Full Analysis

Summary:

Vier Gas Transport GmbH (Open Grid Europe Group)

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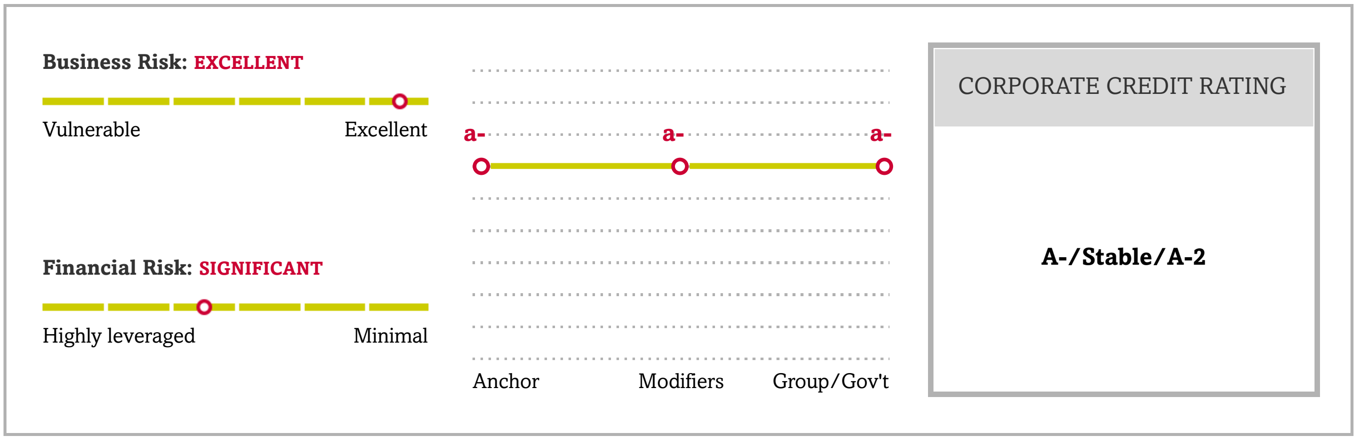

Rationale

Business Risk: Excellent	Financial Risk: Significant
• Largest gas transmission network and operator in Germany with a natural monopoly position in its service area. • Very low risk and regulated earnings profile. • All earnings generated in Germany (very low risk country).	• Stable and predictable cash flow generation over the regulatory period. • Relatively high leverage and some cash flow volatility triggered by volume risk. • Long debt maturities, no material maturities until 2020, and "strong" liquidity.

Outlook: Stable

The stable outlook on Open Grid Europe Group (OGE), comprising the holding company Vier Gas Transport GmbH and its subsidiary Open Grid Europe GmbH, reflects Standard & Poor's Ratings Services' expectation that OGE will continue to achieve solid operating and financial performance over the next two years, reflecting its very low risk and regulated earnings profile. According to our base case, we expect OGE to maintain a funds from operations (FFO)-to-debt ratio of above 12% over the forecast period, in line with a financial risk profile of "significant," applying our low volatility benchmark table.

Downside scenario

We could lower the rating if we anticipated a sustained decline in consolidated FFO to debt to less than 12%. This could occur if OGE was unable to control costs due to poor operating performance, if unforeseen expenses could not be passed on to customers, or if OGE's efficiency factor was lower than expected. We could also lower the rating if we changed our assessment of the business risk profile. This could be triggered by a substantial negative change to the regulatory framework or a change in the business mix toward, by our assessment, more risky industries and countries, which we view as very unlikely at the moment.

Upside scenario

A positive rating action could result from a sustained improvement in credit metrics such that adjusted FFO to debt reached at least 15% on a weighted average basis. We do not see upside potential driven by the business risk profile, given the already excellent business risk profile.

Standard & Poor's Base-Case Scenario

Assumptions

- Efficiency factor of 100% for the regulatory period.
- Capital expenditures in line with the updated network development plan of €150 million-€200 million per year.
- Some volatility relating to the regulatory account mechanism.
- Positive contribution from the efficiency program.

Key Metrics

	2013a	2014p	2015e	2016e
FFO to debt (%)	17.1	>14	about 9	>12
Capex (mil. €)	194	150-160	180-200	180-190
Debt/EBITDA (x)	5	about 5	7-8	5-6

a--Actual. p--Projected. e--Estimated.

Business Risk: Excellent

Our assessment of OGE's "excellent" business risk profile is based on its natural monopoly position in its service area and in our view "very low" risk regulated gas transmission activities and strong regulatory framework. In our opinion, regulated operations generally present low operation risk and predictable revenue streams. Our business risk profile also incorporates our view of "very low" country risk for companies operating in Germany.

Additionally, our assessment is underpinned by our view of OGE's "strong" competitive position. The group has a monopolistic market position in its service area and operates in an incentive-based regulation framework with a revenue cap, allowing relatively stable and predictable revenues and EBITDA over the regulatory period of five years. The Federal Network Agency (BNetzA) regulates gas transmission activities in Germany and introduced the regulatory framework in 2010, which has become more credit-supportive since. OGE is exposed to volume risk, but if revenues fall short of or exceed the revenue cap, the deficit or surplus is compensated by the regulatory account mechanism over the medium term. Nevertheless, in our view, profitability can be more volatile than peers' over the short term.

Financial Risk: Significant

OGE Group's "significant" financial risk profile reflects its low-risk, stable, and predictable cash flow generation over the regulatory period, and its relatively high debt burden. Parts of OGE's capital expenditure (capex) program were postponed beyond 2017 as a result of the updated network development plan. That said, we expect in our base case no material increase of leverage until 2017 and adjusted FFO to debt of more than 12% in the next two to three years on a weighted average basis.

Liquidity: Strong

We assess OGE Group's consolidated liquidity position as "strong" as defined in our criteria, supported by our view that OGE Group's liquidity resources will exceed its funding needs by well over 1.5x in the next 12 months and more than 1.0x in the following 12 months.

OGE Group's liquidity profile is further supported by its well-established relationships with its core banks and generally high standing in the credit markets.

Principal Liquidity Sources	Principal Liquidity Uses
• Reported excess cash of about €290 million as of Dec. 31, 2013; • Access to a revolving credit facility of €200 million maturing in 2018; • Our expectation that OGE will generate cash flow from operations of about €350 million in 2014 and about €200 million in 2015.	• Debt maturities in the next 12 months of €130 million and €50 million in the following 12 months; • Capital expenditures of about €155 million in 2014 and about €190 million in 2015; • Financial investments of about €100 million in 2014; • Cash dividend payments of about €60 million per year.

Other Modifiers

Not applicable.

Ratings Score Snapshot

Corporate Credit Rating

A-/Stable/A-2

Business risk: Excellent

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

Financial risk: Significant

- **Cash flow/Leverage:** Significant

Anchor: a-

Modifiers

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

Related Criteria And Research

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Jan. 2, 2014
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios and Adjustments, Nov. 19, 2013
- Methodology: Industry Risk, Nov. 19, 2013
- Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Group Rating Methodology, May 7, 2013
- Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Business And Financial Risk Matrix

Business Risk Profile	Financial 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-

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