Erste Group Research – Company Report
Fondul Proprietatea | Closed-end fund | Romania
26 March 2014

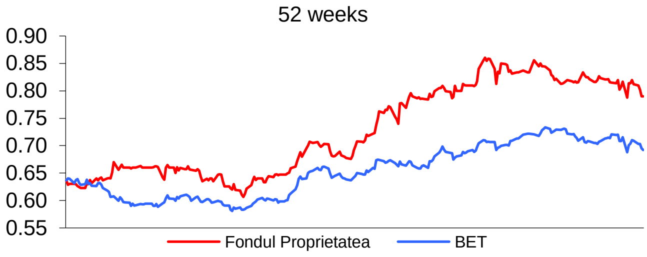
ERSTE GROUP

Fondul Proprietatea

Accumulate

P&L key figures (RON mn)	2011	2012	2013p
Revenues from dividends	519.1	619.0	649.7
Revenues on disposals	13.4	208.1	573.1
Interest revenues	41.1	34.9	36.1
Total revenues	617.9	871.7	1,311.2
Total fund operating expenses	55.1	59.6	87.0
Net profit	543.8	567.0	682.2
Indicator	**2012**	**2013**	**Last**
NAV (RON mn)	14,979.2	15,013.7	14,603.7
NAVS (RON)	1.1371	1.2436	1.2097
DPS (RON)	0.0409	0.0521	-
Discount to NAVS	-51.7%	-33.0%	-34.7%
Dividend yield (2013)			6.5%

Source: Fondul Proprietatea, Erste Group Research



Performance	12M	6M	3M	1M
in RON	24.1%	11.6%	-7.1%	-4.5%

Share price (RON) close as of 24/03/2014	0.7895	Reuters	FP.BX	Free float	75.4%
Number of shares (mn)	13,778.4	Bloomberg	FP RO	Shareholders	Elliott L.P. (15.0%)
Market capitalization (RON mn / EUR mn)	10,878 / 2,416	Div. Ex-date	13/05/13		Morgan Stanley (9.69%)
Enterprise value (RON mn / EUR mn)	0 / 0	**Target price**	**0.8900**	Homepage:	www.fondulproprietatea.ro

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Key topic: Extra cash distributions

We maintain our Accumulate recommendation on Fondul Proprietatea (FP), due to the upcoming reactivation of intensive buyback programs and the implementation of an extra cash distribution policy, contingent upon market watchdog approval. Dividend yields for the 2013 and 2014 ordinary dividend should exceed 5%, fundamentally supporting the share price.

We have reached a target price of RON 0.89/share, derived from our conservative SOTP methodology after applying a 10% discount to the listed holdings' market value and a 15% discount to the fair value of unlisted shares, which is in line with the up-for-sale status of the closed-end fund's holdings.

Reaching the 15% trading discount target set by shareholders for the period October 1, 2014 – June 30, 2015, is largely conditioned upon the approval of the extra cash distribution policy, which would reduce the NAV/share in order to meet the imposed benchmark. Thus, the higher the FP share price (supported by buyback programs), the lower the supplementary dividend distributions financed by asset disposals necessary in order to meet the target. Selling holdings of up to 10% in Petrom by the end of the year seems unavoidable in order to meet the performance criteria for the new mandate of Franklin Templeton. The fund manager has already confirmed its option to reduce the stake in Petrom to below 15%.

Investment case

Ordinary dividend outlook, fundamentally supportive of share price

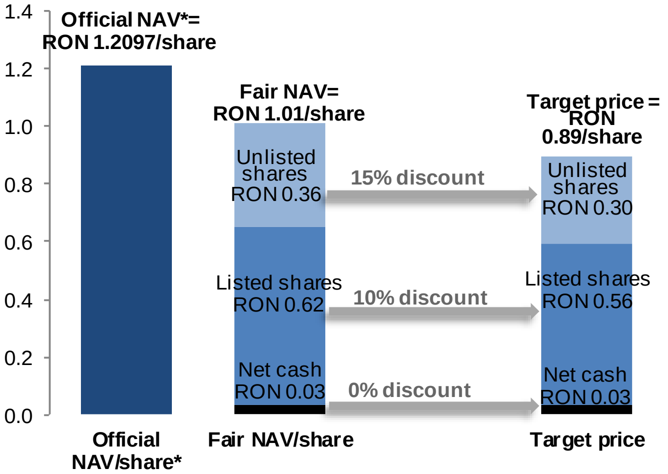
Accumulate call consistent with cash flow generating capability of FP portfolio, as measured by 2013 and 2014 ordinary dividend yield outlook

We have arrived at a target price of RON 0.89/share, associated with an Accumulate rating, which we computed based on our conservative Erste Group SOTP methodology by applying a 10% discount to the listed stocks' market value and a 15% discount to the fair value of unlisted shares from the FP portfolio. The up-for-sale status of the closed-end fund's holdings, in accordance with its financing needs for future buyback programs and (potential) extra cash distributions, has put negative pressure on FP holdings' pricing. This was the reason for the abovementioned discounts applied by us in order to arrive at the target price.

A 2013e dividend yield of 6.5% at the current share price is basically supporting the share price. The ordinary gross dividend on FY13, estimated by us at RON 0.0521/share, was put on hold by Franklin Templeton, which is currently trying to replace it with an almost equal RON 0.05/share extra-cash distribution on the back of share capital reduction. This should be tax free in the view of the fund manager.

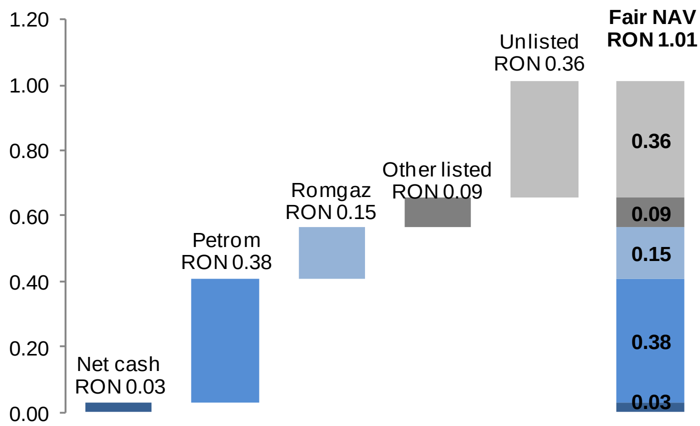
However, we consider the fiscal optimization of the ordinary dividend only a secondary topic. The fundamental question is whether or not the ordinary dividend outlook shows us that FP's asset collection is generating attractive enough cash flows compared to the market capitalization of the closed-end fund. This is the most important criterion for measuring the quality of an investment vehicle's portfolio and deciding whether it is worth investing in it. The size of the dividend yield for FP stock is actually the indicator which provides us with a positive answer to this question. Even considering our lower 2014 ordinary dividend estimation of RON 0.04/share, a dividend yield of 5% should be quite reasonable for investors.

Target price and key NAVs per share (RON)



*) as of February 2014
Note: Shares repurchased within the two buyback programs were considered cancelled
Source: Fondul Proprietatea, Erste Group Research

Fair NAV/share breakdown (RON)



Note: Shares repurchased within the two buyback programs were considered cancelled
Source: Erste Group Research

The outlook for Petrom and Romgaz, supported by gradual gas price deregulation, is a positive factor for the FP valuation, despite the, undoubtedly

Promising Petrom and Romgaz outlook to counterbalance negative impact on FP valuation stemming from power producers' Nuclearelectrica and Hidroelectrica deteriorating profitability profile

tougher, fiscal framework yet to be clarified with the Romanian government by the end of 2014. The promising Petrom and Romgaz outlook will more than offset the negative impact of the deterioration of the profitability profile of power producers Hidroelectrica and Nuclearelectrica in 2014. These two companies are strongly affected by the adverse power price environment, the overwhelming new tax on special infrastructures, as well as the 'arbitrary obligations' imposed by the energy watchdog to partly sell their output on the regulated market, at prices well below the wholesale power price.

On the other hand, the FP valuation has benefitted from the listing of gas producer Romgaz and nuclear power producer Nuclearelectrica, which substantially increased FP portfolio's liquidity profile, further improving investor sentiment related to the stock. The weight of listed shares is currently around 60% of the total value of the closed-end fund's assets and may jump towards 65% in the event of a successful listing of Electrica, the holding company in power distribution grids; this is the only IPO that could realistically take place in 2014 on the BSE.

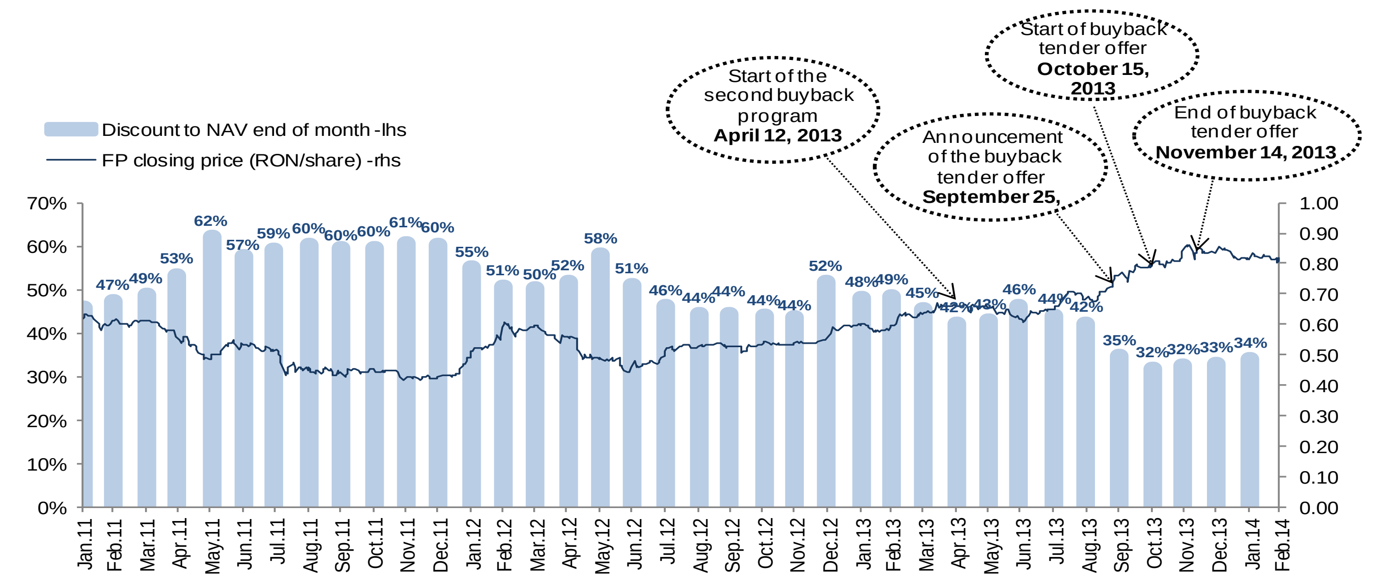
Why extra cash distributions are key

Judgments on the FP investment story radically changed after shareholder approval on November 22 of US hedge fund Elliott's proposal for a new two-year mandate for Franklin Templeton starting on September 30, 2014, with early termination provisions. Considering the recommendations that the fund manager had made to investors to vote against this proposal, the decision came as a surprise.

Reaching 15% discount target set by shareholders largely contingent on extra cash distributions, which would reduce fund's NAV to meet imposed benchmark

The new management agreement, which will be subject to approval at the April 2014 OGM, will include two criteria that have to be simultaneously met by the middle of the coming year: 1) trading discount to official NAV per share of a maximum of 15% for at least two-thirds of the trading sessions in the period October 1, 2014 - June 30, 2015, and 2) adjusted NAV per share as of the end of June 2015 higher than the NAV/share value of RON 1.16 from end-September, 2013 (the adjusted NAV will count any cash return to shareholders following eventual share capital reductions).

Fondul Proprietatea share price vs. discount to NAV development (2011-13)



Source: Bucharest Stock Exchange, Fondul Proprietatea, Erste Group Research

Starting with 2015, each year in October, the fund manager will have to organize a GSM where Franklin Templeton has to submit a performance report on the fulfillment of the two performance objective fixed by shareholders. If any or both of the two performance criteria are not met, shareholders may decide on an early termination of Franklin Templeton's mandate as asset manager. However, according to the draft of the new management agreement, the shareholders' decision will effectively take into account market conditions and regulatory issues affecting the meeting of the performance targets during the reporting period. In this context, the meeting of the 15% discount target cannot be at all considered as a completely undisputable objective for Franklin Templeton. The first reporting period shall be October 1, 2014 until June 30, 2015 and every subsequent year shall be from 1st of July to 30th of June, next year.

Two tools can be employed to meet performance criteria: running successive buybacks and supplementary cash distributions 'fueled' by share capital reduction

Two tools can be employed by Franklin Templeton in order to meet the targets of the new two-year mandate: i) rolling over buyback programs, and ii) extra cash distributions on the back of share capital reduction.

The first tool consists of running successive buyback programs which would become a permanent feature of FP (eventual buyback tenders at prices well above the market price, as was the case in October – November 2013) and is aimed at pushing up the market price. FP shareholders approved/are going to approve in April another two buyback programs for 252mn shares and 990.85mn shares, respectively. These will be activated as soon as the shares redeemed in the first two programs are effectively cancelled. An important inconvenience associated with the buyback programs is that their impact on the share price is actually uncontrollable, considering that, after a more than 50% growth of the stock price last year, shareholders are most probably tempted to mark their capital gains. In consequence, the buyback is cash-intensive, without bringing any certainty in respect of pushing the share price to the level required for meeting the 15% discount to NAV target.

The second tool, as mentioned above, is represented by extra cash distributions on the back of reducing the share capital (via successive face value cuts).

The Extraordinary Shareholders Meeting (ESM) from February 3 approved a first share capital reduction via RON 0.05/share cut of shares' face value. In the meantime, in order to be able to flexibly decide on future cash distributions through share capital reduction, shareholders approved the lowering of quorum requirements from 50% of the voting rights down to at least 25% of voting rights upon the first summoning and at least 20% upon the second summoning.

Extra cash distributions on back of share capital reduction, contingent upon ASF approval

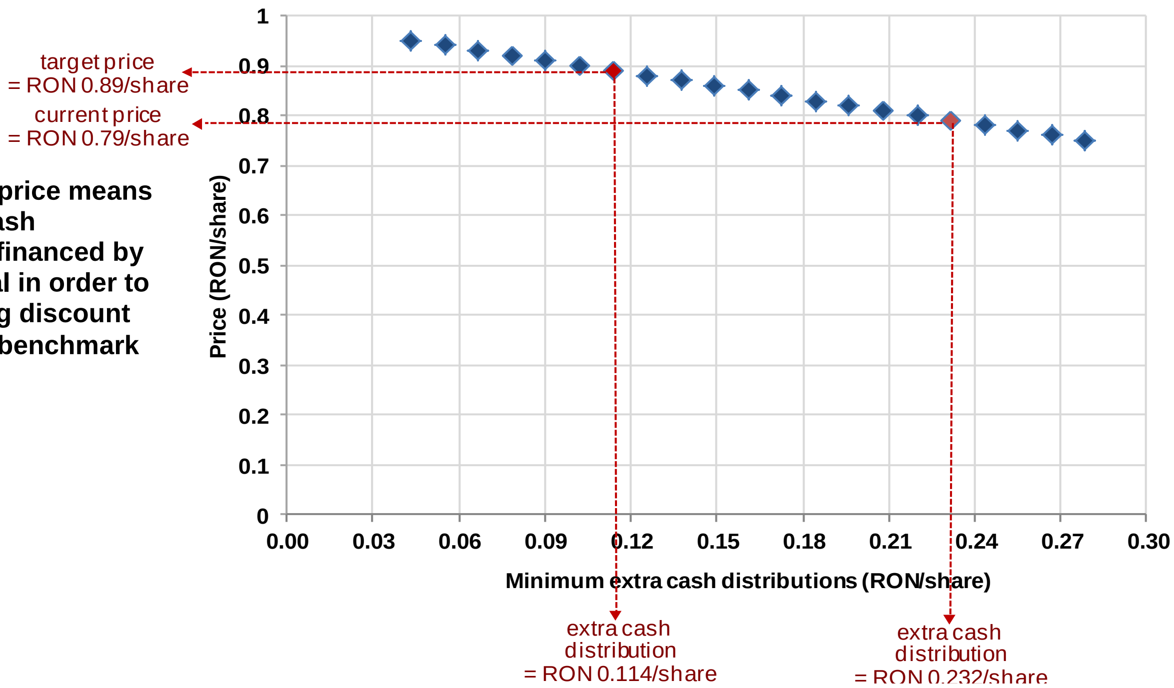
We consider the most efficient tool for meeting the 15% discount target to be the effective implementation of the cash distribution policy on the back of share capital reduction, which is contingent upon the approval of the Romanian Authority for Financial Surveillance (ASF). The adjusted NAV per share also introduced as a performance criterion requires adding cash distribution per share to the NAV/share diminished by asset disposals, incentivizing Franklin Templeton to act in this manner in order to meet shareholder objectives. This approach is consistent with the public statements made by the head of Franklin Templeton, according to whom the size of Fondul Proprietatea is too large compared to the depth of the Romanian equity market; as a result, the fund manager may decide to reduce the fund.

We performed a 'small' exercise using as a starting point the two equations corresponding to the two performance criteria, namely: 1) FP share price / (NAV / share) ≥ 0.85, and 2) NAV / share + extra cash distribution / share >

1.161. We plugged the 'market' price into the first equation and computed, based on the two equations, the minimum necessary extra cash distributions needed to meet the performance criteria. The outcomes offer, in our view, useful guidance for investors regarding the financing needs of FP required for meeting the performance criteria.

Size of cumulative extra cash distributions corresponding to FP share price in order to meet 15% discount target

Higher share price means lower extra cash distributions financed by asset disposal in order to reduce trading discount towards 15% benchmark



Source: Erste Group Research

Ideally, Franklin Templeton will combine the two tools in order to reach the 15% trading discount imposed by shareholders. Thus, the higher the share price of FP, the lower the cash distribution financed by asset disposals (if Romanian regulator ASF agrees with the shareholders' decision).

At its current price of RON 0.79/share, FP should make extra cash distributions worth over RON 0.2/share in order to meet performance criteria

In any case, the main option is, as Franklin Templeton has already confirmed, to sell part of the 19% holding in Petrom, which currently has a weight of almost 40% in FP assets. Based on our calculations, FP has to sell ~3% in Petrom in order to cover its predictable cash needs. We considered this year's cash distribution to shareholders and the implementation of the third and the fourth buyback programs, but without taking into account financing needs for any supplementary cash distribution (other than the RON 0.0521/share ordinary dividend).

On the other hand, we have computed that, at the current price of RON 0.79/share, asset divestment worth more than EUR 600mn (over a 10% stake in Petrom) would be needed in order to meet the two performance criteria. On the other hand, at a FP share price of RON 0.9/share, the value of asset disposals should be close to EUR 300mn (over a 5% stake in Petrom). In this complex context has to be understood the announcement made by Franklin Templeton in March this year regarding its intention to potentially reduce its ownership interest in OMV Petrom to below 15% holding, subject to appropriate market conditions.

Value of asset disposals aimed at financing potential extra cash distributions

Replacing ordinary dividend distribution for FY13 with cash distribution, on back of share capital cut is only a secondary topic; if approved by regulator, extra cash distribution policy activated de facto

Price (RON/share)	Minimum extra-cash distribution (RON/share)	Financing needs (EUR mn)
0.95	0.043	120.0
0.94	0.055	152.6
0.93	0.067	185.1
0.92	0.079	217.7
0.91	0.090	250.3
0.90	0.102	282.8
0.89	0.114	315.4
0.88	0.126	348.0
0.87	0.137	380.5
0.86	0.149	413.1
0.85	0.161	445.7
0.84	0.173	478.2
0.83	0.185	510.8
0.82	0.196	543.4
0.81	0.208	575.9
0.80	0.220	608.5
0.79	0.232	641.0
0.78	0.243	673.6
0.77	0.255	706.2
0.76	0.267	738.7
0.75	0.279	771.3

Note1: Extra cash distributions do not consider any dividend tax
Note2: The two performance criteria imposed to FT by FP shareholders can be translated into two mathematical relations: 1) FP share price / (NAV/share) ≥0.85 and 2) NAV/share + extra cash distribution / share > 1.161. Using these relations and assuming different share price values, we reached the corresponding extra cash distributions.
Source: Erste Group Research

In conclusion, having in mind the performance objective for the new mandate of FT, the current discussions on replacing the ordinary dividend of RON 0.05/share with a potentially more fiscally-efficient cash distribution on the back of the share capital reduction is actually only a secondary topic. Approval by ASF of the respective cash distribution would mean a green light for the supplementary cash distribution policy, with a major impact on the FP profile.

Mixed FP portfolio picture

Petrom and Romgaz outlook supportive for FP portfolio's income generating capability, as opposed to weaker profitability profile expected for power producers and RAB-regulated utilities

The core of the FP portfolio is obviously represented by the holdings in Petrom and Romgaz, which together account for about 53% of the total assets of the fund. The two companies will enjoy net gains from the gas liberalization process, despite the expected new taxes and tougher royalty regime. Their strong dividend payer status, which translates into a contribution of over 70% to FP's dividend inflows, makes the oil & gas producers the most important 'members' of the fund's portfolio. This is why the main exit solutions for FT, in order to finance its major cash needs, are inevitably connected to the divestment of Petrom and Romgaz holdings.

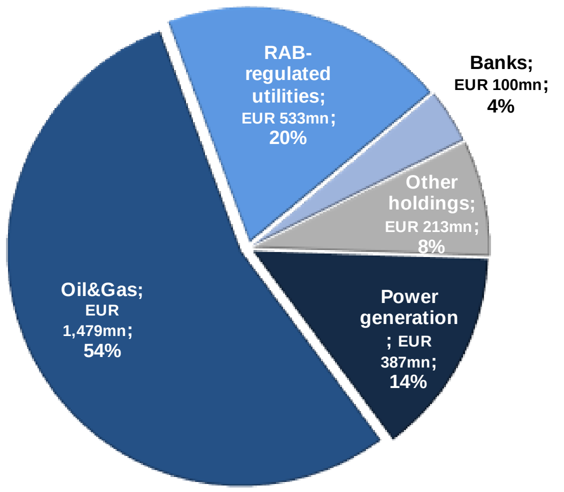
On the contrary, the profitability profile of power producers will be under severe pressure in 2014 as a result of the weak power price environment and the new tax on special infrastructures. In the case of Hidroelectrica, the discretionary price set for 2014 by the regulator ANRE on the regulated market is another negatively overwhelming item for the valuation of this company. This is why the weight of power producers in total assets has dropped below 15% compared to our previous reports on FP.

Limited qualitative exit options besides two oil & gas holdings for meeting estimated cash needs by middle of next year

We have also reduced the fair values of the unlisted regulated utilities from the fund portfolio, in view of higher regulatory risk starting with 2014 following new corporate taxes and statements made by government officials over the course of last year. They blamed the power grids privatized with ENEL, E.ON and CEZ for the weak quality of the distribution services, the lack of relevant investments and for unjustifiably high profits. The regulatory risk outlook, together with the litigation initiated by the Romanian government at the Arbitrage Court of Paris against strategic investors in the power distribution sector, limits FP's exit solutions from unlisted regulated utilities. The only feasible solution in the medium term is an exit together with the Romanian government, which also holds minority stakes in privatized distribution grids.

