MOODY'S ANALYTICS

AUGUST 2011 DEFAULT CASE STUDY

Public Firm Default Report: Horizon Lines Inc (HRZ)

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Default Event

On August 15, 2011, **Horizon Lines Inc**, a container ship operator serving the continental US, missed the interest payment on its $330 million of convertible notes.

Company Profile

Horizon Lines rides the waves to connect the mainland US with its far-flung states and territories. The container shipping company transports cargo such as building materials, consumer goods, and food to and from the continental US, Alaska, Hawaii, Guam, and Puerto Rico. It maintains a fleet of approximately 20 ships and 18,500 containers. Besides marine transportation, the company offers logistics software and services through Horizon Logistics, LLC. The majority of Horizon Lines' revenue (85%) comes from operations subject to the Jones Act, which restricts marine shipping between US ports to US-owned companies operating US-built vessels.

EDF Credit Measure and EDF Drivers

EDF value as of August 15, 2011: 35.00%

Traditional ratings, such as those used by major rating agencies, are currently more commonplace than default probabilities. Therefore, to help facilitate users' understanding, we translate the EDF credit measure into an equivalent Credit Category. HRZ's Credit Category (not an agency rating) at default was C.

Figure 1. One-year Horizon Lines Inc's EDF Values.

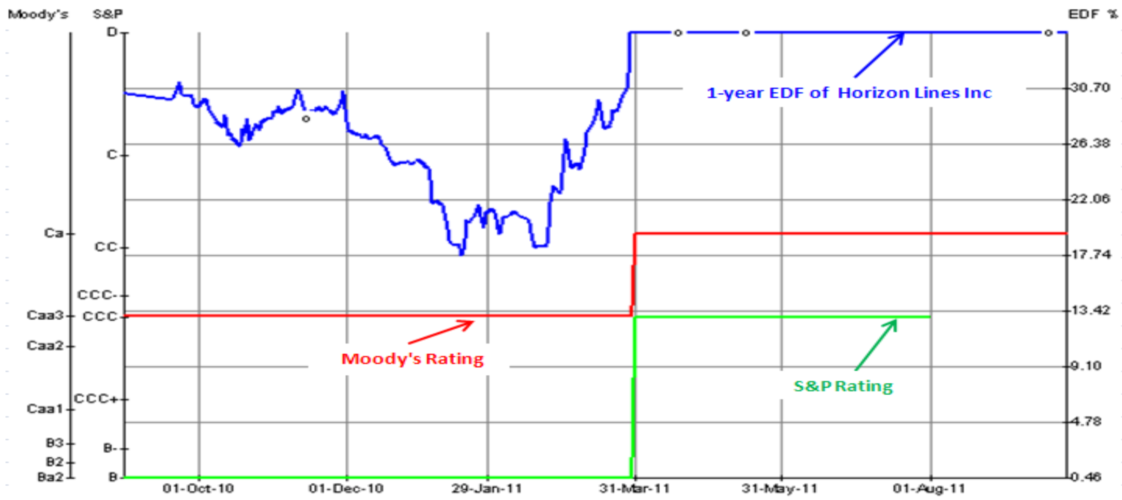

Figure 1 shows that Horizon Lines Inc's EDF credit measure had been increasing since January 2011 and reached 35% in March 2011, five months prior to default.

Figure 2. Drivers of Horizon Lines Inc's EDF Values

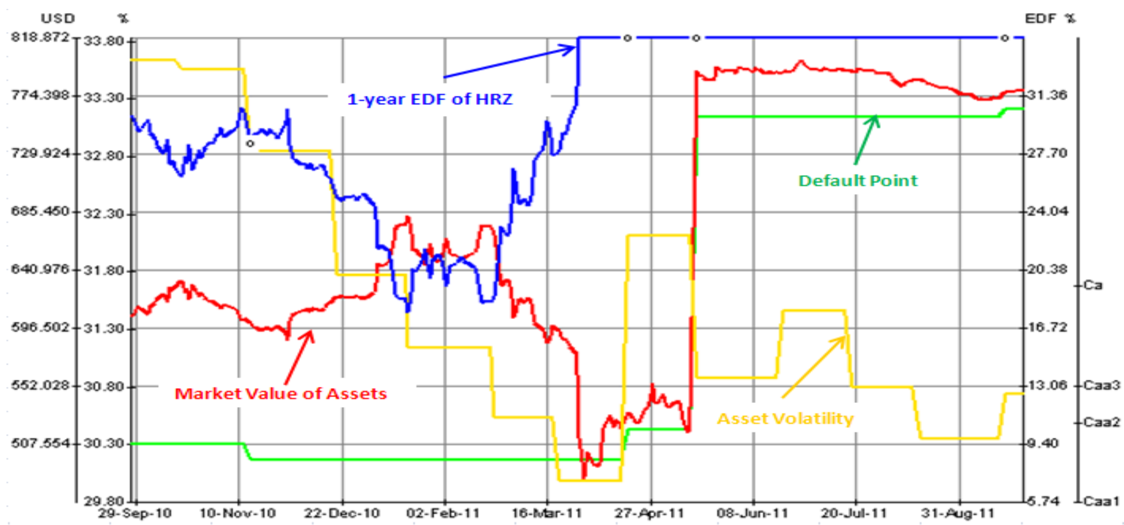

Figure 2 shows the time series of EDF values and EDF drivers, which includes market value of assets, asset volatility, default point, and market leverage. **Table 1** summarizes the EDF driver definitions.

