Energy crisis

Sweden announces emergency support for energy producers as EU considers action

Companies face rapidly rising collateral demands, prompting policymakers to warn of 'financial stability threat'

Magdalena Andersson said Russia's decision to close the Nordstream 1 pipeline could lead to a "war winter" © AFP via Getty Images

Richard Milne in Strömstad, **Alice Hancock** and **Henry Foy** in Brussels and **David Sheppard** in London SEPTEMBER 3 2022

Sweden will give emergency liquidity support to electricity producers as its prime minister warned that Russia's decision to halt gas deliveries to Europe could place its financial system under severe strain.

Magdalena Andersson said on Saturday that the government would offer hundreds of billions of kroner in funding to electricity producers, who have seen the amount of collateral they must post with exchanges balloon in response to soaring gas and power prices and increasing volatility.

EU energy ministers will also consider taking steps to ease the lack of liquidity for energy companies across the bloc at an emergency meeting on Friday, according to two officials briefed on the discussions.

Andersson warned that, left unchecked, rising collateral demands for electricity producers could ripple through the main Nasdaq Clearing market in Stockholm and, in the worst case, spark a financial crisis.

Her remarks came after Russia said on Friday that it would no longer supply gas via the Nordstream 1 pipeline. That announcement came after energy markets had closed for the weekend.

"Yesterday's announcement not only risks leading to a 'war winter' but also threatens our financial stability," Andersson said, standing alongside Sweden's financial regulator, central bank governor and finance minister at an emergency press conference on Saturday.

Finnish finance minister Annika Saarikko said on Twitter that her country would also act. "The concern is shared. Similar preparations are already well under way in Finland," Saarikko tweeted.

The dramatic actions underscored the seriousness of the situation facing Europe as it scrambles to secure enough energy ahead of winter and tries to avoid the spread of distress among electricity producers.

After surging to an all-time high eight days ago gas and electricity prices cooled slightly this week, with the benchmark European gas and German power contracts both declining by around a third — though they remain about 10 times historical levels. But the prolonged shutdown of Nord Stream 1 could increase volatility and boost prices when trading opens again on Monday.

Officials in Brussels are working on several possible ways of helping energy companies, including emergency liquidity support, the two officials said. Margin calls were becoming "far too big" for electricity producers to pay, said one.

Other measures could include price caps on either electricity or gas and ways to decouple the gas and electricity markets ahead of longer term reform. "Russians will play with us and we are not well equipped to face that," said the second official.

The European energy market's big problem

Many European energy companies are profiting from the rise in prices, but there are large discrepancies across the industry.

Those which produce gas or generate electricity using renewables or nuclear — where input costs have not risen — should be making large profits. But those reliant on burning gas for electricity generation are more likely to struggle — especially if they have been cut off from Russian supplies.

"We are not afraid of Putin's decisions, we ask Putin to respect their contracts, but if they don't respect their contracts, we are ready to react," Paolo Gentiloni, the EU's economy commissioner, told reporters on Saturday in comments reported by newswires.

Eurozone policymakers think that decisions should be made at a national level, according to one person with knowledge of their discussions.

Jean Francois Lambert, founder of Lambert Commodities and former head of commodity trade finance at HSBC, said other countries were likely to intervene in their energy markets.

Companies' need to post additional collateral does not mean trades or hedges are unprofitable, but their positions — often linked to providing gas or power to households and businesses — have rapidly become much more expensive to fund.

Companies are struggling to increase their short-term borrowing facilities quickly enough, risking a cash squeeze.

Jakob Magnussen, chief credit analyst at Danske Bank, said the big issue for electricity generators was the need for additional short-term funding.

To hedge their sales generators will normally short electricity futures contracts until the point they actually produce and sell the power into the market, helping guarantee the price they will receive.

But power prices have risen so rapidly in recent weeks that paper losses on the futures contracts have soared, requiring huge amounts of additional collateral to be posted with the exchanges.

"Margin calls are really exploding right now, it's particularly an issue for smaller utilities," said Magnussen. "Once the contracts mature and the utilities sell the power they will get their money back, but there's a huge need for additional short-term funding in the meantime and many banks could be reluctant to increase their exposure so rapidly to the sector."

"The crisis is moving into the next stage. If one of the large energy companies collapses there are fears there could be a domino effect," he said. "The call for liquidity is so enormous that maybe one day we have a problem that could harm the whole market."

While the threat of contagion to the wider financial sector was limited, governments needed to act to stop energy markets from "freezing up", he added.

Andersson said that Sweden's support would apply to all Nordic and Baltic players, and would need approval by the Swedish parliament's finance committee on Monday.

"We need to isolate this in one market so it doesn't infect the financial sector," said Stefan Ingves, governor of the Riksbank, Sweden's central bank.

The Swedish authorities said they saw no immediate risk to financial stability, but were worried that otherwise-solvent companies could struggle to find enough liquidity, causing potential ripple effects.

"Russia is waging an energy war against Europe to divide us. But we will not let Putin succeed," Andersson said.

Andersson's comments come a week before parliamentary elections in Sweden with polls pointing to a tight outcome. She said her centre-left government stood ready to act, just as it did over the Covid-19 pandemic.

Erik Thedéen, head of Sweden's Financial Supervisory Authority, said power prices in Sweden had risen 11-fold in the past year, leading to a jump in collateral demands.

He added that without liquidity support electricity producers could face bankruptcies and large losses that could "rock" the clearing house. "It is under very severe stress," he said.

Lambert said the situation was not yet a financial crisis. "The large banks in Germany, France, Italy and Spain should be able to stomach this. But if one of their large customers traps them in a liquidity squeeze then you could see all the banks pulling back," he said.

In July, the German government agreed a €15bn rescue package for Uniper, Europe's largest buyer of Russian gas, and said it would take a 30 per cent stake in the company. It had been losing tens of millions of euros a day since Gazprom first cut supplies of gas to Germany through Nord Stream earlier this year.

Late last month Uniper requested €4bn more, as soaring gas prices burnt up its cash reserves. Uniper, majority-owned by Fortum of Finland, said it had already drawn down a €9bn credit line from state development bank KfW.

Fortum warned on Monday that its collateral requirements had risen by €1bn to €5bn in the previous week, and that a default by a smaller player would cause "severe disturbances to the Nordic power system".

Additional reporting by Guy Chazan in Berlin and Martin Arnold in Frankfurt