being adversely impacted by the triennial review of nuclear liabilities carried out in that year.

EBITDA performance

	2019 €m	2018 €m	% increase/ (decrease)
Income from operating activities pre-exceptional items	**850.2**	**826.5**	**2.9**
Adjustment for depreciation in inventories, SWU assets and nuclear provisions	18.6	47.5	
Add: depreciation and amortisation	356.2	329.2	
Adjustment for share of results of joint venture	(5.4)	(2.8)	
EBITDA	**1,219.6**	**1,200.4**	**1.6**

Financial performance (pre-exceptional items)



Exceptional items

Exceptional items totalling €643.0 million on a pre-tax basis (€557.2 million post-tax) were reported in 2019 (2018: €nil). The total net income tax credit associated with the exceptional items was €85.8 million (2018: €nil).

The majority of the charge relates to an impairment of the carrying value of the US operations of €500.0 million (€446.0 million post-tax), as a result of further downward pressure on long-term price forecasts for uncontracted SWU volumes, compared with those assumed at the time of the construction of the US operations and also since the impairment charge recorded in 2016. These pressures are due to a combination of factors, including premature closure of nuclear reactors due to economic reasons, primarily in unregulated markets, excess capacity in global enrichment and the build-up of surplus inventories.

In addition, an exceptional charge of €143.0 million on a pre-tax basis (€111.2 million post-tax) arose due to the increase in the value of nuclear provisions held by the European enrichment businesses following a revision to the discount rates applied to the provisions due to continued downward pressure on real interest rates in Europe. Of the €143.0 million, €111.3 million relates to tails provisions and €31.7 million relates to decommissioning provisions.

1 EBITDA is defined as earnings before exceptional items, interest (including other finance costs), taxation, depreciation and amortisation and joint venture results and a reconciliation to income from operating activities (pre-exceptional items) is set out on page 96.
2 Change to inventories of work in progress, finished goods and SWU assets in 2019 were €(5.5) million, (2018: €(146.5) million).
3 Excluding the increase in the value of nuclear provisions held by the European enrichment businesses following a revision to the discount rates, which is treated as an exceptional item.
4 Other operating and administrative expenses are defined as employee costs, other expenses and restructuring provision charges/releases but excluding any associated elements of depreciation. In prior years this term also included changes to inventories and SWU assets.

In 2016 the Group recorded a restructuring provision of €33.0 million associated with the implementation of Strategy 2020. In 2019, €2.9 million (2018: €2.3 million) of this restructuring provision was released to the Income Statement following a re-forecast of the costs to complete the restructuring programme. The release of restructuring provision in each of 2019 and 2018 has not been classified as an exceptional item as each was below the materiality threshold set out in the Group's policy on exceptional items.

Impact of exceptional items

	2019 €m	2018 €m
Income from operating activities – pre-exceptional items	850.2	826.5
Exceptional item (before tax) – US impairment	(500.0)	-
Exceptional item (before tax) – change in discount rates	(143.0)	-
Income from operating activities – post-exceptional items	**207.2**	**826.5**

	2019 €m	2018 €m
Net income – before exceptional items	564.8	511.3
Exceptional item (after tax) – US impairment	(446.0)	-
Exceptional item (after tax) – change in discount rates	(111.2)	-
Net income – after exceptional items	**7.6**	**511.3**

Net income

Net income after exceptional items was €7.6 million in 2019 (2018: €511.3 million).

Net income before exceptional items was €564.8 million in 2019, an increase of €53.5 million (10.5%) compared to the 2018 net income of €511.3 million. The net income margin before exceptional items for 2019 was 31.3% compared to 26.1% for 2018.

Depreciation and amortisation for 2019 was €356.2 million, compared to €329.2 million for 2018, with the higher charge in 2019 reflecting adverse impacts from movements in foreign exchange rates in addition to an increase in the depreciation of decommissioning assets following the triennial review carried out in 2018.

