Teollisuuden Voima Oyj (TVO)

Update

Ratings

Foreign Currency

Long-Term IDR	BBB
Short-Term IDR	F3
Senior unsecured	BBB

Outlooks

Foreign-Currency Long-Term IDR	Stable

Financial Data

Teollisuuden Voima Oyj

	31 Dec 12	31 Dec 11
Revenue (EURm)	352	352
Operating EBITDA (EURm)	72	102
Operating EBITDAR margin (%)	20.5	20.5
Net debt (EURm)	3,912	3,763

Related Research

Fitch Downgrades Teollisuuden Voima Oyj to 'BBB', Outlook Stable (May 2013)

Large European Utilities Have Limited Rating Headroom (March 2013)

2013 Outlook: European Utilities (December 2012)

Rating EMEA Utilities (August 2012)

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Key Rating Drivers

Rating Downgrade: Teollisuuden Voima Oyj's (TVO) ratings were downgraded in May 2013 due to the continued delay in commissioning of its third nuclear plant unit, the 1,600 megawatt (MW) Olkiluoto 3 (OL3), and Fitch Ratings' weakened mid-term outlook for forward Nord Pool wholesale electricity prices. The delay and lower prices will erode value creation for TVO's shareholders, a key consideration for our assessment of TVO's credit profile. The delay of OL3 to 2016 is of about seven years over the original schedule.

Not-for-Profit Nuclear Generator: The ratings reflect TVO's position as a not-for-profit Finnish nuclear generator, producing at-cost electricity for its six shareholders. The two largest shareholders are Pohjolan Voima Oy (58.5% stake), a not-for-profit generator owned by a consortium of Finnish industrials (mainly pulp and paper) and municipalities, and Fortum Power & Heat Oy (25.8% stake), a 100% owned subsidiary of Fortum Corporation (A−/Negative).

Higher Production Costs: TVO's two existing nuclear units, OL1 and OL2, have highly competitive production costs (about EUR20/MWh) compared with forward Nord Pool prices of around EUR35/MWh for 2014-2018. However, TVO's production costs will increase substantially from 2017 when OL3 is operational, due to high depreciation and interest costs.

Solid Shareholder Support: The shareholders remain committed to OL3 even with forecast diminishing competitiveness against Nord Pool prices. A EUR300m shareholder loan has been made by TVO's shareholders in June 2013 in response to the additional delay for OL3.

Weak Credit Ratios: As TVO does not seek to maximise profit, Fitch considers traditional leverage or coverage ratios, which are weak, as less relevant to the ratings. In 2010-2012, TVO's funds from operations (FFO) including cash interest paid was negative and FFO interest cover was below 1x as interest expense related to OL3 debt is not covered by the shareholders in the construction phase but is capitalised under the project.

Rating Sensitivities

Possible Compensation Award: A favourable outcome for TVO regarding litigation with the construction contract supplier Areva, with the award of a significant compensation for the delay, or significantly higher equity funding from TVO's shareholders would be ratings positive.

Further Delays: Reduced shareholder support, further OL3 delays impacting TVO's production costs, and greater litigation costs with Areva would be negative for the ratings. In addition, production costs exceeding Nord Pool prices on a sustained basis when OL3 is completed, a decline in operating performance, safety problems, significantly reduced liquidity, or its equity ratio moving close to the minimum covenanted threshold of 25% would be also negative.

Commencement of Olkiluoto 4: A binding commitment to the construction of the next nuclear unit, OL4 when OL3 is not fully operational, or significant debt funding of OL4 would be ratings negative.

Liquidity and Debt Structure

Adequate Liquidity: TVO had Q113 available cash of EUR122m, and short-term debt of EUR216m. An undrawn revolving credit facility of EUR1.5bn (maturing in 2018) together with committed shareholder loans largely cover capex and maturing debt requirements in 2013-15.

Peer Group

Issuer	Country
A–	
Vattenfall	Sweden
Fortum Corporation	Finland
BBB+	
Statkraft	Norway
DONG Energy A/S	Denmark

Issuer Rating History

Date	LT IDR (FC)	Outlook/ Watch
24 May 13	BBB	Stable
1 Nov 12	BBB+	Stable
1 Jun 12	BBB+	Stable
9 Jun 11	A–	Stable
7 Jun 10	A–	Stable
28 May 09	A–	Stable
23 May 08	A–	Stable
4 May 07	A–	Stable
27 Nov 06	A–	Stable
5 Sep 06	A–	Stable

Snapshot Profile: Major Issuer-Specific Rating Factors and Trends

Rating factor	Status	Trend
Operations	Average	Neutral
Market position	Weak	Neutral
Finances	Weak	Neutral
Governance	Strong	Neutral
Geography	Average	Neutral

Source: Fitch

Related Criteria

Corporate Rating Methodology (August 2013)

Immediate Peer Group – Comparative Analysis

Sector Characteristics

Operating Risks

Pure power generators are higher risk and more volatile than integrated utilities, due to their exposure to changes in fuel and electricity prices and in electricity demand (merchant and volume risk). Some business and financial risks may be mitigated through hedging strategies, long-term power purchase agreements, or by capacity and/or interconnection limitations.

