

**Rating Action: Moody's upgrades Landsvirkjun's ratings to Baa3/Baa1; stable outlook**

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London, 05 September 2016 -- Moody's Investors Service, ("Moody's") has today upgraded Landsvirkjun's unguaranteed senior unsecured debt ratings to Baa3 from Ba1, and the ratings of the \$1 billion EMTN programme to (P)Baa3/(P)P-3 from (P)Ba1/(P)NP. Concurrently, Moody's has upgraded Landsvirkjun's senior unsecured debt ratings that are supported by a guarantee of collection issued by the Government of Iceland (A3 stable) to Baa1 from Baa2, and the guaranteed senior unsecured rating of the \$2.5 billion EMTN programme to (P)Baa1 from (P)Baa2. The (P)P-2 short term rating of the guaranteed EMTN programme was confirmed. Moody's has also assigned a stable outlook.

**RATINGS RATIONALE**

Today's rating action concludes the rating review initiated on 13th June 2016 and it is driven by the upgrade of Iceland's government bond rating to A3 with a stable outlook from Baa2 under review for upgrade on 1st September 2016. For details, please refer to: [http://www.moody.com/viewresearchdoc.aspx?docid=PR\\_351195](http://www.moody.com/viewresearchdoc.aspx?docid=PR_351195).

Given its 100%-ownership by the Government of Iceland, Landsvirkjun is considered a government-related issuer under Moody's methodology. Landsvirkjun's rating is determined by an assessment of its standalone credit quality, expressed as a Baseline Credit Assessment (BCA) and factors pertaining to the likelihood of extraordinary support being provided by the Government of Iceland in the event that this were needed to avoid a payment default. The upgrade of both the guaranteed and unguaranteed debt ratings reflects Moody's view that the government's ability to support Landsvirkjun has strengthened. Accordingly, the upgrade of Landsvirkjun's ratings does not reflect any change in its standalone credit quality, which Moody's continues to assess as a ba3 BCA, or any change in its relationship with the government.

The high level of government support incorporated in Landsvirkjun's unguaranteed debt ratings reflects the company's position as the country's dominant power producer and the role it plays in the provision of electricity to the aluminium smelting industry, which directly contributes to about 40% of Icelandic exports. Moreover, it also considers the high level of commitment that the government has shown in the past by the provision of guarantees of collection to support Landsvirkjun's debt.

The Baa1 and (P)Baa1/(P)P-2 guaranteed ratings of Landsvirkjun's USD2.5 billion EMTN programme and notes issued thereunder reflects the value of the guarantee of collection issued by the Government of Iceland. Moody's notes that guarantees of collection do not offer bondholders the same contractual protection as a timely payment guarantee. Albeit small, there is a potential risk that the Government would not step in with timely repayment should the company fail to meet its obligations, as exhaustive administrative and legal procedures must be followed before the shareholders are obliged to pay. The Baa1 rating reflects a very high likelihood that the Government would pay on a timely basis, but the positioning of the guaranteed debt ratings at one notch below that of the Government of Iceland reflects this residual uncertainty of payment from a single A rated sovereign.

**RATIONALE FOR STABLE OUTLOOK**

The stable outlook is in line with the outlook of the Icelandic government's ratings. It also reflects Moody's expectation that Landsvirkjun will continue to prudently manage its exposure to market risks and improve its financial position, such that credit metrics will be comfortably positioned within the ratio guidance for a ba3 BCA, namely the maintenance of an FFO/ Net debt ratio in the low double digits in percentage terms.

**WHAT COULD CHANGE THE RATING UP/ DOWN**

Moody's could consider an upgrade of Landsvirkjun's ratings (1) following an upgrade of the sovereign rating; or (2) if the company continues to demonstrate the ability to withstand significant volatility in the commodity markets and credit metrics were to materially improve above ratio guidance on a sustainable basis without increasing its financial risk profile. This would also assume no change to the assumption of support from the

government incorporated into Landsvirkjun's rating.

Conversely, downward pressure on Landsvirkjun's ratings could develop (1) following a downgrade of the Icelandic government's ratings; or (2) as a consequence of a substantial deterioration in Landsvirkjun's business risk profile or weakening of its financial position, such that FFO/Net debt in percentage terms was expected to remain consistently below 10%. The ratings would also come under downward pressure if Moody's were to revise the current assumption of timely support from the government.

The methodologies used in these ratings were Unregulated Utilities and Unregulated Power Companies published in October 2014, and Government-Related Issuers published in October 2014. Please see the Ratings Methodologies page on [www.moodys.com](http://www.moodys.com) for a copy of these methodologies.

## CORPORATE PROFILE

Headquartered in Reykjavik, Landsvirkjun is Iceland's dominant power producer. It is responsible for about 70% of Iceland's total electricity production of 18 terawatt hours (TWh) and owns the majority of the transmission grid. It provides 100% renewable energy for domestic users via electricity sales to public utilities, although the majority of sales are to power intensive industries, mostly for aluminium smelting, under long-term take-or-pay contracts.

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