Net finance costs for 2019 were €107.1 million, compared to €106.0 million for 2018.

The net finance costs on borrowings (including the impact of interest rate/cross currency interest rate swaps) were €5.8 million higher at €81.1 million, reflecting the €9.9 million of costs associated with the repurchase and cancellation of €215.6 million of February 2021 Eurobonds. Underlying net finance costs were lower reflecting the lower levels of net debt in 2019, although this is partially offset by the lower levels of interest income on cash balances.

Where appropriate, foreign currency loan balances are placed in accounting hedge relationships, primarily by means of cross currency swaps. Where this is not possible the retranslation of the relevant unhedged loan balances (denominated in US dollars and euros but held by a sterling functional currency entity) generate gains/losses as a result of foreign exchange movements in the year. In 2019 the impact of this was a loss of €15.5 million (2018: €30.1 million loss) reflecting relevant unhedged balances and movements in foreign exchange rates. In 2019, the impact of ineffective cash flow hedges was €nil (2018: €6.4 million gain).

The increase in the unwinding of discounting on provisions was €10.3 million higher at €69.2 million, but this increase was largely offset by an increase in capitalised interest of €5.9 million to €62.4 million.

In 2019 the pre-exceptional tax expense was €178.3 million (an effective tax rate (ETR) of 24.0%), a decrease of €30.9 million over the tax expense of €209.2 million for 2018 (ETR: 29.0%).

The decrease in the ETR from 29.0% to 24.0% is driven by three factors: i) the impact of non-taxable and non-deductible amounts, including foreign exchange financing gains and losses that are excluded from tax under the UK Disregard Regulations (decrease of 4.7%); ii) the impact of adjustments in respect of previous years (decrease of 0.5%); and iii) changes in the relative proportions of profits and losses generated across the four jurisdictions in which Urenco operates (decrease of 0.4%) which are partially offset by the impact of changes in overseas tax rates (increase of 0.6%).

The post-exceptional tax expense of €92.5 million reflects the pre-exceptional expense of €178.3 million after the benefit of the €85.8 million net credit associated with the exceptional items.

Tails deconversion, storage and eventual disposal

Urenco provides for the costs of deconverting the by-product of the enrichment process (chemically converting tails from UF_6 to U_3O_8), interim and long-term storage, and eventual disposal. During the year the Group reviewed the costs associated with tails deconversion, storage and disposal.

Additional total tails provisions created in the year were €323.8 million (2018: €144.7 million), due to tails generated in the period, increases in the applied tails deconversion rates for both the US and European enrichment operations, and a change in discount rates. The impact of the additional total tails provisions created in the year includes the impact of the reduction in the real discount rate for the European jurisdictions. This increased tail provisions by €111.3 million, which has been charged to the consolidated income statement as an exceptional item.

Tails provisions utilised during 2019 were €42.5 million (2018: €34.5 million) and a provision release of €88.8 million (2018: €29.2 million) was recorded as a credit in net costs of nuclear provisions as a result of the impact of the reduction in higher assay tails associated with enrichment services contracts and the optimisation of operations.

Plant and machinery decommissioning

Urenco has an obligation under its operating licences to decommission enrichment facilities safely once they reach the end of their operational life. The costs associated with plant and machinery decommissioning are monitored on an ongoing basis and are also subject to a detailed, periodic review; the last such review was carried out in 2018.

During the year ended 31 December 2019 the decommissioning provision increased by €83.6 million (2018 increase: €125.8 million) due to revised assumptions relating to the decommissioning of plant and machinery of €66.3 million (2018: €123.0 million), the installation of additional plant and machinery of €13.6 million (2018: €0.3 million) and additional cylinder purchases of €3.7 million (2018: €2.5 million). The €66.3 million resulting from revised assumptions mainly relates to the impact of changes to discount rates of €64.9 million, of which €31.7 million has been expensed to the income statement as an exceptional item and €33.2 million has been recognised in decommissioning assets.

