Teollisuuden Voima Oyj (TVO)

Update

Ratings

Foreign Currency	
Long-Term IDR	BBB+
Short-Term IDR	F2
Senior unsecured	BBB+

Outlooks

Foreign-Currency Long-Term IDR	Stable

Key Rating Drivers

Rating Downgrade: The Long-Term IDR and senior unsecured ratings were downgraded in June 2012 due to the impact on Teollisuuden Voima Oyj (TVO)'s credit profile of the continued delay in commissioning the third 1,600 megawatt (MW) nuclear plant Olkiluoto 3 (OL3). The delay to August 2014 is of 64 months. Annual production costs will increase as a result, and while still competitive against forward Nord Pool prices, the gap between the two has narrowed and indicates some erosion of cost advantage.

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

No Merchant, Volume Risk: TVO has no wholesale electricity price or volume exposure, as its shareholders are the at-cost off-takers of the electricity produced. Shareholders are liable to pay fixed costs (around 80% of total costs), including debt instalments one month in advance and variable costs in proportion to the off-take. Shareholders have an incentive to keep costs low. As TVO does not seek to maximise profit, Fitch considers traditional leverage or coverage ratios, which are weak, as less relevant to the ratings.

Operational Performance and Safety: TVO's nuclear power plants are some of the most efficient in the world, with an outstanding safety record. Fitch Ratings expects the financial impact on TVO of any additional safety requirements by the Finnish nuclear watchdog, post-Fukushima, to be limited.

Fully Funded Nuclear Liabilities: under the Finnish Nuclear Act, nuclear operators' (non-discounted) nuclear liabilities, assessed annually, must be funded through contributions to a centrally administered fund.

Asset Concentration Risk: The ratings are constrained by asset concentration risk, although TVO's excellent operational and safety record mitigates this.

What Could Trigger a Rating Action

Downward Pressure on Ratings: A downgrade would probably follow further OL3 delays, impacting TVO's production costs, litigation costs materialising with the construction contract supplier Areva, and any adverse regulatory or fiscal changes. In addition, a decline in operating performance and significantly reduced liquidity reserves could also lead to negative action.

Successful Litigation Resolution: A favourable outcome for TVO regarding litigation with Areva, with the award of a significant compensation for the delay, thus decreasing TVO's production costs, would be ratings positive. A resolution is not expected until after the commissioning of OL3.

Liquidity and Debt Structure

Strong Liquidity: TVO maintains a strong liquidity position, with cash of at least EUR90m. Q112 cash and cash equivalents were EUR303m (end-2011: EUR105m), due to a EUR500m seven-year bond issue in 2012, against short-term debt of EUR358m (end-2011: EUR617m). An undrawn revolving credit facility of EUR1.5bn (maturing in 2017) largely covers capex and maturing debt requirements in 2012-13.

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Peer Group

Issuer	Country
A-	
Fortum Corporation	Finland
BBB+	
Statkraft As	Norway
Teollisuuden Voima Oyj(TVO)	Finland
BBB	
Slovenske elektrarne, a.s.	Slovakia

Issuer Rating History

Date	LT IDR (FC)	Outlook/ Watch
01 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[a]	Trend
Operations	Strong	Neutral
Market position	Weak	Neutral
Finances	Weak	Neutral
Governance	Average	Neutral
Geography	Average	Neutral

[a] Relative to non-integrated peers
Source: Fitch

Related Criteria

Corporate Rating Methodology (August 2011)

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 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

	Fortum A-/Stable	Statkraft BBB+/Stable	TVO BBB+/Stable	Slovenske elektrane BBB/Stable
Headroom within current rating level	Limited	Medium	Medium	Medium
Vertical integration	Full (generation to supply)	Vertically integrated but c.85% EBITDA from generation	None, generation only	Low
Generation mix (%)	47% Nuclear 40% Hydro 5% Coal 1% Renewables 7% Other	0% Nuclear 89% Hydro 0% Coal 2% Renewables 7% Gas	95% Nuclear 0% Hydro 5%Coal 0% Renewables	32% Nuclear 43% Hydro 25%Coal
Merchant generation risk	Medium	Medium/high	None	Medium/high

Source: Fitch, companies

Key Credit Characteristics

Utilities with solid business profiles tend to have strong investment-grade ratings, even if they have relatively high leverage, provided there is a good degree of earnings stability. Ratings depend on both business factors (eg market presence, degree of vertical integration, generation mix and earnings diversification) and financial factors (eg financial policy, leverage, profit margins, capex plans and approach to M&A activity).

