

Fondul Proprietatea

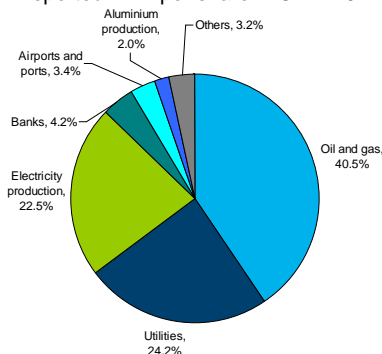
05 April 2012

Greenlight to return value to shareholders

Financial holding

Romania

Reported NAV per share: RON 1.20



Current price*

RON 0.59

Buy

Fair value

RON 0.89

Rating maintained

Net asset value	Official NAV		Fair values	
	RON m	RON/share	RON m	RON/share
Listed shares	6,390	0.48	6,274	0.47
Unlisted shares	9,151	0.68	8,425	0.63
Cash	472	0.04	472	0.04
Total assets	16,063	1.20	15,220	1.13
Debt	-19	0.00	-19	0.00
Deferred taxes	-14	0.00	-14	0.00
NAV	16,030	1.20	15,187	1.13
Adjustments to NAV			-3,220	-0.24
Implied fair value			11,967	0.89
Closing price as of Apr 03, 2012			8,171	0.59
Upside (%)				50.5%

Source: KBC Securities

*priced at COB 03 Apr 2012

Fondul Proprietatea's share price has risen 38.9% and outperformed the BET index by 12.6% year-to-date. However, we see more upside stemming from the eventual sale of shares in the unlisted part of the portfolio, a buy-back program, potential IPOs and SPOs and the potential listing in Warsaw. We have adjusted our fair value for Fondul Proprietatea to reflect the risk of delays in privatizations, the uncertain outcome of litigation over a 10% stake in Nuclearelectrica and changes in the valuation for some of the companies. Our fair value has fallen to RON 0.89 per share, although this still implies 50.5% upside. We maintain our Buy rating.

Buy rating maintained

- **Incentives for fund manager to return value to shareholders:** Given the fund's still high discount to NAV, we would view the gradual return of cash to shareholders positively. The approval in the EGM on 4 April 2012 of a proposal to pay fund manager Franklin Templeton an extra fee for cash returned to shareholders via buy-backs or special dividends from the sale of stakes above book value should help to align the interests of shareholders with those of the administrator. The extra fee will be 1.5% of the distributed value up to 2013 and 1.0% after 2013.
- **Share buy-back and dividends:** The AGM on 25 April 2012 will vote on the distribution of a DPS of RON 0.03854, implying a 6.5% dividend yield. The AGM will also vote on a buy-back program for 8% of the fund's shares with a view to cancellation. These programs match the requirements of shareholders and should help narrow the discount to NAV.
- **Potential disposal of gas and electricity distributors:** The fund has selected an intermediary to help sell some of the stakes in gas and electricity distributors and suppliers in its portfolio. We see putting some of these firms up for sale first as a good choice, as they already have majority private owners (Enel, E.ON, GDF), are highly regulated and are more advanced in the restructuring process than state-owned companies. In addition, these companies have no prospects for stock exchange listing, as the majority owners are themselves listed. In some cases, the fund might receive the support of the state, which is also part owner in the companies for sale.
- **Listing on the Warsaw Stock Exchange:** Eventual listing on the Warsaw Stock Exchange in addition to the BSE could be a potential trigger for the fund due to increased visibility and access to new investors. However, there are several hurdles including the technical connection between the two depositaries and the methodology of the listing. Templeton should announce a plan by end-May 2012.
- **IPOs and SPOs:** After completion of Transelectrica SPO, several companies in the fund's portfolio are preparing for listing or for the sale of additional packages: Transgaz SPOs, Romgaz listing and SPO, Hidroelectrica and Nuclearelectrica IPOs. While we see possible delays due to political risk, the listings should provide a reference point for the valuation of the fund's portfolio and eventually improve the transparency and profitability of the companies, as public company shareholders will be able to closer monitor the policy of the managers.
- **High discount to NAV unjustified:** Fondul Proprietatea currently trades at a 50.4% discount to official NAV and a 47.6% discount to our estimated NAV. We see the discount as too high: the inefficiencies of firms in the portfolio have already been taken into account, while other issues that could potentially justify discounts have been resolved (e.g. voting rights limitations).

Shareholders want the administrator to return value

At the EGM on 4 April 2012, shareholders voted on the request made by Manchester Securities Corp (an affiliate within the Elliott group of companies) to increase the fee received by fund manager Franklin Templeton for returning cash to shareholders via buy-backs or dividends. The EGM on 25 April 2012 will vote on the distribution of a dividend of RON 0.03854 per share (dividend yield 6.5%) and the buy-back of 8% of the fund's shares for cancellation. We would view the eventual disposal of some assets and the return of cash to shareholders positively, as this should narrow the discount to NAV. We do not believe there is any risk of a fire sale: the portfolio is not sufficiently liquid, plus the shareholders have sufficient control via the supervisory board and via the 20% limit on disposals per year.

- **The extra fee** as proposed by the shareholder will amount to 1.5% out of the entire distributions done by 2013 and 1% after 2013. The extra fee will apply to cash distributed only from asset disposals and not from the regular dividend stemming from the fund itself, which receives dividends from the companies in its portfolio. (For example, the dividend from regular 2011 profit like the one proposed for approval on 25 April 2012 would not entitle Templeton to an additional fee, while the buy-back would trigger an extra fee for the administrator.)
- **The share buy-back** should span over a period of 18 months and should take place at a price anywhere between RON 0.2 and RON 1.5 per share. The buy-back would be restricted to buying back only 25% of the average traded volume per day. The fund had already accumulated cash of RON 470m at the end of February, while the dividend and the share buy-back together will require RON 1,175m, with the remaining money to be obtained from dividends (we estimate at least RON 600m to be cashed-in in 2012) and the eventual sale of companies in the portfolio.

