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Vier Gas Transport GmbH

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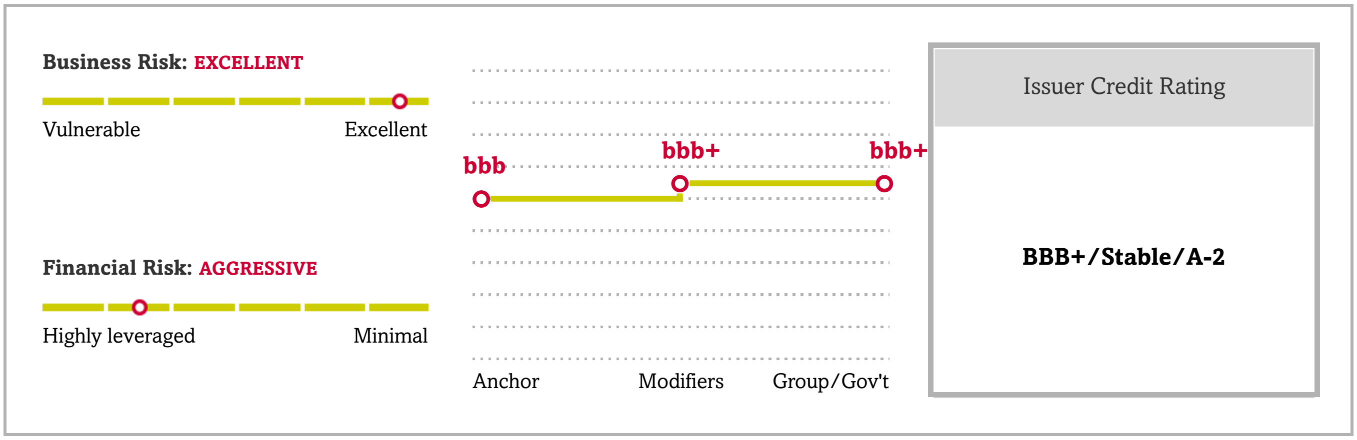
Vier Gas Transport GmbH



Credit Highlights

Overview

Key strengths	Key risks
With EBITDA of about €433 million in 2022, VGT is the largest gas transmission network operator in Germany (out of 16) with a natural monopoly position in its service area.	High capital expenditure (capex) is likely to lead to negative discretionary cash flow.
Operations are focused on low-risk regulated gas transmission operations in Germany, which has a supportive regulatory framework. The fourth regulatory period runs 2023-2027.	Long-term prospects for gas infrastructure are likely to moderate, leaving VGT Group in need of continuing to look for new sources of growth to remain relevant over the medium to long term.
Predictable revenue and EBITDA over time, owing to a regulatory account mechanism that mitigates the effects of volume and commodity risks.	No regulated framework in place for future projects, such as hydrogen and pipeline for carbon capture.
Track record of prudent financial management and flexible financial policy.	

Gas grid operators in Germany will continue to benefit from supportive regulation in the 2023-2027 fourth regulatory period. The regulatory account mechanism mitigates the effects of volume and commodity risks. Regulation allowing for the cost base to be adjusted annually for inflation makes revenue and EBITDA predictable over time. We consider it positive that extraordinary costs, such as fuel gas, are passed through in the regulatory account and we therefore tend to look through the near-term impact of highly volatile prices. Costs are recovered equally over the third, fourth, and fifth years of being incurred. Any financial impact from gas flow or volatile gas prices on the financial profile of Vier Gas Transport GmbH (VGT) is therefore only temporary. Moreover, we understand that the fourth regulatory period has shifted to a capital cost adjustment (CCA) system from 2023. The CCA provides an annual adjustment for growth and replacement capex, while the previous system only recognized growth capex via investment measures, which could bode well for VGT's maturing business. A regulatory framework to remunerate and recover costs of hydrogen infrastructure could also provide further investment stimulus. However, at this stage there is no regulation in place for hydrogen infrastructure. First regulatory principles were enacted in November 2021 ("Wasserstoff Netzentgelt Verordnung"). Nevertheless, it is an opt-in regime and, so far, VGT has not opted to be regulated, owing to the remaining uncertainties related to the risk profile under the future regulation.