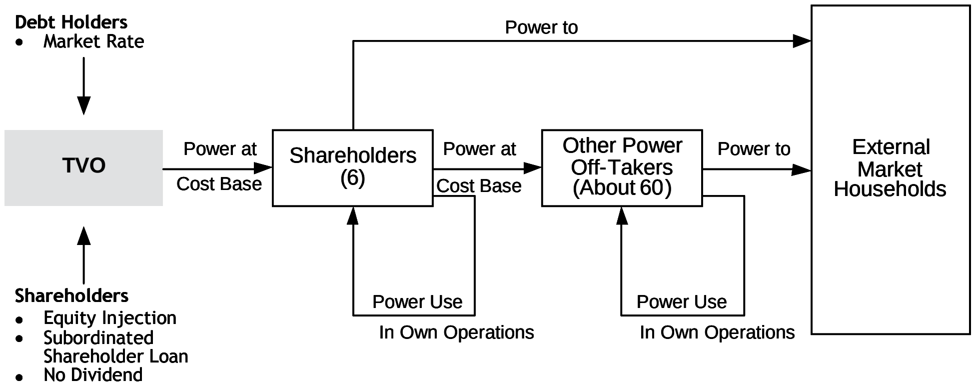
Overview of Companies

Fortum Corporation ('A−'/Stable) – the ratings reflect Fortum's solid business profile due to its market-leading Nordic position, its hedged, low-cost hydro and nuclear generation, and quasi-monopolistic and regulated distribution businesses. Fortum's business risk has increased through its expansion outside the Nordic region, into Russia.

Statkraft A/S ('BBB+'/Stable) – the ratings reflect Statkraft's solid business profile, as the leading generator of green electricity in Europe. The ratings are constrained by Statkraft's high dividend payout policy (85%) to its shareholder, the Norwegian state, as well as a substantial NOK70bn-80bn five-year capex programme. The ratings incorporate a one-notch uplift for state support, following the NOK14bn equity injection from the state in 2010.

Slovenske elektrarne, a.s. (SE, 'BBB'/Stable) – the ratings reflect SE's strong asset base, profitability and cash flows, and good progress on the construction of units 3 and 4 (to be commissioned in 2013) at the Mochovce nuclear power plant. Low production costs, a strong operational track record and Slovakia's electricity shortage place SE comfortably at the current rating.

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



Source: TVO

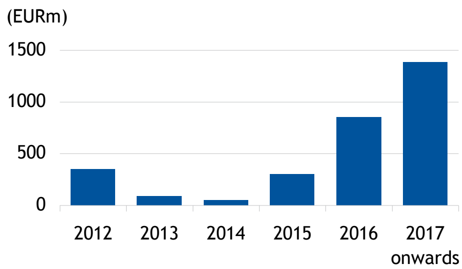
TVO Power Plants

Power plant	Plant type	Capacity (MW)	Commercial operation	Upgrade year
Olkiluoto 1 (OL1)	Nuclear, BWR Westinghouse Atom	880	1979	1984, 1998, 2006, 2010
Olkiluoto 2 (OL2)	Nuclear, BWR Westinghouse Atom	880	1982	1984, 1998, 2005, 2011
Olkiluoto 3 (OL3)	Nuclear, PWR Areva-Siemens	1,600	2014	n.a.
Meri Pori	Coal condensing	257[a]	1994	n.a.

BWR – Boling Water Reactor, PWR – Pressurised Water Reactor
[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

Debt Maturity Profile

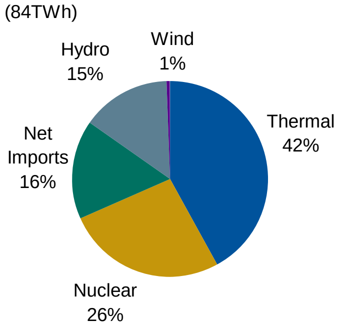
as of 31/03/2012



Source: TVO

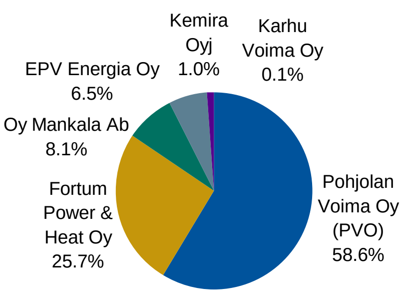
Supply of Electricity Finland

2011 (84TWh)