Potential exit from some of the companies in the portfolio

The first stakes targeted for disposal are the gas and electricity distribution and supply companies in Fondul Proprietatea's portfolio. We believe the administrator is right to select these companies for disposal first, as they are heavily regulated and so have rather limited growth potential in terms of profitability. Also, these firms are already privatized which means there are no opportunities for the fund to sell its stakes (together with the state) as controlling packages to investors. (The only exceptions are the four companies that are still majority state-owned, see table below.) Also, these companies have been partly restructured, so the potential for cost benefits is also somewhat low.

The privatization contracts of these companies do not contain any clauses regarding dividend obligations, thus these firms are not outstanding dividend payers. The cumulated value of the fund's stakes in these gas and electricity companies stands at € 530m according to book value. Investment bank Citigroup Global Markets Limited will assist Templeton in the transaction. The last similar transaction was the sale of CEZ Romania to the main shareholder at a 2.3x P/Bk in 2009. As yet, there has been no indication which of these stakes will be the first up for sale, although the state has a Put option to sell in some of them and the fund might be able to join the state in these transactions. This is the case for E.ON Moldova and Enel, in which the state has an option to sell.

Fondul Proprietatea: Companies targeted for sale

	% owned by the fund	Latest official value (EURm)	
E.ON Moldova Distribuție S.A	22%	50.8	Electricity distribution
E.ON Gaz Distribuție S.A	12%	26.6	Gas distribution
E.ON Energie România S.A	13%	21.7	Gas supply
Enel Distribuție Muntenia	12%	77.7	Electricity distribution
Enel Energie Muntenia	12%	8.6	Electricity supply
Enel Distribuție Banat S.A	24%	72.9	Electricity distribution
Enel Distribuție Dobrogea S.A	24%	50.4	Electricity distribution
Enel Energie S.A	12%	4.5	Electricity supply
GDF Suez Energy Romania	12%	78	Gas distribution & supply
Electrica Distribuție Muntenia Nord S.A	22%	54.8	Electricity distribution
Electrica Distribuție Transilvania Nord S.A	22%	39.3	Electricity distribution
Electrica Distribuție Transilvania Sud S.A	22%	42.3	Electricity distribution
Electrica Furnizare S.A	22%	0	Electricity supply
Total		527.6	

Source: Fondul Proprietatea

SPOs and IPOs planned by the state should improve valuations and provide a reference point

As part of the agreement with the IMF, the Romanian state plans to sell additional stakes in state-owned listed companies on the Bucharest Stock Exchange and also to list some stakes in other companies. We view the listings as positive for Fondul Proprietatea: the extra corporate governance rules and disclosure requirements that apply to listed companies should help investors to closely monitor the management's actions and make sure the strategies target improvements in profitability. In addition, the listings will provide a reference valuation, which should make the NAV more transparent for the fund and allow an easy exit opportunity at a later date, once the companies have started to show improved profitability. However, we also acknowledge the risk of the timetable presented by the government not being followed strictly: the program includes five companies to be sold this year, although the government registered delays in similar transactions in the past. Also, Romanian elections in November pose a threat to the realization of the program. Even so, we believe the realization of even part of this ambitious program would be positive for the fund.

Fondul Proprietatea: Companies targeted for sale

	% owned by the fund	% sold by the state	Value of the company (€ m)*	Timing of the IPO/SPO	Sector
Transelectrica	13.49%	15.00%	268.4	March - completed	Electricity grid
Transgaz	14.98%	15.00%	617.0	June	Gas network operator
Romgaz	14.99%	15.00%	1,862.7	2H12	Gas E&P
Hidroelectrica	19.94%	10.00%	3,833.5	2H12	Hydro electricity producer
Nuclearelectrica	9.72%	10.00%	1,193.6	2H12	Nuclear electricity producer

Source: KBC Securities estimates, company data

*as reported in the latest NAV statement for the unlisted companies

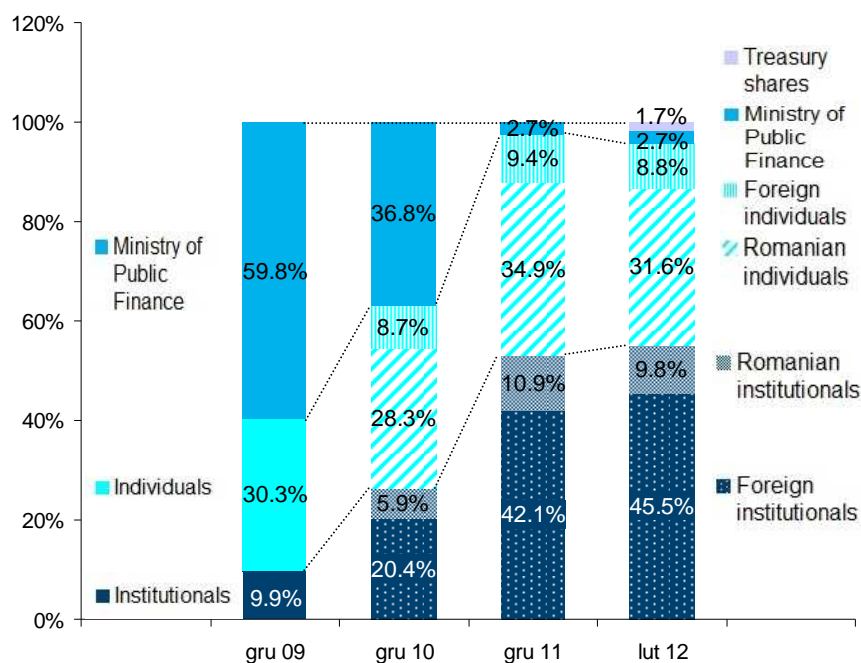
Listing on Warsaw Stock Exchange

The EGM on 4 April 2012 also voted on listing Fondul Proprietatea on the Warsaw Stock Exchange. We view the potential listing positively as it would increase the fund's visibility among foreign investors and would open up the shares to new investors. The management will come up with a more detailed plan by the end of May and will have to overcome the main obstacles to the buy-back plan: first, the initial plan of a share buy-back and resale in Warsaw is hindered by Romanian buy-back regulations which are somewhat unclear and the fund will have to receive the approval of Romania's National Securities Commission; second, to ensure that shares are fungible between the two markets, the two depositaries will have to be connected.