We expect VGT's financial performance to be temporarily high, but including the regulatory account effect we expect the credit ratios to sustainably be in line with the rating over 2023-2025. VGT's metrics are influenced by volume effects under the German regulatory framework, which result in artificial volatility in credit metrics and in a difference between the group's reported results and sustainable financial performance, which excludes volume effects. These deviations can be volatile, especially during years with heavy price volatility in gas or changed consumption patterns, as in 2022 and 2023. On June 22, 2023, VGT therefore materially revised its EBITDA guidance to €750-million-€900 million. This revision was largely due to lower operating costs because energy prices declined and is not regulated earning. We therefore expect 2023 reported EBITDA and funds from operations (FFO) to be temporarily very high, resulting in FFO to debt of around 19%-22% for 2023. These effects are extraordinary and not sustainable. If adjusted for regulatory account effects, FFO to debt remains in line with the rating. We expect the deviation to cancel out over time.

Capex is set to increase under the latest business plan for 2023-2027. It should rise to an annual average of €450 million-€550 million from about €315 million in 2021 and €385 million in 2022, with a majority of funds dedicated to growth investments. This represents a healthy increase of over €1.0 billon compared to the previous business plan for the period. We consider it a positive move because the investment in grid expansion of Open Grid Europe GmbH (OGE) is expected to result in an immediate and sustainable increase in revenue for the company. In the longer term, however, it remains to be seen whether VGT can retain this capex level given the gradual phase-out of gas to meet net zero. Since the start of the Russia-Ukraine conflict and imposition of sanctions on Russia, the German government in 2022 undertook various measures to reduce dependency on Russian gas. This included commissioning construction of several LNG terminals, and gas inflow to the German market from the west. This has been positive for VGT overall, as its network is concentrated in the western part of Germany. About €774 million of the estimated €2.0 billion-€2.5 billion capex forecast for 2023-2027 period is expected to go toward further LNG-related investments, including two additional pipeline projects (about €725 million).

Macquarie Asset Management concluded the sale of its indirect holding in Vier Gas Transport to Fluxys in early 2023. On Jan. 27, 2023, Macquarie Asset Management announced an agreement with the Belgian company Fluxys to sell its indirectly held 24.1% stake in Vier Gas Transport GmbH and Open Grid Europe GmbH (OGE). The sale concluded on March 8, 2023. At this stage, we have not seen any signs of changed strategy or financial policy. However, as Fluxys is more of an operating owner and may therefore have other strategic plans than Macquarie, we don't fully exclude that this could lead to a changes over time

VGT has in the past shown a willingness to reduce shareholder remuneration to protect its credit metrics. We see this as an indication of the group's commitment to retaining its credit quality. Following our downgrade of VGT last year (see “Germany-Based Vier Gas Transport Downgraded To 'BBB+' On Weaker Financial Performance,"published July 8, 2022, on RatingsDirect) we continue to expect that management will be able to steer the company's financial profile in such way that adjusted debt to FFO to debt remains in the 9%-11% range on average. Since the downgrade, management has been able to increase investment and thereby regulated earnings and, at least temporarily, has halted the negative trend in credit ratios we foresaw in previous years.

Outlook: Stable

The stable outlook reflects our view that VGT will continue to benefit from stable fully regulated activities under one of the most supportive regulatory frameworks for gas infrastructure in Europe, and that it will be able to sustain FFO to debt between 9% and 11% over the next two years.

Downside scenario

We could downgrade VGT if the company were to post FFO to debt below 9% on average. We see this scenario as unlikely, as the regulatory returns over the 2023-2027 now are set. Downside rating pressure could instead emerge from a change in financial policy and increased dividend payments, which we don't foresee at this stage, as the company in the past honored its financial policy.

Upside scenario

We could upgrade VGT if the group were to post FFO to debt sustainably above 12% on average, and if we at the same time have visibility over the stability of future business prospects, including hydrogen infrastructure. This would likely stem from investment stimulus over the medium term, including adoption of a regulated framework for hydrogen infrastructure that was strong enough to offset the medium- to long-term declining gas prospects.

Our Base-Case Scenario

Assumptions

- RoE I on new assets at 5.07% and on old assets of 3.5% over the 2023-2027 regulatory period. Productivity factor (Xgen factor) of 0.49% and an individual efficiency factor of 100%;
- Annual capital cost allocation adjustment under the fourth regulatory period starting from 2023 to 2027;
- Capex of about €475 million-€575 million over the next two years, slightly declining thereafter as a result of decreasing Network Development Plan investments;
- Dividend distributions of approximately €100 million in 2023 and approximately €110 million in 2024;
- Lower profitability and relative capex intensity, coupled with sustained shareholder remuneration, expected to result in negative discretionary cash flow over 2023-2024.