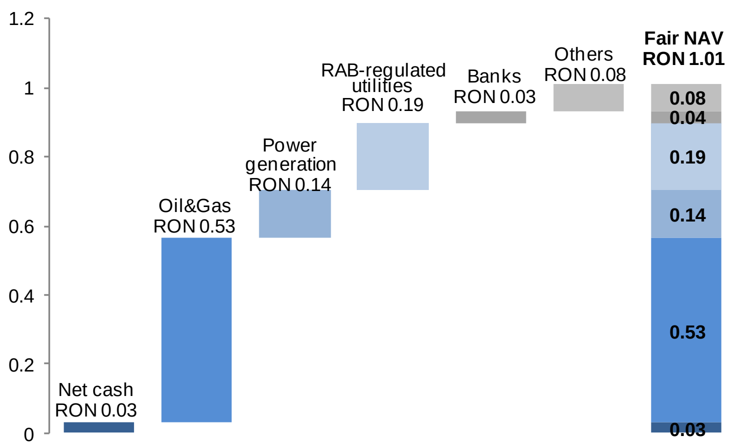
With respect to the three power grids controlled by the state-owned company Electrica, there is, at least theoretically, an exit alternative for FP after the listing of the holding company scheduled to take place in 2014.

Structure of equity portfolio by sector (fair values)



Source: Erste Group Research

Fair NAV/share breakdown by sector (RON)



Note: Shares repurchased within the second buyback program were considered cancelled
Source: Fondul Proprietatea, Erste Group Research

Company	Weight in assets (fair value / Official assets as of December 2013)	Outlook (2014)	Outlook (medium term)	Potential drivers (+)/drawbacks (–)
Petrom	37.5% / 33.5%	Positive (+)	Positive (++)	(+) Gradual gas market liberalization up to 2018 (+ +) Deep-water exploration in Black Sea to confirm commercial gas discoveries able to feed LT growth story (+ +) Stable dividend outlook (40% payout ratio) (–) Tougher fiscal framework starting in 2015
Romgaz	15.3% / 13.1%	Positive (+)	Positive (+)	(+ +) Gradual gas market liberalization up to 2018 (+ +) Stable dividend outlook (75% payout ratio on FY13 to be maintained in coming years) (–) Receivable write-offs risk as result of weak financial stance of some clients (mainly cogeneration gas-fired plants) (–) Tougher fiscal framework starting in 2015
Hidroelectrica	9.9% / 14.9%	Negative (– –)	Positive (+)	(– –) 40% of 2014 output to be sold on regulated market, at price below wholesale power price and production costs (– –) Oversized turbinated water expenses after water tariff jump in 2011 (– –) Oversized new tax on special constructions, with high negative impact on profitability (–) High personnel and third-parties expenses (–) Weak power price environment in Romania (below RON 185/MWh) in medium term (+) Gradual profitability gains from market liberalization (first benefits to be seen in 2015) (+ +) Hydro power flexibility to meet peak demand and balance power system, resulting in higher output price than peers
Nuclearelectrica	2.0% / 2.0%	Negative (– –)	Negative (– –)	(+) Gradual power market liberalization up to 2018; supportive for profitability profile (– –) Oversized new tax on special constructions, with high negative impact on profitability (– –) Overwhelming CAPEX needs of minimum EUR 1.5bn in order to rehabilitate reactor 1, which can safely operate only up to 2022 according to nuclear industry norms (–) Weak power price environment in Romania (below RON 185/MWh) in medium term
CE Oltenia	1.9% / 2.1%	Negative (– –)	Negative (– –)	(– –) Substantial power production contraction since 2013, mainly due to sluggish demand and renewable energy boom (– –) Higher production costs than hydro and nuclear producers (– –) Oversized personnel costs (–) Weak power price environment in Romania (below RON 185/MWh) in medium term (+) Technological system services of 600 MW provided to Transelectrica and guaranteed by ANRE starting with 2013, in order to cover company expenses while ensuring balance and stable functioning of national power system
Electrica	4.5 % / 4.6%	Positive (+)	Negative (–)	(+) Stable and relatively high profitability and no leverage under protection of RAB-regulated methodology (–) Lower regulated return on RAB (key profitability factor) fixed in past by the regulator ANRE for three state-owned distribution grids in comparison with five privatized power grids (–) Higher regulatory risk starting with 2014 or 2015 for regulated utilities, anticipated by statements of government officials, who blamed privatized power distribution grids for recording unjustifiably high profits (–) New tax on special constructions may not be effectively recognized in tariff

Valuation summary – Erste Group SOTP methodology

We assign fair value of RON 0.89/share; Accumulate

Fair value of Fondul Proprietatea assets according to Sum of the Parts approach (SOTP)

No.	Asset Category	Fair value (EUR mn)	Discount	Discounted fair value (EUR mn)	Percentage of fair value of assets (%)
1	Current accounts and monetary investments (deposits, TBills)	97.3	0.0%	97.3	3.5%
2	Unlisted companies	984.9	15.0%	837.2	35.1%
3	Listed companies	1,727.1	10.0%	1,554.4	61.5%
4	Total liabilities	13.6	0.0%	13.6	
Total assets		**2,809.2**	**-**	**2,488.8**	-
Net Assets Value (NAV, EUR mn)					**2,475.2**
No of Shares*					12,437.14
NAV/Share (EUR/share)					**0.199**
NAV/Share (RON/share)					**0.89**

**Shares repurchased within the two buyback programs were considered cancelled*
Source: Erste Group Research

Non-Equity Assets
- *Category 1* – Cash and low-risk fixed income monetary instruments (bank deposits, government securities) were taken into account according to values from the last NAV report (January 2014).

Equity Assets
- We grouped companies from the energy sector into three segments, while from the non-energy part of the portfolio we separately highlight the banks.
- Classification by sector does not account for differences between the listed/unlisted statuses of a company.
- *Category 2*: Power generation (Hidroelectrica, Nuclearelectrica, CE Oltenia).
- *Category 3*: Oil & Gas (Petrom, Romgaz).
- *Category 4*: RAB-regulated utilities (E.ON Moldova Distributie, Electrica Distributie Muntenia Nord, Enel Distributie Muntenia, Electrica Distributie Transilvania Nord, Electrica Distributie Transilvania Sud, Enel Distributie Banat, Enel Distributie Dobrogea, E.ON Gaz Distributie, GDF Suez Energy Romania and Transelectrica). Using a RAB-regulated methodology to value electricity/gas distribution companies, we implicitly valued the supply companies resulting from the split of the old companies into two entities, one for distribution and one for supply, in line with EU directives.
- *Category 5*: Banks.
- *Category 6*: Non-energy sectors including other important companies (airports, port authorities, postal services).
- *Category 7*: Unlisted small companies, which were not included in the fair value of NAV, due to their very low impact.

Unlisted companies

Company	Sector	Valuation tool
Hidroelectrica, CE Oltenia	Power generation	-Linear regression peer companies (EV/IC, EBITDA/IC) -Linear regression peer companies (EV/Output, EBITDA/Output)
E.ON Moldova, ENEL Muntenia, ENEL Banat, ENEL Dobrogea, Electrica Distributie Transilvania Nord, Electrica DistributieTransilvania Sud, Electrica Distributie Muntenia Nord, GDF Suez Energy Romania, E.ON Gaz Distributie	RAB- regulated utilities	-Regulated Asset Base (RAB)-based valuation; EV/RAB target multiple
Aeroporturi Bucuresti, Administratia Porturilor Maritime, Posta Romana, Salrom	Other holdings (Airports, Port Authorities, Postal services)	-Peer multiple (EV/EBITDA, EV/Sales, PE, P/BV)

Source: Erste Group Research

- Listed companies were included in Fondul Proprietatea's NAV at market values as of March 7, 2014.

- The lack of relevant guidance on the business of key unlisted companies, as well as uncertainties regarding their outlook, made the DCF valuation imperfect. The unlisted companies were therefore valued based on the market multiples method.

- Considering the key parameters for the sectors analyzed, our approach was to value the most important unlisted companies using specific metrics (where available) for relevant peer companies: EV/Electricity Output & EV/Installed Capacity (electricity production), EV/RAB (electricity & gas distribution grids).

- For those companies for which we did not use specific metrics, the fair value was computed based on the most appropriate market multiples (EV/EBITDA, P/E, P/BV) at which their peers were traded.

Main unlisted holdings valuation

Company	Former fair value of equity* (EUR mn)	New fair value of equity (EUR mn)	Value of equity assigned by FP** (EUR mn)
Electricity production			
Hidroelectrica	2,803	1,396	2,500
CE Oltenia	620	251	332
Electricity distribution & supply			
E.ON Moldova Distributie	247	289	349
Electrica Distributie Muntenia Nord	221	236	300
ENEL Distributie Muntenia	839	717	877
Electrica Distributie Transilvania Nord	182	162	209
Electrica Distributie Transilvania Sud	191	171	194
ENEL Distributie Banat	329	361	529
ENEL Distributie Dobrogea	250	267	350
Gas distribution & supply			
E.ON Gaz Distributie	343	217	306
GDF Suez Energy Romania	716	385	750
Other			
Posta Romana	52	119	54
Societatea Nationala a Sarii Salrom	137	77	48
Aeroporturi Bucuresti (Otopeni, Baneasa)	351	333	320
Administratia Porturilor Maritime	152	101	74

**) Fair value according to our previous report on Fondul Proprietatea*
***) December 2013, excepting for Hidroelectrica which was evaluated as of February 2014*
Source: Erste Group Research

Fair value of unlisted holdings

Company	Asset category	Value of Equity		Stake held by FP	Value in FP Portfolio		Weight in total assets
		EURmn	RONmn		EURmn	RONmn	
Electricity production							
Hidroelectrica	2	1,396	6,271	19.9%	278	1,250	9.9%
CE Oltenia	2	251	1,126	21.5%	54	243	1.9%
Electricity distribution & supply							
ENEL Distributie Muntenia	4	717	3,221	12.0%	86	386	3.1%
ENEL Distributie Banat	4	361	1,623	24.1%	87	392	3.1%
E.ON Moldova Distributie	4	289	1,297	22.0%	64	285	2.3%
ENEL Distributie Dobrogea	4	267	1,200	24.1%	64	289	2.3%
Electrica Distributie Muntenia Nord	4	236	1,060	22.0%	52	233	1.8%
Electrica Distributie Transilvania Nord	4	162	728	22.0%	36	160	1.3%
Electrica Distributie Transilvania Sud	4	171	770	22.0%	38	169	1.3%
Gas distribution & supply							
E.ON Gaz Distributie	4	217	975	12.0%	26	117	0.9%
GDF Suez Energy Romania	4	385	1,730	12.0%	46	208	1.6%
Other unlisted							
Aeroporturi Bucuresti (Otopeni, Baneasa)	6	333	1,496	20.0%	67	299	2.4%
Societatea Nationala a Sarii Salrom	6	77	346	49.0%	38	169	1.3%
Posta Romana	6	119	535	25.0%	30	134	1.1%
Administratia Porturilor Maritime	6	101	453	20.0%	20	91	0.7%
Total				-	**985**	**4,425**	**35.1%**

Source: Fondul Proprietatea, Erste Group Research

Market value of holdings in listed companies*

Company	BSE ticker	Asset category	Specific expertise	Market capitalization		Stake held by FP	Value in FP portfolio		Weight in total assets
				EURmn	RONmn		EURmn	RONmn	
OMV Petrom	SNP	3	Oil & Gas (E&P, R&M)	5,534	24,867	19.0%	1,051	4,722	37.4%
Romgaz	SNG	3	Gas production	2,852	12,815	15.0%	428	1,921	15.2%
Nuclearelectrica	SNN	2	Nuclear pow er production	568	2,550	9.7%	55	248	2.0%
BRD GSG	BRD	5	Banking	1,351	6,070	3.6%	49	221	1.8%
Transelectrica	TEL	4	Electricity transmission	258	1,157	13.5%	35	156	1.2%
Banca Transilvania	TLV	5	Banking	853	3,830	2.9%	25	112	0.9%
Alro Slatina	ALR	6	Aluminum production	207	929	10.2%	21	95	0.8%
Raiffeisen Bank International	RBI	5	Banking	4,458	20,029	0.3%	15	68	0.5%
Erste Group Bank	EBS	5	Banking	10,886	48,911	0.1%	11	49	0.4%
Other listed	-	-	-	-	-	-	37	168	1.3%
TOTAL							**1,727**	**7,760**	**61.5%**

**) Computed according to last closing price*
Source: Bucharest Stock Exchange, Erste Group Research

Top 25 holdings

No.	Company	Sector	Listed/ Unlisted	Asset category	Stake held by FP	Value of the stake held by FP (EUR mn)	Weight in total assets
1	OMV Petrom	Oil & Gas (E&P, R&M)	Listed	3	19.0%	1,051.0	37.4%
2	Romgaz	Gas production	Listed	3	15.0%	427.5	15.2%
3	Hidroelectrica	Electricity production	Unlisted	2	19.9%	278.3	9.9%
4	ENEL Distributie Banat	Electricity production	Unlisted	4	24.1%	87.1	3.1%
5	ENEL Distributie Muntenia	Electricity distribution & supply	Unlisted	4	12.0%	86.0	3.1%
6	Aeroporturi Bucuresti (Otopeni, Baneasa)	Airport operator	Unlisted	6	20.0%	66.6	2.4%
7	ENEL Distributie Dobrogea	Electricity distribution & supply	Unlisted	4	24.1%	64.3	2.3%
8	E.ON Moldova Distributie	Electricity distribution & supply	Unlisted	4	22.0%	63.5	2.3%
9	Nuclearelectrica	Electricity production	Listed	2	9.7%	55.2	2.0%
10	CE Oltenia	Electricity production	Unlisted	2	21.5%	54.0	1.9%
11	Electrica Distributie Muntenia Nord	Electricity distribution & supply	Unlisted	4	22.0%	51.9	1.8%
12	BRD GSG	Banking	Listed	5	3.6%	49.2	1.8%
13	GDF Suez Energy Romania	Gas distribution & supply	Unlisted	4	12.0%	46.2	1.6%
14	Societatea Nationala a Sarii Salrom	Salt production	Unlisted	6	49.0%	37.7	1.3%
15	Electrica Distributie Transilvania Sud	Electricity distribution & supply	Unlisted	4	22.0%	37.7	1.3%
16	Electrica Distributie Transilvania Nord	Electricity distribution & supply	Unlisted	4	22.0%	35.7	1.3%
17	Transelectrica	Electricity transmission	Listed	4	13.5%	34.8	1.2%
18	Posta Romana	Postal services	Unlisted	6	25.0%	29.8	1.1%
19	E.ON Gaz Distributie	Gas distribution & supply	Unlisted	4	12.0%	26.0	0.9%
20	Conpet	Crude oil transport	Listed	6	29.7%	25.8	0.9%
21	Banca Transilvania	Banking	Listed	5	2.9%	25.0	0.9%
22	Alro Slatina	Aluminum production	Listed	6	10.2%	21.1	0.8%
23	Administratia Porturilor Maritime	Port operator	Unlisted	6	20.0%	20.2	0.7%
24	Raiffeisen Bank International	Banking	Listed	5	0.3%	15.2	0.5%
25	Erste Group Bank	Banking	Listed	5	0.1%	10.9	0.4%

Source: Fondul Proprietatea, Erste Group Research

Top dividend payers

2011		2012		2013*	
Company	**RON mn**	**Company**	**RON mn**	**Company**	**RON mn**
OMV Petrom	201.62	OMV Petrom	353.13	OMV Petrom	318.95
Romgaz	106.01	Romgaz	140.64	Romgaz	158.94
Hidroelectrica	52.48	Transgaz	52.52	Transgaz	37.57
Transgaz	50.77	Alro	19.38	GDF Suez Energy Romania	22.80
ENEL Distributie Banat	20.16	Transelectrica	10.88	Electrica Distributie Muntenia Nord	16.21
Primcom	14.28	Aeroportul Henri Coanda	9.42	CE Oltenia	12.31
ENEL Distributie Dobrogea	13.53	Conpet	6.61	Societatea Nationala a Sarii	9.30
Alro	13.46	Administratia Porturilor Maritime	6.57	Electrica Furnizare	9.26
Aeroportul Henri Coanda	9.93	CE Rovinari	6.46	CN Aeroporturi Bucuresti	9.14
Conpet	6.98	Raiffeisen Bank	3.85	Conpet	8.40
Others	29.84	Others	9.53	Others	46.82

**) Fondul Proprietatea 3Q13 report*
Source: Fondul Proprietatea, Erste Group Research

Corporate profile update

Fondul Proprietatea was actually an active investor in 2011, especially in domestic banks and foreign banks with exposure to Romania. The closed-end fund invested over EUR 130mn in Banca Transilvania, BRD-GSG, Erste Group Bank and Raiffeisen Bank.

Franklin Templeton put new investments on hold since 2012, with assets disposals only topic on fund manager's agenda, due to the strategy imposed by shareholders

Since the GSM of April 2012, US hedge fund Elliott, the main shareholder of FP, has become more visible and has actually managed to impose upon FP's strategy to a large extent, with a key principle being that the major objective of Fondul has to be the reduction of trading discount supported by the use of two tools: buyback programs and additional dividend distributions. From that point on, Franklin Templeton stopped investment plans, with the official message assumed by the fund manager being that the best FP investment is in its own shares, due to the high trading discount. The only investment made by Franklin Templeton since then has been in Nuclearelectrica shares, with the closed-end fund exercising its pre-emption rights within the nuclear power producer's share capital increase associated with the IPO.

Since 2013, Fondul Proprietatea has started to sell from its key holdings, in order to support the financing of the second buyback program, which has absorbed around RON 963mn (EUR 215mn). The main deals in 2013 were the sale of a 1% stake in Petrom, as well as the disposal of the entire 15% holding in Transgaz, with proceeds from the two transactions reaching EUR 125mn. As we have previously explained, one or several major transactions of up to 10% of Petrom shares seem likely before the end of the year, with Franklin Templeton following to use buybacks and/or cash distributions in order to meet the 15% discount target.

Fondul Proprietatea investments since listing

Ticker	Company	Date	Stake purchased in 3M period ending	Value of investment (RON mn)	Stake held in company at end of period
BRD	BRD-Groupe Societe Generale	1Q11	1.13%	96.78	1.69%
BRD	BRD-Groupe Societe Generale	2Q11	0.55%	53.17	2.24%
BRD	BRD-Groupe Societe Generale	3Q11	1.37%	95.16	3.60%
BRD	BRD-Groupe Societe Generale	4Q11	0.04%	2.60	3.64%
EBS	Erste Group Bank AG	1Q11	0.26%	138.82	0.25%
EBS	Erste Group Bank AG	2Q11	0.07%	34.09	0.32%
TLV	Banca Transilvania	2Q11	0.13%	2.01	0.12%
TLV	Banca Transilvania	3Q11	2.18%	31.19	2.30%
TLV	Banca Transilvania	4Q11	0.63%	8.42	2.93%
RBI	Raiffeisen Bank International AG	1Q11	0.43%	133.75	0.43%
RBI	Raiffeisen Bank International AG	2Q11	0.12%	30.63	0.55%
COTE	Conpet	3Q11	9.64%	25.88	29.69%
AZO	Azomures	1Q11	1.07%	3.54	8.75%
AZO	Azomures	2Q11	1.98%	8.24	10.74%
AZO	Azomures	3Q11	0.35%	1.49	11.09%
AZO	Azomures	4Q11	0.03%	0.21	11.12%
SNN	Nuclearelectrica	3Q13	Preemption rights before IPO	30.6	9.73%
Total investments (RON mn)				**696.6**	
Total investments (EUR mn)				**154.8**	

Source: Fondul Proprietatea, BSE, Erste Group Research estimates

Fondul Proprietatea exit deals since listing

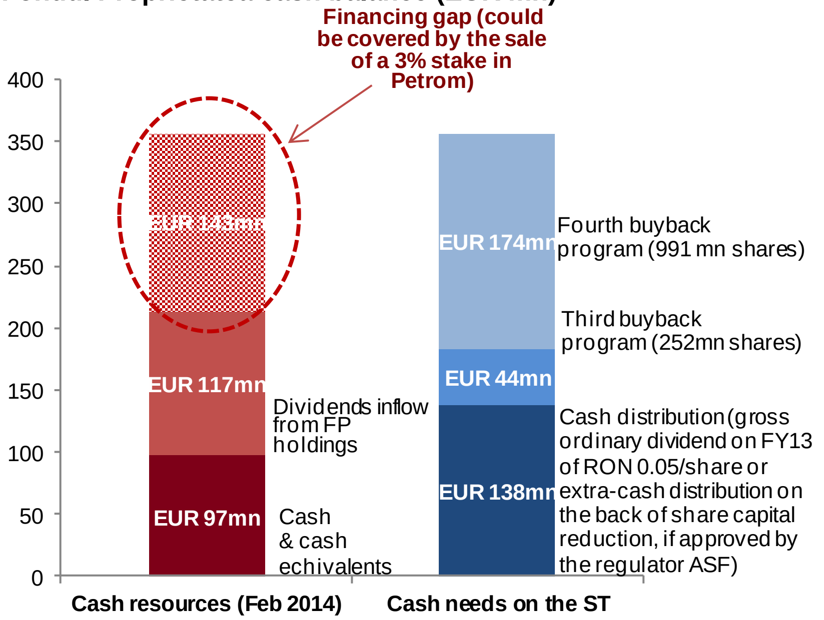
Ticker	Company	Date	Stake sold in 3M period ending	Value of divestment (RON mn)	Stake held in company at end of period
EBS	Erste Group Bank AG	2Q12	-0.21%	49.44	0.10%
RBI	Raiffeisen Bank International AG	2Q12	-0.12%	22.23	0.43%
AZO	Azomures	2Q12	-11.13%	129.94	0.00%
SNP	Petrom	17.05.2013	-1.11%	246.7	18.99%
TGN	Transgaz	12.12.2013	-14.98%	303.5	0.00%
Disinvestments from Banks (RON mn)				**71.7**	
Disinvestments from Banks (EUR mn)				**15.9**	
Total disinvestments (RON mn)				**751.8**	
Total disinvestments (EUR mn)				**167.1**	

Source: Fondul Proprietatea, BSE, Erste Group Research estimates

Cash deficit of around EUR 140mn in short term, if we are including the financing needs for the announced buyback programs

In addition to the cash needs required by the ordinary dividend distribution or extra cash distribution of RON 0.05/share (if approved by ASF), FP has for this year a cash deficit of almost EUR 140mn, including the cash needs for financing its buyback programs.