Decreased pressure from the lowering of the state's stake

Fondul Proprietatea's price was on an accelerated upward path in the first three months of 2012 as the state's supply of shares in the fund dwindled. The state's stake in the fund decreased at an accelerated rate in 2011 as more shares were transferred from the state to those persons entitled to receive them under Romanian law. The state's percentage holding in the fund decreased from 36.8% to 2.8% in 2011, the fastest rate since the fund's inception. We believe many of these new investors sold their shares in order to cash-in quickly, which put some pressure on the market price. Thus, despite the fact that the state distributed 34% of its shares in the fund to Romanian individuals, the stake held in the fund by Romanian individuals only grew 6.6% in 2011, indicating that most of the new shares must have been sold quickly on the market, with the majority probably ending up with foreign institutionals. However, the state ran out of shares in Fondul Proprietatea at the end of 2011, which has reduced the selling pressure. This could be one of the reasons for the significant increase in the fund's share price in the last three months.

Fondul Proprietatea: Evolution of shareholders structure



Source: Fondul Proprietatea

Improved corporate governance of state-owned companies

Governmental Ordinance (OUG) 109/2011 introduced new corporate governance rules for state-owned companies. In our view, this should help to improve the profitability of the state-owned companies in the fund's portfolio as well as their transparency. The new rules should also help the fund manager to become more consistently involved in the life of the fund's companies. The main changes brought by OUG 109/2011 are as follows:

- **The establishment of “professional management”:** Professional management must be established with the help of a recruitment company. The announcement for hiring must be published in two financial newspapers. The management must also have a strategic plan established with clear financial targets to be achieved. Remuneration will be based on the achievement of these targets.
- **The board should also be independent and professional:** The board of administrators can be made up of between five to nine members with experience in management. Only two members can be state employees; the rest must be professionals and at least one of them must have more than five years experience in the financial sector. The board members must be selected with the help of a recruitment agency.
- **Clear financial targets should be established:** The board must present a strategic plan for the period in which it is elected and the plan has to be approved at a shareholders' meeting. The plan must have clear financial targets to be achieved by the board members.
- **Cumulative voting rights:** Shareholders with stakes of 10% or more can ask for the introduction of cumulative rights voting when electing board members. Any shareholder with 10% or more voting rights can ask to dissolve the previous board and elect a new one based on cumulative rights.
- **Access to information:** The shareholders of the company must have access to information required by law, published on the company's website. The AGM and EGM information must be published 30 days in advance.

Energy companies to benefit from market liberalization

In accordance with the IMF agreement, the Romanian government is working on a calendar for the liberalization of the country's energy market. A draft law for establishing the schedule for liberalization of prices on electricity markets has already been forwarded by the government for approval in parliament. The law stipulates that industrial and home consumers will receive energy from a mixture of regulated energy and energy bought from the market. The percentage of energy bought from the market will increase as follows:

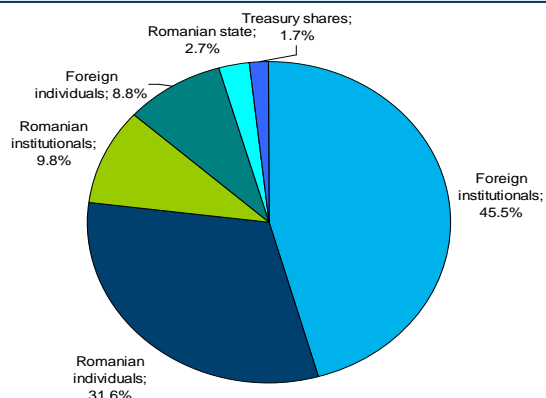
- For households: 10% as of July 2013, 20% as of January 2014, 30% as of July 2014, 40% as of January 2015, 50% as of July 2015, 60% as of January 2016, 70% as of July 2016, 80% as of January 2017, 90% as of July 2017, 100% as of January 2018.
- For industrial consumers: 15% as of September 2012, 30% as of January 2013, 45% as of April 2013, 65% as of July 2013, 85% as of September 2013 and 100% as of January 2014.

Energy regulator ANRE will have the power to block the increase for six months if there is a major disequilibrium between supply and demand. Gradually, all consumers should be able to choose the supplier who offers better prices so changes between suppliers are anticipated. In the current situation, on the other hand, all companies supply energy at the same regulated price and there is no competition between them.