Key metrics

Vier Gas Transport GmbH--Forecast Summary

Industry sector: Gas

	--Fiscal year ended Dec. 31--					
(Mil. €)	**2019a**	**2020a**	**2021a**	**2022a**	**2023e**	**2024f**
Revenue	1,074	1,151	1,091	1,427	1,500-1,600	1,400-1,500
EBITDA	543	577	521	433	750-900	500-600
Funds from operations (FFO)	382	418	408	364	650-700	350-400
Debt	3,078	3,287	3,283	3,364	3,100-3,300	3,400-3,600
Adjusted ratios						
Debt/EBITDA (x)	5.7	5.7	6.3	7.8	4.2-3.5	6-7
Debt/EBITDA (x)*					8.5-9.5	
FFO/debt (%)	12.4	12.7	12.4	10.8	17-19	10-12
FFO/debt (%)*					7.5-8.5	

*Excluding the regulatory account effect, i.e., without the temporary effect on earnings stemming from volume, price, or changes in operating costs that leads to over- or under-shooting under IFRS accounting, but which are not sustainable. All figures are adjusted by S&P Global Ratings, unless stated as reported. a--Actual. e--Estimate. f--Forecast.

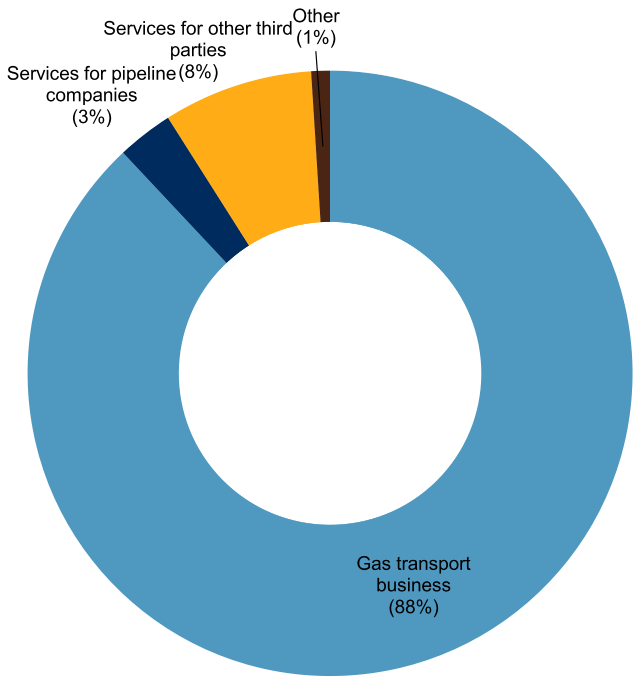
Credit metrics are expected to improve from 2024 after slightly weakening in 2023. We expect that low costs for fuel energy and higher revenue will boost EBITDA and FFO in 2023, but that the effect will only be temporary. This follows the company's June 22, 2023, revised outlook for 2023, which signaled a substantial increase during 2023 to €750 million-€900 million EBITDA, stemming from lower costs. This will, however, only be a temporary effect. The excess earning will be reflected by the regulatory account effect and returned over 2026-2028. There are similar effects from 2021 and 2022, although not as extensive, at €14 million and €38 million, respectively. As in the past, this should normalize over the period and we expect the sustainable FFO to debt to remain in the 9%-12% range.

Company Description

VGT is the parent company of Open Grid Europe GmbH (OGE), the largest of Germany's 16 gas transmission system operators. Through OGE, the group designs, constructs, operates, and markets gas transmission networks. As of 2022, almost all of VGT Group's revenues came from its gas transportation business, with services to pipeline companies and third parties accounting only for a small part of the remainder.

Chart 1

Most Revenues Derive From The Gas Transportation Business
VGT Group--Revenue split 2022



Source: S&P Global Ratings.

OGE transmits gas through its 12,000-kilometer network, making it the largest supra-regional pipeline network in Germany. Its pipeline systems connect the border-crossing points to cities, municipalities, and industrial users in German regions and to pipeline systems of neighboring countries, such as the Netherlands, Belgium, France, Switzerland, Austria, and the Czech Republic.

The Vier Gas Transport Group comprises VGT (the parent), its subsidiary OGE, and its equity investments, which include a number of gas transmission assets with different levels of ownership. VGT largely performs a holding company function for OGE. Vier Gas Services GmbH & Co. KG is the sole shareholder of VGT. It is a long-term investment consortium including British Columbia Investment Management (32.15%), Abu Dhabi Investment Authority through Infinity Investments (24.99%), Fluxys (24.13%), and Munich Re (18.73%).

