



Moody's Investors Service

## Rating Action: **Moody's downgrades ratings of RWE to A2 and Essent to A3; outlook negative**

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Global Credit Research - 04 Nov 2009

### **Approximately EUR18 billion of debt securities affected**

London, 04 November 2009 -- Moody's Investors Service downgraded to A2 from A1 the long-term senior unsecured debt ratings of RWE AG (RWE or 'the Group') and the backed senior unsecured debt ratings of RWE Finance BV. The Prime-1 ratings of both issuers were confirmed. The senior unsecured debt and issuer ratings of Essent NV (Essent) were downgraded to A3/Prime-2 from A2/Prime-1. The outlook on all ratings is negative. These rating actions conclude the reviews initiated in January 2009.

"The rating actions follow the completion by RWE of its acquisition of 100% of Essent NV in a transaction valued at approximately EUR7.3 billion. While acknowledging the positive impact which the combination with Essent has on certain aspects of RWE's business risk profile, these are offset, in Moody's view, by the weaker financial flexibility implied by the enlarged Group's debt burden. The negative outlook reflects the risk in Moody's view that in the current challenging operating environment and given its substantial capital investment programme the Group's earnings might not grow sufficiently to compensate for higher debt levels and that credit metrics therefore remain weaker than appropriate for the A2 rating category," explains Niel Bisset, a Senior Vice President in Moody's Infrastructure Finance Group.

RWE's A2 rating factors in that the acquisition of Essent's generation and supply business is consistent with the Group's 'More Growth, Less CO2' strategy to diversify geographically and into less carbon intensive assets. The rating takes account that the acquisition strengthens RWE's position in north-western Europe and that it will rank as one of the leaders in power generation and supply in the Netherlands, and will in total have 2.4GW of installed renewables capacity. It also assumes that integration risks should be mitigated by RWE's experience of the Dutch market. More cautiously Moody's business risk assessment factors in that within the combined group the contribution to EBITDA from lower risk regulated activities is set to reduce from more than 30% to the mid-20s percent as a result of the increase in unregulated assets.

Moody's says that the rating downgrade reflects primarily the increase in the Group's borrowings as a result both of the debt used to fund the acquisition and approximately EUR600 million of Essent's assumed debt. Taken together with the impact of RWE's sizeable capital investment programme and likely negative free cash flow generation net debt is expected to have increased substantially in 2009 from the approximately EUR21 billion reported at end-2008, even if the effect has been mitigated by the deconsolidation of American Water.

As a result, in Moody's view, and factoring also a partial contribution only of Essent in 2009, the outlook is for RWE's 2009 credit metrics to decline sharply from 2008 when RWE reported retained cashflow (RCF)/net debt of roughly 26% and funds from operations (FFO)/net debt of more than 35%. RWE's A2 rating incorporates an assumption of stronger cash flow generation in 2010 from the Group's existing businesses principally due to forward power sales and increased nuclear output, which together with a full year's contribution from Essent, and a normalised dividend pay-out should enable credit metrics to recover from 2010 to levels consistent with that rating level, including sustainable RCF/net debt at least in the upper-teens, and FFO/debt in the low 20s per cent. The negative outlook reflects the risk that in the current uncertain economic environment the recovery in credit metrics might take longer than anticipated. In the event that that were to happen, whether as a result of weaker than expected cash flow generation or debt funded investment then negative pressure would develop on the A2 rating, Moody's adds.

Essent's A3 ratings factor in the company's stand-alone credit strength, based upon its generation and supply assets and prospective capitalisation, combined with some uplift for its inclusion as part of the A2 rated RWE Group. Moody's adds that it considers Essent's own business risk profile to have weakened following the restructuring prior to its acquisition by RWE given its now exclusive focus on unregulated activities, and assumes that it will be capitalised and funded as part of the RWE Group. The negative outlook reflects RWE's own outlook.

The following ratings were lowered:

- RWE AG: the senior unsecured debt rating to A2, from A1
- RWE Finance BV: the guaranteed senior unsecured debt rating to A2, from A1
- Essent NV: the senior unsecured debt rating to A3/Prime-2, from A2/Prime-1
- Essent Nederland BV senior unsecured debt rating to A3/Prime-2, from A2/Prime-1

The following ratings were confirmed:

- RWE AG: the Prime-1 senior unsecured debt ratings
- RWE Finance BV: the guaranteed Prime-1 senior unsecured debt rating

The previous rating actions on Essent and RWE were implemented on 14 January 2009 and 15 January 2009 respectively, when Moody's placed the ratings on review for downgrade.

The principal methodologies used in rating these entities was Moody's rating methodology for Unregulated Utilities and Power Companies published in August 2009 and available on [www.moodys.com](http://www.moodys.com) in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

Headquartered in Essen, Germany, RWE AG is one of the largest listed European utilities with core activities in electricity, gas, oil and gas upstream. In the six months ended 30 June 2009, it reported group turnover of EUR24.4 billion and EBITDA of more than EUR5 billion.

Essent, based in Arnhem, in the Netherlands, is the country's largest energy company and delivers electricity, gas and heating. Essent is the business unit of RWE in the Netherlands and Belgium. As at H1 2009, it had revenues of EUR4 billion, FYE 2008 revenues were EUR7.5 billion.

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