Financial Risks

The financials of integrated utilities with a high share of regulated or quasi-regulated business often benefit from solid and stable cash flow generation, while those of pure merchant generators on an open market with excess capacity tend to be more volatile and risky. Negative free cash flow will remain common across the sector due to large capex plans with limited short-term flexibility. Generally, utilities have good access to capital-market funding.

Peer Group Analysis

	Vattenfall A–/Stable	Fortum A–/Negative	Statkraft BBB+/Stable	DONG BBB+/Negative	TVO BBB/Stable
EBITDA (EURm)	6,356	2,403	1,483	930	72
EBITDA margin (%)	33.3	39	34.3	10.5	20.5
Vertical integration	Medium	High	Low	Medium	None
Generation mix (%)	Hydro: 21 Nuclear: 25 Coal: 44 Renewables: 2 CCGT: 8	Hydro: 40 Nuclear: 47 Coal: 5 Renewables: 1 CCGT: 3 Other: 4	Hydro: 89 Nuclear: 0 Coal: 0 Renewables: 2 CCGT: 9 Other: 0	Hydro: 4 Nuclear: 0 Coal: 28 Renewables: 20 CCGT: 33 Other: 15	Nuclear: 95 Coal: 5

Source: Fitch, companies

Key Credit Characteristics

Large utilities with solid business profiles and good financial profiles generally command strong investment-grade ratings. Ratings depend both on business factors, including market presence, degree of vertical integration, generation mix and earnings diversification, and on financial factors such as financial policy, profit margins, capex plans and approach to M&A activity.

Overview of Companies

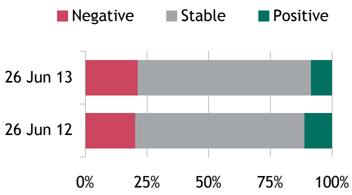
Vattenfall AB (A−/Stable) – the Stable Outlook reflects Fitch's view that despite a substantial capex programme, the negative cost effects of the full auction of carbon dioxide emissions in 2013, and a challenging operating market environment, Vattenfall's credit profile should remain stable, with for example, FFO net leverage remaining at around 3.6x in 2013-16.

Fortum Corporation (A−/Negative) – the Negative Outlook reflects downward pressure on Fortum's ratings from low electricity prices in the Nordic region over the medium term, driven by weak supply and demand dynamics, a period of high capital expenditure with corresponding earnings only feeding through with a time lag and a high dividend payout policy.

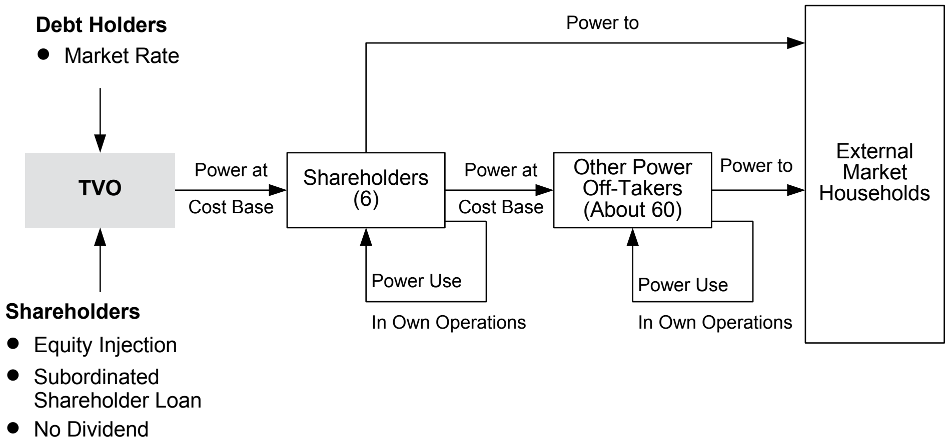
Statkraft AS (BBB+/Stable) – the rating reflects a one-notch uplift for Norwegian state support, the group's strong business profile in the Nordic region, as well as increasing diversification through heavy investments into hydropower in emerging markets and wind power mostly in Europe. Fitch forecasts FFO net adjusted leverage of above 4x in the medium term.

