

Financial risk management

General policies

The Alpiq Group's operating activities expose it to strategic and operational risks, and in particular credit, liquidity and market risks (energy price risk, interest rate risk and foreign currency risk). During the annual business risk assessment process, strategic and operational risks throughout the Group are recorded and assessed and then assigned to the identified risk owners for management and monitoring. The Corporate Risk Management functional unit monitors the implementation of the measures. Exposure limits are set for credit, liquidity and market risks (energy price risk, interest rate risk, foreign currency risk), with compliance monitored on an ongoing basis, and adjusted in the context of the company's overall risk-taking capacity.

The principles of the Group's risk management policy are established by the Board of Directors. The Executive Board is responsible for their development and implementation. The Risk Management Committee (RMC) monitors compliance with the principles and policies. The Corporate Risk Management (CRM) functional unit in the Financial Services functional division is responsible for managing risks and reports to the CFO. The CRM provides methods and tools for implementing risk management and also assists the business divisions, functional divisions and business units in their risk management activities. The CRM coordinates the activities and reporting with line management through to unit manager level and ensures timely reporting to the Board of Directors, Executive Board and RMC.

Principles for managing risks in the Alpiq Group's energy business are set out in its energy risk management policy. They comprise guidelines on the incurrence, measurement, management and limitation of exposure to business risks in energy business and specify the organisation and responsibilities for risk management. The objective is to maintain a reasonable balance between the business risks incurred, earnings and risk-bearing equity.

The Group's financial policy defines the substance, organisation and system for risk management within the Alpiq Group. The units responsible manage their financial risks within the framework of the risk management policy and limits defined for their areas of activity. The objective is to reduce financial risks, bearing in mind the hedging costs and risks being incurred.

Capital management

Across the Alpiq Group, capital is managed in line with the Group's overall financial strategy. The strategy is focused on the Group's reported consolidated equity and net debt to EBITDA ratio. As the framework for managing its capital structure, the Board of Directors has defined an equity ratio of at least 35 %, on which it is seeking to generate a return on equity of at least 9 %.

The Group is also financed by interest-bearing borrowings. The level of these borrowings must bear a reasonable proportion to earnings to ensure a strong credit rating in line with industry norms. The ratio of net debt to EBITDA should not exceed 3 times, but range from 2.0 to 2.5 times in the medium term.

The above-mentioned limits and targets are fully consistent with the covenants under financing arrangements entered into.

During the planning and budgeting process, the Board of Directors is advised annually of the planned performance of the targets set. The current medium- and long-term budget figures are within these targets.

The Group's financing strategy remained unchanged year on year. The business combination between Atel and EOS and the planned capital expenditure projects have temporarily resulted in a higher debt gearing ratio, but it remains within the limits.

Financial instruments

Carrying amounts and fair values of financial assets and liabilities

CHF million	Note	Carrying amount at 31 Dec 2008	Fair value at 31 Dec 2008	Carrying amount at 31 Dec 2009	Fair value at 31 Dec 2009
Financial assets at fair value through profit or loss					
Securities held for trading	16	7	7	20	20
Positive fair values of derivatives					
Currency and interest rate derivatives		6	6	7	7
Energy derivatives		1,152	1,152	1,233	1,233
Total financial assets at fair value through profit or loss (excl. financial assets designated in this category)		1,165	1,165	1,260	1,260
Financial assets designated in this category					
Financial investments	12	34	34	35	35
Held-to-maturity investments					
Assets with fixed maturity					
Loans and receivables					
Cash and cash equivalents	15	950	950	1,364	1,364
Term deposits		267	267	408	408
Trade receivables	14	1,531	1,531	1,887	1,887
Unbilled revenue	14	192	192	179	179
Other financial receivables	14	291	291	342	342
Loans receivable	12	8	8	43	43
Total loans and receivables		3,239	3,239	4,223	4,223
Total financial assets		4,438	4,438	5,518	5,518
Financial liabilities through profit or loss					
Negative fair values of derivatives					
Currency and interest rate derivatives				9	9
Energy derivatives		1,155	1,155	1,335	1,335
Total financial liabilities through profit or loss		1,155	1,155	1,344	1,344
Other financial liabilities					
Trade payables	21	1,047	1,047	1,249	1,249
Bonds	19	1,163	1,198	2,604	2,762
Loans payable	19	1,018	1,026	2,520	2,522
Other financial liabilities, incl. put options		451	452	949	949
Total other financial liabilities		3,679	3,723	7,322	7,482
Total financial liabilities		4,834	4,878	8,666	8,826