Political risk

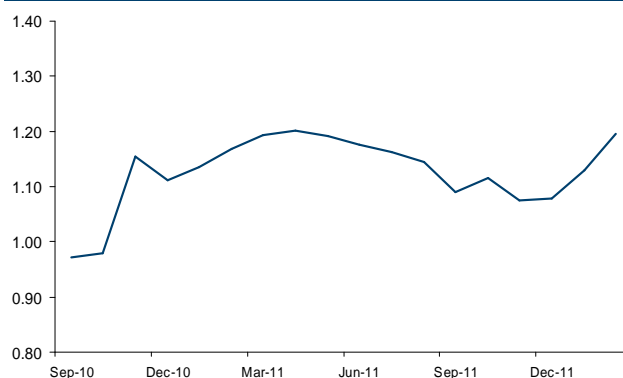
While we acknowledge the potential triggers for the fund mentioned above (i.e. the sale of some companies, the start of the buy-back program, the listing of some companies in the short term, restructuring of state-owned companies over the longer term), we also acknowledge the risk and potential implications for the fund's activity attached to any change in the political sphere in Romania. Romania will hold legislative elections in November 2012. In addition, the IMF agreement is expiring and will not be renewed. While it is currently too early to tell if an eventual change in political power will lead to any impediments to the development of Fondul Proprietatea and the companies in the fund's portfolio, we believe the set of measures being pushed forward by the current government are likely to offer some protection: for the legislative part, the new laws, once passed, should offer the fund some protection against any potential future impediments. Regarding the listings, the government is likely to push ahead with the current pipeline and, while there might be delays, we hope to see at least some of the listings being realized before elections.

Fondul Proprietatea: Shareholders structure



Source: Fondul Proprietatea

Fondul Proprietatea: Official NAV history



Source: Fondul Proprietatea

Fondul Proprietatea: Dividends cashed-in history

	2008	2009	2010	2011
OMV Petrom	195.81	0.00	0.00	201.6
Romgaz S.A.	34.82	40.91	87.83	106.0
E.ON Gaz Romania S.A.	0.00	0.00	24.65	0.0
Transgaz S.A.	15.34	18.48	22.98	50.8
E.ON Gaz Distribuție S.A.	0.00	0.00	11.42	0.0
Hidroelectrică S.A.	0.00	0.00	6.50	52.5
Aeroportul Internațional Henri Coandă	8.44	10.13	5.87	9.9
Conpet S.A.	2.11	7.12	3.81	7.0
Primcom S.A.	1.15	1.52	1.73	14.3
Complexul Energetic Rovinari S.A.	8.19	0.00	0.12	0.0
Complexul Energetic Turceni S.A.	8.17	2.33	0.00	0.0
ENEL Distribuție Banat S.A.	26.52	n.m.	0.00	20.2
ENEL Distribuție Dobrogea S.A.	11.90	n.m.	0.00	13.5
Alro S.A.	n.m.	n.m.	11.17	13.5
GDF Suez Energy S.A. (fostul Distrigaz Sud S.A.)	20.48	14.50	0.00	9.6
Others	13.14	6.07	2.97	20.22
TOTAL	346.1	101.1	179.0	519.1

Source: Fondul Proprietatea

Fair value NAV

Fondul Proprietatea: NAV calculation (our fair values)

	% owned	RON m	% of NAV	RON per share
Total cash		472	3.1%	0.035
Share portfolio		14,748	96.8%	1.096
Listed		6,274	41.3%	0.468
Petrom	20.1%	4,443	29.3%	0.331
Transgaz	15.0%	470	3.1%	0.035
Transelectrica Bucuresti	13.5%	203	1.3%	0.015
Alro Slatina	10.2%	290	1.9%	0.022
Oil Terminal	8.5%	12	0.1%	0.001
Azomures Targu Mures	11.1%	41	0.3%	0.003
BRD- Groupe Societe Generale	3.6%	307	2.0%	0.023
Erste Group Bank AG	0.3%	128	0.8%	0.010
Raiffeisen Bank International AV	0.6%	126	0.8%	0.009
Others		254	1.7%	0.019
Unlisted		8,425	55.5%	0.628
Hidroelectrica	19.9%	2,066	13.6%	0.154
Romgaz	15.0%	1,468	9.7%	0.109
Nuclearelectrica	9.7%	371	2.4%	0.028
Complexul Energetic Turceni	24.8%	469	3.1%	0.035
CN Aeroporturi Bucuresti	20.0%	396	2.6%	0.030
Distrigaz Sud	12.0%	317	2.1%	0.024
E.ON Gaz Distributie	12.0%	117	0.8%	0.009
E.ON Moldova Distributie	22.0%	267	1.8%	0.020
E.ON Energie	13.4%	68	0.4%	0.005
ENEL Electrica Dobrogea Distributie	24.1%	307	2.0%	0.023
Electrica Transilvania Sud Distributie	22.0%	197	1.3%	0.015
ENEL Electrica Banat Distributie	24.1%	349	2.3%	0.026
Electrica Muntenia Nord Distributie	22.0%	222	1.5%	0.017
Electrica Transilvania Nord Distributie	22.0%	189	1.2%	0.014
Enel Distributie Muntenia SA	12.0%	422	2.8%	0.031
Posta Romana	25.0%	203	1.3%	0.015
Complexul Energetic Craiova	24.4%	132	0.9%	0.010
Complexul Energetic Rovinari	23.6%	254	1.7%	0.019
Others		610	4.0%	0.045
Total assets		15,220	100.2%	1.135
Debt		-19	-0.1%	-0.001
Deffered taxes (RONm)		-14	-0.1%	(0.001)
Estimated NAV (RONm)		15,187	100.0%	1.132

Source: KBC Securities estimates, company data

Fondul Proprietatea: Valuation summary (RONm) □

Portfolio value	14,748.0
- Fair discount applied	-2,949.6
+ Cash	472.0
- Potential negative effect of dilution at Nuclearelectrica	-270.0
- Debt	-19.0
- Deferred taxes	-14.2
Implied fair value	11,967.2
Number of shares (m)	13,412.6
Implied fair value per share (RON)	0.89
Closing price as of April 03, 2012 (RON)	0.59
Upside (%)	50.5%