Dong Energy A/S (BBB+/Negative) – The Negative Outlook is due to stretched forecast leverage ratios for the 'BBB+' rating level in 2013-14. The company faces a challenging operating environment, as well as high capex. A potential Outlook stabilisation depends on the progress of the company's 2013-14 financial action plan.

Distribution of Sector Outlooks
Directional Outlooks and Rating Watches



TVO's Operating Principle " Mankala " (At Cost Electricity for Shareholders)



Source: TVO

Debt Maturities and Liquidity at 31 Mar 13

Debt maturities	(EURm)
2013	215
2014	47
2015	305
2016	856
After 2017	1,621
Cash and equivalents	122
Undrawn committed facilities	
EUR 1.5bn RCF due 2018	1,500

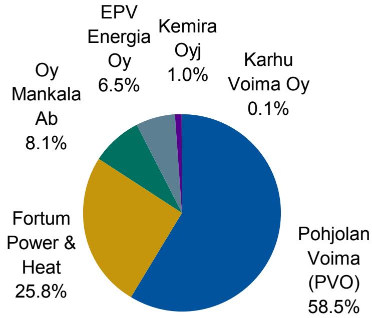
Source: Fitch

TVO Power Plants

Power plant (fuel)	Capacity (MW)	Commercial operation
Olkiluoto 1 (nuclear)	880	1979
Olkiluoto 2 (nuclear)	880	1982
Olkiluoto 3 (nuclear)	1,600	2017
Meri Pori (coal)	257[a]	1994

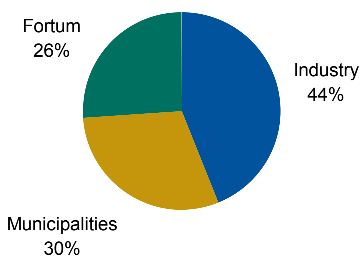
[a] 257MW stake in 565MW coal condensing plant, representing TVO's 45% stake (the other 55% is owned by Fortum Power & Heat Oy, which operates the plant)
Source: TVO, Fitch

TVO Shareholders



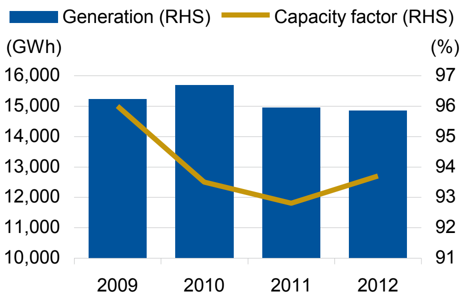
Source: TVO

Underlying Shareholders by Sector



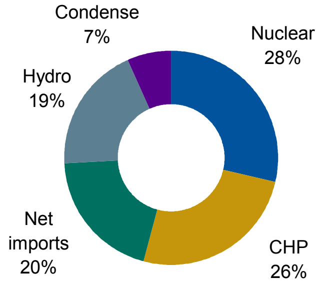
Source: TVO

Electricity Generation (GWh) and Capacity (%)