Peer Comparison

Table 1

Vier Gas Transport GmbH--Peer Comparison

Industry sector: Gas

	Vier Gas Transport GmbH	N.V. Nederlandse Gasunie	National Grid PLC	Enagas S.A.	SNAM SpA
Ratings as of July 18, 2023	BBB+/Stable/A-2	AA-/Stable/A-1+	BBB+/Stable/A-2	BBB/Stable/A-2	BBB+/Stable/A-2
	--Fiscal year ended--				
	Dec. 31, 2022	Dec. 31, 2022	March 31, 2023	Dec. 31, 2022	Dec. 31, 2022
(Mil. €)					
Revenue	1,426.9	2,353.5	24,622.1	970.3	3,913.8
EBITDA	432.9	1,345.1	7,319.6	726.1	2,502.6
Funds from operations (FFO)	363.8	1,114.1	5,084.3	607.0	1,843.2
Interest expense	16.7	70.3	1,951.7	97.3	195.9
Cash interest paid	3.3	95.5	1,583.9	70.9	156.9
Cash flow from operations	446.9	1,406.2	5,929.2	725.5	4,198.2
Capital expenditure	346.9	417.4	7,847.9	90.3	1,338.7
Free operating cash flow (FOCF)	100.0	988.8	(1,918.7)	635.2	2,859.5
Discretionary cash flow (DCF)	(8.5)	771.3	(3,793.0)	178.9	1,990.5
Cash and short-term investments	1,028.2	472.3	2,152.1	1,359.3	1,804.3
Debt	3,364.5	3,596.6	47,640.1	3,756.0	12,541.6
Equity	1,530.0	6,304.4	34,856.7	3,218.3	7,524.0
Adjusted ratios					
EBITDA margin (%)	30.3	57.2	29.7	74.8	63.9
Return on capital (%)	4.7	9.6	6.3	6.9	7.7
EBITDA interest coverage (x)	25.9	19.1	3.8	7.5	12.8
FFO cash interest coverage (x)	111.2	12.7	4.2	9.6	12.7
Debt/EBITDA (x)	7.8	2.7	6.5	5.2	5.0
FFO/debt (%)	10.8	31.0	10.7	16.2	14.7
Cash flow from operations/debt (%)	13.3	39.1	12.4	19.3	33.5
FOCF/debt (%)	3.0	27.5	(4.0)	16.9	22.8
DCF/debt (%)	(0.3)	21.4	(8.0)	4.8	15.9

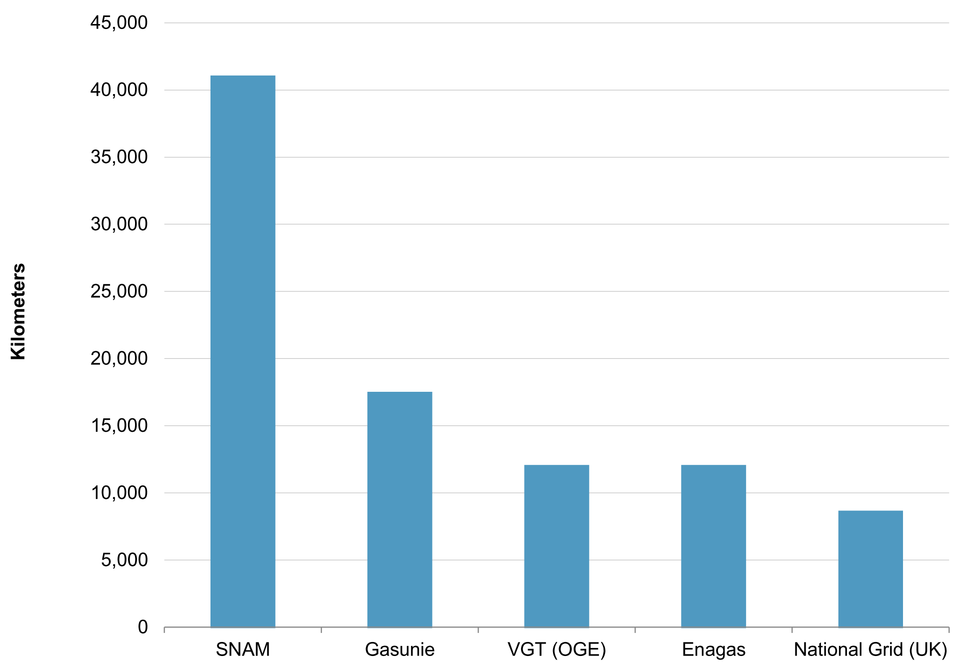
OGE's operations are concentrated in Germany, which we consider to have among the strongest regulatory frameworks in Europe, in line with the Netherlands, the U.K., and Italy, and more favorable than Spain. This is an advantage compared with, for example, Enagas, and partially explains why we rate VGT higher despite weaker metrics, the remaining component being Enagas' larger share of unregulated activities.