At 31 December 2009, the Alpiq Group measured the following assets and liabilities at fair value. The fair value hierarchy shown below was used to classify the financial instruments:

Level 1: quoted prices in active markets for identical assets or liabilities

Level 2: valuation technique based on quoted prices in active markets that have a significant effect on the fair value

Level 3: valuation techniques using inputs that are not derived from quoted prices in active markets and have a significant effect on the fair value.

CHF million	31 Dec 2009	Level 1	Level 2	Level 3
Assets measured at fair value				
Securities held for trading	20	1	19	
Currency and interest rate derivatives	7	7		
Energy derivatives	1,233	13	1,220	
Financial investments	35	27	8	
Financial liabilities measured at fair value				
Currency and interest rate derivatives	9	9		
Energy derivatives	1,335		1,335	

During the reporting period ended 31 December 2009, there were no transfers between Level 1 and Level 2 and no transfers out of Level 3.

Expense/income related to financial assets and liabilities

CHF million	Income statement 2008	Equity 2008	Income statement 2009	Equity 2009
Net gains/losses				
On financial assets and liabilities at fair value through profit or loss	-7	-24	-21	-22
On financial assets designated in this category	21		-9	
On loans and receivables				
On available-for-sale assets				
Interest income and expense				
Interest income on financial assets not measured at fair value	45		29	
Interest expense on financial liabilities not measured at fair value	-77		-155	
From the application of the effective interest rate method	-20		-65	

In 2009, an impairment loss of CHF 28 million (2008: CHF 11 million) was recognised in respect of trade receivables. No impairment loss was recorded for other financial instruments. More information about movements in the provision for impairment is presented in the “ageing analysis of trade receivables”.

Hedging activities (hedge accounting)

Forward contracts

At 31 December 2009, the Alpiq Group recognised forward transactions to hedge the price risk of future deliveries in respect of small to medium-sized end customers in Spain. The transactions will occur as the necessary energy cannot be purchased in the local market.

The instruments used to hedge the cash flows of contractual commitments to deliver electricity were assessed to be highly effective. Therefore an unrealised loss of CHF 28 million, with a related deferred tax asset of CHF 8 million was included in equity at 31 December 2009 in respect of these contracts.

1,200 tonnes of copper are going to be purchased for a contract in the Energy Services segment. To manage exposure to price fluctuations, the price has been hedged by copper swaps for a term until May 2011. At 31 December 2009, the valuation of the highly effective hedges showed a gain of CHF 1 million, including a deferred tax liability, which has been recognised in equity.

Interest rate swaps

At 31 December 2009, the Group held four interest rate swaps used to fix the interest rates under a project financing facility. The hedge strategy eliminates potential financial risks arising from an increase in the variable interest rates on which the financing is based.

CHF million	Assets 2008	Liabilities 2008	Assets 2009	Liabilities 2009
Forward commodity contracts	0	19	1	20
Interest rate swaps	0	5	0	3

The hedge relationship for hedging interest payments (cash flows) was assessed to be highly effective. The unrealised loss of CHF 4 million (2008: CHF 7 million), with a related deferred tax asset of CHF 1 million (CHF 2 million) was included in equity at 31 December 2009.

The amounts recognised in equity at 31 December 2009 are transferred to the income statement over the life of the hedge relationship as energy and commodities are purchased or interest paid under the underlying contract.

During 2009, the CHF 19 million recognised in equity at 31 December 2008 for hedges of coal-indexed contracts (BAFA, HFO) was transferred to the income statement. This transfer was recognised because the underlying transaction was terminated at the end of 2009.

The hedge ineffectiveness recognised immediately in the income statement during the reporting year was immaterial.

