



Moody's Investors Service

Rating Action: Moody's downgrades Orkuveita Reykjavikur to Ba1, stable outlook from Baa1, negative outlook

Global Credit Research - 11 Nov 2009

London, 11 November 2009 -- Moody's Investors Service has today downgraded to Ba1 stable outlook from Baa1 negative outlook the long term senior unsecured issuer rating of Orkuveita Reykjavikur (OR also known as "Reykjavik Energy").

OR is a Government-Related Issuer under Moody's methodology given its 100% ownership by the City of Reykjavik (93,5%) and other local authorities. The rating action primarily reflects the recent change in the sovereign rating from Baa1/negative to Baa3/stable prompted by the enduring fiscal, financial and monetary challenges resulting from the crisis. The sovereign rating change also factors the divergent trends of an improving economic outlook, severe strains on public finances and the still uncertain exit strategy from capital controls.

OR's rating downgrade also incorporates a shift in the Baseline Credit Assessment of the company from 15 (equivalent to B2) to 16 (equivalent to B3). The still weak krona has led to a rise in the company's debt burden, as it is principally funded in foreign currency. Conversely, most of the company's revenues are in domestic krona which have been moderately negatively impacted by subdued domestic demand. These factors have led to a weakening of an already stretched financial profile. Moody's also factors the rather stressed liquidity profile of the company, although the company expects that access to domestic and some other funding should allow it to refinance debt maturities falling due in 2010 as well as meeting maintenance capex. Moody's also notes that the company is likely to go ahead with the completion of the Hellisheidi plant assuming further funding is received, which should allow for increased US dollar revenues from a new aluminium smelting contract as from 2012 following completion of the plant.

The downgrade to Ba1, at one notch below that of the sovereign, reflects a moderate reduction in the high level of institutional support that Moody's applies to OR's rating. Given the guarantee of collection from its owners, Moody's would expect that, in the first instance, the City of Reykjavik and other municipal owners would support the company in case of extraordinary need to pay any shortfall in interest and principal. However should further support be needed, Moody's would expect the central government to coordinate with the local governments to arrange timely intervention. Nonetheless given the greater level of institutional stress as a result of the current economic weakness, Moody's has moderately reduced the level of support to reflect the fact that were there to be large and conflicting demands on the government, timely support may not always be forthcoming. It additionally reflects the absence of a direct guarantee from the government in favour of the company.

The last rating action on OR was implemented on 11 December 2008 when the rating was downgraded to Baa1 negative outlook from A1.

The principal methodology used in rating OR was the Application of Joint Default Analysis for Government Related Issuers, April 2005 available on www.moody's.com in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

Orkuveita Reykjavikur based in and around Reykjavik Iceland is the country's largest multi utility providing electricity, hot water heating, cold water and waste services to more than 50% of the Icelandic population. The company focuses on generating environmentally-friendly energy from geothermal sources. As at FYE 2008, the company had revenues of ISK24billion.

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