OGE's closest peer is Gasunie, because they both have operations in Germany and are exposed to the same regulatory environment. However, Gasunie's operations are more diversified, being also the Dutch gas transmission system operator (TSO), and it has healthier credit metrics. More importantly, the company benefits from the Dutch government's support, which translates into a higher rating.

OGE ranks among the largest European TSOs in terms of network length, behind SNAM and Gasunie (see chart 3), close to Enagas, and ahead of National Grid (when only accounting for the U.K. grid). We see OGE as still able to capture growth in the German market over the next two-three years. This represents an advantage compared with other jurisdictions, where we see new projects slowing. This is why the group's metrics exhibit the third-highest capex-to-sales ratio among its European peers at 24% as of 2022. This is behind SNAM SpA with 34% and National Grid with 32%, but ahead of Enagas, which has a ratio of 9% due to very limited room for growth in Spain.

Chart 2

OGE Ranks Among The Largest European Transmission System Operators In Terms Of Network Length



Source: S&P Global Ratings.

Business Risk: Excellent

A supportive German regulatory framework is the main pillar of VGT Group's business risk profile. We see the German regulatory framework as one of the strongest in Europe because of the regulator's solid track record of stability and five-year regulatory period with well-defined and transparent tariff-setting procedures. This enables the group to fully recover its costs--as long as deemed efficient by the regulator--and mitigates the effects of volume and commodity risks via a regulatory account mechanism. The current regulatory period started in 2023. This is relevant for the VGT Group because almost all of the company's earnings stem from German regulated gas transmission activities and we don't expect this to change in our base-case scenario.

The regulated nature of VGT Group's earnings profile fundamentally supports the group's credit quality from S&P Global Ratings' perspective, because it makes financial performance stable and predictable. It also renders cash flows less dependent on short-term macroeconomic swings, such as the pandemic, and more so on long-term trends. Conversely, VGT Group's business is more exposed to regulatory decisions and energy policy directives.

Network Development Plan (NDP) provided to develop OGE grid. In line with the Energy Industry Act (EnWG), TSOs operating in Germany must jointly submit a 10-year Network Development Plan (DP in each even-numbered calendar year. Projects under this plan are necessary for the energy transition to a new energy mix, grid stability, and integration of the German network.

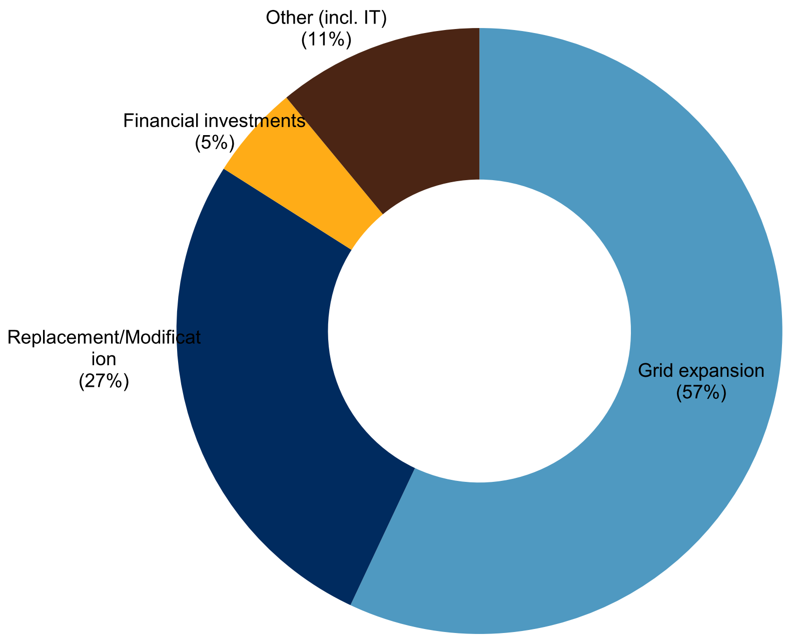
The updated, but yet to be approved NDP, which all TSOs supplied in 2022, contemplates close to €4.4 billion (subject to approval and change requests by regulator BNetzA) in capex for the 2022-2032 period, down from €7.8 billion under the 2020-2030 NDP, out of which OGE accounts for €0.8 billion (€1.6 billion previously). The TSOs determined investments to reduce gas imports dependency from Russia by substitution with LNG and higher gas imports from Western Europe in NDP 2022–2032.

About 57% of OGE's capex was destined for grid expansion (see chart 4) in 2022. We expect to see slightly higher growth capex in 2023-2025, including LNG-related investment. This shows that OGE has room to add to its regulatory asset base, which we see as favorable for the Group's business risk profile.