Source: TVO

Finnish Electricity Supply
2012



Source: TVO

Teollisuuden Voima Oyj(TVO)
FINANCIAL SUMMARY

	31 Dec 2012 EURm Year End	31 Dec 2011 EURm Year End	31 Dec 2010 EURm Year End	31 Dec 2009 EURm Year End	31 Dec 2008 EURm Year End
Profitability					
Revenue	352	352	363	305	257
Revenue Growth (%)	(0.06)	(2.81)	18.73	18.69	10.76
Operating EBIT	16	44	158	4	(29)
Operating EBITDA	72	102	215	58	23
Operating EBITDA Margin (%)	20.44	28.89	59.29	18.96	8.86
FFO Return on Adjusted Capital (%)	1.56	1.77	1.71	2.55	1.19
Free Cash Flow Margin (%)	(69.14)	(83.91)	(70.11)	(257.79)	(221.84)
Coverages (x)					
FFO Gross Interest Coverage	0.37	0.54	0.39	0.53	0.15
Operating EBITDA/Gross Interest Expense	0.42	0.71	1.47	0.46	0.20
FFO Fixed Charge Coverage (inc. Rents)	0.37	0.54	0.39	0.53	0.15
FCF Debt-Service Coverage	(0.15)	(0.20)	(0.31)	(1.01)	(0.85)
Cash Flow from Operations/Capital Expenditures	(0.48)	(0.45)	(0.33)	(0.11)	(0.11)
Debt Leverage of Cash Flow (x)					
Total Debt with Equity Credit/Operating EBITDA	56.22	38.00	16.76	58.60	118.47
Total Debt Less Unrestricted Cash/Operating EBITDA	54.34	36.97	16.30	56.62	109.58
Debt Leverage Including Rentals (x)					
Annual hire lease rent costs for long-term assets (reported and/or estimate)	0	0	0	0	0
Gross Lease Adjusted Debt/Operating EBITDAR	56.02	37.92	16.74	58.43	117.51
Gross Lease Adjusted Debt /FFO+Int+Rentals	60.01	50.34	59.39	47.81	186.39
FCF/Lease Adjusted Debt (%)	(6.01)	(7.64)	(7.05)	(23.19)	(21.12)
Debt Leverage Including Leases and Pension Adjustment (x)					
Pension and Lease Adjusted Debt /EBITDAR + Pension Cost	56.02	37.92	16.74	58.43	117.51
Liquidity					
(Free Cash Flow+Available Cash+Committed Facils)/(ST Debt + Interest) (%)	403.43	191.07	523.69	178.68	220.32
Balance Sheet Summary					
Cash and Equivalents (Unrestricted)	136	106	98	115	203
Restricted Cash and Equivalents	n.a.	n.a.	n.a.	n.a.	n.a.
Short-Term Debt	207	617	170	517	460
Long-Term Senior Debt	3,841	3,072	3,253	2,697	2,061
Subordinated debt	n.a.	179	179	179	179
Equity Credit	n.a.	n.a.	n.a.	n.a.	n.a.
Total Debt with Equity Credit	4,048	3,869	3,602	3,393	2,701
Off-Balance-Sheet Debt	2	2	2	2	2
Lease-Adjusted Debt	4,050	3,871	3,605	3,395	2,703
Fitch- identified Pension Deficit	n.a.	n.a.	n.a.	n.a.	n.a.
Pension Adjusted Debt	4,050	3,871	3,605	3,395	2,703
Cash Flow Summary					
Operating EBITDA	72	102	215	58	23
Gross Cash Interest Expense	(184)	(143)	(154)	(133)	(98)
Cash Tax	0	0	0	0	0
Associate Dividends	1	1	1	1	1
Other Items before FFO (incl. interest receivable)	10	(15)	(137)	50	18
Funds from Operations	**(101)**	**(56)**	**(75)**	**(25)**	**(56)**
Change in Working Capital	23	(36)	13	(51)	(0)
Cash Flow from Operations	**(78)**	**(92)**	**(62)**	**(75)**	**(56)**
Total Non-Operating/Non-Recurring Cash Flow	n.a.	0	n.a.	n.a.	n.a.
Capital Expenditures	(161)	(204)	(192)	(712)	(515)
Dividends Paid	(4)	n.a.	n.a.	n.a.	n.a.
Free Cash Flow	**(244)**	**(296)**	**(254)**	**(787)**	**(571)**
Net (Acquisitions)/Divestitures	0	(0)	(0)	(0)	(1)
Net Equity Proceeds/(Buyback)	n.a.	65	79	100	96
Other Cash Flow Items	94	(28)	(51)	(92)	(736)
Total Change in Net Debt	(149)	(259)	(226)	(780)	(1,212)
Working Capital					
Accounts Receivable Days	38	54	51	61	61
Inventory Days	1,292	617	2,286	507	472
Accounts Payable Days	55	33	183	47	34

Figure 1

Reconciliation of Key Financial Metrics for TVO

(EURm)	31 Dec 12	31 Dec 11
Total debt[a]	4,048	3,869
- Equity credit	0	0
= Total debt with equity credit	4,048	3,869
+ Total off-balance sheet debt (8 x long-term leases)	2	2
= Total lease-adjusted debt (a)	**4,050**	**3,871**
- Cash and equivalents (unrestricted)	136	106
= Net lease-adjusted debt (b)	3,915	3,766
Cash flows from operating activities (as reported)	69	25
+ Reversal finance charge	21	15
- Dividend received (recurring)	1	1
+ Reversal taxation paid	0	0
= Net cash from operating activities (adjusted by Fitch)	**89**	**40**
- Net finance charges[b] (c)	168	132
- Taxation paid	0	0
+ Dividend received (recurring)	1	1
= Cash flow from operations	**-78**	**-92**
- Change in working capital	23	-36
= Funds from operations (FFO) (d)	**-101**	**-56**
Gross interest paid[b] (e)	184	143
Long-term (LT) leases (f)	0.3	0.3
FFO adjusted net leverage (x)		
Net lease-adjusted debt/(FFO + net finance charge + LT leases) (b/(d+c+f))	58.0	49.0
FFO fixed charge cover (x)		
(FFO + net finance charge + LT leases)/(gross interest paid + LT leases) ((d+c+f)/(e+f))	0.4	0.5
FFO gross interest coverage (x)		
(FFO + net finance charge)/gross interest ((d+c)/e))	0.4	0.5

[a] Including loan from the Finnish State Nuclear Waste Management Fund
[b] Including capitalised interest
Source: Fitch based on company reports

The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.