Decommissioning provisions utilised during 2019 were €8.9 million (2018: €8.9 million) and a provision release of €9.7 million (2018: €8.8 million) was recorded as a credit in net costs of nuclear provisions.

Further information on nuclear provisions can be found in note 30 of the Group's Consolidated Financial Statements.

Group pension funds

Urenco operates pension schemes for our employees in the Netherlands, UK and Germany. These are a mixture of defined contribution and defined benefit schemes.

In March 2019 the funds from the Dutch defined benefit pension scheme were transferred to Pensioenfonds Grafische Bedrijven ("PGB"), a collective third-party pension scheme, and from 1 April 2019 all historic and future pension liabilities are built up in PGB. The pension plan of PGB has all the features of a defined contribution scheme and UNL's pension obligation for each period will be determined by the amounts to be contributed to PGB for that period. As a result of the closure of the defined benefit pension scheme a loss of €6.9m was recognised in the income statement, comprised of a curtailment gain of €14.9m offset by a settlement loss of €21.8m. The net loss is presented as pension costs within employee costs. In addition, a gain of €6.9m was recognised in retained earnings, representing the recognition of the surplus net pension assets that had not been recognised at the date of closure. This gain is presented within other comprehensive income.

The net liability for the Group's defined benefit pension schemes at 31 December 2019 was €65.2 million (2018: €46.0 million). This increase was due to a €190.7 million decrease in the present value of the defined benefit obligations together with a decrease in the fair value of the plan assets of €209.9 million. Excluding the impacts of the Dutch pension curtailment from 1 April 2019 described above, the present value of the defined benefit obligations would have increased by €74.2 million due primarily to a reduction in discount rates and the fair value of the plan assets would have increased by €61.9 million.

In 2018, following the triennial valuation of the UK scheme, a revised deficit repair plan was agreed with the UK trustees. The plan includes deficit repair payments of £6.6 million annually until 2022. The trustees intend to manage the pension scheme so that the economic and investment risks will be reduced through the adoption of a more cautious investment policy and the use of interest and inflation derivative contracts.

Cash flow

Operating cash flow before movements in working capital was €1,288.3 million (2018: €1,293.8 million) and cash generated from operating activities was €1,094.3 million (2018: €1,401.0 million). The lower cash flows from operating activities primarily result from lower revenues and adverse movements in working capital compared to 2018.

Tax paid in the period was €141.5 million (2018: €119.3 million) due to the timing and phasing of cash payments which can often span multiple years.

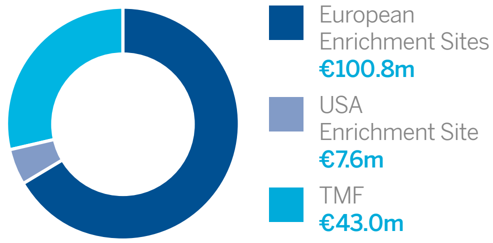
Net cash flows from operating activities were €952.8 million (2018: €1,281.7 million). Net cash flows from operating activities are used to finance investing activities, service the Group's debt, fund dividends to shareholders and, in the future, to fund the long term decommissioning and tails liabilities currently reported in provisions in the Group's Consolidated Statement of Financial Position.

Capital expenditure[1]

In 2019 Group capital expenditure was €151.4 million (2018: €183.1 million), reflecting a lower level of expenditure on both core enrichment assets and the TMF. Expenditure on core enrichment assets is now broadly at a level forecast as part of our strategy and appropriate to maintain the existing fleet of enrichment assets for the near to mid-term.

Investment in TMF in 2019 was €43.0 million (2018: €76.0 million, 2017: €184.4 million) reflecting construction being completed in late 2018 and active commissioning is ongoing. Management's current forecast of the costs to complete TMF remain in line with those as at the end of 2018 and the associated cost estimates are included in the tails deconversion rate referred to above in the commentary on EBITDA and tails deconversion, storage and eventual disposal.