In September 2010, the company's default point was $507 million. Three years of continuous decline in container volumes and a tightening market forced the company refinance its entire capital structure and carry more debt. As a result, the company's default point soared to $760 million in May 2011, close to its market value of assets, $790 million. The company's asset volatility has remained high, near 32%, since September 2010. The highly leveraged capital structure, combined with poor asset quality, led the company to default.

Table 1. Drivers for EDF Values

EDF DRIVERS	DEFINITION
Market Value of Assets	The market's view of the enterprise value of the firm as determined by the firm's equity value, equity volatility, and liability structure
Default Point	The liabilities that matter in case of default. If the market value of assets falls below this value, it is assumed that the firm will be unable to sell assets or raise additional capital to pay its debt. A firm's default point is a value close to its short-term liabilities plus half of its long-term liabilities
Market Leverage	Ratio indicating how much of the market value of assets is financed by debt. It is calculated as the default point/market value of assets
Asset Volatility	Standard deviation of the annual change in the market value of the assets

The two main EDF value drivers are asset volatility and market leverage. **Figure 3** depicts a meter showing the level of risk for each of the two measures. The levels are relative values, computed on the United States & Canada Large Corporates Group.

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Figure 3. United States & Canada Large Corporates Group

Asset Volatility. EDF credit measures for the United States & Canada Large Corporates Group issuers such as Horizon Lines Inc reflect an average of asset volatility levels during the past three years. As of the default date, Horizon Lines Inc's asset volatility was 30.35%, within the 75th percentile relative to the entire United States & Canada Large Corporates Group.

Market Leverage. Horizon Lines Inc's market leverage is 96.43%, which falls within the 99th percentile of the entire United States & Canada Large Corporates Group.

Relative Analysis

The relative analysis feature allows users to chart EDF, fundamental data, and bond values for a selected company or group relative to other companies and/or groups. Users may manually select their own list of peer companies or groups for comparison or view a Moody's Analytics' predefined peer list, based on an automated algorithm. To determine peers for each company, Moody's Analytics finds all of the companies that share the company's Bloomberg Subgroup. Users can also customize and save their own peer company and peer group choices for future use.

Figure 4. One- Horizon Lines Inc vs. US Transportation Group

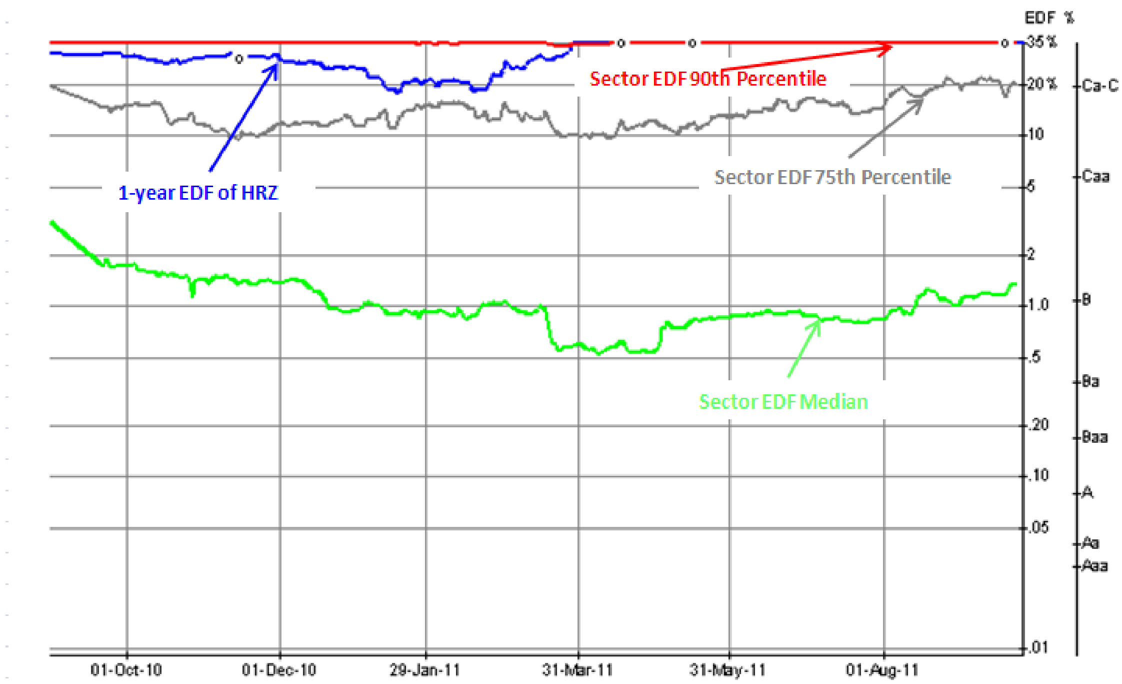

Figure 4 shows Horizon Lines Inc's EDF value surpassed the 90th percentiles of the US Transportation Group in March 2011. The company defaulted in August 2011.

Conclusion

Horizon Lines Inc's EDF credit measure indicated high default risk before default occurred. Firm EDF values remained above the 90th percentile relative to the US Transportation peer group beginning in April 2011. A highly leveraged capital structure, combined with poor asset quality, led the company to default.