Chart 3

More Than Half Of OGE's Capex Went On Grid Expansion In 2022

Capex by category as of 2022



Source: S&P Global Ratings.

However, long-term prospects are moderating for gas infrastructure. We believe that investments in gas infrastructure need to be ever more selective across Europe to avoid overinvesting and stranded investments on the continent's road to decarbonization (carbon-neutrality no later than 2050, in Germany even 2045). We continue to believe that gas will play an important role in the energy transition, particularly in Germany. However, over the past year gas consumption declined rapidly by about 17.6%. We foresee little need for aggressive long-term investments more than was needed to allow gas streams from the West rather than from Russia, which has nevertheless been positive for VGT. Although we continue to see the role of gas as crucial over the next decades, this trend raises questions about the long-term relevance of gas grids. In fact, the German government recently approved legislation that allows operators to depreciate their new gas infrastructure entirely by 2045.

Although in the early stages, hydrogen and carbon capture could bridge the energy transition, but uncertainty about the regulatory framework remains. We see gas operators across Europe, together with other stakeholders, lobbying to prove the viability of coupling the sector with green hydrogen in an effort to remain relevant beyond the energy transition. This should spark discussion over the inclusion of hydrogen assets into the regulatory asset base (at least until commercial market participants would take over). Currently, this infrastructure is not part of regulated remuneration, and therefore investment doesn't have the same cash-flow predictability.

Nevertheless, VGT is involved in several green hydrogen and CO2 transportation infrastructure projects. The most important is the H2ercules project. These projects aim to establish specific transportation solutions that would be necessary for the development of hydrogen projects. We would only expect VGT to take significant investment decisions if there was enough visibility regarding regulatory conditions and risk profile.

In our opinion, the development of large-scale hydrogen solutions could gain traction over the medium term in Europe. Still, projects will continue to require a substantial degree of political will and the cooperation of many stakeholders, mainly including network operators, industrial consumers, and regulators.

Financial Risk: Aggressive

We expect VGT's metrics to show moderate improvement, but to remain within adjusted FFO to debt in the 9%-11% range (excluding regulatory account effect), with a somewhat upward trend. Investment is expected to increase significantly over 2023-2025 to about €450 million to €550 million annually on average, compared with about €350 on average for the past three years. Expansion of the grid, however, will lead to immediate sustainable increased revenue under the framework.

The other factor influencing VGT Group's metrics over the rest of the regulatory period is volume effects, which are temporary and do not influence the company's long-term financial stability. This will have a strong impact on reported numbers in 2023, as gas prices have declined and therefore operating costs decreased. VGT Group's metrics exhibit some artificial volatility due to volume effects that are neutralized through the regular account mechanism, although with a time lag running two-to-five years after the over- or under-shooting of allowed revenues. Therefore, when assessing the company's financial risk profile, we weight its metrics equally over a five-year span. We benchmark VGT Group's metrics against the low volatility table.

Financial summary

Table 2

Vier Gas Transport GmbH--Financial summary					
Industry sector: Gas					
	--Fiscal year ended Dec. 31--				
	2022	**2021**	**2020**	**2019**	**2018**
(Mil. €)					
Revenue	1,426.9	1,091.2	1,151.1	1,073.9	1,008.2
EBITDA	432.9	521.2	577.2	542.8	551.3
Funds from operations (FFO)	363.8	407.9	418.3	381.7	387.0
Interest expense	16.7	63.2	76.4	77.7	58.7
Cash interest paid*	3.3	59.4	80.4	72.6	65.8
Cash flow from operations	446.9	392.6	364.8	333.5	406.4
Capital expenditure	346.9	280.0	419.9	472.4	436.2
Free operating cash flow (FOCF)	100.0	112.6	(55.1)	(138.9)	(29.8)
Discretionary cash flow (DCF)	(8.5)	18.8	(186.2)	(261.8)	(133.8)
Cash and short-term investments	1,028.2	115.2	105.4	1,060.4	409.2

Table 2

Vier Gas Transport GmbH--Financial summary (cont.)

