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## Energie AG Oberoesterreich

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# Energie AG Oberoesterreich

## Major Rating Factors

### Strengths:

- Electricity distribution monopoly
- Market leader in electricity supply in the State of Upper Austria
- Prosperity of core electricity service area
- Moderate financial risk profile

### Corporate Credit Rating

A/Stable/--

### Weaknesses:

- Weakening power demand in the current environment
- Regulatory pressure on Energie AG's electricity network operations
- Exposure to increasing competition in the Austrian electricity retail market
- Increasing share of profits coming from the higher risk waste management and generation activities and from transition economies

## Rationale

The ratings on Energie AG Oberoesterreich (Energie AG) reflect the company's regional electricity distribution monopoly, its strong position as the leading utility in the prosperous State of Upper Austria (AAA/Stable/A-1+), and its moderate financial profile. However, these strengths are offset by weakening power demand and prices in the current environment, regulatory pressure on Energie AG's electricity network operations, and a degree of competition in the Austrian electricity retail market. Further risk factors are its increasing exposure to the higher-risk waste sector and lower-rated transition economies in Eastern Europe, and its long-term investment strategy in thermal generation facilities.

### Key business and profitability developments

In the fiscal year-ended Sept. 30, 2008, the group recorded a still robust performance. Revenues reached €1.5 billion and EBITDA €298 million, increasing respectively by 33% and 8.8% compared with the previous year, on the back of increased generation and sales as well as acquisitions. However, overall results in fiscal 2009 are likely to weaken due to the impact of the economic crisis at a time when the company is set to carry out sustained investments. In addition, Energie AG has incurred some restructuring costs from its cross-border leasing transactions. We anticipate a recovery in 2010, but its extent is uncertain and planned investments remain significant.

### Key cash flow and capital-structure developments

In fiscal 2008, reported net debt increased significantly to €627 million from €466 million. This increase was a result of growth investments and acquisitions, mostly driven by the increase to 65% from 50% of Energie AG's stake in, and full consolidation of, the Austrian gas company OO Ferngas AG. In the same year, however, Energie AG also received a €216 million capital increase in the context of its shareholder structure redefinition.

We expect Energie AG to be moderately cash flow negative in the short term, due to planned investments. Nevertheless, Energie AG retains a degree of flexibility to adapt its investments to the evolution of the macroeconomic environment.

## Liquidity

We consider Energie AG's liquidity to be adequate. After the recent completion of a refinancing through a €250 million medium-term facility, debt maturing before March 31, 2010, has declined to about €100 million. On the other hand, as of March 31, 2009, Energie AG reported it had €39 million available in cash and equivalents and €316 million in investment funds. At the same time, the group also had available undrawn bank lines of €153 million, although the majority are uncommitted for taxation reasons. However, several of the lines are either confirmed or provided by financial institutions that are also shareholders of Energie AG.

We expect Energie AG to be moderately cash flow negative in the short term, but available liquidity should cover its funding needs. In addition, planned investments are deferrable to some extent.

## Outlook

The stable outlook is based on our view that Energie AG can weather a certain degree of economic downturn over the short term while maintaining coverage of funds from operations to debt of about 30%. We could revise the outlook to negative if the current crisis affects the group more than we anticipate or if its financial profile deteriorates further. The rating does not factor in material changes in business risk, acquisitions, or changes in financial and dividend policies. Rating upside is limited in the medium term.

## Business Description

Energie AG is Austria's fourth-largest electricity company, serving 440,000 customer accounts representing about one million end-users in Upper Austria. Energie AG's main activities are the generation, distribution, and supply of electricity, which accounted for 76% of EBITDA (of which 23% from regulated network businesses) in the fiscal year ended Sept. 30, 2008. Waste management and water are the other two core pillars of its business, accounting for 21% and 3% respectively. About 90% of EBITDA is generated in Austria, with the balance in the Czech Republic (6%) and Hungary (3%).

### Ownership structure

Following a private placement in July 2008, the company's majority shareholder remains, as required by law, the State of Upper Austria (51% stake). The remainder of capital is held by other Austrian utilities, financial institutions, and employees. The private placement reduced Upper Austria's shareholding from 93% and increased Energie AG's capital by €216 million. Austrian and state laws still prohibit majority privatizations of regional utilities such as Energie AG; this acts as a legal barrier to foreign utilities buying majority stakes in Austrian electricity utilities. We expect no changes to this policy in the medium term.

Energie AG receives no government support or guarantees and the rating is on a stand-alone basis. Energie AG is not listed.

## Business Risk Profile: Reflects Solid Competitive Position, Sound Operations, And Contribution From Regulated Noncompetitive Businesses

Energie AG's business risk profile is supported by:

- Its prosperous electricity service area and stable market conditions in its core Austrian electricity market. Energie

AG's traditional service area, Upper Austria, has one of the highest economic growth rates and lowest unemployment rates in Austria. That said, the area is unlikely to be immune to the current economic slowdown.