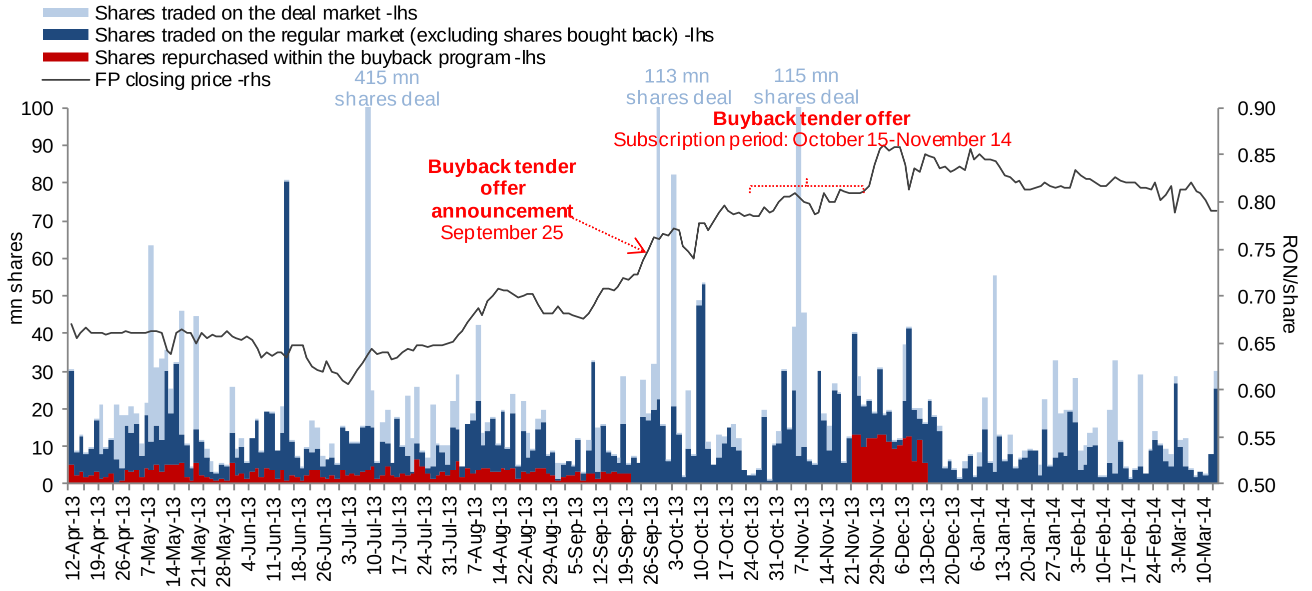
Fondul Proprietatea cash balance (EUR mn)



Note:
1) Ordinary dividend on FY13 or extra cash distribution of RON 0.05 /share
2) FP shares were considered to be redeemed at the current price (RON 0.79/share)
Source: Fondul Proprietatea, BSE, Erste Group Research

Fondul announced that on February 21 the ASF endorsed the decrease of the subscribed share capital by 1.8% through the cancelling of shares repurchased by the fund within its first buyback program, which ended in 2011. The ASF approval allows the asset manager to initiate the third buyback program, targeting the repurchase of 252mn shares (1.9% of all outstanding shares). According to FP's official release, the program will be initiated as soon as shareholder approval is published in the Official Gazette. The approval effectively unlocks the third buyback program, which targets a share volume almost equal to that in the first buyback.

Volumes of Fondul Proprietatea shares traded on the Bucharest Stock Exchange (April 2013 - March 2014)



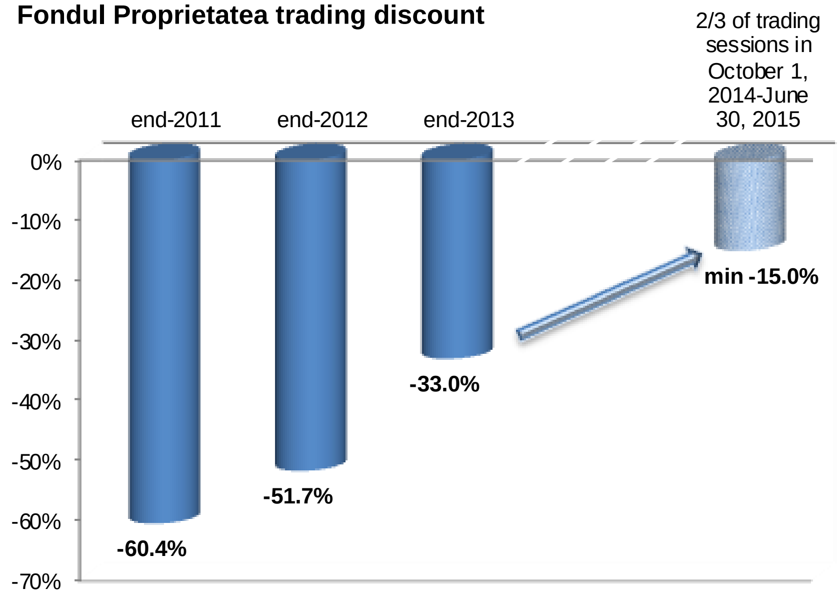
Source: Bucharest Stock Exchange, Erste Group Research

New major buyback program to be proposed at next GSM in April

The acquiring of its own shares will continue to be used by Franklin Templeton as the main tool to support FP's share price. At the GSM scheduled for April 28, 2014, Franklin Templeton proposed to shareholders the initiation of a fourth buyback program targeting the redemption of 990.85mn shares after the completion of the third buyback program. The buyback will be run over an 18-month period.

At the next GSM, it is likely that shareholders will approve the cancellation of shares representing 7.9% of the share capital acquired within the second buyback program and the initiation of the fourth buyback program. The buyback pipeline could thus become a strong supporter of the FP share price and the main dummy for stock demand. The buybacks could be more or less aggressive, depending on the effective implementation of the extra cash distribution initiative.

Fondul Proprietatea trading discount



Source: Fondul Proprietatea, BSE, Erste Group Research

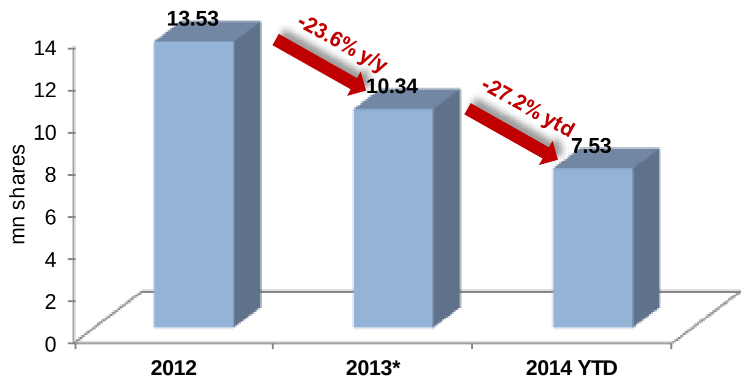
A natural consequence of running buyback programs is the contraction of stock liquidity on the market. It is suggestive that the average liquidity of FP on the regular segment of the Bucharest market in 2014 was 7.5mn shares per trading session, 27% lower compared to 2013 and more than 44% lower compared to 2012 average volume on the regulated market.

FP share price in 2014 not helped by buyback program - major explanation for negative YTD share price performance

The share price was not helped this year by the buyback programs, an important detail when we look at the -5 % YTD share price performance. However, in order to meet the 15% discount target, the use of this tool is imperative, especially in the event that the extra cash distribution policy does not become effective (i.e. it is not approved by ASF).

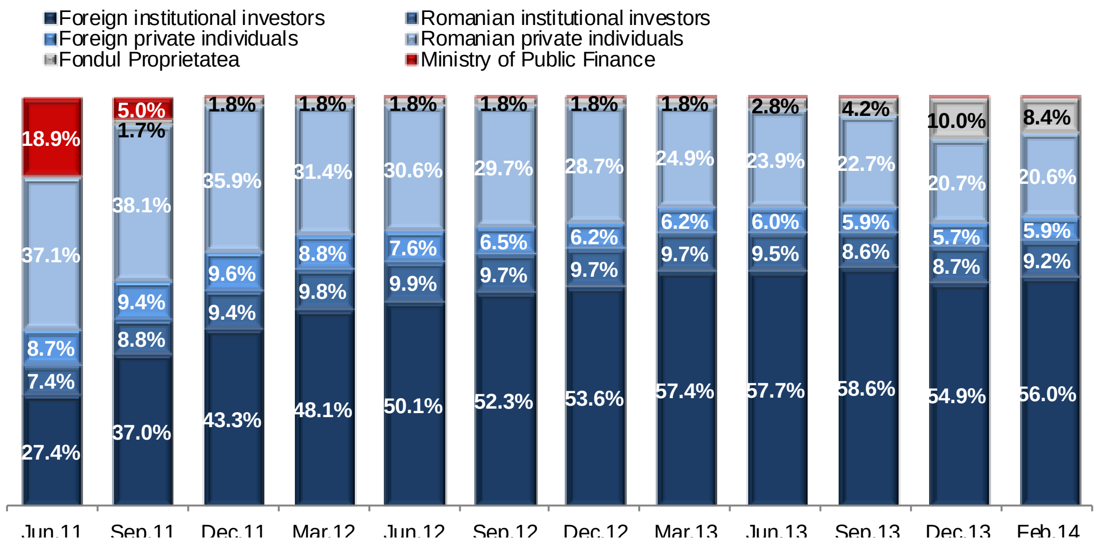
We mentioned that, over the period when the second buyback was run (April – December 2013), the share price increased by more than 25%. The impact of the second buyback on the share price return in 2013 was definitely major. The secondary listing of Fondul shares on the London Stock Exchange, as Franklin Templeton proposes, would support the share price, but, on the other hand, it would negatively impact liquidity on the Bucharest market.

Fondul Proprietatea volume on regular market



**excluding shares volumes repurchased within the second buyback program*
Source: Bucharest Stock Exchange, Erste Group Research

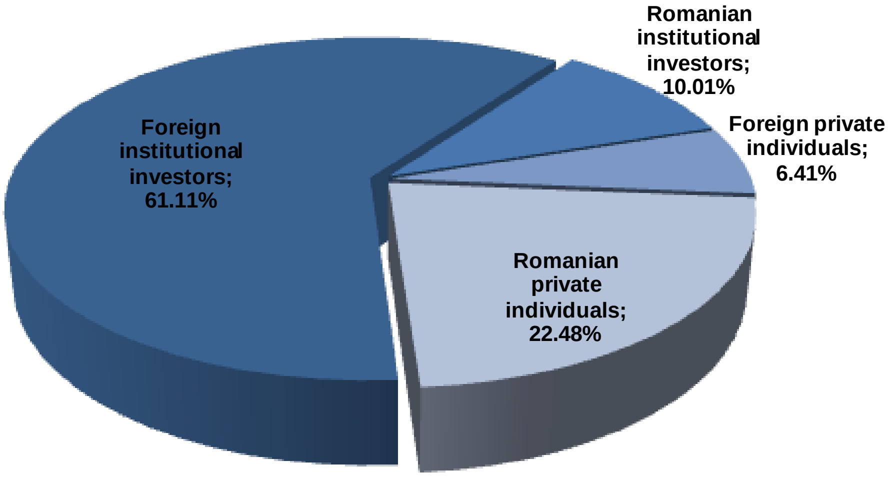
Fondul Proprietatea shareholder breakdown development



Source: Fondul Proprietatea, Erste Group Research

Foreign institutional shareholders actually increased their weight in share capital of FP to over 60% (if own shares acquired not taken into account)

Fondul Proprietatea shareholder breakdown (February 2014)



Note: Shares repurchased within the two buyback programs were considered cancelled
Source: Fondul Proprietatea, Erste Group Research

Key P&L figures Romanian Accounting Standards (RAS)

Indicator (RON mn)	2010	2011	2012	2013p
Revenues from dividends	179.0	519.1	619.0	649.7
Revenues on disposal of financial investme	0.0	13.4	208.1	573.1
Capital gains on disposal of financial investr	0.0	8.8	13.1	44.4
Provision reversals	217.4	30.5	5.6	48.3
Interest revenues	131.5	41.1	34.9	36.1
Total revenues	576.6	617.9	871.7	1,311.2
Total fund operating expenses	52.0	55.1	59.6	87.0
Depreciation & provision expenses	0.2	11.7	49.7	13.0
Total expenses	109.2	72.3	304.8	629.0
Gross profit	467.4	545.6	567.0	682.2
Income tax	11.2	1.8	0.0	0.0
Net profit	456.2	543.8	567.0	682.2

Source: Fondul Proprietatea, Erste Group Research

Official NAV - NSC (norm no. 4/2010 for 2011 and no. 11/2012 for 2012 and 2013)

Indicator (RON mn)	Dec-10	Dec-11	Dec-12	Dec-13	Feb-14
Fixed assets, out of which	**9,175.9**	**9,169.4**	**8,151.6**	**6,385.9**	**6,251.7**
Intangible assets		0.0	0.3	0.8	0.7
Tangible assets	0.0	0.0	0.0	0.0	0.0
Financial fixed assets, out of which	9,175.9	9,169.4	8,151.3	6,385.1	6,251.0
Listed shares	30.8	18.8	35.0	10.0	10.1
Unlisted shares	9,145.0	9,150.6	8,116.3	6,375.1	6,240.9
T-Bonds	0.0	0.0	0.0	0.0	0.0
Bank deposits	0.0	0.0	0.0	0.0	0.0
Municipal bonds	0.0	0.0	0.0	0.0	0.0
Corporate bonds	0.0	0.0	0.0	0.0	0.0
Mutual funds units (UCITS and NON-UCITS)	0.0	0.0	0.0	0.0	0.0
Other financial assets	0.1	0.0	0.0	0.0	0.0
Current assets, out of which	**6,235.9**	**5,352.4**	**6,865.4**	**8,688.3**	**8,387.5**
Receivables	6.0	55.0	2.6	2.8	2.0
Cash & equivalents	7.2	1.9	1.9	5.6	1.4
Short term financial investments, out of which	4,903.5	4,803.2	6,088.9	8,234.2	7,948.4
Listed shares	4,903.5	4,803.2	6,088.9	8,234.2	7,948.4
Unlisted shares	0.0	0.0	0.0	0.0	0.0
T-Bills	248.0	195.9	454.7	213.6	319.92469
Bank deposits	1,071.3	296.4	317.3	232.1	115.8
Municipal bonds	0.0	0.0	0.0	0.0	0.0
Corporate bonds	0.0	0.0	0.0	0.0	0.0
Mutual fundss units (UCITS and NON-UCITS)	0.0	0.0	0.0	0.0	0.0
Other financial assets	0.0	0.0	0.0	0.0	0.0
Derivatives financial instruments	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Prepaid expenses	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Total assets	**15,411.9**	**14,521.8**	**15,017.1**	**15,074.2**	**14,639.2**
Total liabilities	**69.3**	**42.2**	**21.1**	**31.2**	**22.3**
Provisions	**14.4**	**14.2**	**16.8**	**29.3**	**13.2**
Unearned revenue	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Equity	**15,328.2**	**14,465.4**	**14,979.2**	**15,013.7**	**14,603.7**
Off-balance sheet	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Net Assets Value (NAV)	**15,328.2**	**14,465.4**	**14,979.2**	**15,013.7**	**14,603.7**
NAV per share (RON)	**1.1124**	**1.0788**	**1.1371**	**1.2436**	**1.2097**

Source: Fondul Proprietatea, Erste Group Research

Romanian energy market

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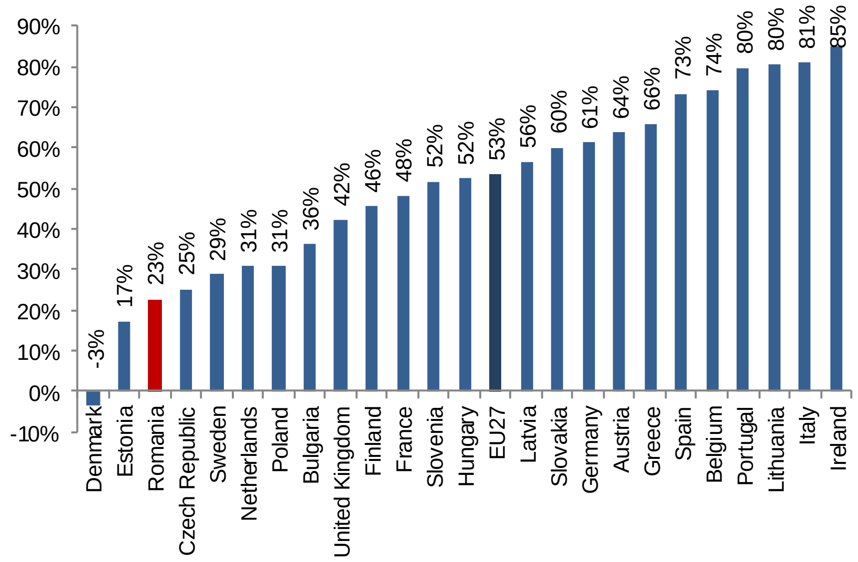
Romanian energy market

Low import dependence for energy-intensive economy

Romanian industrial consumers to pay fully liberalized energy price, with no option of indirect subsidy mechanisms

Romania is the third-last European country in terms of primary energy import dependence, but owning significant hydrocarbon resources cannot effectively protect the domestic manufacturing industry starting from 2015, when industrial consumers are to pay a fully liberalized energy price. Energy import dependence has been even lower as of last year, after a severe contraction of gas imports by around 40% y/y.

Energy dependence rate 2012 (%)



Source: Eurostat, Erste Group Research computes

Romanian authorities agreed a clear timetable with the IMF, EU and World Bank to entirely liberalize power and gas markets by end 2014 for industrial consumers and by end 2018 for households.

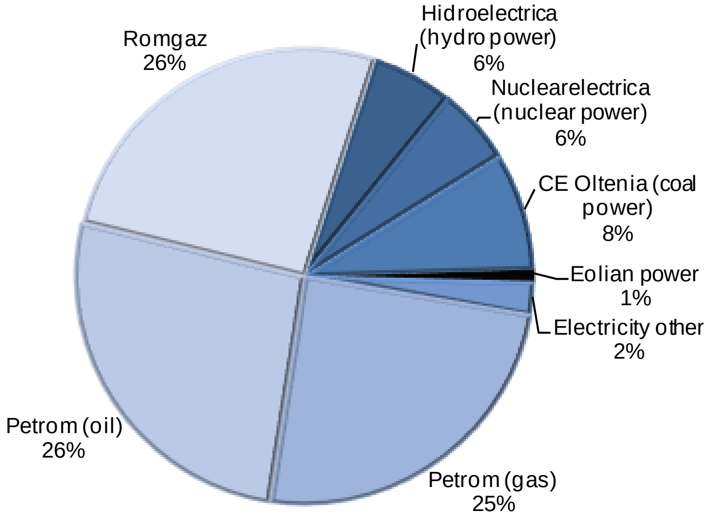
Romania assumed to completely liberalize energy market by 2018, IFIs agreed with direct governmental subsidies for vulnerable households

The complete removal of regulated prices will be a delicate topic for 2014 and 2015 for industrial gas consumers, while, in the case of power market, the price is already fully liberalized since January 2014 for non-residential consumers, without any negative impact on their production costs due to the collapse of electricity price since 2013.

In comparison with industrial consumers, the impact of the liberalization of the power and gas market on households is much more under the control of the government. The IFIs agreed that the government can designate 'vulnerable consumers' who will be eligible to receive a direct subsidy to counteract the higher energy price.

High reliance (over 50%) of domestic gas consumption on primary Romanian energy resources draws attention to high impact of gas market liberalization on disposable consumer income

Contribution of energy producers to domestic consumption (2012)

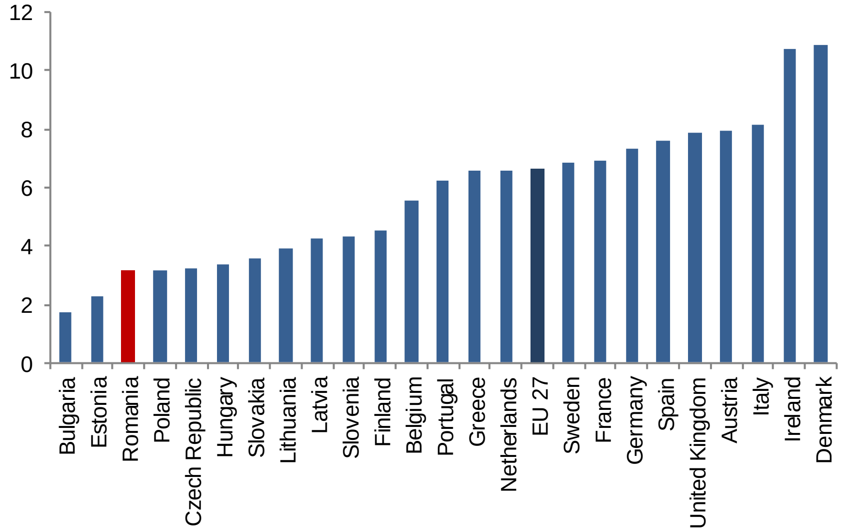


Note 1: Imports of oil products or internal oil products refined from imported oil were not considered
Note 2: Electricity from gas-fueled power plants was not considered
Source: ANRE, Companies, Erste Group Research

Romania is an energy-intensive economy, so there is huge room for reducing energy consumption via the implementing of energy efficiency measures in the medium and long term. The consumption of one tonne of oil equivalent (toe) in Romania generates gross value added of EUR 3mn, which is closer to its peers such as the Czech Republic, Poland and Hungary and well below the EU-27 average of EUR 6.7mn.

Substantially lower gas price paid by Romanian industrial consumers compared with EU competitors does not result in higher domestic industrial productivity

Gross value added / Gross inland consumption 2011 (EUR mn/toe)



Source: Eurostat, Erste Group Research

Power market

Demand dropping, outlook remains gloomy

Power consumption fell around 7% in 2012 and 6% in 2013, demand outlook remains weak

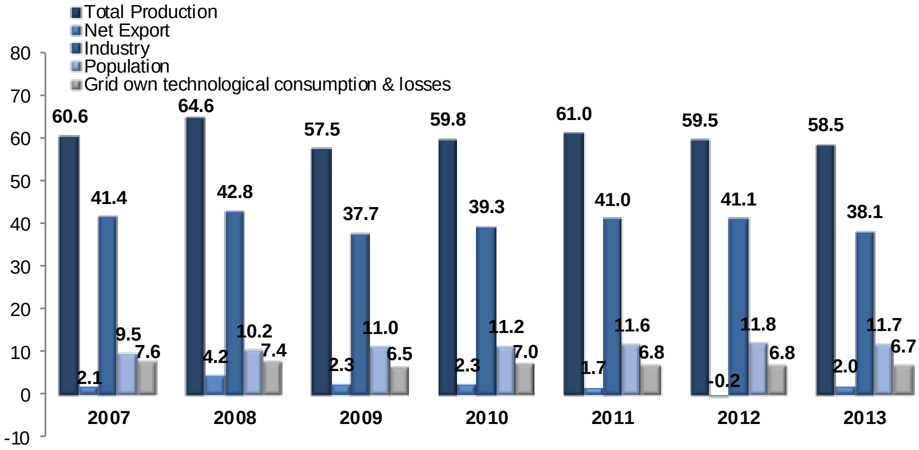
Power production plummeted by 1.7% y/y in 2013, after an annual contraction of 2.5% in 2012. The amplitude of power production reduction is the largest since 2009, when an adjustment of 11% y/y marked the severe impact of the financial crisis on the domestic economy. The foremost reason for the power production contraction is the drop in industrial consumption (-10% y/y in January-November 2013, after flat evolution in 2012). Romanian industrial consumption actually reached 2009 levels last year, but the structure of non-residential consumption has fundamentally changed in the meantime.

In the coming years, we envisage that power consumption will remain depressed, with significant influence coming from destocking pressures in heavy industry (the situation is similar in other CEE countries). On the other hand, there is expected to be concrete impact from the gradual capitalization of the large existing space for improvements in energy efficiency for industrial consumers and in transmission and distribution grids. It is worth mentioning that the weight of own consumption and losses within the power infrastructure network account for over 12% of total electricity produced, highlighting the CAPEX needs for the modernization and rehabilitation of old transmission and distribution grids. Energy efficiency investments will thus inevitably put pressure on electricity demand in the LT.