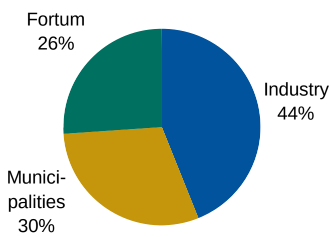
Source: TVO, Finnish Energy Industries

TVO Shareholders



Source: TVO

Underlying Shareholders by Sector



Source: TVO

	31 Dec 2011 EURm Original	31 Dec 2010 EURm Original	31 Dec 2009 EURm Original	31 Dec 2008 EURm Original
Profitability				
Revenue	352	363	305	257
Revenue Growth (%)	(2.8)	18.7	18.7	10.8
Operating EBIT	44	158	4	(29)
Operating EBITDA	102	215	58	23
Operating EBITDA Margin (%)	28.9	59.3	19.0	8.9
FFO Return on Adjusted Capital (%)	1.8	1.7	2.5	1.2
Free Cash Flow Margin (%)	(83.7)	(70.1)	(257.8)	(221.8)
Coverages (x)				
FFO Gross Interest Coverage	3.4	2.7	2.5	1.3
Operating EBITDA/Gross Interest Expense	9.0	19.0	3.2	1.3
FFO Fixed Charge Coverage (inc. Rents)	3.4	2.7	2.5	1.3
FCF Debt-Service Coverage	(0.4)	(1.1)	(1.3)	(1.1)
Cash Flow from Operations/Capital Expenditures	0.1	0.2	0.0	0.0
Debt Leverage of Cash Flow (x)				
Total Debt with Equity Credit/Operating EBITDA	38.0	16.8	58.6	118.5
Total Debt Less Unrestricted Cash/Operating EBITDA	37.0	16.3	56.6	109.6
Debt Leverage Including Rentals (x)				
Annual hire lease rent costs for long-term assets (reported and/or estimate)	0	0	0	0
Gross Lease Adjusted Debt/Operating EBITDAR	38.0	16.8	58.6	118.5
Gross Lease Adjusted Debt /FFO+Int+Rentals	44.0	45.8	31.3	64.5
FCF/Lease Adjusted Debt (%)	(7.6)	(7.1)	(23.2)	(21.1)
Debt Leverage Including Leases and Pension Adjustment (x)				
Pension and Lease Adjusted Debt /EBITDAR + Pension Cost	38.0	16.8	58.6	118.5
Liquidity				
(Free Cash Flow+Available Cash+Committed Facils)/(ST Debt + Interest) (%)	207.8	789.2	191.2	236.0
Balance Sheet Summary				
Cash and Equivalents (Unrestricted)	106	98	115	203
Restricted Cash and Equivalents	0	0	0	0
Short-Term Debt	617	170	517	460
Long-Term Senior Debt	3,072	3,253	2,697	2,061
of which subordinated debt	179	179	179	179
Equity Credit	0	0	0	0
Total Debt with Equity Credit	3,869	3,602	3,393	2,701
Off-Balance-Sheet Debt	0	0	0	0
Lease-Adjusted Debt	3,869	3,602	3,393	2,701
Fitch- identified Pension Deficit	0	0	0	0
Pension Adjusted Debt	3,869	3,602	3,393	2,701
Cash Flow Summary				
Operating EBITDA	102	215	58	23
Gross Cash Interest Expense	(26)	(29)	(44)	(33)
Cash Tax	0	0	0	0
Associate Dividends	1	1	1	1
Other Items before FFO (incl. interest receivable)	(15)	(137)	50	18
Funds from Operations	**62**	**50**	**65**	**9**
Change in Working Capital	(36)	13	(51)	(0)
Cash Flow from Operations	**26**	**63**	**14**	**8**
Total Non-Operating/Non-Recurring Cash Flow	0	0	0	0
Capital Expenditures	(321)	(317)	(801)	(579)
Dividends Paid	0	0	0	0
Free Cash Flow	**(295)**	**(254)**	**(787)**	**(571)**
Net (Acquisitions)/Divestitures	(0)	(0)	(0)	(1)
Net Equity Proceeds/(Buyback)	65	79	100	96
Other Cash Flow Items	(29)	(51)	(92)	(736)
Total Change in Net Debt	(259)	(226)	(780)	(1,212)

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