

**Rating Action: Moody's changes outlook on Landsvirkjun's Baa3/P-3 ratings to negative**

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**Global Credit Research - 30 Jul 2010**

London, 30 July 2010 -- Moody's Investors Service has today changed the outlook on the Baa3/P-3 senior unsecured ratings of Landsvirkjun to negative from stable. This outlook revision is in line with the rating agency's decision to change the outlook on the Icelandic government's Baa3 ratings to negative from stable.

The sovereign rating action was triggered by the recent Supreme Court ruling on the illegality of foreign-exchange-linked loans and government's continuing difficulties in achieving a resolution to its "Icesave" dispute with the UK and Dutch governments. Specifically, the Supreme Court ruling has the potential to cause substantial bank losses on foreign currency-denominated loans to domestic borrowers and may therefore require additional government support to the banking system. Moreover, a failure to resolve the "Icesave" dispute could lead the Nordic countries and the IMF to withhold future disbursements to the Icelandic government.

These two sources of macroeconomic uncertainty are indicative of the generally asymmetric risks facing Iceland and explain the rationale for the negative outlook on its ratings.

Moody's says that downward rating pressure on Iceland's sovereign rating could result from (1) indications that the ongoing uncertainties will negatively impact the real economy, and (2) renewed stress in the banking system and a resultant need for further capital injections by the government, which would further increase the already elevated levels of government debt and (3) pressure on Iceland's external liquidity.

Conversely, the rating agency says that positive pressure on Iceland's rating could develop if there are signs of a sustained economic recovery and successful solutions to the current uncertainties.

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

This very 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.

Landsvirkjun's Baseline Credit Assessment remains unchanged at 15 (equivalent to a B2) reflecting its stretched financial profile. Landsvirkjun's cash flow remains exposed to a rise in interest rates and aluminium rate movements via its contracts with power intensive industry. However, whilst highly indebted, Landsvirkjun now has limited investment needs and available liquidity through cash flow and under committed backup lines should be sufficient into 2012.

The last rating action on Landsvirkjun was on 26 April 2010 when the outlook of the Baa3 rating was changed from negative to stable in line with the sovereign action.

The principal methodologies used in rating Landsvirkjun are Government Related Issuers: Methodology Update published in July 2010, and Unregulated Utilities and Power Companies, published in August 2009, which are available on [www.moody's.com](http://www.moody's.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.

Landsvirkun is headquartered in Reykjavik, Iceland and generates, transmits and sells electricity to public utilities and energy intensive industries. As at FYE 2009, it had turnover of approximately USD296 million.

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