Source: KBC Securities

*priced at COB 03 April 2012

Annex 1 – Official NAV calculation

Fondul Proprietatea: Official NAV calculation – February 2012

	RONm	% of NAV	RON per share
Official NAV	16,030	100.0%	1.195
Split of NAV by type			
Listed shares	6,390	34.0%	0.476
Unlisted shares	9,151	62.8%	0.682
Cash and receivables	489	3.3%	0.036
Split of NAV by sector			
Cash and receivables	489	3.3%	0.036
Electricity production	4,928	30.7%	0.367
Oil&Gas	6,054	37.8%	0.451
Electricity distribution and transport	2,901	18.1%	0.216
Banks	556	3.5%	0.041
Infrastructure	433	2.7%	0.032
Aluminium	221	1.4%	0.016
Heavy industry	258	1.6%	0.019
Postal services	139	0.9%	0.010
Others	50	0.3%	0.004
Top holdings			
OMV Petrom SA	4,727	29.5%	0.352
Hidroelectrica SA	3,345	20.9%	0.249
Romgaz SA	1,220	7.6%	0.091
Nuclearelectrica SA	507	3.2%	0.038
Complexul Energetic Turceni SA	523	3.3%	0.039
Transgaz SA	438	2.7%	0.033
GDF Suez Energy Romania	338	2.1%	0.025
Enel Distributie Muntenia SA	337	2.1%	0.025
CN Aeroporturi Bucuresti SA	322	2.0%	0.024
ENEL Distributie Banat SA	317	2.0%	0.024
Others	3,956	24.7%	0.295
Current trading price	8,171		0.593
Discount of current trading price vs NAV			-50.4%

Source: KBC Securities estimates, company data

*priced at COB 03 Apr 2012

Annex 2 – Valuation of companies

A. Oil and gas producers

Petrom

Company data						
Oil&Gas producer in Romania		FY Dec 31	2010	2011F	2012F	2013F
Crude oil reserves (m. boe)	453.0	Operating revenues (RONm)	18,616.0	22,534.0	22,867.0	24,603.0
Natural gas reserves (m. boe)	359.0	EBITDA (RONm)	5,797.0	7,707.0	7,615.0	7,751.0
Gas distribution network (km)	803	margin (%)	31.1%	34.2%	33.3%	31.5%
Gas stations	793	EBIT (RONm)	2,986.0	4,907.0	4,657.0	4,645.0
1 Operating refinery	90kbpd	Net profit (RONm)	2,201.0	3,773.0	3,718.0	3,699.0
Fuel storages	540,000 cm storage	margin (%)	11.8%	16.7%	16.3%	15.0%
Fair value (RON m)	21,823	P/E (x)	8.1	5.9	6.0	6.0
Shareholders structure:		EV/EBITDA (x)	3.4	3.2	3.3	3.2
OMV	51.0%	P/Bk (x)	1.2	1.1	1.0	0.9
Economy Ministry	20.6%	P/S (x)	1.2	1.0	1.0	0.9
Fondul Proprietatea	20.1%	Dividend yield (%)	5.6%	5.9%	5.8%	5.8%
Free-float	8.24%	Pay-out ratio (%)	46.3%	34.5%	35.0%	35.2%

Source: Company data, KBC Securities

*priced at COB 04 April 2012

Investment case

Petrom is the largest oil and gas producer in Romania. Petrom has 812m boe of proven reserves and produces 91kbpd tonnes of crude oil and NGL and 95kbpd of gas. The company has integrated refining capacity of 90kbpd and 793 filling stations.

- **Eye-catching dividend yield:** The dividend proposal (to be approved by AGM) stands at RON 0.031 per share, which implies a dividend yield of 7.9%. Given our expectation for a strong oil price environment we remain confident that Petrom will offer very generous dividend yields going forward (6.0% in 2012-2014).
- **Black Sea exploration starts:** ExxonMobil and OMV Petrom confirmed a potentially significant gas discovery offshore Romania. The exploration well (Domino-1) encountered 70.7 meters of net gas pay, resulting in a preliminary recoverable resource estimate ranging from 1.5tcf to 3.0tcf (42bcm to 84bcm). If translated into reserves this would represent some 15-30% (or 23-45%) of the group's (Petrom's) current 2P oil and gas reserves. Although we continue to view this area as one of the most exciting plays within OMV/Petrom's exploration portfolio, there are several drawbacks: OMV expects first production offshore Romania no earlier than the end of the decade, while the cost of exploration and development could reach several billion dollars. Moreover, there are no guarantees that the Neptun block will ultimately prove to be commercially viable. This depends as much on factors underground as above-ground (i.e. fiscal regime, natural gas prices in Romania, export opportunities, etc).
- **Mining tax regime to deteriorate beyond 2014:** Petrom pays a flat 9% royalty on its hydrocarbon production (fixed until 2013), which is highly favourable in an international comparison. We see an increasing risk of domestic price liberalization prompting the Romanian government to strengthen its tax policy on Petrom.

Investment case

- **Potential increase in free float:** After the unsuccessful attempt to sell a 9.8% stake in 2011, the government might again try to sell this stake on the Bucharest Stock Exchange at some point. However, the sale has been delayed for now and there is no precise information on when it might occur. Despite the share overhang risk the move would lower the trading liquidity discount on the stock
- **Brazi CCGT improves profitability:** Petrom is scheduled to inaugurate its 860MW combined cycle gas turbine (CCGT) at the Petrobrazi refinery in 2012, after technical delays. The power plant is expected to lower the energy costs of refining (by up to US\$ 1.2 /bbl), allow Petrom to use equity gas (up to 20% of production) and improve the pressure in the gas pipeline system, which limits flows in the summer period.
- **Gas market regulation hurts profits:** Romanian domestic gas prices have remained at RON 495/mcm in the last two years, which is 60% below the current import price. Delays in market liberalization, increasing import quotas (40% in 1Q11) as well as the latest ANRE order obliging companies to use imported gas for internal consumption, have cut deeply into gas trading margins and will have a negative impact on the profitability of the Brazi power plant, which is planned to start operations in 2H12.
- **Stagnating hydrocarbon production beyond 2010:** Due to a very mature reserve base, we believe Petrom will be unable to boost its production volumes beyond 2010 as the Mamu, Delta and Komsomolskoe fields reach their production plateau. Commercial production from Neptun block (Black Sea) is unlikely in this decade.
- **Attractively valued:** Petrom trades at a 2012F P/E of 6.0x and offers a dividend yield of 5.8%. We see buying a stock on a P/E almost equal to its dividend yield as a pretty good bet.