Industry sector: Gas	--Fiscal year ended Dec. 31--				
	2022	2021	2020	2019	2018
Gross available cash	1,028.2	115.2	105.4	1,060.4	409.2
Debt	3,364.5	3,282.8	3,287.1	3,078.2	2,821.2
Equity	1,530.0	1,330.3	1,240.9	1,193.4	1,178.9
Adjusted ratios					
EBITDA margin (%)	30.3	47.8	50.1	50.5	54.7
Return on capital (%)	4.7	6.7	8.7	8.8	9.7
EBITDA interest coverage (x)	25.9	8.2	7.6	7.0	9.4
FFO cash interest coverage (x)	111.2	7.9	6.2	6.3	6.9
Debt/EBITDA (x)	7.8	6.3	5.7	5.7	5.1
FFO/debt (%)	10.8	12.4	12.7	12.4	13.7
Cash flow from operations/debt (%)	13.3	12.0	11.1	10.8	14.4
FOCF/debt (%)	3.0	3.4	(1.7)	(4.5)	(1.1)
DCF/debt (%)	(0.3)	0.6	(5.7)	(8.5)	(4.7)

*For 2022, we reduced cash interest payment with the cash inflow from a hedge position that was realized in 2022. The positive market value at the time of the reversal amounted €56.9 million.

Reconciliation

Table 3

Vier Gas Transport GmbH--Reconciliation of reported amounts with S&P Global Ratings' Adjusted Amounts (Mil. €)

	--Fiscal year ended Dec. 31, 2022--					
Vier Gas Transport GmbH reported amounts						
	Debt	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**	**Cash flow from operations**
Reported	4,314.2	417.4	195.4	66.3	432.9	450.2
S&P Global Ratings' adjustments						
Cash taxes paid	--	--	--	--	(65.8)	--
Cash interest paid	--	--	--	--	(3.3)	--
Reported lease liabilities	19.8	--	--	--	--	--
Postretirement benefit obligations/deferred compensation	--	0.1	0.1	1.0	--	--
Accessible cash and liquid investments	(1,028.2)	--	--	--	--	--
Capitalized interest	--	--	--	6.3	--	--
Dividends received from equity investments	--	15.4	--	--	--	--
Asset-retirement obligations	56.4	--	--	--	--	--
Nonoperating income (expense)	--	--	28.9	--	--	--
Reclassification of interest and dividend cash flows	--	--	--	--	--	(3.3)

Table 3

Vier Gas Transport GmbH--Reconciliation of reported amounts with S&P Global Ratings' Adjusted Amounts (Mil. €) (cont.)						
Debt: Guarantees	2.3	--	--	--	--	--
Interest expense: Other (situational)	--	--	--	(56.9)	--	--
Total adjustments	(949.7)	15.5	29.0	(49.6)	(69.1)	(3.3)
S&P Global Ratings' adjusted amounts						
	Debt	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**
Adjusted	3,364.5	432.9	224.4	16.7	363.8	446.9

Liquidity: Strong

We assess VGT's liquidity as strong because we forecast sources to uses over 1.5x in the 12 months following March 31, 2023, and above 1.0x in the following 12 months. Our assessment also includes qualitative factors, such as proven access to debt capital markets and sound relationships with banks, reflected in the group's diverse sources of funding. We also believe the group displays prudent risk management that underpins its liquidity position. This was demonstrated by the early refinancing of its €750 million bond, which is due after second-quarter 2023 and is a sizable part of the capital structure. VGT already last year issued a bond with a total value of €1.0 billion to meet the upcoming maturity.

The current €600 million and €15.3 million RCF expire in August and September 2024, respectively. We expect VGT to refinance these instruments well ahead of maturity.

Principal liquidity sources

- Reported access to unrestricted cash and short-term marketable securities of about €1,122 million.
- Access to unused revolving credit facilities totaling about €615 million, which mature in August 2024.
- FFO of €600 million-€700 million in 2023.
- Working capital inflows of about €85.8 million.