2019 Capital expenditure



Capital structure

The Group's equity decreased to €1,885.8 million during the year (2018: €2,119.8 million) due to a decrease in retained earnings of €310.0 million (reflecting the net income of €7.6 million and losses of €17.6 million in other comprehensive income for the year, together with €300.0 million of dividends paid), an increase in the foreign currency translation reserve of €95.8 million, primarily due to foreign exchange gains on property, plant and equipment held in US dollars as a result of the strengthening of the US dollar against the euro, and a decrease in the hedging reserve (including cost of hedging reserve) of €19.8 million. The movement in the hedging reserve is primarily associated with mark to market losses on cash flow hedges, which protect the Group's future revenues in foreign currencies.

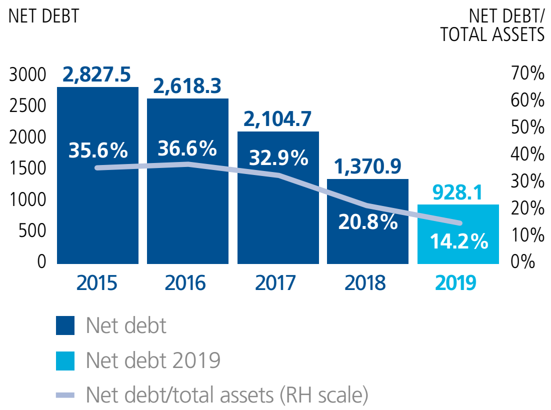
Net debt[2] decreased to €928.1 million (2018: €1,370.9 million) including lease liabilities of €22.0m (2018: €nil).

In 2019, the Group repurchased and cancelled €215.6 million of the February 2021 Eurobonds for a price of €225.5 million (104.6%). The transaction was completed in January 2019 for a total amount of €230.5 million, which included €5.0 million of accrued interest on these Eurobonds. As at 31 December 2019, a nominal amount of €534.4 million remained outstanding on the February 2021 Eurobonds.

Net debt to total asset ratio remained strong at 14.2% (2018: 20.8%), well within the Group's target ratio of less than 60%.

[1] Capital expenditure includes net cash flows from investing activities (excluding interest received) of €145.3 million and capital accruals (included in working capital payables) of €6.1 million.
[2] Net debt is defined in the Glossary on page 158 and the calculation of net debt is set out on page 126.

Net debt and Net debt/total assets



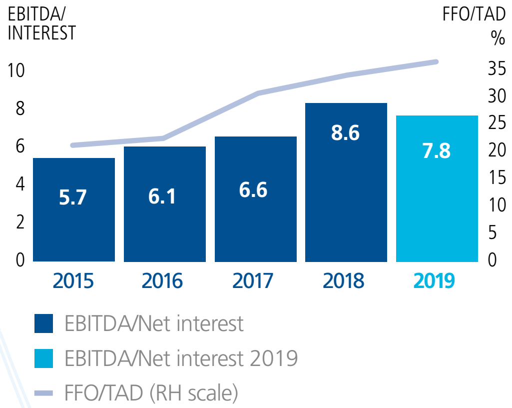
In 2019 the Group monitored its capital structure through the use of financial ratios, principally those of net debt to total assets and funds from operations to total adjusted debt (FFO/TAD). The Group targets an FFO/TAD ratio that results in a strong investment grade credit rating.

The FFO/TAD ratio at the end of 2019 was 38.2% compared to 34.3% at the end of 2018, due to an increase in FFO and a decrease in TAD. Further information on FFO/TAD can be found on page 122.