Despite the fact that Romania was traditionally a power exporter, lower internal demand cannot be offset by exports due to sluggish demand on European power markets, which restricts selling opportunities abroad. The stagnation of power production appears to be an optimistic scenario, while annual contractions of up to 2% would be a relatively pessimistic scenario for power production in Romania in the medium term.

Major room for energy efficiency improvements to cap domestic power demand in long run

Gross power production, net exports and consumption development 2007-13 (TWh)



Source: National Institute of Statistics, Erste Group Research

Eolian boom forced new market reality

Eolian boom created durable oversupply conditions, even in relatively modest hydrological year

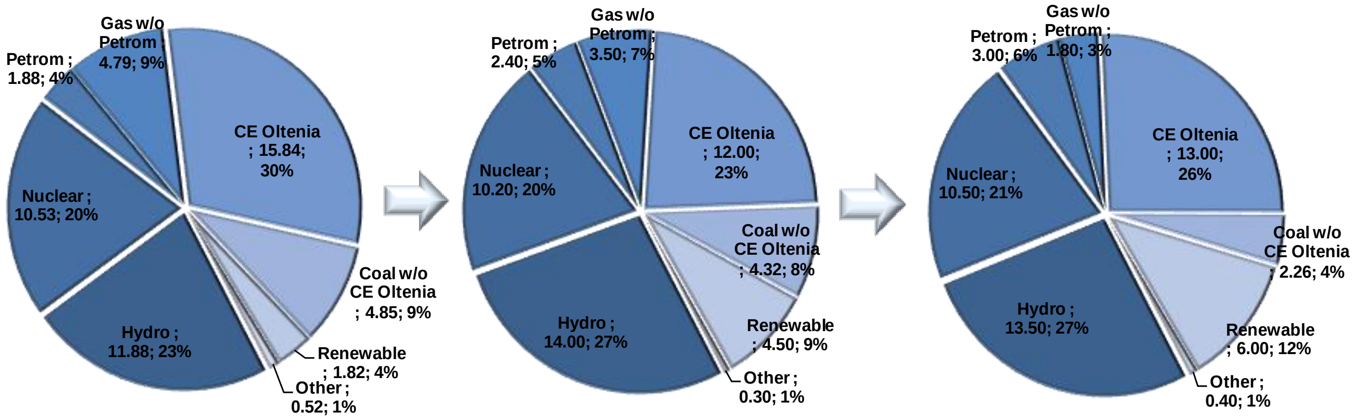
The over-generous subsidy scheme for renewable energy has already fed an eolian boom and exerted a complex influence on the power market, forcing the government to look for different ways to favor those coal-fired power producers which severely lost market share starting in 2013. The subsided renewable power has priority over electricity from other sources in terms of accessing transmission/distribution grids, which directly results in a cut in conventional power producers' output.

Wind power attracted significant investments of over EUR 3.5bn, with electricity production of eolian units advancing from almost zero in 2009 to 2,600 MW as of the end of December 2013. Strategic investors (such as CEZ, EDP Renovables, Iberdrola and ENEL) are the most important players in the domestic wind farms sector. Following investments worth EUR 1.1bn between 2010 and 2012, CEZ currently holds – in Dobrogea (a province in the southeast of the country) – one of the largest European wind farms, with an IC of 600 MW. CEZ alone estimated its 2013 production to be about 1 TWh, out of a total quantity of 4.5 TWh estimated as output of renewables. The second largest renewable technology which has been extensively developed is photovoltaic generation – with an IC of 1,124.3 MW as of the end of 2013 (most of the solar units became operational last year).

Market share of coal-fired power producers (CE Oltenia) harshly adjusted since 2013

In July 2013, the government decided to modify the support scheme for renewable energy, postponing until after 2018 the effective payment for one of the two green certificates received for each MWh in wind farms produced over the period from July 2013 to December 2017. Romanian authorities attempted to reduce the impact of extensive renewable projects (mainly wind and photovoltaic solar energy) on the final consumer bill, which reached around 10% weight in the final power price. However, the initiatives planned by the Romanian government remain unclear, with the mechanism of the actual recovery of the lost subsidies by the owners of the renewable units still remaining under question.

Production breakdown 2012 (TWh) **Production breakdown 2013e (TWh)** **Production breakdown 2014e (TWh)**



Source: ANRE, Erste Group Research

Besides the wind power boom, there are two other factors which have a severe impact on the structure of the power market. On the one hand, the full commercial operation of Petrom's greenfield combined cycle gas turbine (CCGT), with an IC of 850 MW, should result into additional at least 4 TWh per year, with a targeted market share of 8-9% being the official objective of the oil & gas producer. Petrom's key objective is to capitalize its CCGT technical flexibility for balancing the power system, selling its output on the balancing market, where the most expensive power is traded.

Renewable energy and Petrom's CCGT might provide up to 10 TWh starting in 2014, fundamentally changing power generation mix

On the other hand, looking at the production mix of the Romanian power market, it is mandatory to consider that the gross hydro power output is over 15 TWh in a medium hydrological year, as was the case in 2013, compared to the severe drought of 2012, when hydro power plant's contribution reached a historical minimum of 13.2 TWh. 2014 seems to be a relative weak hydrological year, with the output estimated by Hidroelectrica at 13.5 TWh.

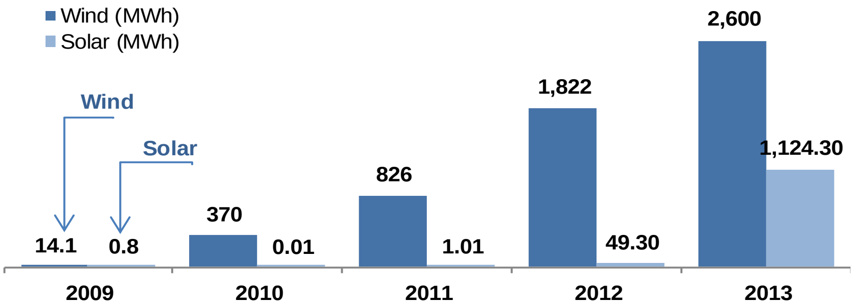
Under the new market circumstances, the lignite-fired power producer CE Oltenia, has faced a severe market share contraction since 2013, as direct effect of large-scale wind farms commissioning, as well as due to its production costs, which are much higher than those of other large power producers, namely Hidroelectrica, Nuclearelectrica and Petrom's CCGT (which exclusively uses gas from own production).

Obviously, 2013 was not only a 'special' year for the power market: the significant drop in coal producers' market share is also part of the new reality in the power generation sector.

Green energy changed power generation mix

Apart from the impact on the production mix, a complementary problem is that, jointly with the generous subsidy mechanism for renewable energy, Romanian authorities have omitted stimulating investment efforts in new units (especially gas) necessary in order to balance the volatile eolian power. The sensitive subject of the effective absorption capacity of wind farms' production by national transmission grids was neglected in the energy law and, consequently, the transmission and system operator Transelectrica provided connection permits for an IC of 8,000 MW. Such a scale of wind power infrastructure is effectively a fantasy, firstly due to the lack of demand, and secondly due to the technical impossibility of Transelectrica to integrate more than 3,000 MW into the grid.

Wind farms and photovoltaic solar installed capacity development (2009-2013)



Source: ANRE, media

The irony is that even the size of the operational wind farms sector in 2013 of roughly 2,000 MW was overwhelming due to the imbalances induced in the grid, requiring the relatively intensive use in 2013 of lignite-fired units held by CE Oltenia in order to balance the national power system, a practice which is a cost-intensive process for the company.

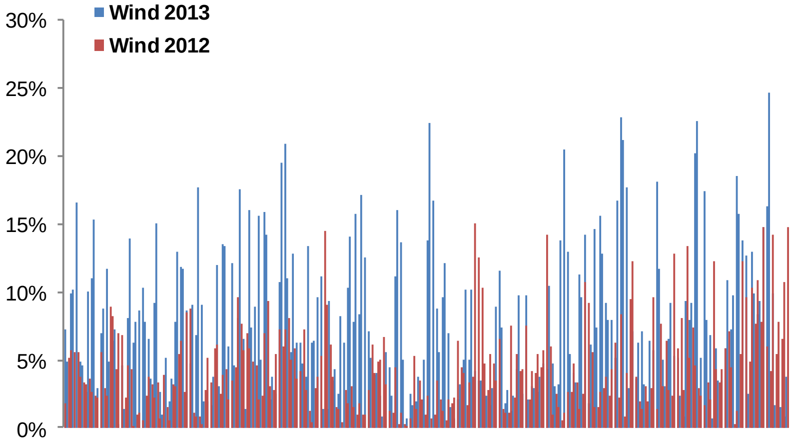
Dimensioning wind farms sector in connection with investments in system balancing capacities and enforcing transmission grid completely neglected

Romania has approved one of the most generous European support schemes for renewable energy, with two GC obtained by wind power for each MWh supplied into the network until 2017 and one GC per MWh onwards, with the duration of the support being 15 years. The eligible renewable sources participating in the GC trading system are hydro energy used in power plants with an IC of at maximum 10 MW, wind power, solar power, geo-thermal power, etc.

In the case of projects commissioned starting on January 1, 2014, the support scheme was cut by the regulator ANRE because of overcompensation. In the case of new projects, the support scheme was reduced from 2 to 1.5 GC for wind farms, from 6 to 4 GC for solar power and from 3 to 2 for micro hydro units.

In approx. three years, wind farms facilities rocketed from almost zero to around 2,700 MW currently

Wind generation units' weight in total used capacity



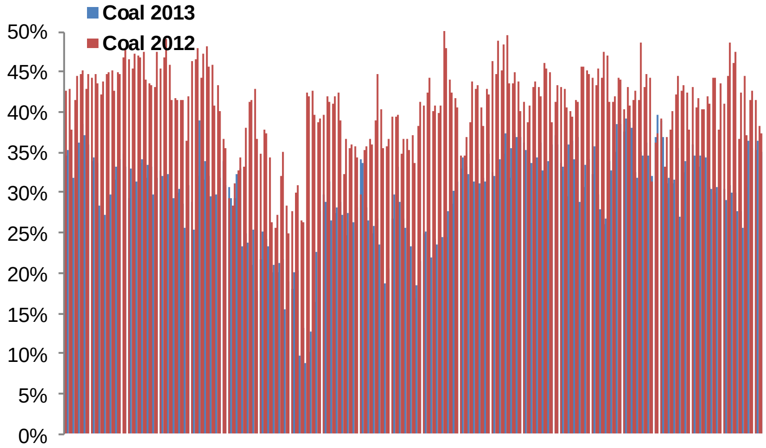
Source: Transelectrica, Erste Group Research

The price for GC was legally set from between EUR 27 to EUR 55. According to law, GC have to be mandatorily acquired by the electricity suppliers, which must ensure a certain amount of renewable energy for consumers, in gradually increasing weights, from 10% in 2011 to 20% in 2020. The GCs costs are ultimately passed on to the final consumer bill. As the weight of renewable energy in total electricity consumed in Romania is less than 10%, the demand for GC brought the market price close to the maximum legal value.

However, it also seems that the mandatory quota for acquiring green energy may be reduced by the government, which would create an oversupply of GCs, with a negative impact on their market price. This is why we believe that prices of GC may drop to the bottom of the regulated range of EUR 27-55 by 2017.

Old coal-fired producers most disadvantaged by subsidized renewable boom, due to much higher production costs compared to hydro and nuclear power producers

Coal generation units' weight in total used capacity



Source: Transelectrica, Erste Group Research

Power price drop on wholesale and spot markets

New lasting reality – oversupply conditions hit electricity price

Weak demand and new power producers entering the market last year (especially wind farms), as well as a good hydrological year put pressure on electricity prices on the day-ahead (spot) market and bilateral contracts (wholesale) market, which dropped last year up to an average of RON 160/MWh and RON 170-180/MWh, respectively, well below 2012's average level of about RON 220/MWh.

Spot market and effective wholesale power market pricing and volume

Day Ahead Market	2011	2012	2013
Volume (TWw h)	8.21	10.72	16.35
Average w eighted price (RON/MWh)	238.99	223.53	162.61
Average w eighted price (EUR/MWh)	56.26	50.23	37.31
Weight in net consumption (%)	16.18%	19.89%	31.50%
Electricity effectively provided based on year-ahead wholesale contracts	**2011**	**2012**	**2013**
Volume (TWh)	4.66	7.87	21.69
Average w eighted price (RON/MWh)	161.97	217.82	209.53
Average w eighted price (EUR/MWh)	38.27	48.86	47.35
Weight in net consumption (%)	9.18%	14.61%	41.79%

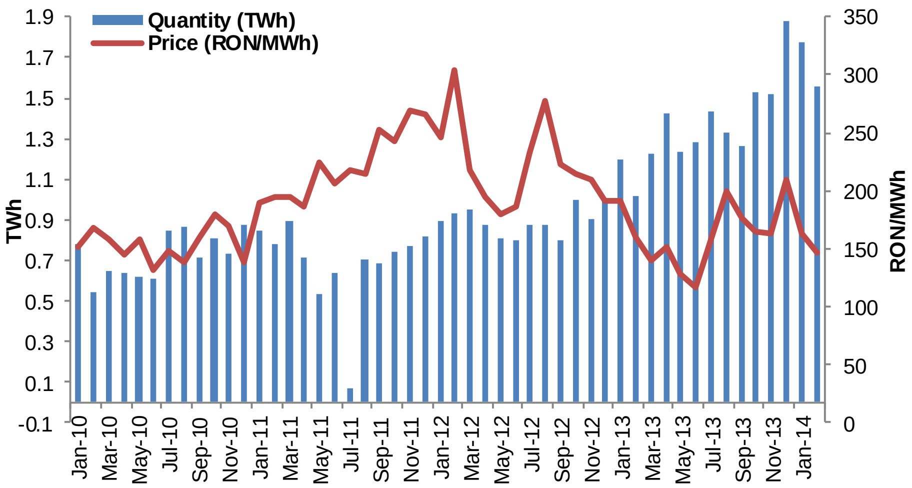
Source: OPCOM, Erste Group Research

Weak wholesale power price to be visible in power producers' P&L mainly starting in FY14

An important detail is that the new power price environment was reflected last year only to a limited extent by power producers' P&Ls. The explanation is that they sold power at effective wholesale prices based on forward contracts signed up to the end of 2012, which were well above the forward prices available on the power exchange since January 2014. The new low wholesale power prices will be transparent in the profitability of the power producers mainly starting with FY14.

Eolian boom puts direct pressure on spot power price

Day ahead (spot) market



Source: OPCOM, Erste Group Research

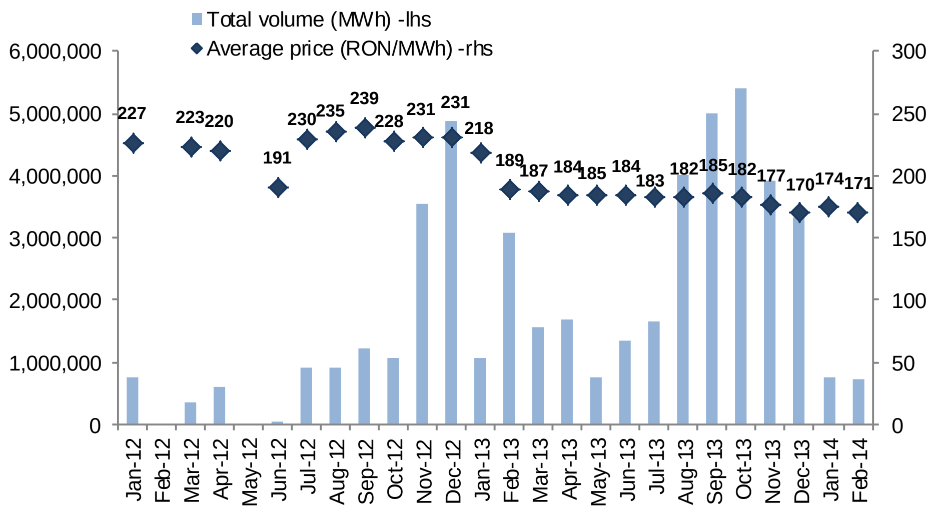
The average price on the spot market adjusted last year by more than 25% y/y, to RON 163/MWh, while the day-ahead market volume advanced by ten percentage points, mainly fuelled by cheap wind power.

Coming two years to see wholesale prices in Romania in the range RON 160-185/MWh (EUR 35-40/MWh)

The collapse of power price on the spot market incentivized last year industrial consumers to request the cancelling of forward contracts signed at the end of 2012 at prices above RON 200/MWh. Thus, they preferred to buy power on the day-ahead market at much lower prices. For instance, Nuclearelectrica disclosed the annulment of 23 contracts at an average selling price of RON 229.4/MWh, with clients paying penalties of about EUR 10mn in 1H13 in order to effectively access the new prices from the power exchange.

Liquidity and Price on OPCOM Wholesale Market (Bilateral Market of Contracts)

Romanian power pricing consistent with prices for benchmark year-ahead electricity contract from Germany (largest European market), which remain around EUR 37/MWh



Source: OPCOM, Erste Group Research

The power price on the wholesale market dropped towards RON 170/MWh (EUR 37/MWh) from an average weighted price of RON 231/MWh in December 2012. In the context of prolonged oversupply and weak demand, we have seen prices on the wholesale market in the range of RON 160-185/MWh for a long time. On the other hand, the volume of the wholesale segment will remain elevated compared to levels before 2012, when Hidroelectrica sold its electricity on the power exchange through unfair preferential contracts, at prices well below the market price.

Petrom's CGGT, Nuclearelectrica and Hidroelectrica will be more or less profitable even if the current electricity price condition persists, as we consider this to be the new reality in the power sector. On the other hand, at a price ranging between RON 160/MWh and RON 185/MWh, the sustainability of CE Oltenia and of other coal-fired power plants remains contentious, considering also the quantity for which those players can realistically find buyers.

Dropping power prices made liberalization process bearable for final consumers

Size of regulated market in 2014 is about 22% of total consumption

Power market liberalization assumes the phasing-out of the regulated market from 15.3 TWh in 2013 (~30% of total consumption) to zero until 2018.

The regulated market size is dimensioned in 2014 at around 11 TWh (~ 22% of the total estimated consumption), roughly fitting the estimated consumption of households, for which the liberalization process is still at the beginning. The liberalization of the power market for industrial consumers started in September 2012 and ended in 2013. As of January 2014, the market is fully liberalized for non-residential consumers. In the context of power price contraction since the beginning of 2013, the liberalization process for industrial consumers did not hurt their purchasing power at all.

On the other hand, with a 2014 basket price fixed on the regulated market at RON 155/MWh, the convergence towards a wholesale average market price of RON 170-180/MWh looks bearable for households, considering the current low price environment.

Power market for non-residential consumers is already fully liberalized as of January 2014, with market price collapse from 2013 leading to easy absorption

Liberalization calendar (competitive market as % of consumption)

Implementation date	Non Households	Households
Sep.12	15	0
Jan.13	30	0
Apr.13	45	0
Jul.13	65	10
Sep.13	85	10
Jan.14	100	20
Jul.14	100	30
Jan.15	100	40
Jul.15	100	50
Jan.16	100	60
Jul.16	100	70
Jan.17	100	80
Jul.17	100	90
Dec.17	100	100

Source: ANRE

In 2014, Hidroelectrica and Nuclearelectrica are obliged by the regulator ANRE to sell on the regulated market quantities of 5.4 TWh and 3.74 TWh. In the case of Hidroelectrica, the regulator set a price of RON 114/MWh (well below the wholesale market price of over RON 170/MWh), while for Nuclearelectrica the recognized price is RON 145.88/MWh.

Prices and quantities sold fixed for regulated market by ANRE

Company	Quantity (TWh)				Price (RON/MWh)				% of total production			
	2011	2012	2013	2014e	2011	2012	2013	2014e	2011	2012	2013	2014e
Hidroelectrica	3.87	4.10	3.97	5.40	86	71	125	114	21%	32%	27%	40%
Nuclearelectrica	6.85	7.50	5.31	3.74	129	131	142	146	62%	69%	50%	35%
CE Oltenia	7.70	3.03	2.46	0	n.a.	172	190.3	0	44%	30%	22%	0%

Source: Companies, ANRE, Fondul Proprietatea, Erste Group Research

Nuclearelectrica was main beneficiary of liberalization process in 2013 and 2014

Hidroelectrica was by far the most disadvantaged power producer, considering that, in accordance with the decision of the regulator, it enjoyed the lowest price (well below market price) for electricity sold on the regulated market. Moreover, the regulator imposed a higher quantity to be sold this year on the regulated market of 5.4 TWh (compared with 4 TWh in 2013), while the selling price was adjusted to RON 114/MWh (from RON 125/MWh previously). On the contrary, in the case of Nuclearelectrica, the regulator reduced for the 2012-14 period the quantity demanded to be sold on the regulated market, gradually recognizing higher selling prices.

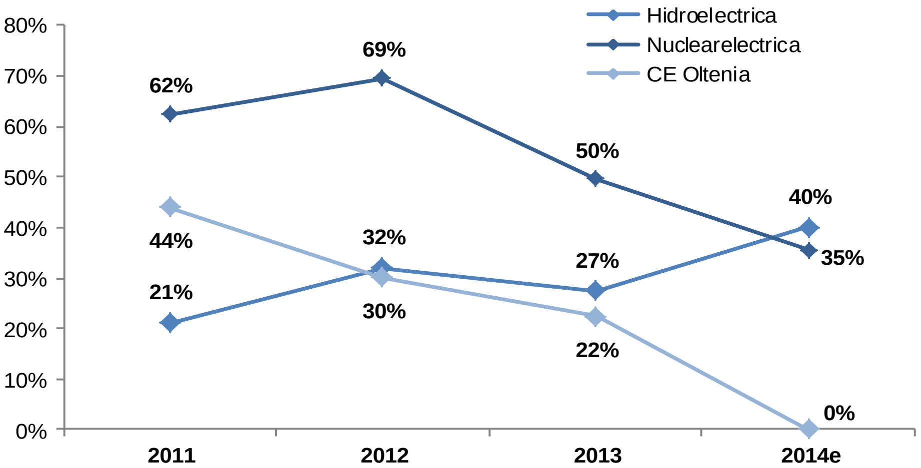
The price and quantities set to be sold on the regulated market by power producers are established at the complete discretion of the regulator. For the first time, both Hidroelectrica and Nuclearelectrica have already contested their obligations on the regulated market imposed by regulator for 2014. Following complaints filed by Hidroelectrica and its minority shareholder FP, the Romanian Competition Council will undergo an investigation into the prices fixed by ANRE. Nuclearelectrica also announced that it has filed complaints with the Bucharest Court of Appeal against the decision made by the regulator

ANRE, mentioning that the authority had not recognized all the cost elements requested and justified.

The electricity price on the regulated market is a basket price, with much higher prices recognized for coal-fired power plants up to 2013 in comparison with Hidroelectrica and Nuclearelectrica. Starting with 2014, after the power price collapsed and the regulated market size contracted, it became advantageous for coal producers to be excluded from the regulated basket price and be able to sell their output on the competitive market, at prices as high as possible.

Hidroelectrica to gradually enjoy concrete profitability gains from market liberalization starting in 2015

Weight of regulated market in total power production (2011-14e)



Source: Companies, Erste Group Research

As we have shown, the liberalization of the power price did not put pressure on the final consumer price, mainly due to oversupply and weak demand, which we consider to be the new reality of the power market for the foreseeable future. On the other hand, the renewable support scheme (around 10% weight in the final power price), the support scheme for electricity produced in high efficiency cogeneration (around 4-6% weight in final electricity power) and the distribution and supply tariffs (over 30% weight in the final power price) are three important areas when it comes to the bearability of power bill for the final consumer.