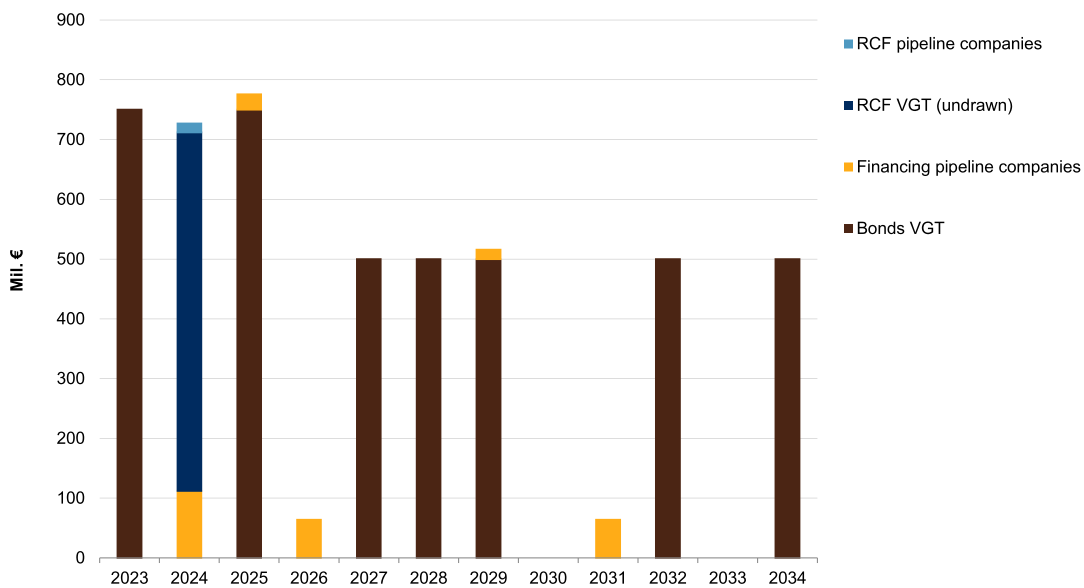
Principal liquidity uses

- Debt maturities of €750 million in the next 12 months, and €600 million in the 24-month timeframe.
- Capex of about €470 million-€550 million per year.
- Cash dividend payments of about €100 million in 2023.

Debt maturities

Chart 4

VGT Group--Maturity Schedule
As of Dec. 31, 2022



Source: S&P Global Ratings.

Environmental, Social, And Governance

ESG Credit Indicators

E-1	E-2	**E-3**	E-4	E-5	S-1	**S-2**	S-3	S-4	S-5	G-1	**G-2**	G-3	G-4	G-5

Environmental	Social	Governance
- Climate transition risks.	- N/A	- N/A

N/A--Not applicable. ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicators: Definition And Applications," published Oct. 13, 2021.

Environmental and social aspects are relevant to VGT Group's business. Although not yet a relevant component of the company's earnings, we see the efforts in green hydrogen pioneering as relevant. On the one hand, this is helping spark discussion on the adoption of clean energies and decarbonizing the German economy and to create the framework that supports it. On the other hand, these are the first steps toward ensuring the long-term sustainability of VGT Group's business, because gas infrastructure relevance will decline as the energy mix moves toward zero carbon emissions.

Notwithstanding this, for now, the German energy transition creates opportunities for gas infrastructure companies, such as OGE. In our opinion, gas will remain a crucial component of the the medium- and long-term energy mix transition, particularly in light of plans to bring forward its coal exit from the official deadline of 2038, and the nuclear shutdown in Germany that concluded in April 2023.

The majority of VGT Group's capex is related to the Network Development Plan, which represents gas infrastructure that will be key for the energy transition in Germany and is fully aligned with the country's long-term climate policy.

We believe that the company's technical and operational standards will continue to ensure a high degree of network security and reliability, thereby mitigating environmental risks over the coming years, which is key to managing regulatory risk and public opinion.

In our view, VGT Group's management and governance framework meets industry standards and is driving to align stakeholder interests toward long-term sustainability goals.

Issue Ratings - Subordination Risk Analysis

Capital structure

As of Dec. 31, 2022, the group's capital structure consisted of:

- €4 billion of bonds issued at the VGT level; and
- €281 million at the pipeline company level, which is reported at pro rata share (51%).

Analytical conclusions

We rate VGT's debt at the level of the issuer credit rating because we believe debt sitting at pipeline companies does not represent a material disadvantage to bondholders.

Ratings Score Snapshot

Issuer Credit Rating

BBB+/Stable/A-2

Business risk: Excellent

- **Country risk:** Very low
- **Industry risk:** Very low
- **Competitive position:** Strong

Financial risk: Aggressive

- **Cash flow/leverage:** Aggressive

Anchor: bbb

Modifiers

- **Diversification/portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Strong (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Positive (+1 notch)

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings , Oct. 10, 2021
- General Criteria: Group Rating Methodology , July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments , April 1, 2019

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers , Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology , Nov. 19, 2013
- General Criteria: Methodology: Industry Risk , Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry , Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions , Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities , Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings , Feb. 16, 2011
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating , Oct. 1, 2010

Business And Financial Risk Matrix

	Financial Risk Profile					
Business Risk Profile	Minimal	Modest	Intermediate	Significant	**Aggressive**	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	**bbb**	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of July 18, 2023)*

Vier Gas Transport GmbH	
Issuer Credit Rating	BBB+/Stable/A-2
Senior Unsecured	BBB+
Issuer Credit Ratings History	
08-Jul-2022	BBB+/Stable/A-2
29-Apr-2021	A-/Negative/A-2
30-Apr-2018	A-/Stable/A-2

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.