FFO was higher by €38.3 million due to slightly higher EBITDA and lower current tax expenses. TAD was lower by €171.4 million, primarily reflecting a decrease in net debt of €442.8 million but partially offset by an increase in tails and decommissioning provisions of €369.8 million, The increase in nuclear provisions reflects the increase in provisions arising during the year as well as the impact of the reduction of discount rates for both tails and decommissioning. Details of the FFO/TAD calculation are set out in note 28 of the Group's Consolidated Financial Statements.

The Group's interest cover also remains strong at 7.8x (2018: 8.6x).

Five-year summary funding ratios



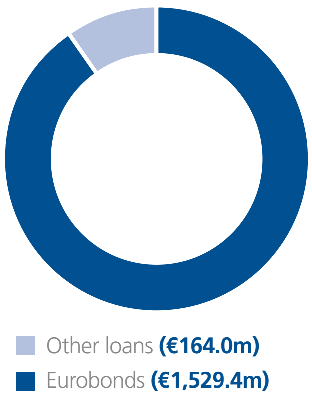
Funding position

Liquidity continues to remain strong as a result of cash flow generation. As at 31 December 2019, the Group had €750 million of committed undrawn revolving credit facilities which expire in June 2023, as well as cash, cash equivalents and short-term deposits of €787.3 million (2018: €531.2 million).

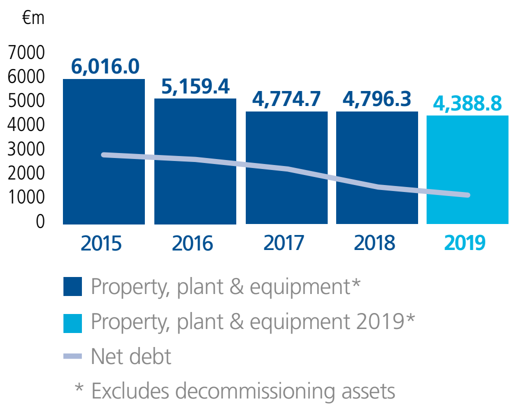
Our funding position remains robust and continues to be underpinned by our established contract order book, which gives high levels of revenue visibility and robust EBITDA margins, resulting in strong cash flow generation.

The Group's debt is rated by Moody's (Baa1/Stable) and Standard & Poor's (BBB+/Stable); these external ratings were unchanged during 2019.

Interest bearing loans and borrowings



Property, plant & equipment vs net debt



Funding programme

The Group's funding strategy is to:

- Maintain a core of longer-dated debt and committed borrowing facilities, consistent with the long-term nature of the Group's investments and the need to maintain an optimised long-term capital structure;
- Use a range of financial instruments and financial markets in order to execute attractive funding opportunities as they emerge; and
- Manage debt maturities by raising funds in advance of ultimate repayment dates of debt instruments.

The average time to maturity of the Group's debt at 31 December 2019 was 4.3 years (at 31 December 2018: 4.9 years).

Managing foreign currency risk

Our foreign currency hedging policy has the objectives of reducing volatilities in net cash flow and income, and to protect the income statement from balance sheet re-measurements of debt. However, a long-term reduction in income exposure is much more difficult to achieve due to the strict requirements with respect to hedge accounting under IFRS. The functional currency of Urenco Limited is sterling, although the company reports its results in euros.

The Group receives most of its customer revenues in US dollars and euros. The net cash flows of Urenco's European business have been hedged by selling US dollar customer revenue and buying forward the sterling required to meet the costs of the UK operations, and selling the remaining US dollars to buy euros. The net cash flows of Urenco's USA business have been used to pay US dollar denominated costs.

The Group hedges the impact of changes in foreign exchange rates by using a progressive rolling programme of buying and selling currency over a period of up to three years ahead of the current year. This medium-term hedging period strikes a balance between the objective of maximising cash flow certainty (which suggests a long hedging period) and the objective of maintaining a hedge portfolio that largely qualifies for hedge accounting under IFRS. Urenco has a stable future revenue stream that is managed using a portfolio of hedges. There is always an element of uncertainty due to changes in quantities and timing of deliveries based on market movements and customers' requirements, which makes it difficult to achieve effective hedge accounting over the longer term.