Business triggers for Romanian power producers

Trigger/Power producer	Hidroelectrica	Nuclearelectrica	CE Oltenia
Renewable energy boom	(**+**) Higher demand for hydro power could quickly balance NPS, as the most expensive electricity source on the market (**–**) Contraction of output selling price	(**–**) Contraction of output selling price	(**–**) Due to the lack of balancing capacities of the NPS, lignite-fired plants were used to balance the system, a cost-intensive process (with frequent starts and stops) (**–**) Contraction of output selling price (**–**) Contraction of the quantity of power sold (market share drop since 2013)
Market liberalization	(**–**) 2014 / (**+**) starting with 2015 Higher quantity of power sold at market prices starting with 2015 (regulator imposed sale of ~40% of production on regulated market for 2014, at a price below the wholesale price)	(**+**) Higher output sold at market prices since 2012 (regulator imposed sale of ~ 35% of production on regulated market for 2014, at a price relatively close to the wholesale price)	(**+**) Entire output sold on free market starting in 2014
Sluggish power demand	(**–**) Contraction of output selling price	(**–**) Contraction of output selling price	(**–**) Contraction of output selling price (**–**) Contraction of quantity of power sold
New tax on special constructions starting with 2014	(**–**) Estimated at RON 180mn (35% reduction of 2014 Clean EBIT of RON 512mn)	(**–**) Estimated at RON 110mn (35% reduction of 2014 Clean EBIT of RON 307mn)	(–) Estimated at around RON 30mn

Source: Erste Group Research

New tax on special constructions to strongly hurt the profitability profile of Nuclearelectrica and Hidroelectrica

- The profitability profile of Hidroelectrica in 2014 is particularly depressed by: i) unexpectedly unfavorable terms set for this year by the regulator regarding the quantity and price of electricity sold on the regulated market; ii) relatively weak hydrological year (output below 2013); iii) oversized turbinated water expenses; iv) new special buildings tax
- In the case of *Nuclearelectrica,* the strong improvement in profitability in 2013 is explained by the decrease in the quantity of electricity sold on the free market, from about 70% in 2012 to 35% in 2014.
- In the case of *CE Oltenia*, oversized personnel expenses, an old generation fleet and the contraction of the market share due to the eolian boom, together with the collapse of the power price, put in question the sustainability of the company's business model in the medium and long term

Romanian power producers' valuation

Valuation of power producers strongly connected to operating profitability per IC and per Output

We have selected in the peer group 15 power producers from Europe, Russia and Brazil, considering specific multiples EV/IC and EV/Output as the most appropriate criteria for running a comparison exercise among electricity producers. We also put the valuation level in accordance with a specific profitability metric, namely operating profitability per IC, respectively per electricity output.

In this way, two linear regressions were developed, with a high correlation coefficient: 1) EV/IC (dependent variable) and EBITDA/IC (independent variable) and 2) EV/Output (dependent variable) and EBITDA/Output (independent variable).

New tax on special infrastructure cut our valuation on Hidroelectrica and Nuclearelectrica by 15% and 24%, respectively

Power producer	Core country	Installed Capacity(MWh)	Output (TWh)	EBITDA*/IC (EUR kw)	EBITDA*/Output (EUR/MWh)
CEZ	Czech Republic	15,800	68.8	149.5	34.3
PGE	Poland	11,194	56.1	84.9	16.9
Tauron	Poland	5,183	19.1	38.4	10.4
Verbund	Austria	10,386	35.2	118.3	34.9
Fortum	Finland	11,271	53.9	147.4	30.8
Iberdrola	Spain	46,039	134.4	85.9	29.4
EDP	Portugal, Spain	23,380	54.7	111.7	47.8
Rushydro	Russia	36,500	112.6	41.0	13.3
OGK-2	Russia	17,857	75.2	3.0	0.7
OGK-5	Russia	9,677	44.5	33.7	7.3
Tractebel Energia	Brazil	6,909	36.2	150.7	28.8
AES Tiete	Brazil	2,658	14.3	231.3	43.1

**) only EBITDA from power generation is considered*

Romanian power producer	Target EBITDA* (EUR mn)	IC (MW)	Target output 2014 (TWh)	EBITDA/ IC (EUR/Kw)	EBITDA/Output (EUR/MWh)
Hidroelectrica	297	6,470	13.5	46.0	22.0
Nuclearelectrica	134	1,414	10.5	94.5	12.7
CE Oltenia	97	3,750	13.0	25.9	7.5

**) computes include the estimated impact of the new tax on special constructions*
Source: Companies, Erste Group Research

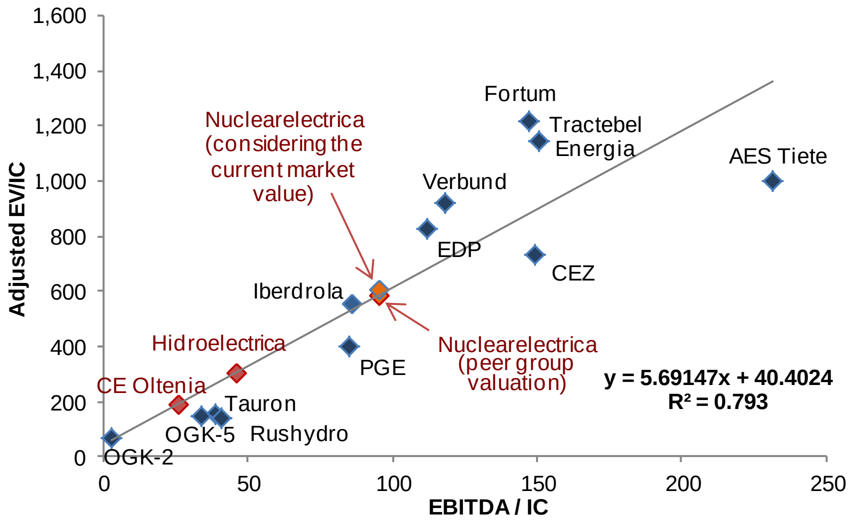
From the two linear equations built based on the peer group, we derived the target values of EV/IC and EV/Output for the three Romanian power producers where Fondul Proprietatea is a minority shareholder. In order to find the fair values for Hidroelectrica, Nuclearelectrica and CE Oltenia, we used EBITDA/IC and EBITDA/Output estimated for 2013, considering that the new reality of the Romanian power market makes it mandatory using the updated profitability profile.

We gave up valuating the Romanian power producers based on the Depreciated Replacement Cost method, as we did in the previous reports on Fondul Proprietatea. The major reason is that, in accordance with the closed-end fund's strategy, all its assets have an up-for-sale status. In this context, the fair value has to be seen as strictly connected to the profitability profile of the company, while its assets collection remains a secondary item as long as the owner is unwilling to wait for the capitalization of hypothetical strengths. On the other hand, structural changes on the domestic power market make it inappropriate to use the asset replacement method for CE Oltenia's valuation, for as long as the company is inevitably losing market share without a chance to recover the protected position it held up to 2012.

Valuation tool	Hidroelectrica (EUR mn)	Nuclearelectrica (EUR mn)	CE Oltenia (EUR mn)
I. (EV/IC)/(EBITDA/IC) peers regression	1,457.64	528.17	365.92
II. (EV/Output)/(EBITDA/Output) peers regression	1,333.66	468.81	135.49
Fair value (equal weight of each method)	**1,395.65**	**498.49**	**250.70**
Market capitalization	-	567.57	-

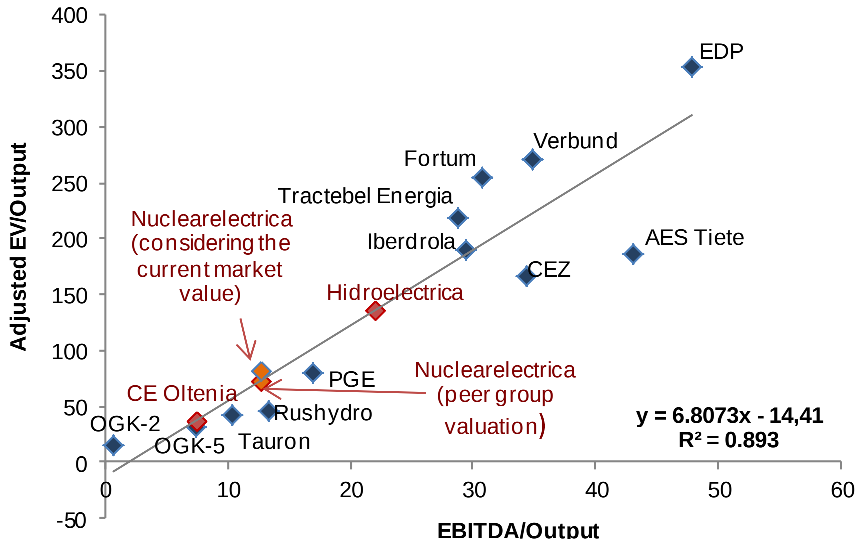
Source: Companies, Erste Group Research

I. EV/IC (EUR/kw) vs. EBITDA/IC (EUR/kw)



Source: Erste Group Research

II. EV/Output (EUR/MWh) vs. EBITDA/Output (EUR/MWh)



Source: Erste Group Research

Power producers' valuation

Company	Country	EV/EBITDA			PE			Dividend yield			Net debt/EBITDA
		2012	2013e	2014e	2012	2013e	2014e	2012	2013e	2014e	2012
AES TIETE SA-PREF	Brazil	5.8	5.5	4.9	9.4	9.4	8.2	12.0%	11.4%	13.5%	0.3
CEZ	Czech Republic	5.3	5.6	6.3	6.7	7.4	9.0	8.6%	7.7%	6.3%	1.9
EDP	Portugal	6.3	6.1	n.a.	8.4	8.1	n.a.	7.6%	8.0%	0.0%	5.0
Fortum Oyj	Finland	8.5	8.5	8.7	10.8	11.0	11.4	7.0%	7.0%	7.0%	5.0
Iberdrola	Spain	7.3	6.8	6.5	8.4	9.7	9.6	7.9%	7.8%	7.8%	3.9
OGK-2	Russia	6.9	6.3	n.a.	8.3	6.2	n.a.	0.9%	1.8%	0.0%	1.9
OGK-5 OJSC	Russia	5.5	4.1	3.6	8.2	6.4	6.1	0.0%	4.5%	5.5%	3.3
PGE	Poland	4.3	3.8	5.0	9.9	8.3	11.4	6.6%	6.4%	5.0%	-0.5
RusHydro	Russia	5.8	5.5	4.0	6.9	9.8	5.0	1.5%	0.4%	3.5%	6.0
Tauron Polska Energia	Poland	3.1	3.4	4.8	5.1	5.4	9.6	5.9%	4.7%	3.3%	1.2
Tractebel Energia SA	Brazil	7.9	7.7	7.0	15.4	13.8	12.9	6.7%	6.6%	7.3%	0.7
Verbund	Austria	8.1	7.8	10.3	14.6	13.3	19.6	3.6%	6.1%	2.9%	3.4
Median peer group		**6.1**	**5.8**	**5.7**	**8.4**	**8.9**	**9.6**	**6.7%**	**6.5%**	**5.2%**	
Nuclearelectrica	Romania	-	3.5	4.3	-	6.1	16.4	-	13.9%	5.2%	2.8
Hidroelectrica*	Romania	-	4.5	6.4	-	7.0	15.5	-	12.1%	5.5%	2.4

**Fair value considered of EUR 1.39bn, based on our peers regresion*

Source: FactSet, Bucharest Stock Exchange, Erste Group Research

Power & gas distribution grids

We see higher regulatory risk starting with 2014 for regulated utilities, following new corporate taxes and statements by government officials

Following several public statements made by the former Romanian Minister of Energy, as well as the action taken by the government during 2013, we see a much higher regulatory risk, especially for the power distribution grids. On the one hand, the Ministry of Energy blamed the power grids privatized with ENEL, E.ON and CEZ for the weak quality of the power distribution services and the lack of relevant investments in grid modernization and unjustified high profits. On the other hand, the Romanian government approved, at the beginning of 2013, an ordinance regarding the introduction of a new tax on business in volume terms for regulated utilities in power and gas sectors in 2013 and 2014. The government mentioned in the explanatory notes of the respective government ordinance that power & gas utilities record profits high enough in order to support such a tax.

The high net margins (of over 10%) for most regulated utilities (even over 20% in the case of three privatized power grids), as well as a high stock of cash and the lack of leverage put in question the overcompensation of the operators of the power and gas grids from the point of view of the government officials.

Government-initiated international litigation against ENEL, EON and CEZ feeding higher regulatory risk perception

Moreover, unprecedented international legal action was unexpectedly initiated by the Romanian authorities at the end of 2011 against strategic investors which had acquired majority stakes in five power grids. This suggests a deterioration of the relationship between the Romanian government and the privatized power grids. Electrica, the state-owned holding company in the power distribution sector, brought CEZ, ENEL and E.ON to the arbitrage court of Paris, requiring penalties of around EUR 1bn for not meeting the investment obligations assumed within privatization contracts. The main litigation is against ENEL, with the story expected to be clarified this year.

Financial results

Company	Sector	Sales (RON mn)		EBITDA (RON mn)		EBIT (RON mn)		Net profit (RON mn)		Net debt (RON mn)	
		2011	2012	2011	2012	2011	2012	2011	2012	2011	2012
E.ON Distributie Moldova	Power	636.10	665.61	189.17	212.76	22.02	83.80	7.21	71.34	-85.34	-100.44
ENEL Distributie Muntenia	Power	705.88	869.86	211.34	357.88	51.64	172.40	50.47	206.28	-1314.25	-1210.49
ENEL Distributie Banat	Power	585.78	603.16	313.69	292.44	238.35	181.15	220.46	167.23	-429.81	-610.65
ENEL Distributie Dobrogea	Power	459.00	480.31	185.56	189.71	126.37	103.01	108.85	94.47	-147.72	-298.91
Electrica Distributie Transilvania Nord*	Power	535.41	571.12	141.45	180.18	40.16	68.81	29.10	53.08	22.31	-5.40
Electrica Distributie Transilvania Sud*	Power	598.51	632.84	139.59	176.08	27.78	61.71	19.57	45.80	39.99	8.45
Electrica Distributie Muntenia Nord*	Power	685.74	720.20	151.09	182.55	72.40	99.14	67.41	87.15	-178.14	-265.53
GDF Suez Energy Romania	Gas	4090.87	4315.83	270.08	463.27	142.04	299.86	209.56	379.40	44.83	-58.24
E.ON Gaz Distributie	Gas	800.46	744.36	354.27	204.71	264.75	82.65	230.49	73.02	21.37	61.12

**) Majority stake held by state-owned holding company Electrica*
Source: Companies, Erste Group Research

Financial ratios

Company	Sector	EBITDA margin		EBIT margin		Net margin		ROE		Net debt/ EBITDA	
		2011	2012	2011	2012	2011	2012	2011	2012	2011	2012
E.ON Distributie Moldova	Power	29.74%	31.96%	3.46%	12.59%	1.13%	10.72%	0.40%	3.77%	-0.45	-0.47
ENEL Distributie Muntenia	Power	29.94%	41.14%	7.32%	19.82%	7.15%	23.71%	1.76%	5.70%	-6.22	-3.38
ENEL Distributie Banat	Power	53.55%	48.48%	40.69%	30.03%	37.64%	27.73%	11.94%	8.31%	-1.37	-2.09
ENEL Distributie Dobrogea	Power	40.43%	39.50%	27.53%	21.45%	23.72%	19.67%	8.70%	7.02%	-0.80	-1.58
Electrica Distributie Transilvania Nord*	Power	26.42%	31.55%	7.50%	12.05%	5.44%	9.29%	3.39%	5.82%	0.16	-0.03
Electrica Distributie Transilvania Sud*	Power	23.32%	27.82%	4.64%	9.75%	3.27%	7.24%	2.12%	4.74%	0.29	0.05
Electrica Distributie Muntenia Nord*	Power	22.03%	25.35%	10.56%	13.77%	9.83%	12.10%	5.36%	6.52%	-1.18	-1.45
GDF Suez Energy Romania	Gas	6.60%	10.73%	3.47%	6.95%	5.12%	8.79%	7.40%	12.34%	0.17	-0.13
E.ON Gaz Distributie	Gas	44.26%	27.50%	33.08%	11.10%	28.80%	9.81%	19.30%	4.96%	0.06	0.30

**) Majority stake held by state-owned holding company Electrica*
Source: Companies, Erste Group Research

Higher taxes introduced by government will inevitably translate into lower profitability despite revenue cap methodology principle

At the beginning of 2013, the head of the regulator ANRE stated that a change in revenue cap methodology is possible, aimed at excluding from tariffs the royalty paid by these companies for the concession of power and gas transmission and distribution grids. Removing the royalty fee from the tariff calculation formula is an example of a major risk for regulated utilities over the long term, as further increases in taxes could not be recouped by these companies and would lower their profitability. While this intention was not subsequently confirmed, official comments by representatives of the regulator highlight that un-controllable expenses (as is the case with any tax) have to be fully recognized within tariffs (and in this manner transferred to final consumers).

The high weight, of over 30%, of power and gas distribution and supply tariffs in final energy price feeds a potential regulatory risk

However, the relatively persistent governmental messages regarding the too high profitability of power distribution grids indicates increasing regulatory risks for the next regulatory period 2014-18. This could result in lower than justified tariffs which are unable to cover the new taxes, or fully renegotiating of some controllable cost items. The high level of around 30% of distribution and supply tariffs in the final price for both power and gas indicates the vulnerability of the business model of regulated utilities in terms of the bearability of the energy price for final consumers. This is actually feeding the regulatory risk for power and gas distribution grids in the coming period.

The risk related to the new tax on existing special infrastructure assets, which was introduced by the Romanian government starting with the FY14, also has to be taken into account. Obviously, this new tax is detrimental to owners of power and gas distribution grids, with its impact to be clarified in the coming weeks.

Regulated utilities valuation

We reduced the fair value of regulated utilities compared to our previous reports due to the higher regulatory risk outlook, which may result, starting in 2014, in the lower profitability of these companies compared to levels achieved in the past.

Fair value of electricity/gas distribution grids based on RAB approach

Company	Sector	Cash 2012 (RON mn)	Financial debt 2012 (RON mn)	RAB 2012e (RON mn)	Target EV/RAB	Target EV (RON mn)	Fair Value of Equity (RON mn)	Fair Value of Equity (EUR mn)
E.ON Distributie Moldova	Power	100.4	0.0	1,682.8	0.7	1,178.0	**1,278.4**	**288.7**
ENEL Distributie Muntenia	Power	1,210.5	0.0	2,805.6	0.7	1,963.9	**3,174.4**	**716.8**
ENEL Distributie Banat	Power	610.7	0.0	1,413.4	0.7	989.4	**1,600.0**	**361.3**
ENEL Distributie Dobrogea	Power	298.9	0.0	1,262.9	0.7	884.0	**1,182.9**	**267.1**
Electrica Distributie Transilvania Nord*	Power	23.3	17.9	1,187.2	0.6	712.3	**717.7**	**162.1**
Electrica Distributie Transilvania Sud*	Power	17.0	25.4	1,278.5	0.6	767.1	**758.7**	**171.3**
Electrica Distributie Muntenia Nord*	Power	301.3	35.7	1,298.3	0.6	779.0	**1,044.5**	**235.9**
GDF Suez Energy Romania	Gas	424.3	366.1	2,058.4	0.8	1,646.7	**1,704.9**	**385.0**
E.ON Gaz Distributie	Gas	0.8	62.0	1,277.9	0.8	1,022.3	**961.2**	**217.0**

**) Majority stake held by state-owned holding company Electrica*
Source: Companies, Erste Group Research

We assigned lower fair values for regulated utilities by applying discounts ranging between 20% and 40% to their Regulated Asset Base (RAB), substantially higher than the levels used in our previous valuation exercise from Fondul Proprietatea reports. This approach is consistent with the fact that the most relevant listed peer, the national power transmission operator Transelectrica, is traded at a 40% discount to its RAB due to a still high regulatory risk perception among equity investors.

Regulated distribution valuated grids at 3.5 to 6 times level of EBITDA

Romanian RAB-regulated utilities target multiples

Company	EV/Sales 2012	EV/EBITDA 2012	P/E 2012	P/BV 2012
E.ON Distributie Moldova	1.8	5.5	17.9	0.7
ENEL Distributie Muntenia	2.3	5.5	15.4	0.9
ENEL Distributie Banat	1.6	3.4	9.6	0.8
ENEL Distributie Dobrogea	1.8	4.7	12.5	0.9
Electrica Distributie Transilvania Nord*	1.2	4.0	13.5	0.8
Electrica Distributie Transilvania Sud*	1.2	4.4	16.6	0.8
Electrica Distributie Muntenia Nord*	1.1	4.3	12.0	0.8
GDF Suez Energy Romania	0.4	3.6	4.5	0.6
E.ON Gaz Distributie	1.4	5.0	13.2	0.7

**) Majority stake held by state-owned holding company Electrica*
Source: Companies, Erste Group Research

On the other hand, the fact that the Romanian power and gas distribution grids are not regular dividend payers despite their stable profitability is not consistent with their defensive profile. Similar companies listed on European stock markets have the status of stable and consistent dividend payers. This is another inconvenient that negatively affects the corporate profile of Romanian regulated utilities and results in substantial valuation discounts compared to Western listed peers, despite their much higher indebtedness.

European RAB-regulated utilities valuation

Company	Country	EV/RAB	EV/EBITDA 2012	EV/EBITDA 2013e	EV/EBITDA 2014e	PE 2012	PE 2013e	PE 2014e	Dividend yield 2012	Dividend yield 2013e	Dividend yield 2014e	Net debt / EBITDA 2012
Elia system Operator	Belgium	0.86	10.8	9.7	9.9	13.0	13.6	12.8	4.7%	4.7%	4.8%	6.4
Red Electrica de Espana	Spain	n.a.	7.6	7.6	7.4	11.0	10.2	9.8	5.9%	6.4%	6.5%	3.8
Terna	Italy	1.35	8.6	8.9	9.1	13.8	13.2	12.8	6.3%	6.3%	6.3%	4.7
Snam Rete Gas	Italy	1.10	8.6	8.9	9.0	11.8	12.7	11.8	7.3%	7.3%	7.3%	4.4
Federal Grid Company	Russia	0.48	5.7	4.2	4.1	9.9	5.3	3.8	37.0%	0.0%	0.0%	2.0
National Grid	UK	1.62	9.4	9.6	9.4	13.9	14.4	13.5	5.4%	5.5%	5.7%	3.9
Redes Energeticas Nacionais	Portugal	0.95	7.3	6.3	6.2	9.4	10.3	9.0	7.8%	7.8%	7.8%	4.9
Median peer group		**1.02**	**8.6**	**8.9**	**9.0**	**11.8**	**12.7**	**11.8**	**6.3%**	**6.3%**	**6.3%**	**4.4**
Transelectrica	**Romania**	**0.58**	**4.4**	**3.2**	**3.2**	**27.0**	**7.1**	**10.2**	**4.2%**	**11.9%**	**8.4%**	**2.2**
Transgaz	**Romania**	**n.m.**	**4.8**	**3.0**	**3.6**	**7.8**	**6.7**	**5.8**	**9.8%**	**9.3%**	**8.9%**	**-0.2**

**) Majority stake held by state-owned holding company Electrica*
Source: Companies, Erste Group Research

Low negotiating power of Franklin Templeton to force exits from privatized distribution grids

The regulatory risk outlook, together with the litigation initiated by the Romanian government at the arbitrage court of Paris, limits the exit solutions for FP from unlisted regulated utilities. On the other hand, Franklin Templeton (FT) has reduced negotiating power with strategic investors for the sale of the stake Fondul owns in these companies. In this context, the only feasible solution in the medium term is an exit together with the Romanian government, which also holds minority stakes in privatized distribution grids. However, an alliance between the Romanian government and FT is only a hypothetical scenario at the moment.