Credit risk management

Credit risk management deals with potential losses arising from the inability of business partners to meet their contractual obligations to the Alpiq Group. Energy credit risk management in the Energy segment encompasses all business units and subsidiaries that have a significant trading volume with external counterparties. It involves regular monitoring of outstanding receivables from counterparties and expected future changes as well as an analysis of the creditworthiness of new and existing counterparties. Besides energy derivatives recorded as financial instruments, it also covers contracts entered into for physical receipt or delivery.

Credit risk is primarily managed using credit limits set by reference to ratings. The Alpiq Group classifies counterparties or groups of counterparties (with similar risk characteristics) in risk categories (AAA–CCC) based on the probability of default. Once established, these ratings are used as the basis for setting the credit limits. The limits may be increased if collateral, such as guarantees, advances or insurance cover, is provided. The ratings of active counterparties are reviewed periodically and the credit limits adjusted, where appropriate.

Binding minimum requirements apply in selecting customers. Particular requirements are approved credit limits and the appropriate guarantees as well as a valid contractual basis. The policy in energy business is to enter into contracts only with counterparties who meet the criteria of energy risk policy. Outstanding credit exposures are monitored and managed on an ongoing basis using a formalised process.

Credit exposure in the Energy Services segment is managed and monitored on a decentralised basis, mainly focusing on receivables management. The local operational management is periodically provided with comprehensive reporting containing all the necessary information required for assessing the outstanding receivables.

Under IFRS 7, the total carrying amount of financial assets recognised represents the Alpiq Group's maximum exposure to credit risk at the reporting date. Calculated accordingly, the maximum credit exposure was CHF 5,518 million at 31 December 2009 (31 December 2008: CHF 4,438 million). For a detailed summary, we refer to the fair values presented in the table of "carrying amounts and fair values of financial assets and liabilities". Credit risk is reduced by collateral held as security and by contractual agreements for netting all receivables and payables with the same counterparty, even those not recognised under IAS 39. Conversely, the credit risk is increased by costs incurred by the Alpiq Group in closing out outstanding positions on more unfavourable terms.

At the beginning of 2009, the Risk Management Committee gave instructions to tighten credit risk management in view of the financial and economic crisis.

The Alpiq Group's exposure to concentrations of risk is minimised due to the number of customers spread across diverse geographical areas and the consolidation of positions. As in the previous year, there were no significant concentrations of risk at the reporting date.

Cash and term deposits are placed with banks that have a rating of at least "A" from an internationally recognised rating agency. The investments are limited in amount, widely diversified and staggered over time. The limits are reviewed semi-annually or when particular circumstances require. No write-offs have been necessary to date.

Collateral

A substantial portion of the energy contracts entered into by the Alpiq Group is based on agreements containing a netting arrangement. Receivables and payables are only presented net in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis. Furthermore, additional collateral, such as guarantees, variation margin payments or insurance cover, is collected where necessary.

As in the previous year, no collateral was collected and converted into financial assets.

Ageing analysis of trade receivables

CHF million	31 Dec 2008	31 Dec 2009
Carrying amount before impairment	1,570	1,939
Impaired	39	52
Provision at beginning of year	54	39
Acquisition/ disposal of subsidiaries	2	1
Charge for the year	11	28
Amounts written off as uncollectible	- 14	- 7
Unused amounts reversed	- 10	- 9
Exchange differences	- 4	0
Provision at end of year	39	52
Not impaired	1,531	1,887
Not past due	1,344	1,711
1 - 90 days past due	136	128
91 - 180 days past due	10	25
181 - 360 days past due	8	11
Over 360 days past due	33	12

In the reporting year (and previous year), an insignificant amount of trade receivables was written off directly under a certificate of unpaid debts, for which no provision had been made because there was no indication of impairment.

The Alpiq Group holds collateral (bank guarantees) with an estimated fair value of CHF 92 million (2008: CHF 13 million) as security for impaired and for past due but not impaired trade receivables.

At the reporting date, there were no indications that debtors owing unimpaired receivables would not be able to meet their payment obligations.

