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Summary:

S.N.T.G.N. Transgaz S.A. Medias

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Credit Rating: BB+/Positive/--

Rationale

The rating on Romania-based gas transmission and distribution company S.N.T.G.N. Transgaz S.A. Medias is constrained by an aged asset base that will require continuous investment, planned investment in a key international pipeline project, below-average financial risk management practices, weak liquidity, and some remaining transition economy features in the Republic of Romania (foreign currency BBB-/Negative/A-3; local currency BBB/Negative/A-3).

The rating is supported by the company's favorable business profile as the sole licensed natural gas transmission operator in Romania, stable cash flows from regulated gas transmission activities, robust financial profile, indirect government support related to its natural monopoly status, and its strategic importance to the energy sector.

At Dec. 31, 2006, Transgaz had total adjusted debt of Romanian leu (RON) 196 million.

The Romanian government has announced an IPO of 10% of shares in Transgaz to be subscribed by Dec. 7, 2007. Following this, government ownership is expected to decrease to 70%. Further privatization is not envisaged over the medium term. The rating reflects Transgaz's stand-alone credit quality and factors in ongoing government support such as the company's natural monopoly status in Romania and its strategic importance within the energy sector.

Transgaz's participation in the planned Nabucco pipeline project connecting the Caspian Sea region and Middle East to Western Europe is likely to require precompletion guarantees during the construction phase. The rating on Transgaz factors in government counterguarantees supporting the company's future commitments under the financial structure envisaged. But if the government fails to provide or reduce such support, the rating on Transgaz could come under pressure.

Transgaz operates Romania's natural gas transmission system, which consists of 12,200 kilometers of pipeline and related equipment. The major part of the gas transmission assets, however, is technically aged and will require investments of at least RON1 billion through 2011.

About 70% of Transgaz's revenues consist of regulated gas transmission revenues whereas slightly less than 25% of revenues consist of unregulated transit fees. Transgaz operates under a revenue cap regime, introduced in 2004, which is viewed as transparent and supportive.

Transgaz's financial profile is robust; the company's ratio of funds from operations (FFO) to adjusted debt was 174% at the end of 2006, and FFO to interest was 24x. Over the medium term, credit metrics are expected to remain at a level that is strong for the rating.

Liquidity

Transgaz's liquidity position is weak. At June 30, 2007, the company had RON85 million in cash and bank deposits, compared with short–term debt of RON120 million. The company has access to RON75 million in available bank lines, which were fully used at June 30, 2007. Financial risk management practices are regarded as weak in the absence of stated financial policies for managing debt leverage and financial risks, including currency and interest rate exposure.

Outlook

The positive outlook reflects the prospect of an improved liquidity position on the back of the ongoing IPO. It also reflects Transgaz's potential to reach investment grade following a period of successful operational performance as a publicly listed entity, while maintaining credit ratios at strong levels and visibly improving financial risk management practices.

Factors that could lead to an outlook revision include a material increase in investment expenditures and insufficient government support for the Nabucco project.

The rating on Transgaz is not directly linked to the sovereign rating. Nevertheless, the rating could be positively influenced by a positive change in the sovereign rating or outlook. Conversely, a sovereign downgrade could lead to an outlook revision and put pressure on the rating.

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