



Moody's Investors Service

## Rating Action: Moody's downgrades Landsvirkjun to Baa3/P-3 stable from Baa1/P-2 negative

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Global Credit Research - 11 Nov 2009

London, 11 November 2009 -- Moody's Investors Service has today downgraded the senior unsecured ratings of Landsvirkjun to Baa3/P-3 stable outlook from Baa1/P-2 negative outlook. These rating downgrades are in line with the rating agency's recent decision to downgrade the Icelandic government's bond ratings to Baa3/P-3 with a stable outlook.

The downgrade of the sovereign rating reflects the enduring fiscal, financial and monetary challenges resulting from the crisis set against Iceland's high wealth, economic flexibility and sound institutions. The stable outlook additionally reflects the balance of risks between the divergent trends of an improving economic outlook, severe strains on public finances and the still uncertain exit strategy from capital controls.

Given 100% direct and indirect ownership by the Government, Landsvirkjun's current ratings attribute high support to the company from the Icelandic government given the explicit support for the company from the State given its guarantee of Collection under which it ultimately has a joint and several liability for the obligations of Landsvirkjun.

This high support is reinforced by the strategic importance of Landsvirkjun given its position as the country's dominant electric utility and the significant role played in the economy by the aluminium smelting industry in Iceland which relies in large part on the electricity provided by Landsvirkjun.

At the same time Moody's has moved the company's baseline credit assessment (BCA) from a 14 (equivalent to a B1) to a 15 (equivalent to a B2). This reflects Landsvirkjun's exposure to fairly low aluminium prices through its contracts with power intensive industries and Moody's belief that these prices will remain under pressure given the current overcapacity in the aluminium industry. Whilst Landsvirkjun has benefited from lower interest rates over the past year, it remains vulnerable to both a general rise in interest rates as well as overall higher funding costs as a result of a lower rating than in the past. Both these factors could stress the company's already stretched financial profile.

At the same time, Moody's acknowledges the reduction in execution risk as the company has finished its major projects and the fact that it is relatively well insulated against the weak krona, as 70% of the company's revenues are paid in dollars and its funding base has limited exposure to the domestic currency. The company also has adequate liquidity well into 2011 and a well-spread maturity profile. In a reasonably benign environment, the company could gradually improve financial metrics and reduce debt.

The last rating action on Landsvirkjun was on 5 December 2008 when the ratings were downgraded to Baa1/P-2 from A1/P-1.

The principal methodologies used in rating Landsvirkjun are The Application of Joint Default Analysis to Government Related Issuers, April 2005 and Unregulated Utilities and Power Companies published in August 2009 and available on [www.moodys.com](http://www.moodys.com) in the Rating Methodologies sub-directory under the Research and Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Ratings Methodologies sub-directory on Moody's website.

Landsvirkjun is headquartered in Reykjavik, Iceland and generates, transmits and sells electricity to public utilities and energy intensive industries. As at FYE 2008, it had turnover of approximately USD450 million.

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