Liquidity risk

In European energy trading, a substantial portion of the receivables is offset and settled on specified dates, reducing the maximum liquidity requirements. Margin agreements are commonly used on energy commodity exchanges and among large energy traders so as to reduce the counterparty risk. As a result, movements in energy prices can lead to substantial outstanding debts in the short term. The Alpiq Group manages these variable liquidity requirements by using an early warning system, maintaining sufficient liquid resources and obtaining committed credit facilities from first-rate banks. Corporate Treasury in the Financial Services functional division is responsible for Group-wide cash and liquidity management under the direction of the CFO. Its role is to forecast, monitor, provide and optimise liquidity throughout the Group.

The contractual maturities of financial liabilities are presented below. The counterparty's redemption option has been taken into account even if redemption currently seems unlikely. Where it is intended to refinance loans at the end of the contract term, but refinancing has not yet been contractually secured, a cash outflow on maturity is assumed. Accordingly, actual cash flows may differ significantly from the contractual maturities.

Cash flows from derivatives are presented on a gross basis when the amounts are actually settled gross. To reflect the actual liquidity risk arising from such financial instruments, the cash inflows from derivatives are shown on a separate line in addition to the cash outflows.

2009: Maturity analysis of financial liabilities

CHF million	Carrying amount						Cash flows	
		< 1 month	1-3 months	4-12 months	1-5 years	> 5 years	Total	
Non-derivative financial liabilities								
Trade payables	1,249	- 915	- 297	- 23	- 14		- 1,249	
Bonds	2,604		- 31	- 53	- 1,124	- 2,017	- 3,225	
Loans payable	2,520	- 4	- 14	- 55	- 2,250	- 477	- 2,800	
Other financial liabilities	949	- 26	- 190	- 186	- 462	- 93	- 957	
Derivative financial instruments								
Net carrying amount of derivative financial instruments	- 104							
Net carrying amount of energy derivatives	- 102							
Gross cash inflows		1,635	3,092	13,437	9,020	1	27,185	
Gross cash outflows		- 1,673	- 3,143	- 13,788	- 9,237		- 27,841	
Net carrying amount of interest rate/currency derivatives	- 2							
Gross cash inflows		271	107	184	348	57	967	
Gross cash outflows		- 274	- 108	- 194	- 375	- 51	- 1,002	

2008: Maturity analysis of financial liabilities

CHF million	Carrying amount						Cash flows	
		< 1 month	1-3 months	4-12 months	1-5 years	> 5 years	Total	
Non-derivative financial liabilities								
Trade payables	1,047	- 695	- 314	- 23	- 15		- 1,047	
Bonds	1,163		- 14	- 23	- 466	- 946	- 1,449	
Loans payable	1,018	- 13	- 4	- 43	- 911	- 240	- 1,211	
Other financial liabilities	451	- 3	- 224	- 154	- 72	- 7	- 460	
Derivative financial instruments								
Net carrying amount of derivative financial instruments	3							
Net carrying amount of energy derivatives	- 3							
Gross cash inflows		1,745	3,229	13,101	8,057		26,132	
Gross cash outflows		- 1,716	- 3,223	- 13,107	- 8,526		- 26,572	
Net carrying amount of interest rate/currency derivatives	6							
Gross cash inflows		433	114	244	228	64	1,083	
Gross cash outflows		- 420	- 113	- 255	- 245	- 61	- 1,094	

The potential outflow of resources arising from guarantees is shown in note 24.

Market risk

The Alpiq Group's exposure to market risk primarily comprises energy price risk, interest rate risk, foreign currency risk and equity price risk. These risks are monitored on an ongoing basis and managed using various derivative financial instruments.

Market risk is measured within the framework of a Group-wide risk policy setting out rules on the incurrence, measurement, limitation and monitoring of risks. Compliance with these risk limits is monitored on an ongoing basis by the Risk Management Committee based on regular reporting by the Corporate Risk Management functional unit.