- Low risk domestic network operations: the tariff system that has been in place since 2006 is relatively transparent and is less aggressive than the previous regulatory regime that was put in place at the onset of regulation in 2001. Following a heavy 22.7% cut in tariff at the outset of the regulation period, Energie AG has experienced relatively benign tariff reductions over the past three years: negative 2.7%, negative 1.1%, and 0.0% respectively. Operations are solid: the service quality in the networks business is high, reflecting a conservative investment and maintenance policy, shared within the Austrian utility sector. This is also reflected by Energie AG's low electricity transmission losses of about 2.7%, which is below the Austrian average.
- A fairly balanced generation portfolio between its own hydro-generation facilities, procurement rights from hydro plants, and small-scale thermal generation facilities. The addition of the Timelkam CCGT since November 2008 has further diversified and enhanced the portfolio, increasing the percentage of self-generated electricity to about 45% of total sales from 34% (or to 68% from 58% if referring to sales to final customers).
- A substantial share of the waste management business is characterized by fixed price long-term contracts with the public sector, thereby reducing business risk.
- Growth in higher risk segments is pursued but with the aim to mitigate risk through joint ventures in Austrian electricity generation, management contracts, and small transactions in water and waste in Central and Eastern Europe.

These strengths are to some extent offset by:

- A strategy that has become more aggressive and acquisitive over the past few years. The company profile is shifting toward an increasing focus on Austrian electricity generation and trading, and international expansion predominantly in the waste and water businesses in Central and Eastern European countries.
- Uncertainty over the reset of domestic network tariffs in 2010: Although it is not yet clear what the adjustments will be, Energie AG expects to continue to receive moderate tariff cuts over the four-year regulatory period.
- A competitive position that is expected to soften over time due to retail customer churn and the competition of Verbund (A/Stable/--), the country's largest generator.
- Supply margins that are likely to come under pressure from declining regulated tariffs; especially as it will become more difficult to pass through these cuts if customer churn rates rise.

## Financial Risk Profile: Moderate, But Weakening Credit Metrics

The main strengths of Energie AG's moderate financial risk profile are:

- A track record of conservative financial planning and robustly growing results, underpinned by operations mostly located in the domestic market and partially regulated.
- An overall adequate debt structure, strengthened after the recent refinancing, with manageable short-term maturities, a fairly long-dated maturity profile, and moderate leverage.
- A policy of keeping substantial liquidity reserves invested in cash and low-risk securities to cover pension liabilities and financial obligations.
- A certain flexibility in planned investments, about 30% of which are deferrable.
- A dividend policy that is not overly aggressive, with distributions fixed at €54 million annually.

These strengths are moderated by:

- Growing higher risk generation and trading activities and risk that currently volatile and declining power prices combined with contracting demand affect performance more severely than anticipated, notwithstanding the mitigation stemming from operating cost savings and the hedging that is in place.
- Usage of cross-border lease agreements that could reduce recovery prospects in the event of bankruptcy due to potential higher priority ranking compared with senior unsecured debt and could trigger liquidity requirements. However, recourse to these instruments has recently declined since one of the two outstanding transactions, the one pertaining to the grid assets, was terminated in March 2009 at a cash cost of €10 million. Energie AG had already restructured this transaction in November 2008 at a cost of €15 million following the downgrade of AIG in September 2008. The hydro power plant transaction remains in place but was restructured as well for the same reason through recourse to a cash-collateralized letter of credit of €70 million.
- A preference for using uncommitted bank lines for taxation reasons, albeit several of the lines are either confirmed or provided by financial institutions that are also shareholders of Energie AG.

## Financial Statistics/Adjustments

Table 1

Reconciliation Of Energie AG Oberoesterreich Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. €)*									
--Fiscal year ended Sept. 30, 2008--									
Energie AG Oberoesterreich reported amounts									
	Debt	Shareholders' equity	Operating income (before D&A)	Op. income (before D&A)	Op. income (after D&A)	Interest expense	Cash flow from operations	Cash flow from ops	Capex
Reported	850.9	1,288.90	298.1	298.1	163.7	37.9	244.4	244.4	203.6
Standard & Poor's adjustments									
Operating leases	49.3	--	4.3	2.6	2.6	2.6	1.8	1.8	1.4
Postretirement benefit obligations	175	(11.4)	9.1	9.1	9.1	9.1	3.6	3.6	--
Accrued interest not included in reported debt	14.4	--	--	--	--	--	--	--	--
Surplus cash and near cash investments	(475.6)	--	--	--	--	--	--	--	--
Deconsolidation/consolidation (Timelkam)	105.0	--	--	--	--	5.0	--	--	--
Asset retirement obligations	41.5	--	--	--	--	--	--	--	--
Reclassification of nonoperating income (expenses)	--	--	--	--	18.4	--	--	--	--
Reclassification of working-capital cash flow changes	--	--	--	--	--	--	--	(7.9)	--
Minority interests	--	69	--	--	--	--	--	--	--
Total adjustments	(90.4)	57.6	13.4	11.7	30.1	16.7	5.4	(2.6)	1.4
Standard & Poor's adjusted amounts									
	Debt	Equity	Operating income (before D&A)	EBITDA	EBIT	Interest expense	Cash flow from operations	FFO	Capex
Adjusted	760.5	1,346.50	311.5	309.8	193.8	54.5	249.7	241.8	205

**Table 1****Reconciliation Of Energie AG Oberoesterreich Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. €)\* (cont.)**

\*Please note that two reported amounts (operating income before D&A and cash flow from operations) are used to derive more than one Standard & Poor's-adjusted amount (operating income before D&A and EBITDA, and cash flow from operations and funds from operations, respectively). Consequently, the first section in some tables may feature duplicate descriptions and amounts. FFO--Funds from operations. Capex--Capital expenditure.