In respect of the three power grids controlled by the state-owned national company Electrica (namely Electrica Distributie Transilvania Nord, Electrica Distributie Transilvania Sud and Electrica Distributie Muntenia Nord), there is, at least theoretically, an exit alternative for FP through the listing of the holding company Electrica scheduled to take place in 2014. Franklin Templeton is currently trying to negotiate an equity swap with the government in order to become a shareholder in Electrica on the back of its holdings in the three state–owned power grids. This would be a concrete positive development for the RAB-regulated utilities segment from FP portfolio.

Listing of Electrica would create exit solutions for FP from state-owned power grids in coming years

Another concrete example of the regulatory risk and arbitrary decisions of the regulator ANRE is that, in the previous regulatory period 2008-12, the regulator approved for the three state-owned power distribution grids regulated returns on RAB of 7%, compared to 10% for privatized distribution grids. This resulted in lower profitability compared to the five grids held by CEZ, ENEL and E.ON. The key principle of RAB-based methodology for computing transmission and distribution tariffs is that, on average, these companies should have a regulated profitability determined as a regulated return multiplied by the value of RAB.

The third regulatory period of five years will start in July 2014, after a transitional period in 2013 and 1H14, when the parameters of the methodology have to be negotiated between the companies and the regulator. However, considering the new taxes introduced by the government in 2013 and 2014, we see a substantial risk of less than expected tariffs in the coming regulatory period. We do not believe that the new taxes will be simply transferred to final consumers. On the other hand, based on the last statements of the authorities, the regulator ANRE may become more rigid in respect of easily negotiating some investments and controllable costs. We estimate that the persistence of those risks may result into lower profitability, especially for power distribution grids.

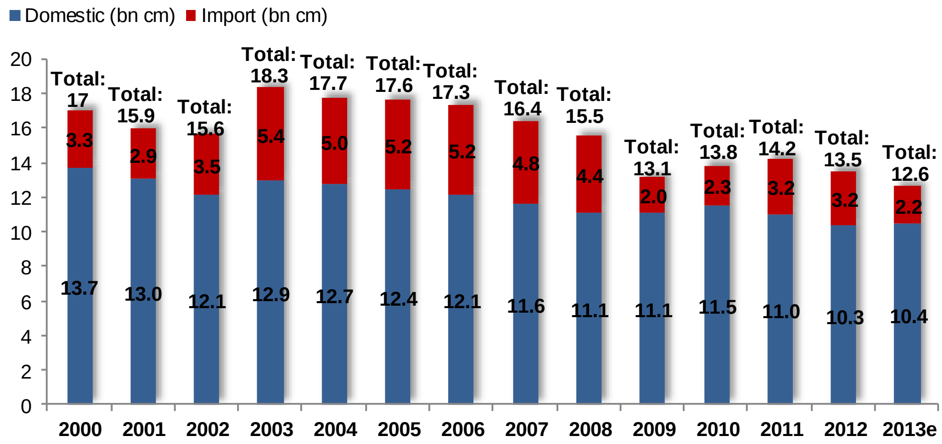
Gas market

Market overview

Domestic gas production covers more than 80% of country's consumption

Romania has the third largest gas reserves in the EU (excluding the recent discoveries from the Black Sea), with, starting in 2013, less than 20% of gas demand being covered via imported gas. Domestic gas production is 95% in the hands of two companies, namely Romgaz and OMV Petrom, which jointly supported ~70-75% of Romania's gas demand up to 2012.

Gas consumption development (2000–13e)

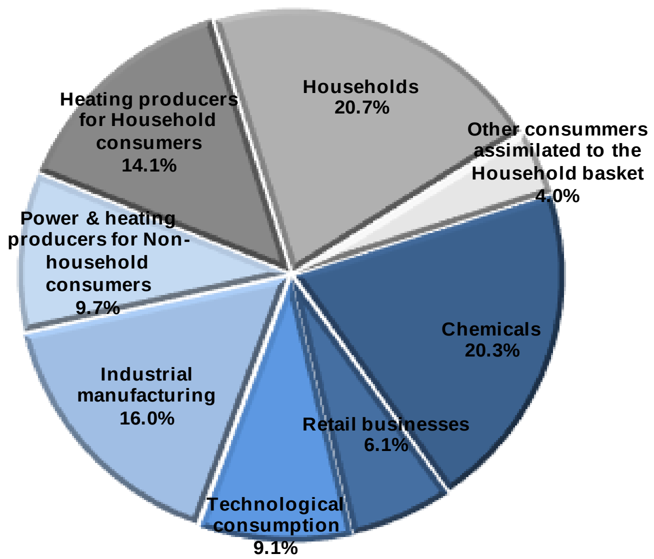


Source: Romgaz, Erste Group Research

Since 2013, the two domestic producers have covered together more than 80% of internal consumption, with gas production of Romgaz below Petrom's output by around 20% in 2013. The severe contraction of demand by 8% in 1-3Q13 is the main reason for a substantially lower weight of imports in total domestic consumption, which, in our view, will stay from now on well below 20%.

Households and affiliated customers categories cover about 40% of total consumption, with the balance represented by non-residential consumption

Gas consumption breakdown 2012



Source: Romanian Energy Regulatory Authority (ANRE), Erste Group Research

Gas consumption to be under pressure by higher price, as well as energy efficiency investments, including modernization of transmission and distribution gas grids

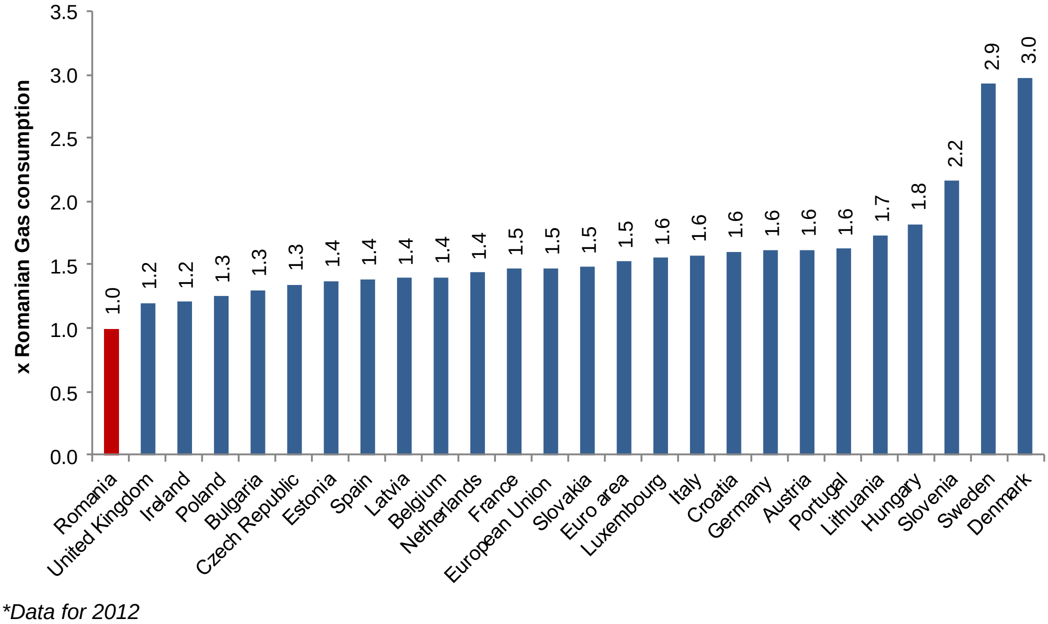
Households' weight in total consumption exceeds 20%, while other consumers (hospitals, public institutions, etc.) cover about 4% of the consumption. Another category covered by the same regime as households is represented by heating producers for households, with a weight of about 14% in total consumption in 2012. All three categories account for about 40% of total consumption, with the remaining 60% represented by effective non-residential consumption of which chemicals and industrial manufacturing are the most important segments.

Gas price liberalization is set to trigger a decline of gas consumption in Romania for both households and industry, with the latter expected to meet a steeper decrease, given that most of domestic companies' equipment is obsolete, not revamped and energy intensive.

Up to 2012, gas prices paid by industrial consumers in Romania were well below those paid in other EU countries, and thus gas price liberalization will put substantial pressure on Romanian companies' competitiveness.

Up to 2012, Romanian consumers paid the lowest price in Europe, benefitting from the advantage of exploiting substantial domestic reserves

Price for industrial consumers in Romania relative to EU countries* (nominal terms, all taxes included)



*Data for 2012
Source: Eurostat, Erste Group Research

Energy efficiency improvements following investments made by large industrial consumers (such as the largest Romanian fertilizer producer Azomures), as well as the modernization of gas transmission & distribution grids, is expected to be a key pressure factor in the medium and long term.

Gas price regulated formula

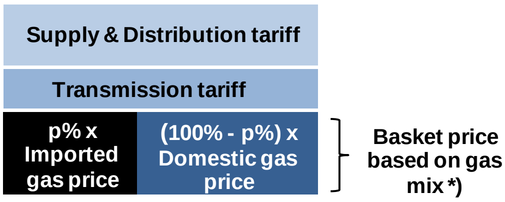
Gas is supplied based on regulated basket, differentiated between household and non-household customers

The gas price for end customers is fully regulated by the National Energy Regulatory Authority (ANRE) and computed based on both the domestic gas price and imported gas price, weighted with the percentage contribution of each source to cover local demand. At this blended price, regulated tariffs for transportation, distribution and supply services are added. Excepting gas supply activity, the other tariffs are set by the energy regulator based on revenue-cap methodology.

Practically, the only component which is not under ANRE's direct control is the price of imported gas, while all the other items, such as the price of domestic gas, percentage contribution of imported gas in the basket generation price, as well as transmission, distribution and supply tariffs being set by the regulator.

Only gas price item not directly controlled by ANRE is price of imported gas

GAS PRICE for end-consumers



*) p = percentage contribution of imported gas quarterly set by ANRE, separately for households and non-residential consummers (since July 2011); for 1Q14, p= 5% for households (including district heating plants supplying heat to households), respectively p=24% for non-households

Source: Romanian Energy Regulatory Authority (ANRE), Erste Group Research

Since July 2011, the gas basket is differentiated between households (including district heating plants supplying heat to households) and non-household customers. As a social protection measure, household customers have benefited from a lower share of imported gas (about 5% on average in 2013) compared to non-households (29% for 2013).

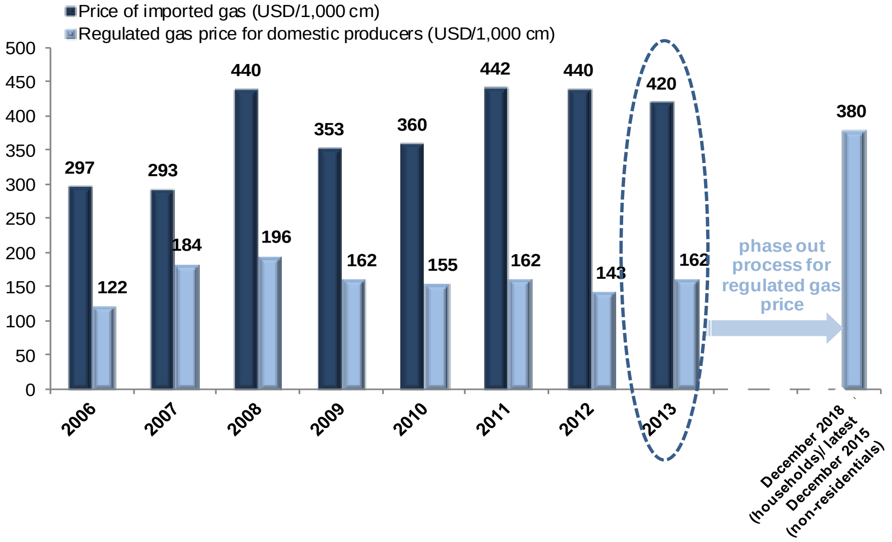
Gas market liberalization mechanism

Basket price accounts for more than 60% in final end-customer gas price, for both households and non-households (excluding VAT)

Gas from domestic production was sold at ANRE's recommended low discretionary prices. After several postponements, the Romanian authority agreed with IFIs that the internal gas price has to be gradually fully liberalized between 2013 and 2018, targeting alignment with the European market price environment. From mid-2008 until February 2013, the price for domestic gas was kept at approx. the same level in RON terms (RON 495/1,000 cm, respectively RON 45.7/MWh) being more than two times cheaper than the price of imported gas.

Domestic gas price – kept at ~USD 150/1,000cm – to be aligned with convergence price estimated at USD 380/1,000 cm in official liberalization roadmap. Current import gas price is USD 420/1,000cm. Given that this is a moving target, a contraction of the Russian gas price would effectively result into a lower convergence price by 2019 (probably a target below USD 350/1,000cm, which is more realistic)

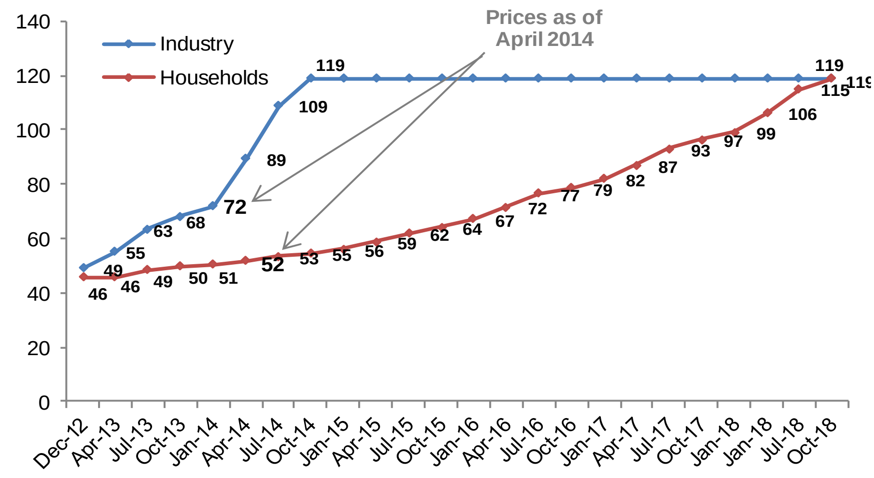
Import vs. domestic gas price



Note1: 1,000 mc ~ 10.6 MWh; Note 2: 1 USD = 3.3 RON – the current exchange rate used for conversion of the official convergence price of RON 119/MWh into USD 377/1,000 cm
Source: OMV Petrom, Erste Group Research

The misalignment between import and domestic gas prices is scheduled to be progressively 'corrected' in accordance with a roadmap adopted by the Romanian government in June 2012 following negotiations with the IMF, EU and World Bank. The phase-out process for the regulated gas price paid by industrial consumers was scheduled to be completed by October 2014, while for residential consumers the liberalization process is scheduled to end in December 2018.

Internal gas production price deregulation schedule (RON/MWh)



Source: Romanian Energy Regulatory Authority (ANRE), Erste Group Research

Gas price liberalization process for industrial consumers seems locked for the moment at RON 72/MWh

Following the lobby of large industrial consumers and labor unions for a much more flexible convergence process, the government is considering to freeze the gas price at the current level of RON 72/MWh, after the latest update in January 2014. This way, the other growth steps may be frozen and the process could be resumed next year. In this scenario, the entire liberalization schedule for industrial consumers could end with at least one-year delay. This postponement is somehow already assumed according to the negotiations between the Romanian authorities and the IMF & EU.

Final gas price for non-household consumers should increase by around 50% between December 2012 and end of liberalization process

However, there is an important reason which makes the coming one-two year period the most appropriate one for finally implementing the gas price deregulation. For large industrial consumers, the liberalization process will be itself an incentive for investment in increasing the energy efficiency initiative, something which was not so far encouraged, given the access to cheap gas, even after Romania joined the EU in 2007.

Gas liberalization benefits - shared between gas producers and state budget

The gas price deregulation will obviously exert a positive impact on gas producers' profitability profile. However, the effective impact deriving from the price convergence mechanism will be limited by the new fiscal regime, which is detrimental to OMV Petrom and Romgaz.

At least in the first stage, the profit for oil & gas producers deriving from the gradual liberalization of the domestic gas price is partially capped by the new package of fiscal measures introduced in February 2013 (when the first price increase was implemented for non-household consumers), which is scheduled to remain in place until the end of 2014. The package involves the charge of a new 60% tax on incremental revenues recorded by domestic gas producers given the price liberalization process, net of incremental royalties and upstream investments up to 30% of taxable base. Considering all deductions, the effective additional tax is closer to 33%, which thus leaves gas producers with substantial benefits from the liberalization process.

Despite tougher fiscal framework, profitability profile of Petrom and especially Romgaz to be improved by gas market liberalization

Starting in 2015, a new tougher fiscal regime for OMV Petrom and Romgaz should come into effect, with the initiative being in the preparation stage by the Romanian government. Since 2004, after the privatization of Petrom with OMV, the oil and gas producer paid as royalty about 7.5% of exploration and production revenues, while Romgaz has benefitted from the same favorable royalty regime, paying a level of royalties of around 7% of production revenues.

Our base scenario is that Petrom and Romgaz will enjoy net gains after the deduction of higher taxes and after paying higher royalties (or most likely maintaining over-taxation of additional revenues from liberalization after 2014).

We mention that the Romanian government plans to introduce, starting in 2014, a new tax on existing special infrastructure assets (hydro, nuclear and thermo plants, oil, gas and salt pipelines, electricity/gas transmission / distribution infrastructure, telecom infrastructure, port and waterway infrastructure, etc.). The new tax is obviously detrimental for oil & gas producers, which, according to the rumors, should be around RON 90mn for Romgaz and a minimum of RON 250mn for Petrom.

Petrom and Romgaz profitability and valuation comparison before gas liberalization process

Indicator \ Company	Petrom	Romgaz	Romgaz as % of Petrom
Hydrocarbon reserves & production			
2p reserves (mn boe)	1,091	508	46.6%
1p reserves (mn boe)	775	403	52.1%
Annual hydrocarbon production 2012 (mn boe)	67	35.6	53.2%
2p reserves / Annual hydrocarbon production (years)	16.3	14.3	-
1p reserves / Annual hydrocarbon production (years)	11.6	11.3	-
Operating eficency			
E&P Sales 2012 (RON mn)	12,992.0	3,595.0	
EBITDA 2012 (RON mn)	8,514.0	1,854.0	21.8%
E&P EBITDA in total EBITDA	88.3%	95.6%	-
E&P Sales 2012/Hydrocarbon production (RON/boe)	194.3	101.0	52.0%
OPEX*/Hydrocarbon production (RON/boe)	47.1 (13.6 USD/boe)	48.2 (13.9 USD/boe)	102.3%
E&P EBITDA 2012/Hydrocarbon production (RON/boe)	112.5	49.8	44.3%
Romgaz valuation via Petrom EV/2p multiple			
EV / 2p reserves (RON mn/boe mn)	22.82	22.15	-
EV (RON mn)	24,901.3	11,251.7	45.2%
Net Debt 2013 (RON mn)	34.5	-1,563.6	-
MkCap/Fair value of Equity (RON mn)	24,866.8	12,815.3	51.5%
MkCap/Fair value of Equity (EUR mn)	5,534.4	2,852.2	51.5%

**Including royalty expensesand amortization, excluding exploration expenses*

- There is a similar level of OPEX per boe of around USD 13.5-14, which reveals that, in comparison with their peers, Romgaz and Petrom are low-cost hydrocarbon producers
- EBITDA per boe as a specific profitability factor is more than double in the case of Petrom in comparison with Romgaz, the main explanation being that the oil products market is fully liberalized, with Petrom selling oil products at the market price, while Romgaz has sold output at a regulated price
- The difference between the profitability of the two companies measured by the specific metric EBITDA/boe is actually suggestive for the coming much higher benefits in relative terms of gas liberalization in the case of Romgaz, as exclusively a gas producer
- Romgaz holds around half of Petrom's reserves, while the ratio between their EV and market cap ratio is in the same proportion

Major gas discoveries in the Black Sea becomes a major story

It is becoming increasingly transparent, according to different sources, that the size of commercial discoveries from the Romanian waters of the Black Sea should reach between 300bcm and 600bcm, which would translate into a higher value added project for the companies involved and for the country's budget.

OMV Petrom has major interests in the Black Sea deep water, where there are high chances to be confirmed that large gas deposits are commercially available

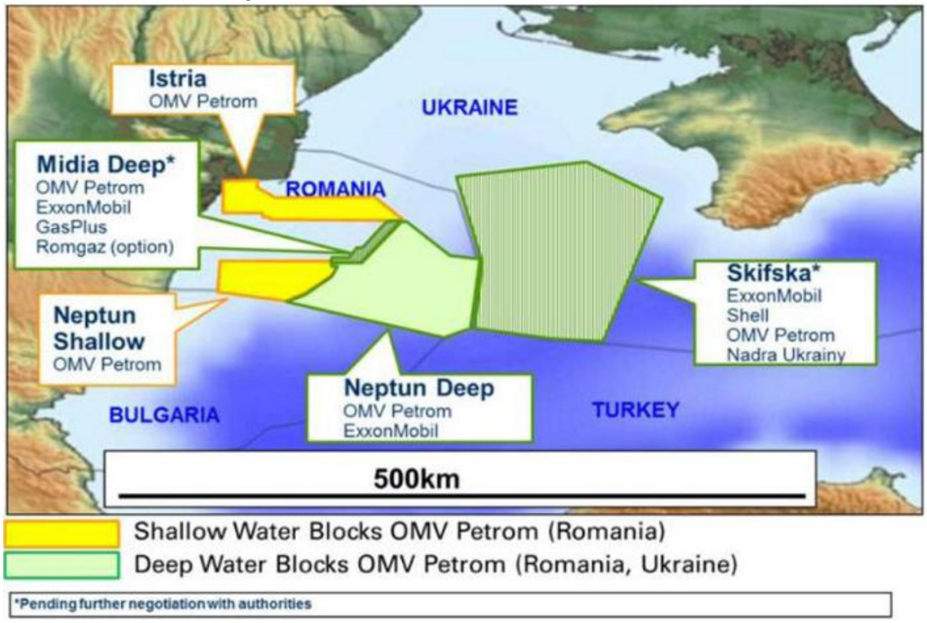
Together with ExxonMobil, Petrom has already executed a successful drilling at Domino 1 in the Neptun deep sea perimeter with a second drilling being scheduled for the latter half of 2014, the natural gas discovery being estimated at 42-84bn cm. This comes in the context wherein Petrom has announced last year that it has finalized over 6,000sq km of 3D seismic acquisitions in order to identify new potential accumulations. Provided a decision of commerciality for the Neptun project, the earliest commercial extractions are to be expected in 2018 according to Petrom's CEO.