Energy price risk

Energy price risk refers to potential price fluctuations that could have an adverse impact on the Alpiq Group. These can arise from factors such as variations in price volatility, market price movements or changing correlations between markets and products. Energy liquidity risks also belong in this category. These occur when an open energy position cannot be closed out or can only be closed out on very unfavourable terms due to a lack of market bids.

Derivative financial instruments are used to hedge underlying physical transactions in line with the risk policy.

Interest rate risk

The Alpiq Group is exposed to risks arising from volatility in interest rates. Under its financial policy, liquid assets are invested on a short-term basis, while the necessary funding is obtained on a long-term basis. This means that a change in interest rates for assets has a direct impact on finance income. A change in interest rates for liabilities does not directly affect finance costs due to the long-term nature of the financing arrangements. However, substantial differences may arise between the carrying amounts and fair value.

Foreign currency risk

The Alpiq Group seeks to mitigate foreign currency risk by offsetting operating income and expenses denominated in foreign currencies. Any net balance remaining is hedged by foreign exchange contracts (forward contracts, options) in accordance with the Group's financial policy.

Net investments in foreign subsidiaries are also exposed to changes in foreign exchange rates, but the difference in inflation rates should offset these changes over the long term. For this reason, investments in foreign subsidiaries are not hedged.

Foreign currency risk arising from energy generation or purchasing is contractually transferred to the counterparty wherever possible. Where this is not possible or is only partially possible, forward currency contracts and currency options with a hedging horizon of up to 24 months are used to manage exposure in line with the Group's financial policy. Foreign currency risk is generally monitored centrally. The foreign currency risk related to the euro is considered acceptable and expected to be offset over the long term by differences in interest rates so this risk is generally not hedged.

The foreign currency risk associated with assets and liabilities denominated in foreign currencies (translation risk) is not hedged.

Equity price risk

The Alpiq Group holds a number of minor financial investments that are recognised at fair value and are susceptible to equity price fluctuations. As a rule, they are not hedged.

Sensitivity analysis

An analysis of market risk exposures is presented below, showing how profit would have been affected by reasonably possible changes in the relevant risk variable. The 2009 analysis revealed that the possible impact on equity would have been +/- CHF 3 million from interest rate derivatives (2008: +/- CHF 5 million) and +/- CHF 19 million (+/- CHF 19 million) from hedging transactions related to energy and energy services business.

Foreign currency risk sensitivity is based on financial instruments held at the reporting date. The reasonably possible changes in the relevant risk variable were determined based on historical fluctuations (over 3 years). A variation by +/- 1 standard deviation around the calculated mean is considered to be reasonably possible.

The exposure to equity price movements is based on the weighted average 180-day volatility of the current securities portfolio during 2009. Sensitivity to interest rate risk is measured by stress testing based on the six-month Euribor.

The possible annual percentage changes in the fair values of energy derivatives are determined from the commodity market prices for electricity, gas, coal and oil over the past three years. The sensitivities are calculated using the maximum deviations from the mean to a confidence level of 99%.

Each type of risk is quantified assuming that all other variables remain constant.

CHF million	+/- Change 2008	+/- Impact on the income statement 2008	+/- Change 2009	+/- Impact on the income statement 2009
Energy price risk	99.8 %	2.0	106.6 %	108.7
EUR/CHF currency risk	9.7 %	78.9	5.3 %	61.6
EUR/USD currency risk	16.2 %	14.4	12.4 %	20.6
EUR/CZK currency risk	11.7 %	5.1	9.3 %	0.9
EUR/HUF currency risk	18.2 %	1.8	13.9 %	0.8
EUR/NOK currency risk	12.9 %	1.1	9.3 %	2.3
EUR/PLN currency risk	15.9 %	0.5	13.3 %	0.9
EUR/RON currency risk	14.9 %	0.4	18.4 %	0.7
USD/CHF currency risk	13.3 %	1.4	12.0 %	0.3
USD/HUF currency risk	30.0 %	7.1	-	-
CHF/CZK currency risk	-	-	16.6 %	4.2
CHF/HUF currency risk	-	-	22.4 %	1.1
Interest rate risk	1.0 %	31.6	1.0 %	32.2
Equity price risk	46.0 %	6.6	7.0 %	3.6