Energie AG presents its annual accounts according to International Financial Reporting Standards. For the financial year-ended Sept. 30, 2008, we have adjusted Energie AG's debt for:

- A cash position of €224 million and about €252 million in investment funds, which can be accessed on short notice.
- Energie AG consolidates with the equity method the Timelkam gas-fired plant, in which it holds a 50% stake, and which is financed on a nonrecourse basis. However, Energie AG has agreed to offtake 70% of the electricity produced in this power plant under a long-term power purchase agreement. To reflect this financial commitment, we add 70% (about €105 million) instead of 50% of the project debt back to Energie AG's consolidated debt.

**Table 2****Energie AG Oberoesterreich -- Peer Comparison\***

	<b>Energie AG Oberoesterreich</b>	<b>Verbundgesellschaft (Oesterreichische Elektrizitaetswirtschafts Aktiengesellschaft)</b>	<b>KELAG</b>
Rating as of May 15, 2009	A/Stable/--	A/Stable/--	A+/Watch Neg/--
(Mil. €)	<b>--Fiscal year ended Sept. 30, 2008--</b>	<b>--Fiscal year ended Dec. 31, 2008--</b>	
Revenues	1,604.80	3,744.7	1,181.5
Net income from cont. oper.	116.4	686.6	69.2
Funds from operations (FFO)	241.8	1,197.5	140.7
Capital expenditures	205	441.4	119.2
Debt	760.5	2,551.4	308.8
Equity	1,346.50	3,636.6	532.1
<b>Adjusted ratios</b>			
Oper. income (bef. D&A)/revenues (%)	19.4	37	13.6
EBIT interest coverage (x)	3.6	6.9	6.5
EBITDA interest coverage (x)	5.7	7.1	8.7
Return on capital (%)	9.1	23.2	14.5
FFO/debt (%)	31.8	46.9	45.6
Debt/EBITDA (x)	2.5	1.9	1.9

\*Fully adjusted (including postretirement obligations). Excess cash and investments netted against debt.

**Table 3****Energie AG Oberoesterreich -- Financial Summary\***

<b>(Mil. €)</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
Rating history	A+/Negative/--	A+/Negative/--	A+/Negative/--	A+/Stable/--
Revenues	1,604.80	1,227.9	1,147.0	1,005.5
Net income from continuing operations	116.4	114.9	68.4	67.0
Funds from operations (FFO)	241.8	317.4	198.5	156.8

Table 3

Energie AG Oberoesterreich -- Financial Summary* (cont.)				
Capital expenditures	205	282.0	228.1	163.1
Cash and short-term investments	0	42.5	42.1	42.5
Debt	760.5	589.9	581.3	464.3
Preferred stock	0	0.0	0.0	0.0
Equity	1,346.50	1,219.0	1,080.5	1,007.8
Debt and equity	2,107.00	1,808.9	1,661.7	1,472.1
<b>Adjusted ratios</b>				
EBIT interest coverage (x)	3.6	4.1	3.4	3.1
FFO interest cov. (x)	5.1	7.4	6.6	5.2
FFO/debt (%)	31.8	53.8	34.1	33.8
Discretionary cash flow/debt (%)	0.8	2.1	(12.9)	4.8
Net cash flow/capex (%)	99	106.2	79.8	86.7
Debt/debt and equity (%)	36.1	32.6	35.0	31.5
Return on common equity (%)	9.4	10.2	6.7	7.0
Common dividend payout ratio (un-adj.) (%)	46.4	0.0	0.0	0.0

\*Fully adjusted (including postretirement obligations). Excess cash and investments netted against debt.

#### Ratings Detail (As Of May 15, 2009)\*

##### Energie AG Oberoesterreich

Corporate Credit Rating	A/Stable/--
Senior Unsecured (1 Issue)	A

##### Corporate Credit Ratings History

16-Mar-2009	A/Stable/--
21-Mar-2006	A+/Negative/--
28-Jun-2001	A+/Stable/--

##### Business Risk Profile

1 2 3 4 5 6 7 8 9 10

##### Financial Risk Profile

Moderate

##### Debt Maturities

(as of Sept. 30, 2008)  
 Year ending Sept. 30 2009: €369 mil.  
 Sept. 30 2010- Sept. 30 1011: €26 mil.  
 Thereafter: €456 mil. (of which, €300 mil. in 2025)

\*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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