Early this year, the government approved the license transfer signed in 2012 from Sterling to ExxonMobil and Petrom of exploration and production rights over the Midia XV (Midia Deep) perimeter adjacent to Neptune. The participation quotas being 42.5% for ExxonMobil, 42.5% for OMV Petrom and 15% for Gas Plus, with Romgaz holding an option to acquire a 10% stake, once proved a commercial discovery. Romgaz also holds a stake in the offshore Black Sea East Rapsodia and Trident blocks operated by Lukoil.

If the gas discoveries are commercially exploitable, the national gas transmission company Transgaz will definitely be part of the project, in charge of building the onshore segment of the transportation infrastructure necessary to connect the off-shore transmission grid with the NTS and, this way, towards Western Europe.

According to Transgaz, the national gas transmission company is ready to assume an extra EUR 560mn capital expenditure between end 2015 and 2018, contingent on confirmation of resources in order to justify the investment in the full interconnection between the Black Sea region and Hungary. In the current CAPEX plan are assumed investments of EUR 280mn up to 2016 in order to develop interconnection facilities with Bulgaria and especially Hungary, which would anyway represent a first stage in the development of the transport infrastructure of natural gas resources from the Black Sea towards Western Europe. In several months, the management of the company is intending to come with details on the CAPEX plan for the development of the on-shore transmission infrastructure for the gas in the Black Sea.

Gas accumulation perimeters in the Black Sea



Source: Transgaz, Petrom

Petrom I Oil & gas producer
Hold

Shareholding Structure

OMV	51.01%
Ministry of Economy	20.64%
Fondul Proprietatea	18.99%
Free-Float	9.36%

Target price (RON/share)	0.503
Share price (RON/share)	0.439
MkCap (RON mn)	24,866.76
MkCap (EURmn)	5,534.43

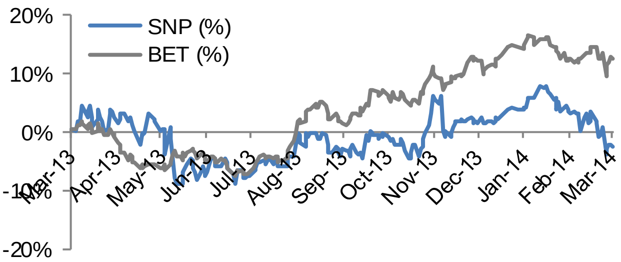
Company description

OMV Petrom is Romania's flagship integrated oil company and the sole crude oil producer, while the natural gas production is roughly half the country's output. The company holds ~728boe proven reserves and 1.03mn boe proven & probable reserves. Over the last three years, Petrom's reserve replacement ratio stood at 48% in average terms, while for 2013 alone, Petrom's RRR was 31%. Production was stabilized by accelerating workovers and drilling, developing state-of-art technologies and partnerships. The company currently uses modern technics to increase recovery rate (~25% for oil, respectively ~49% for gas). Regarding the refining activity, the only operating refinery of the company, Petrobrazi, has gone through a modernization process since 2010, being optimized to process domestic crude oil. Petrom is also no. 1 Romanian downstream operator, with a market share of ~37%.

Key Figures (RON mn) -IFRS-	2011	2012	2013p	2014e
Sales	18,626	22,614	24,185	28,450
EBITDA	5,797	7,766	9,313	8,808
EBIT	2,986	4,936	5,958	5,404
Financial result	-380	-327	259	-17
Gross result	2,605	4,609	5,699	5,387
Net result	2,190	3,759	4,824	4,525
Non-current assets	27,725	31,022	34,560	35,728
Inventories	2,500	2,349	1,996	2,338
Receivables	1,398	1,826	1,429	2,259
Cash	1,589	754	1,408	2,200
Trade payables	1,398	1,826	2,958	n.a.
Total assets	34,765	36,488	40,047	43,391
Total shareholder equity	18,459	21,077	26,642	28,921
Bank debt	3,857	2,637	1,443	1,755
Total liabilities	16,280	15,412	13,405	14,469
EBITDA margin	34.34%	32.43%	38.51%	30.96%
EBIT margin	21.83%	21.56%	24.63%	19.00%
Net margin	16.62%	15.03%	19.95%	15.91%
ROE	10.30%	10.35%	12.05%	10.43%
Quick ratio	50.91%	51.16%	67.55%	72.41%
Equity ratio	57.76%	61.36%	66.53%	66.65%
Net debt/EBITDA	0.24	0.18	0.004	-0.05

Source: OMV Petrom, Erste Group Research

Price development (52 weeks)



Source: Bucharest Stock Exchange, Erste Group Research

Price performance

	1M	3M	6M	12M	Ytd
in RON	-5.7%	-4.0%	0.5%	-2.4%	-6.6%

Source: OMV Petrom, BSE, Erste Group Research

Target multiple	Value
EV/EBITDA 2014	2.83
P/E 2014	5.50
P/Sales 2014	0.87
P/BV 2014	0.93
DivY 2013e	7.76%

**)Multiples computed with Sales, EBITDA, Net profit estimated for FY14; dividend yield based on net profit for FY13 and 40% payout ratio*
Source: OMV Petrom, Erste Group Research

SWOT Analysis

Strengths/Opportunities

• Strong upstream profile
• Gradual gas market liberalization up to 2018, will strengthen the profitability profile
• Strong position on the power market with state-of-art gas-fired power plant (CCGT) in Brazi, which is able to balance the system
• Major interests (in partnership with Exxon) in off-shore deep water Black Sea, where significant gas reserves upside is expected
• Indebtedness well below European peers
• Stable dividend payer outlook (40% payout ratio)

Weaknesses/Threats

• Depreciation of USD eroded profits from higher oil price
• Tougher LT fiscal framework starting with 2015 may cap benefits from gas market liberalization
• Charge of the new tax on special constructions since 2014

Romgaz I Gas producer
Buy

Shareholding Structure

Ministry of Economy	70.01%
Fondul Proprietatea	14.99%
Free-Float	15.00%

Target price (RON/share)	49.50
Share price (RON/share)	33.25
MkCap (RON mn)	12,815.29
MkCap (EURmn)	2852.22

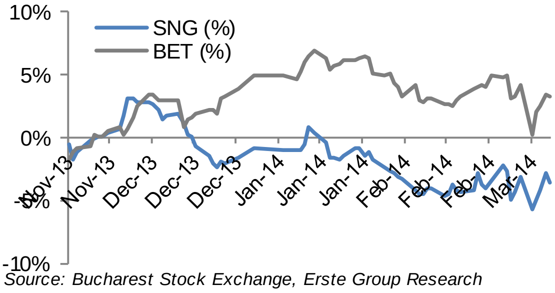
Company description

Romgaz, besides Petrom, is Romania's main gas producer, its output covering in 2013 more than 35% of the domestic demand. The company highly relies on gas exploration and production, with a contribution of over 75% to the operating performance, while the other business lines are gas imports, gas storage and power production. Romgaz has started in 2007 major investments in field redevelopments and seismic acquisitions and exploration drillings, aiming to renew its reserve base and maintain production. The company currently sells ~ 40% of its gas to households and 60% to industrial consumers, at regulated prices set by ANRE (more than 40% respectively 20% cheaper than the price of imported gas). Regulated tariffs should be completely phased out by end -2014 for industrial consumers, respectively by end -2018 for residential consumers, according to the timetable agreed by the Romanian authorities and IFIs.

Key Figures (RON mn) -IFRS-	2011	2012	2013p	2014e
Sales	4,195	3,838	3,894	4,562
EBITDA	1,939	1,878	2,007	2,527
EBIT	1,236	1,272	1,190	1,770
Financial result	107	124	110	74
Gross result	1,342	1,396	1,300	1,844
Net result	1,188	1,119	931	1,549
Non-current assets	7,734	6,190	6,235	7,633
Inventories	451	508	464	625
Receivables	1,096	1,039	2,209	1,207
Cash	1,429	1,739	1,564	1,280
Trade payables	n.a.	n.a.	n.a.	n.a.
Total assets	10,710	10,405	10,472	10,746
Total shareholder equity	9,164	9,345	9,218	9,644
Bank debt	7	0	0	0
Total liabilities	1,510	1,060	1,254	1,102
EBITDA margin	46.22%	48.92%	51.55%	55.40%
EBIT margin	29.45%	33.13%	30.55%	38.81%
Net margin	28.31%	29.16%	23.90%	33.96%
ROE	12.96%	11.98%	10.10%	16.06%
Quick ratio	2.70	6.46	4.94	4.10
Equity ratio	85.56%	89.81%	88.02%	89.75%
Net debt/EBITDA	-0.73	-0.93	-0.78	-0.51

Source: Romgaz, Erste Group Research

Price development (52 weeks)



Source: Bucharest Stock Exchange, Erste Group Research

Price performance

	1M	3M	6M	12M	Ytd
in RON	0.5%	-5.3%	n.a.	n.a.	-2.7%

Source: Romgaz, BSE, Erste Group Research

Target multiple	Value
EV/EBITDA 2014	4.45
P/E 2014	8.27
P/Sales 2014	2.81
P/BV 2014	1.39
DivY 2013e	5.45%

**)Multiples computed with Sales, EBITDA, Net profit estimated for FY14; dividend yield based on net profit for FY13 and 75% payout ratio*

Source: Romgaz, Erste Group Research

SWOT Analysis

Strengths/Opportunities

• Gradual gas market liberalization up to 2018, will strengthen the profitability profile
• Strong cash generation capabilities
• Profitable trading & storage business
• By implementing new enhanced recovery technologies and redevelopment of gas fields, the company could not only stop declining production, but even reverse the downward trend
• Major prospective resources (P50) of 80bn cm, which can be partially turned into reserves
• Ambitious exploration program, in the coming 5 years
• Strong dividend payer status (75% payout ratio in 2013)

Weaknesses/Threats

• Redevelopment of mature fields could bring operating expenses significantly higher
• The company may lose its natural gas storage business due to EU unbundling regulations
• Tougher LT fiscal framework starting in 2015 may cap benefits from gas market liberalization
• Receivable write-off risk given the weak financial stance of some clients
• Sluggish demand outlook might push down gas prices on medium/LT
• Charge of the new tax on special constructions since 2014
• Potential overwhelming future contribution to two national projects (hydro-power plant Tarniţa and submarine power cable to Turkey)

Nuclearelectrica I Nuclear power producer
N.R.

Shareholding Structure

Ministry of Economy	81.27%
Fondul Proprietatea	9.72%
Free-Float	9.01%

MkCap (RON mn)	2,550.13
MkCap (EURmn)	567.57

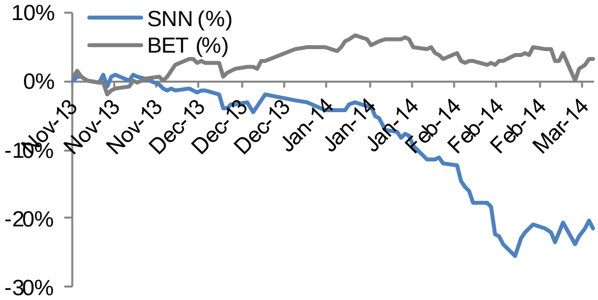
Company description

Cernavoda NPP branch operates units 1 and 2, and Pitesti Nuclear Fuel Plant branch, a qualified manufacturer for CANDU-6 type nuclear fuel that covers the entire demand of the two operational units from Cernavoda NPP. Both reactors are CANDU-6, natural uranium & heavy water type of 706.5 MW IC each, with the first being commissioned in April 1996, and the second one in May 2007. In 2013, about half of the company's output was sold on the regulated market at an imposed price, well below the wholesale power price. The same pattern will be replicated also for 2014 when 35% of the projected output is to be sold on the regulated market, at a price slightly higher than a year earlier, but still well below the wholesale market price. Nuclearelectrica holds a 84.65% stake in a project company for building reactors 3 and 4, new partners for completing the reactors being searched, with the total investment effort being estimated at EUR 6bn.

Key Figures (RON mn) -IFRS-	2010	2011	2012	2013p
Sales	1,515	1,593	1,653	1,932
EBITDA	565	556	556	854
EBIT	184	169	160	448
Financial result	-176	-66	-91	57
Gross result	8	103	70	505
Net result	4	83	24	417
Non-current assets	9,370	9,591	9,536	7,918
Inventories	477	391	369	386
Receivables	351	227	163	197
Cash	474	696	929	1,444
Trade payables	182	181	286	243
Total assets	10,715	10,922	11,007	11,338
Total shareholder equity	7,712	8,092	8,125	7,448
Bank debt	2,369	2,253	2,150	1,888
Total liabilities	3,003	2,830	2,883	3,890
EBITDA margin	37.3%	34.9%	33.6%	44.2%
EBIT margin	12.1%	10.6%	9.7%	23.2%
Net margin	0.3%	5.2%	1.5%	21.6%
ROE	0.1%	1.0%	0.3%	5.6%
Quick ratio	2.2	2.2	1.8	1.6
Equity ratio	72.0%	74.1%	73.8%	65.7%
Net debt/EBITDA	3.4	2.8	2.2	0.5

Source: Nuclearelectrica, Erste Group Research

Price development



Source: Bucharest Stock Exchange, Erste Group Research

Price performance

	1M	3M	6M	12M	Ytd
in RON	-6.6%	-20.4%	n.a.	n.a.	-19.1%

Source: Nuclearelectrica, BSE, Erste Group Research

Target multiple	Market price
EV/EBITDA 2014	5.03
P/E 2014	16.37
P/Sales 2014	1.40
P/BV 2014	0.34
DivY 2014e	5.19%

**)Multiples computed with 2014 estimated figures and 85% payout ratio considered on 2014*
Source: Nuclearelectrica, Erste Group Research

SWOT Analysis

Strengths/Opportunities

- Second lowest production cost among domestic power producers, after Hidroelectrica
- Vertically integrated power plant with in-house production of nuclear fuel, which translates into a high cost efficiency
- Profitability profile will improve following the gradual power market liberalization up to 2018
- Very experienced and highly professional staff
- Very good technical performance of the two CANDU-6 reactors

Weaknesses/Threats

- Weak power price environment in the medium term
- Huge CAPEX needs (~EUR 1.5bn) for the update of reactor 1 in order to extend its safely use lifetime (reactor 1 can safely operate up to 2022)
- Oversized RON 110mn new tax on special constructions will affect the profitability profile starting with 2014
- Large CAPEX needs for building the reactors 3 and 4 putting pressure on leverage if Nuclearelectrica will finally hold a majority stake in the joint venture company
- Potential overwhelming future contribution to two national projects (hydro-power plant Tarniţa and submarine power cable to Turkey)

Hidroelectrica I Hydro-power producer N.R.

Shareholding Structure

Ministry of Economy	80.06%
Fondul Proprietatea	19.94%
Equity Value (RON mn)	6,270.79
Equity Value (EURmn)	1,395.65

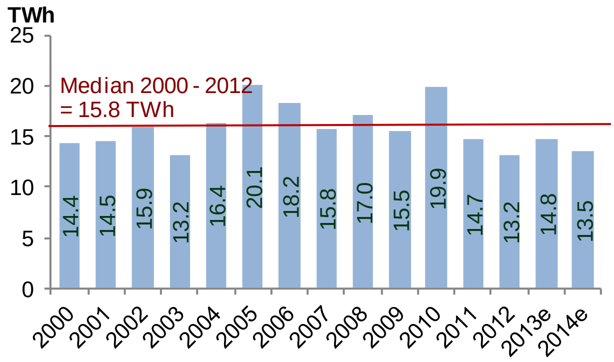
Company description

Hidroelectrica is the largest Romanian electricity producer, with an installed capacity of 6,470.4MW and a market share ranging between 23% and 35%, depending on the hydrological year. Power production in an average hydrological year is over 15 TWh, output varying from 13.2 TWh in 2012 (severe drought) to 20 TWh in 2010 (exceptional rainy year). The most valuable asset is Iron Gates I on the Danube river, with an IC of 1,050 MW, providing 10% of the national electricity output and 30% of the electricity produced by the company. After a one-year insolvency procedure ended in June 2013, Hidroelectrica returned in insolvency in February 2014 following a decision of the Bucharest Court of Appeal after a contestation made by power traders against the decisions taken by the judicial administrator during the first insolvency procedure ran between June 2012 and June 2013.

Key Figures (RON mn) -RAS-	2010	2011	2012	1H13
Sales	3,274	3,021	2,403	1,601
EBITDA	1,377	899	906	1,022
EBIT	503	161	-322	525
Financial result	-113	-122	-166	-43
Gross result	390	40	-488	481
Net result	292	6	-508	383
Non-current assets	19,667	20,339	19,914	19,516
Inventories	79	105	107	107
Receivables	297	418	246	255
Cash	100	89	57	283
Trade payables	888	1,126	1,022	n.a.
Total assets	20,144	20,962	20,326	20,165
Total shareholder equity	16,822	16,529	16,079	16,461
Bank debt	1,901	2,518	2,272	n.a.
Total liabilities	3,220	4,349	4,085	3,545
EBITDA margin	42.06%	29.76%	37.69%	63.81%
EBIT margin	15.36%	5.34%	-13.38%	32.76%
Net margin	8.93%	0.21%	-21.14%	23.91%
ROE	1.74%	0.04%	-3.16%	2.33%
Quick ratio	22.96%	19.21%	11.66%	27.55%
Equity ratio	83.51%	78.85%	79.11%	81.62%
Net debt/EBITDA	1.31	2.70	2.45	1.71

Source: Hidroelectrica, Erste Group Research

Gross power production development



Source: Hidroelectrica, Erste Group Research

Target multiple	Share price (fair value assigned by Erste)
EV/EBITDA 2014	6.40
P/E 2014	15.45
P/Sales 2014	2.35
P/BV 2014	0.39
DivY 2014e	5.50%

**)Multiples computed with 2014 estimated figures and an 85% payout ratio considered for 2014*
Source: Hidroelectrica, Erste Group Research

SWOT Analysis

Strengths/Opportunities

- The cancellation of disadvantageous contracts by the judicial administrator in 2012 (selling power at low prices, acquiring power at very high prices from old thermo plans) strongly improved the profitability profile
- Gradual profitability gains from market liberalization (first benefits to be seen in 2015)
- Main system service provider, with pivotal role in the NPS
- Hydro-power flexibility to meet peak demand and to quickly balance the power system, resulting into higher average output price than peers'
- Most sustainable energy source, with longer economic life of hydro-power plants

Weaknesses/Threats

- Very weak price recognized on the regulated market for 40% of the electricity sold
- Weak power price environment in the medium term
- Oversized personnel and third-parties expenses
- Oversized turbinated water expenses after the four-time tariffs jump in 2011 as result of an arbitrary decision taken by the Romanian Water Agency
- Business performance sensitive to weather conditions
- Oversized RON 180mn tax on special constructions starting with 2014
- Potential overwhelming future contribution for building hydro-power plant Tarniţa and submarine power cable to Turkey

CE Oltenia I Lignite-fired power producer
N.R.

Shareholding Structure

Ministry of Economy	77.17%
Fondul Proprietatea	21.53%
Equity Value (RON mn)	1,126.44
Equity Value (EURmn)	250.70

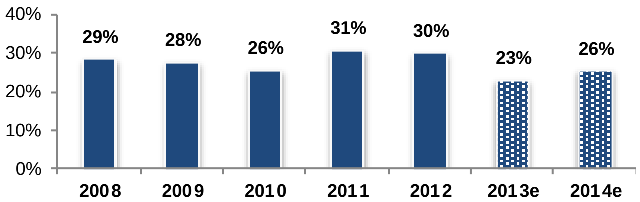
Company description

CE Oltenia was formed in May 2012 through the merger of three lignite-fired power plants, namely CE Turceni, CE Rovinari, CE Craiova, together creating the largest domestic coal power producer with an IC of 3,900 MW. The new company also included lignite-producer SNL Oltenia which easily ensures the entire consumption needs. Plants are obsolete, being commissioned between 1978 and 1987 (Turceni TPP - 5x 330 MW), between 1976 and 1979 (Rovinari TPP– 4 x 330 MW), respectively between 1987 and 1989 (Craiova TPP – 2x315 MW and 2x 150MW in cogeneration). Complete or partial modernization and environment works were done for a few units, additionally prolonging their lifetime by 15 years.

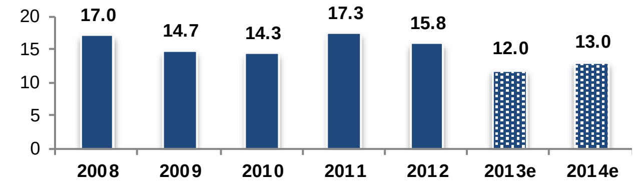
Key Figures (RON mn) -RAS-	2012
Sales	2,237
EBITDA	410
EBIT	44
Financial result	132
Gross result	176
Net result	118
Non-current assets	6,859
Inventories	335
Receivables	875
Cash	224
Trade payables	425
Total assets	8,341
Total shareholder equity	5,482
Bank debt	1,732
Total liabilities	2,551
EBITDA margin	18.32%
EBIT margin	1.99%
Net margin	5.29%
ROE	2.16%
Quick ratio	1.24
Equity ratio	65.73%
Net debt/EBITDA	3.68

Source: CE Oltenia, Erste Group Research

Market share development 2008 - 2014e (%)



Net production development 2008 - 2014e (TWh)



Note: For 2008-11, the cumulative figures for CE Turceni, CE Rovinari and CE Craiova were considered

Source:ANRE, Erste Group Research

Target multiple	Share price (fair value assigned by Erste)
EV/EBITDA 2014	6.08
P/Sales 2014	0.47
P/BV 2013	0.21

Source: CE Oltenia, Erste Group Research

SWOT Analysis

Strengths/Opportunities

• Important role in ensuring the stable functioning of Romanian and regional power network
• Turceni TPP has a strategic 400 kV connection with Iron Gates interconnection node, which creates favourable export opportunities on medium/LT
• Rovinari TPP has the lowest production costs among domestic coal producers, being set very near the brown coal mines
Technological system services of 600 MW provided to Transelectrica and guaranteed by the regulator ANRE
• Modernization and environment works are already done (partially or in progress) in the case of eight units of 330 MW from Turceni and Rovinari TPP
• Lignite needs comfortable covered by own mines

Weaknesses/Threats

• Collapse of the market share since 2013, mainly due to the sluggish demand and the eolian power boom
• Higher production costs than hydro and nuclear producer raises significant challenges to the business model, considering also the weak power price environment
• Oversized personnel costs (18,800 workers out of which 13,000 are involved in coal mines' activities)
• Old generation fleet which negatively impacts the operating efficiency and maintenance costs
• Extensive CAPEX of over EUR 500mn for the period 2013-18 for fully answering to modernization and environment needs

Transelectrica I Power transmission and system operator
Buy

Shareholding Structure

Ministry of Finance	58.69%
Fondul Proprietatea	13.50%
Free Float	27.81%

Target price (RON/share)	15.2
Share price (RON/share)	15.79
MkCap (RON mn)	1,157.46
MkCap (EURmn)	257.61

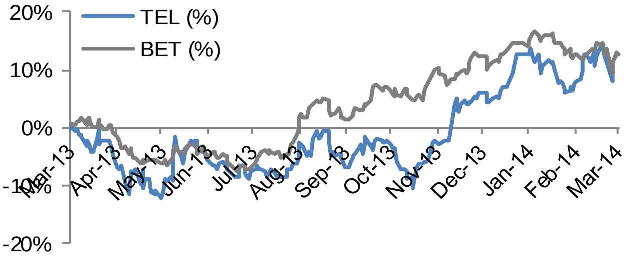
Company description

Transelectrica is the Romanian TSO, which manages and operates the electricity transmission system and provides electricity exchanges among Central and Southeastern European countries, as a member of UCTE and ETSO. Transelectrica is responsible for the transmission of electricity, system and market operations, grid and market infrastructure development and for ensuring the security of the Romanian power system. It also serves as the main link between electricity supply and demand, and holds the key role in matching power generation to demand. Transelectrica's tariff is set by the Energy Authority (ANRE), the regulatory formula allowing for a controlled operating profitability determined as the regulated return times the regulated asset base (RAB).