Catalysts

- The prospective liberalization of Romania's gas market.
- The start of the Brazi power plant.
- Exploration upside in offshore Romania (Black Sea).
- Increase in crude oil price on Iranian tensions.
- Potential exports of gas to neighbouring countries at higher prices.

Risks

- Risks of delays in price liberalization.
- Increase in royalties beyond 2014.
- Decrease in oil price.
- Falling production.

Valuation

- Our DCF model puts the value of Petrom at RON 21,823m or RON 0.39 per share.

Romgaz

Company data							
Gas producer in Romania			FY Dec 31	2010	2011E	2012F	2013F
Estimated reserves (m. boe)	544		Sales (RON m)	4,123.4	4,622.8	4,419.9	4,451.8
Gas sold in 2010 (m c/m)	5,618		EBITDA (RON m)	1,497.8	1,442.1	1,424.8	1,506.4
			margin (%)	36.3%	31.2%	32.2%	33.8%
Fair value (RON m)	9,791		EBIT (RON m)	905.6	861.3	841.9	899.4
			Net profit (RON m)	651.4	762.0	761.7	789.5
			margin (%)	15.8%	16.5%	17.2%	17.7%
Shareholders structure:			P/E (x)	15.0	12.8	12.9	12.4
Economy Ministry	85.0%		EV/EBITDA (x)	5.9	6.2	6.5	6.2
Fondul Proprietatea	15.0%		EV/EBITDA adj for development quota	4.3	4.6	4.8	4.7
			P/Bk (x)	1.2	1.2	1.2	1.2
			P/S (x)	2.4	2.1	2.2	2.2
			Dividend pay-out (%)	61.4%	85.0%	85.0%	85.0%

Source: Company data, KBC Securities estimates

Investment case

Romania's Romgaz is a state-owned natural gas producer and is currently unlisted. The firm supplies approximately 40% (5.8bn cubic metres) of Romania's total natural gas consumption. Romgaz has around 153 gas fields (we estimate reserves of 554mboe), six underground storage deposits (2.76bn cubic metres) and more than 3,500km of transmission pipelines. The company is active on an oligopolistic market, sharing domestic production with Petrom.

- **Romgaz to be listed on Bucharest Stock Exchange:** The Romanian government plans to list Romgaz on the Bucharest Stock Exchange by the end of 2H12. The listing should take place via the sale of a 15% stake owned by the Ministry of Economy and should be concluded in 2H 2012.
- **Government to announce a gas price liberalization timetable:** The price of natural gas is regulated in Romania, thus Romgaz currently sells gas at a much lower price than the price paid by the Romanian state for imports from Gazprom: Romgaz realized a price of RON 431.3 (US\$ 147.6) per thousand cubic metres in 2010 versus an import price of US\$ 360.8 per thousand cubic metres. In accordance with the IMF agreement, the government has to establish a timetable for the liberalization of natural gas prices. This will be a gradual process, possibly running until 2020, with more accelerated development for industrial consumers and a slower pace for domestic consumers.
- **Record results in 2011:** Romgaz posted a preliminary record profit of RON 762m (up 17% y/y) and turnover of RON 4.05bn (up 13% y/y) for full-year 2011. The increase was due primarily to a higher volume of gas sold by the company as demand increased significantly in 2H11 as the drop in hydroelectricity production had to be replaced by electricity produced in gas-fired power plants. In addition, a cold winter led to an increase in gas consumed by the population.

- **Significant dividends for Fondul Proprietatea from Romgaz's profit:** After the special donation to the Romanian state last year, Romgaz has to pay a 90% dividend to all shareholders this year (in accordance with the law on state-owned companies). This implies that Fondul Proprietatea will receive a dividend of RON 103m. Romgaz had a net cash position of RON 997.7m at the end of 2010 and we believe the company remained on the net cash side in 2011 despite the donation to the state budget.
- **Extraction costs in line with peers:** Despite the lack of an exact disclosure of extraction costs for Romgaz, we calculate operating expenses at US\$ 10 per boe, which puts Romgaz's operating expenses in line with those of peers.
- **Other activities to help improve margin:** Romgaz's turnover derives from gas extraction (67.0%), gas storage (10.0%) and sales of imported gas (20.0%). Romgaz posted a margin of 15% on imported gas sales and a margin of 3.0% on gas storage activity in 2010. ANRE approved higher tariffs on storage activity after Romgaz's margins came in the red in 2009 so the activity became profitable in 2010. The company is the sole operator of underground gas storage facilities in Romania.
- **New investments to maintain production and improve storage capacity:** By 2015, Romgaz plans to invest close to € 400m on new explorations for gas fields and a further € 135m on increasing storage capacity and the rate of gas outflow from the deposit.

Catalysts

- The prospective liberalization of Romania's gas market should allow Romgaz to increase its gas prices. The EU is currently pushing for a liberalization calendar although no timeline has been disclosed.
- Gas consumption in Romania looks set to increase as more gas-fired power plants are scheduled to open (e.g. Petrom) and Romgaz's domestic production accounts for more than 40% of the country's total consumption.

