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Summary:
EVN AG

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Credit Rating:	A-/Negative/--

Rationale

The rating on Austrian energy and environmental services company EVN AG reflects Standard & Poor's Ratings Services' view of its position as the main provider of electricity and energy-related services in Lower Austria and its large share of stable income and cash flow from regulated and lower-risk domestic electricity and gas network activities. In addition, we view the 51% ownership by the State of Lower Austria (AA+/Stable/A-1+) as a further support for the rating.

We consider the rating on EVN to be constrained by the company's significant and increasing exposure to higher risk energy markets in Southeast Europe, where its competitive position and profitability are significantly weaker than in its domestic market. Furthermore, EVN has increased its debt following acquisitions and capital expenditure that have been largely debt financed in recent years. In our opinion, EVN's currently modest but expanding environmental project business in Russia and Central and Eastern Europe have a higher business risk than its core domestic activities.

Our rating on EVN further reflects our methodology for rating government-related entities (GREs). In our opinion, there is a "moderate" likelihood that the State of Lower Austria would provide timely and sufficient extraordinary support in the event of financial distress. We assess EVN's stand-alone credit profile at 'bbb+'.

Key business and profitability developments

In the fiscal year ended Sept. 30, 2010, EVN's revenues increased only moderately, by about 1% to €2,752 million, compared with the level in the previous fiscal year. This was primarily caused by higher volumes of energy supplied in Austria and Southeast Europe--as a result of an economic recovery and cold weather--the impact of which, however, was offset by decreased energy prices. We note that revenues related to electricity and gas networks, as well as environmental services, increased. Revenues in power generation notably decreased.

EVN's profitability and operating result improved across most of its business segments during the fiscal year ended Sept. 30, 2010, with only the generation segment posting a lower EBITDA contribution than in the corresponding period a year earlier. We note that the company's reported EBITDA increased by 12% to €417 million, and its EBITDA margin increased to about 15%, compared with about 14% in the previous fiscal year.

Key cash flow and capital-structure developments

EVN generated positive free operating cash flow (FOCF) in fiscal 2010, despite investments mainly related to electricity and gas networks in Lower Austria, generation operations, Southeast Europe, and the environmental services segment. Cash flow from operations (CFO) for the fiscal year ended Sept. 30, 2010, totaled €499 million, an increase of 49% compared with the amount in the previous year, and capital expenditure reached €390 million, a year-on-year decrease of 5%.

As of Sept. 30, 2010, EVN reported €1.9 billion of long- and short-term financial debt compared with €1.7 billion at the end of previous fiscal period. Reported net debt increased less than the increase in reported gross financial debt because of a simultaneous increase in cash and cash funds held by the company. In November 2010, EVN completed a capital increase of €179 million, which was placed among existing shareholders and new private investors. Also in November, EVN participated in a capital increase of Verbund AG (A-/Stable/--) via a consortium with Austrian Wiener Stadtwerke Holding AG (not rated). According to the company, the two partners together hold more than a 25% share of Verbund AG.

We understand that EVN plans to make further substantial investments in its domestic and international operations, and we expect the company not to reduce its dividend. Consequently, we also expect negative to neutral discretionary cash flow to restrict meaningful debt reduction over the next few years.

Liquidity

We consider EVN's overall liquidity to be "adequate". As of Sept. 30, 2010, the company held a total of €124 million in cash and cash equivalents, as well as a further €211 million in cash funds. According to management, the company also had access to an undrawn committed syndicated credit facility totaling €600 million, which matures in 2013.

We expect EVN's discretionary cash flow to remain negative to neutral over the next two years. However, we think its scheduled debt amortizations of about €430 million until third-quarter 2012 are likely to be either refinanced or covered by available cash and committed credit lines.

Outlook

The negative outlook reflects our concerns regarding EVN's continuously high investments and the low profitability of its international operations, which could continue to restrict the company's financial profile over the next few years.

We could consider lowering the rating if we believe that EVN is unable to comfortably sustain a ratio of funds from operations (FFO) to debt of more than 20%. Ratings downside could also stem from adverse changes in the company's perceived business risk profile, possibly resulting from a higher proportion of income generated in countries that we regard as higher risk, as well as from riskier business activities, a more aggressive financial policy, or higher financial leverage.

Conversely, we could revise the outlook to stable if we believe that EVN can comfortably maintain an FFO-to-debt ratio of more than 20%, assuming that we do not perceive a weakening of EVN's business risk profile.

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