Key Figures (RON mn) -IFRS-	2011	2012	2013p	2014e
Sales	3,089	2,719	1,786	2,869
EBITDA	473	398	543	547
EBIT	176	83	208	175
Financial result	-32	-36	-9	-23
Gross result	143	47	199	152
Net result	110	34	162	114
Non-current assets	3,656	3,787	3,671	4,126
Inventories	42	40	37	39
Receivables	1,171	823	847	973
Cash	305	295	601	152
Trade payables	1,186	738	748	n.a.
Total assets	5,181	4,945	5,155	5,291
Total shareholder equity	2,424	2,431	2,563	2,587
Bank debt	1,146	1,153	1,177	989
Total liabilities	2,757	2,514	2,592	1,940
EBITDA margin	15.32%	14.63%	30.41%	19.08%
EBIT margin	5.69%	3.05%	11.64%	6.10%
Net margin	3.56%	1.27%	9.09%	3.97%
ROE	4.54%	1.42%	6.33%	4.40%
Quick ratio	1.06	1.17	1.47	1.16
Equity ratio	46.79%	49.16%	49.71%	48.90%
Net debt/EBITDA	1.78	2.16	1.06	1.53

Source: Transelectrica, Erste Group Research

Price development (52 weeks)



Source: Transelectrica, Erste Group Research

Price performance

	1M	3M	6M	12M	Ytd
in RON	4.6%	6.5%	21.0%	12.8%	0.0%

Source: Transelectrica, BSE, Erste Group Research

Target multiple	Value
EV/EBITDA 2014	3.17
P/E 2014	10.16
P/Sales 2014	0.40
P/BV 2014	0.22
DivY 2013e	11.9%

Source: Transelectrica, Erste Group Research

SWOT Analysis

Strengths/Opportunities

- Low-risk business model (RAB-based transmission tariff formula)
- Reduced weight (less than 6.5%) of transmission tariff in final power price leaves room for reasonable growth of tariff in the future
- Major CAPEX in 2014-18 should result in higher profitability, if methodology is fairly applied
- Administrative plan for 2014-17 assumed by new Supervisory Board increase predictability of financials
- Stable and considerable lower leverage compared to Western peers
- Bond program in LC worth RON 900mn up to 2017 aimed to reduce reliance on FX funding and to naturally hedge the FX risk

Weaknesses/Threats

- High regulatory risk perception
- Untransparent annual transmission tariff
- High volatility of the operating performance
- Increased production of green energy that adds volatility to the energy production patterns
- Uncontrollable unrealized FX gain/losses which highly influences volatility of net result
- Currency mismatch: loan payments in FX, revenues in RON
- High reliance on ST financing in FC puts refinancing risks in question

Aeroporturi Bucuresti I Airports Operator (Baneasa & Otopeni) N.R.

Shareholding Structure

Ministry of Economy	80.00%
Fondul Proprietatea	20.00%
Equity Value (RON mn)	1,496.00
Equity Value (EURmn)	332.95

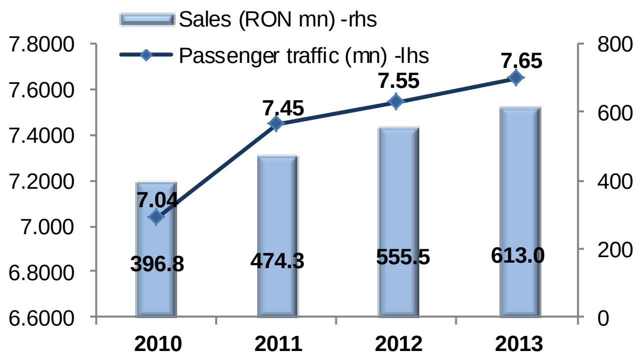
Company description

CN Aeroporturi Bucuresti operates Romania's two largest airports, located in Bucharest, namely Henri Coanda (Otopeni) and Aurel Vlaicu (Baneasa), being set up in 2010 through the merger of the two companies that had separately managed them. The two airports cumulatively accommodate ~85% of the national air traffic, with 95,984 take offs and landings and more than 7.65mn passengers in 2013. In March 2012, the traffic from Baneasa was moved to Otopeni, only small aircrafts of up to 10 seats, still operating at Baneasa airport thereafter. On Henri Coanda airport are currently operating 34 airlines, transporting passengers to 71 destinations. The highest weight in total flight number comes from Tarom (>30%), Aegean Airlines, Lufthansa, and Austrian Airlines.

Key Figures (RON mn) -RAS-	2011	2012	2013
Sales	474	556	613
EBITDA	213	215	n.a.
EBIT	88	81	n.a.
Financial result	-21	-13	n.a.
Gross result	68	68	78
Net result	53	53	n.a.
Non-current assets	5,640	5,704	n.a.
Inventories	12	14	n.a.
Receivables	66	73	n.a.
Cash	23	47	n.a.
Trade payables	60	32	n.a.
Total assets	5,743	5,838	n.a.
Total shareholder equity	4,976	4,979	n.a.
Bank debt	185	281	n.a.
Total liabilities	704	782	n.a.
EBITDA margin	44.87%	38.76%	n.a.
EBIT margin	18.66%	14.56%	n.a.
Net margin	11.09%	9.56%	n.a.
ROE	1.06%	1.07%	n.a.
Quick ratio	89%	96%	n.a.
Equity ratio	86.64%	85.29%	n.a.
Net debt/EBITDA	0.76	1.09	n.a.

Source: Intelli News, Fondul Proprietatea, Erste Group Research

Sales vs. Passenger traffic evolution



Source: Intelli News, Fondul Proprietatea, Erste Group Research

Target multiple	Share price (fair value assigned by Erste)
EV/EBITDA	8.04
P/E	28.16
P/Sales	2.44
P/BV	0.30
DivY	3.15%

**)Multiples computed with EBITDA, Net profit, Net Debt and Shareholders Equity for FY12, respectively Sales for FY13*

Source: Intelli News, Fondul Proprietatea, Erste Group Research

SWOT Analysis

Strengths/Opportunities

• Sound balance sheet
• Low indebtedness
• Upward trend of the passenger traffic (+1.35% in 2013, +1.33% in 2012, +5.86% in 2011)
• Entrance into the visa-free Schengen zone expected for 2014 (in 2012, 65% of the airline curses initiated from the Henri Coanda airport had states from the Schengen Aria as destination)
• Stable dividend payer

Weaknesses/Threats

• Vulnerability to LC appreciation against Euro (most of the company's revenues originate in the operating tariffs charged to airline companies, which are expressed in euros; consequently, company's revenues are helped by a depreciated local currency)
• Vacancy of commercial spaces (revenues from rents had a 3% weight in total revenues in 2012)

Posta Romana I Postal Services Provider N.R.

Shareholding Structure

Ministry of Economy	75.00%
Fondul Proprietatea	25.00%
Equity Value (RON mn)	534.93
Equity Value (EURmn)	119.06

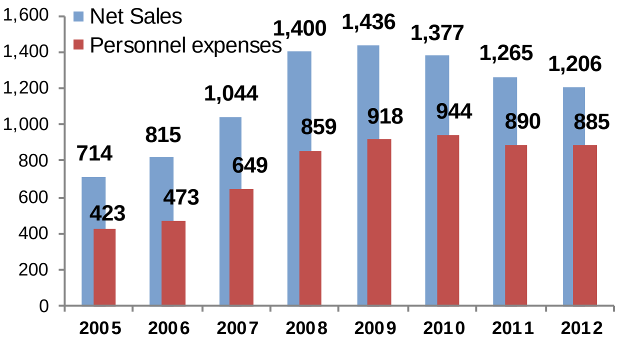
Company description

Posta Romana is the national provider of postal and non-postal services, including electronic mail services, magazine subscriptions, printing and insertion, direct marketing, counter collection and payment agency services. On the delivery services side, Posta Romana is the market leader, operating about 70% of the national deliveries. Around 50% of the annual counter collections are also made by Posta Romana as result of its long-term partnerships with companies (Romtelecom, Electrica, Vodafone, Orange, etc.) and public institutions. At the end of 2013, Posta Romana operated a territorial network of over 5,500 post offices and 30,000 personnel, making it the largest Romanian employer.

Key Figures (RON mn) -RAS-	2010	2011	2012
Sales	1,377	1,265	1,206
EBITDA	-66	-103	0.5
EBIT	-128	-190	-61
Financial result	7	7	9
Gross result	-121	-183	-52
Net result	-121	-183	-52
Non-current assets	911	924	820
Inventories	23	15	12
Receivables	121	149	142
Cash	49	53	37
Trade payables	159	133	120
Total assets	1,108	1,131	1,013
Total shareholder equity	558	386	340
Bank debt	78	80	20
Total liabilities	544	746	669
EBITDA margin	n.m.	n.m.	0.04%
EBIT margin	n.m.	n.m.	n.m.
Net margin	n.m.	n.m.	n.m.
ROE	n.m.	n.m.	n.m.
Quick ratio	34%	37%	32%
Equity ratio	50.41%	34.09%	33.57%
Net debt/EBITDA	n.m.	n.m.	n.m.

Source: Intelli News, Fondul Proprietatea, Erste Group Research

Net sales vs Personnel expenses evolution (RON mn)



Source: Intelli News, Fondul Proprietatea, Erste Group Research

Target multiple	Share price (fair value assigned by Erste)
P/Sales	0.44
P/BV	1.57

**)Multiples computed with Sales and Shareholders Equity for FY12*

Source: Intelli News, Fondul Proprietatea, Erste Group Research

SWOT Analysis

Strengths/Opportunities

- Largest territorial network among domestic delivery services providers, with good coverage in the rural areas
- Valuable real estate assets
- Sequential rebranding of its activity (ex: Prioripost for the express services activity)
- Significant brand attachment considering the 151 years of tradition on the Romanian delivery services market
- Privatization exercise to be run for a 51% stake in the company by end-October 2014 according to the last official calendar (advisory consortium already selected) subsequently to a debt-to-equity conversion for overdue payables towards the Romanian state

Weaknesses/Threats

- Oversized personnel expenses
- Unprofitable obligations as national postal provider which were prolonged by law until December 2014, with negative impact on the ST operating performance
- Downward trend of postal services business volume (Romania is among the last European countries in the top by letters and postal card traffic)
- Fierce competition from private players
- Large investments required for implementing an integrated IT system (less than 30% of post offices are computerized)
- Large debts towards the state budget (by end-September, 2013, Posta Romana's arrears were RON 190.7mn, being the 7th largest debtor to the Romanian state's budget)

Salrom I Salt Producer
N.R.

Shareholding Structure

Ministry of Economy	51.01%
Fondul Proprietatea	48.99%
Equity Value (RON mn)	345.57
Equity Value (EURmn)	76.91

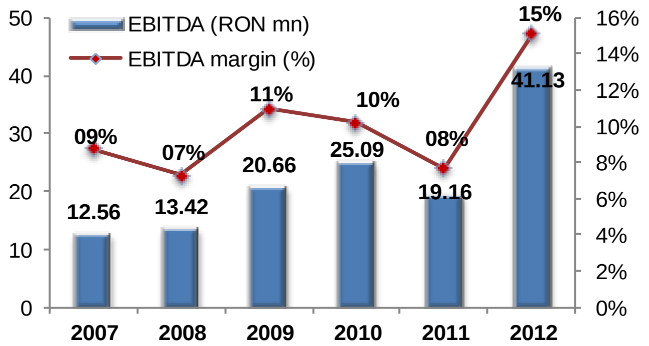
Company description

Founded in 1997, the state-owned company Salrom is the sole Romanian salt producer, ranking 4th in the specific top of companies from CEE. With access to significant salt reserves, the company operates two business lines represented by mining and quarrying of salt (rock and recrystallized salt, salt solution) along with other non-metallic minerals (chalk, feldspar), and by health and recreational tourism in the saline (as a secondary activity). The company currently holds seven salines (Ramnicu Valcea, Slanic, Ocna Dej, Ocna Mures, Targu Ocna, Praid and Cacica) and owns a product portfolio encompassed of edible and industrial salt, salt solutions, tablets of salt for water softening, salt briquettes for animals breeding, salt for roads de-icing.

Key Figures (RON mn) -RAS-	2010	2011	2012
Sales	245.3	250.2	272.0
EBITDA	25.1	19.2	41.1
EBIT	12.2	5.2	25.3
Financial result	-1.0	0.7	0.7
Gross result	11.2	5.9	27.0
Net result	6.0	1.4	20.8
Non-current assets	125.5	134.1	163.0
Inventories	10.1	12.9	14.8
Receivables	35.4	27.6	37.6
Cash	4.9	8.0	2.5
Trade payables	18.4	12.6	17.7
Total assets	231.9	230.6	286.6
Total shareholder equity	177.1	200.1	236.0
Bank debt	0.0	0.0	0.0
Total liabilities	38.3	25.1	37.1
EBITDA margin	10.23%	7.66%	15.12%
EBIT margin	4.97%	2.08%	9.32%
Net margin	2.43%	0.55%	7.64%
ROE	3.37%	0.68%	8.81%
Quick ratio	2.55	3.39	2.97
Equity ratio	76.39%	86.78%	82.34%
Net debt/EBITDA	-2.39	-2.88	-1.71

Source: Intelli News, Erste Group Research

Profitability margin development 2007 - 2012



Source: Intelli News, Erste Group Research

Target multiple	Value
EV/EBITDA	6.69
P/E	16.63
P/Sales	1.27
P/BV	1.21
DivY	0.05%

**)Multiples computed with 2012 figures*

Source: Intelli News, Fondul Proprietatea, Erste Group Research

SWOT Analysis

Strengths/Opportunities
• Upward trend of exports in total sales (33% in 2012)
• No indebtedness (investments are self-financed)
• Five out of seven salines (Salina Slanic, Ocnele Mari, Targu Ocna, Salina Cacica and Praid) can be efficiently used as tourism assets enjoying high business potential (1mn tourists/year in 2010-2012), without relevant CAPEX needs
• Vertically integrated salt production with own deposits and distribution network
• Eligible for withdrawing European granted funds (RON 5.9mn in 2012)

Weaknesses/Threats
• Salt price's high sensitivity to railway transport, fuel and energy costs
• High reliance on weather conditions during the cold season, as a significant part of the company's rock salt (roughly 33%) is used for roads de-icing
• Highly competitive market in the region caused by the cheap salt from Ukraine and Belarus
• Exposure to exchange rate risk, as the company imports the needed raw material for the salt manufacturing (potassium Ferro cyanide, potassium iodate)
• High CAPEX needs as a major part of its production equipment has exceeded the normal useful life and has to be updated
• Entrance in insolvency of one of its important clients, Oltchim (30% of Salrom's sales being generated by sales in the chemical industry)

Alro I Aluminum Producer
N.R.

Shareholding Structure

Vimetco NV	84.19%
Fondul Proprietatea	10.21%
Free Float	5.60%

Market Cap (RON mn)	928.63
Market Cap (EURmn)	206.68

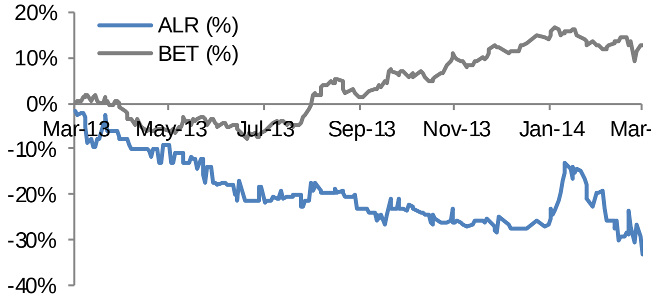
Company description

Part of the Russian Group Vimetco, Alro is Romania's only primary aluminum and aluminum alloy producer and the largest one in Central and East Europe (excluding Russia), with an installed production capacity of 265,000 mt electrolytic aluminum, and 300,000 mt primary aluminum. Main subsidiaries include Vimetco Extrusion focusing on processed aluminum products and Alum Tulcea, Romania's only alumina refinery, as well as a bauxite mine in Sierra Leone. The company's products are used in the manufacturing of cables and wires for energy and telecommunication, construction materials, components and parts for auto, as well as durable goods industries.

Key Figures (RON mn) -IFRS-	2010	2011	2012	2013p
Sales	1,833	2,250	2,301	2,017
EBITDA	350	484	286	-21
EBIT	276	405	286	-21
Financial result	-41	-146	-474	-43
Gross result	235	259	-188	-64
Net result	169	218	-155	-76
Non-current assets	1,318	1,542	1,280	1,284
Inventories	331	447	443	430
Receivables	126	114	144	179
Cash	300	254	214	57
Trade payables	81	98	116	180
Total assets	2,163	2,678	2,281	2,069
Total shareholder equity	1,178	1,720	1,186	1,049
Bank debt	614	624	681	544
Total liabilities	985	958	1,096	1,020
EBITDA margin	19.09%	21.51%	12.42%	-1.05%
EBIT margin	15.05%	18.01%	12.42%	-1.06%
Net margin	9.21%	9.70%	-6.75%	-3.75%
ROE	14.33%	12.68%	-13.10%	-7.22%
Quick ratio	1.59	2.29	1.20	0.92
Equity ratio	54.46%	64.23%	51.97%	50.69%
Net debt/EBITDA	0.90	0.76	1.63	-22.99

Source: Alro, Erste Group Research

Price development (52 weeks)



Source: BVB, Erste Group Research

Price performance					Market price
	1M	3M	6M	12M	Ytd
in RON	-16.9%	-9.7%	-13.3%	-33.4%	-10.1%

Source: BVB,

Target multiple	Market price
P/Sales	0.46
P/BV	0.89

**)Multiples computed with Sales, EBITDA, Net Debt and Shareholders Equity for FY13*
Source: Alro, Erste Group Research

SWOT Analysis

Strengths/Opportunities

• Large weight of exports in sales, 80% of sold output being exported via LT contracts (55% of primary aluminum, ~90% of processed aluminum- 2012)
• Sustainable integrated business model through ownership of bauxite mine in Sierra Leone and Romania's alumina refinery, Alum Tulcea
• Increasing focus on sales of high value added products (processed aluminum) as percentage of total sales (19% in 2008 vs. 49% in 2012)
• Auto manufacturers' shift towards the substitution of steel with aluminum
• Diversified client portfolio
• Potential higher demand for primary and processed aluminum from Asian countries

Weaknesses/Threats

• High reliance on electricity price (largest domestic power consumer)
• Electricity bills spiked after losing the preferential contract with power producer Hidroelectrica (from ~RON 130/MWh in 2011 to liberalized market prices of over RON 180/MWh in 2013)
• Supplementary pressure on power expenses, stemming from EUR 15.8/MWh in early 2012 to EUR 33.8/MWh past mid 2013 from green certificates and an additional EUR 5/MWh since 2011 from cogeneration tax
• Weak demand from construction and transportation industries which are two of the biggest aluminum consumers

CN Administratia Porturilor Maritime I Port Administrator N.R.

Shareholding Structure	
Ministry of Transportation	60.00%
Fondul Proprietatea	20.00%
Constanta City Council	20.00%
Equity Value (RON mn)	452.97
Equity Value (EURmn)	100.81

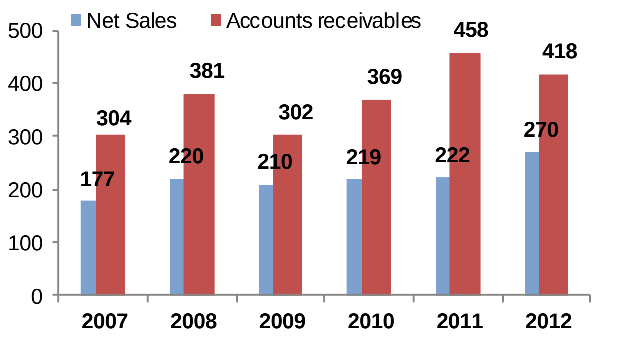
Company description

CN Administratia Porturilor Maritime is the port authority for Constanta, Midia, Mangalia maritime ports, providing repair, maintenance and modernization works for the infrastructure under administration, also issuing licenses and operational permits for activities within the ports. The Port of Constanta, the main Romanian port under the company's administration, is an important hub between landlocked countries in Central and Eastern Europe and Trans Caucasus, Central Asia and the Far East. The port is located at 85nM from the Danube River to which it is connected by the Danube-Black Sea, canal having a dedicated barge terminal in the southern part in close connection to the Danube.

Key Figures (RON mn) -RAS-	2010	2011	2012	1H13
Sales	219	222	270	123
EBITDA	70	83	86	50
EBIT	35	51	51	34
Financial result	-3	1	1	2
Gross result	32	52	47	35
Net result	25	42	36	30
Non-current assets	550	584	596	668
Inventories	2	2	4	3
Receivables	369	458	418	365
Cash	47	85	109	115
Trade payables	28	19	17	n.a.
Total assets	1,028	1,167	1,143	1,157
Total shareholder equity	309	370	359	364
Bank debt	71	49	26	n.a.
Total liabilities	709	783	753	764
EBITDA margin	32.04%	37.16%	31.74%	40.97%
EBIT margin	15.86%	22.92%	18.91%	27.35%
Net margin	11.28%	18.99%	13.19%	24.14%
ROE	7.98%	11.42%	9.92%	8.16%
Quick ratio	4.16	5.66	6.41	6.63
Equity ratio	30.04%	31.69%	31.40%	31.51%
Net debt/EBITDA	0.88	0.49	0.18	n.a.

Source: Intelli News, Fondul Proprietatea, Erste Group Research

Net sales vs Accounts Receivables evolution (RON mn)



Source: Intelli News, Fondul Proprietatea, Erste Group Research

Target multiple	Share price (fair value assigned by Erste)
P/Sales	1.70
EV/EBITDA	5.65
P/E	12.86
P/BV	1.27

Source: Erste Group Research

SWOT Analysis

Strengths/Opportunities

• Good connections with all means of transport (railway, road, airway and pipelines) and the Danube river
• Land availability for future expansion
• Strong negotiating power with customers due to the port authority status (revenues have seen little contraction during the crisis years)
• Good access to funding for investments from ERDF funds (~EUR 100mn in investments budgeted for 2014, out of which ~EUR 90mn from ERDF)
• High profitability margins

Weaknesses/Threats

• Low port traffic following the economic crisis affects the profit of port operators which is the companies' main clientele
• Historically high receivables collection period of over 1.5yrs, which have deteriorated even more in recent years as the company offered payment deferrals to several port operators
• Low provisioning for doubtful receivables compared to high stock account receivables

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Company	ISIN	Disclosure
Fondul Proprietatea	ROFPTAACNOR5	2, 3

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Accumulate	+10% < target price < +20%
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Distribution of ratings

	Coverage universe		Inv. banking-relationship	
Recommendation	**No.**	**in %**	**No.**	**in %**
Buy	48	24.5	5	22.7
Accumulate	47	24.0	4	18.2
Hold	54	27.6	9	40.9
Reduce	13	6.6	2	9.1
Sell	19	9.7	1	4.5
N.R./UND.REV./RESTR.	15	7.7	1	4.5
Total	**196**	**100.0**	**22**	**100.0**

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