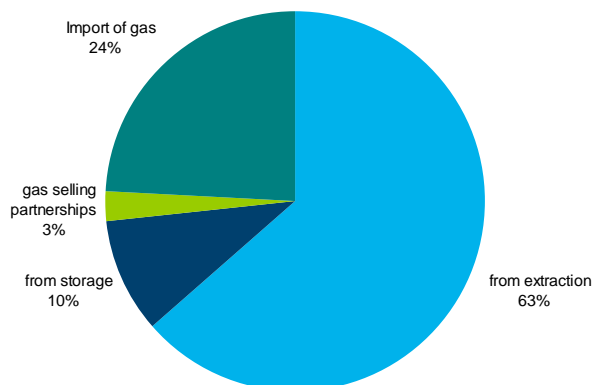
Risks

- The firm's gas fields are mature and no significant improvement in flow rates can be expected.
- Romania's fertilizer producers were allowed to buy cheaper domestic gas until October 2011. The facility has not been renewed and this could pose a threat to Romgaz's selling volumes, although it could also be positive and allow the company to charge higher prices.

Valuation

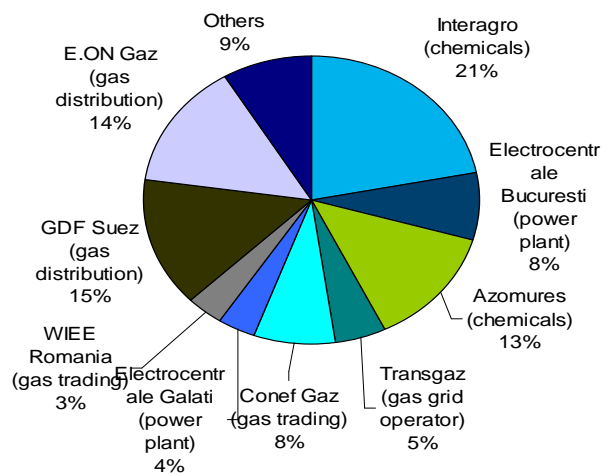
- Our DCF model puts Romgaz's value at RON 9,791m. This value implies a 2012 EV/EBITDA of 6.5x and a 2012 P/B of 1.2x.

Romgaz: Revenues breakdown



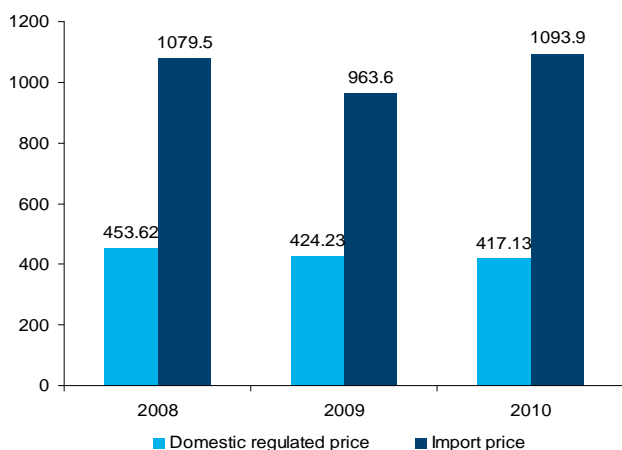
Source: company data, KBC Securities

Romgaz: split of revenues by customers



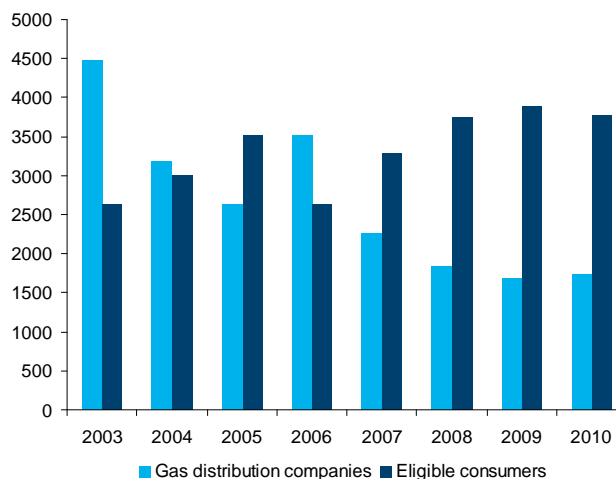
Source: company data, KBC Securities

Romgaz: selling price vs. import price (RON/MWh)



Source: company data, KBC Securities

Romgaz: Domestic gas deliveries



Source: company data, KBC Securities

Romgaz: Two-stage FCFF valuation

RON m, unless stated otherwise	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F
EBIT	841.9	899.4	965.6	1,013.9	1,064.5	1,107.1	1,151.4	1,186.0
growth (%)	-2.3%	6.8%	7.4%	5.0%	5.0%	4.0%	4.0%	3.0%
Tax on EBIT	134.7	143.9	154.5	162.2	170.3	177.1	184.2	189.8
NOPLAT	707.2	755.5	811.1	851.6	894.2	930.0	967.2	996.2
Depreciation	582.9	607.0	622.9	641.6	660.8	680.7	701.1	722.1
Gross Cash Flow	1,290.1	1,362.5	1,434.0	1,493.2	1,555.1	1,610.7	1,668.3	1,718.3
Change in working capital	(138.1)	(145.0)	(152.3)	(144.66)	(137.43)	(130.55)	(124.03)	(117.83)
CAPEX	(800.0)	(750.0)	(700.0)	(650.0)	(650.0)	(650.0)	(650.0)	(650.0)
Gross investments	(938.1)	(895.0)	(852.3)	(794.7)	(787.4)	(780.6)	(774.0)	(767.8)
Free Cash Flow	352.0	467.5	581.7	698.6	767.6	830.1	894.3	950.5
PV of Free Cash Flow	317.0	379.3	425.1	459.8	455.1	443.3	430.1	411.8
Sum of PV of FCF (2012-19)	3,321.6							
PV of terminal value	5,472.2							
Enterprise value	8,793.8							
Net debt	-997.7							
Equity value	9,791.5							