The Group has a total of €939 million (2018: €1,034 million) cross currency swaps, mainly to convert the economic exposure of part of the Group's debt from euros to US dollars that are then net investment hedged for Group accounting purposes. This better aligns the currency of the debt with the asset base and cash flows of the Group.

Urenco Group Financial Policy Statement

The Financial Policy Statement defines the broad parameters for financing the Urenco Group and has the agreement and support of all of our shareholders.

The Group will finance itself through a combination of equity, including retained reserves and debt. Due consideration is given to the Group's long-term unfunded nuclear liabilities when considering financing options. Urenco Limited cannot issue new equity without the agreement of all of its shareholders.

In order to achieve an efficient financial profile, the gearing level and financial ratios will be maintained to retain a solid investment grade credit rating for the Group.

At all times, the Group will maintain sufficient liquidity to ensure that it is a going concern and will manage the composition of its debt to minimise risks from market deterioration in liquidity, interest rates or currencies. Detailed treasury management policies set parameters for the management of these risks.

Dividend policy

The Group will aim to pay a dividend out of its annual earnings. The dividend shall be set to take account of net income, cash flows, reserves and the level of credit ratios. Until financial ratios comfortably exceed the minimum threshold for BBB+ at S&P and Baa1 at Moody's, the annual dividend will not exceed 100% of the net income for the year. A lower dividend may be set when credit ratios, cash flow or funding conditions dictate that this is necessary and, equally, a higher dividend may be declared when the minimum thresholds of the key financial ratios are comfortably exceeded.

In 2019, €300.0 million in dividends for the year ended 31 December 2018 were paid to shareholders (2018: €300.0 million).

The Board has approved that dividends of €300.0 million be paid on 18 March 2020. The level of the final dividend for 2019 is less than the net income (pre-exceptional items) but exceeds the level of net income (post-exceptional items). Consideration has been given to all of the following (i) the fact the net income (post-exceptional items) has been generated by adverse non-cash charges during the year; and (ii) the Group's favourable net debt position and credit ratios; and (iii) the availability of sufficient distributable reserves.

As at 31 December 2019, the Company had distributable reserves available of €1,059.3 million (31 December 2018: €956.3 million).

Order book

Urenco has a strong contract order book which extends into the 2030s with an approximate value at 31 December 2019 of €10.6 billion based on €/$ of 1 : 1.12 (2018: €11.9 billion based on €/$ of 1 : 1.15).

Outlook

Uranium enrichment is the heart of our business, complemented by services which benefit our customers and utilise our technology and core expertise. We continue to explore growing markets: in enrichment services through our new representative office in China; in Stable Isotopes through our extended facility in the Netherlands; and in nuclear stewardship through our two UK subsidiaries dedicated to this area, Urenco Nuclear Stewardship Limited and Urenco ChemPlants Limited.

The principal risks and uncertainties to which Urenco is exposed remain broadly in line with those disclosed in 2018. Our contract order book leaves us well-placed to meet challenges from the enrichment market. We have accepted new business at levels which give us optimism that customers understand the importance of having a market that can promote reinvestment. Enriched uranium inventories have led to excess capacity in the market, and we forecast they will further decrease in the mid-term.

Policy decisions in some European countries and North America support the nuclear industry, with investment in current reactors and delays to phase-outs of capacity. Investment in new nuclear is most pronounced in Asia, where the industry is growing rapidly. Our broad offering, and the large geographic reach of our four facilities, enables us to meet this demand and make a strong contribution to the need for sustainable energy globally to meet climate change goals.

We are also continuously monitoring and mitigating geopolitical challenges. Our sites are prepared for the UK's full withdrawal from the European Union and Euratom. We are confident we will continue to meet our global customer commitments and remain a long-term supportive partner to the nuclear industry.