Source: KBC Securities estimates

Romgaz: DCF assumptions

WACC calculation	For 2012-19	Term. value	Terminal value calculation	RON m
Risk-free rate	7.0%	5.0%	FCFF/(WACC-g)	18,678
Beta	100.0%	100.0%	PV of terminal value	5,472
Equity premium	4.5%	4.5%	LT WACC is 7.7%, LT growth is 2.5%	
Cost of equity	11.5%	9.5%	Using WACC of 9.3% to discount	
Debt premium	1.0%	1.0%		
Cost of debt	8.0%	6.0%		
Effective tax rate	16.0%	16.0%		
WACC	11.0%	7.7%		

Source: KBC Securities estimates

B. Electricity producers

Hidroelectrica

Company data						
Hydro energy producer		FY Dec 31	2010	2011E	2012F	2013F
		Operating revenues (RON m)	3,287.1	2,888.7	2,976.6	3,394.6
CAPACITY	6,335 MW	EBITDA (RON m)	1,377.0	935.9	1,190.3	1,481.4
Energy produced in 2010	19,380 GWh	margin (%)	42%	32%	40%	44%
Energy supplied in 2010	22,567 GWh	EBIT (RON m)	502.8	116.5	360.8	637.9
Utilization ratio (2010)	34.30%	Net profit (RON m)	292.4	10.0	201.5	420.3
		margin (%)	9%	0%	7%	12%
KBC Fair value (RON m)	10,358	P/E (x)	35.4	n.m.	51.4	24.6
		EV/EBITDA (x)	8.8	13.2	10.7	8.7
Shareholders structure:		P/Bk (x)	0.6	0.6	0.6	0.6
Economy Ministry	80.05%	P/S (x)	3.2	3.6	3.5	3.1
Fondul Proprietatea	19.95%	Dividends paid (RON m)	263.1	9.0	181.3	210.2
		pay-out ratio (%)	90.0%	90.0%	90.0%	50.0%

Source: Company data, KBC Securities

Investment case

Hidroelectrica is a state-owned hydroelectricity producer in Romania that supplies approximately 18TWh or 27% of the country's total electricity resources. Hidroelectrica has 12 main electricity generation assets and a total of 587 production groups, built between 1960 and 1990.

- **State to list 10% in Hidroelectrica:** As part of the IMF agreement, the Romanian state has to list a 10% stake in Hidroelectrica. According to official statements, the IPO will take place before the end of September 2012. The tender offer for selecting the intermediary has just finished. The IPO will take place via a share capital increase of 12.5%, with Fondul Proprietatea having pre-emptive rights to maintain its stake and the rest being available for subscription to other investors.
- **Significant increase in profit could come from renegotiating bilateral contracts:** About 66.0% of Hidroelectrica's annual production went to energy traders and big industrial consumers at an average price of RON 121.6 per MWh (€ 28.3, up 19.1% y/y) in 2010, 48% below the German base load price. This is due to very unprofitable bilateral contracts signed by the previous management. As part of the IMF agreement, Hidroelectrica has to cancel these contracts or increase the prices. According to media sources, the firm targets a 20% cut in the energy delivered to these contracts and a 25% increase in prices in 2012. The cancellation of the contracts and an increase in energy sold on the free market should lead to a direct increase in profit.
- **Tough 2011:** Hidroelectrica posted profit of RON 10m for 2011, down significantly from RON 292m in 2010. The decrease was mainly due to poor meteorological conditions, which led to a significant decline in the volume of energy produced. The company has a large number of bilateral contracts that demand the supply of electricity at very low prices, thus the decline in production meant the firm had to buy energy from the market at high prices and deliver it to clients at low prices. A force majeure clause was activated, which helped minimize the losses last year.

- **Calendar for energy price liberalization:** According to an IMF agreement, the Romanian government has to establish a calendar for the liberalization of electricity prices. The calendar targets full liberalization for the general population by 1 July 2017 and for companies by 1 January 2014. The changes in prices are outlined in a draft law that has to be approved by parliament. In order to avoid social pressure, a mechanism might be set up to help vulnerable consumers. The liberalization of electricity prices should help Hidroelectrica, which sells about 18% of its energy to distributors at a price of RON 86.2 (€ 20.5) per MWh. We forecast electricity prices for distributors in Romania to post a 2011-2014 CAGR of 5%.
- **High operating leverage:** As costs are rather fixed, Hidroelectrica's profit is highly leveraged to the selling price of electricity and the achieved production volumes. Moreover, the existence of bilateral contracts to provide electricity at low prices leads to the situation that the firm has to buy more expensive energy when production volumes decrease in order to cover the requirements of the contracts. According to Fondul Proprietatea's administrator Franklin Templeton, Hidroelectrica lost more than € 160m in 2010 due to not selling electricity at market prices.
- **Investments to bring additional cost savings:** Hidroelectrica spent RON 1.4bn on new investments (expected to increase production capacity by about 5% by end-2012) and the reconditioning of old investments (work carried out on 20% of capacities) in 2009. Additional investments will be financed through new debt and funds raised at the IPO. One of the largest investments planned for the mid-term is the construction of a pumped storage hydro power plant at Tamita Lapustesti at a cost of € 1.16bn. The facility will provide better system services for the electricity network and allow the firm to sell the resultant electricity. The facility will also contribute to improved cost control and should lower the amount of electricity required from external sources. Hidroelectrica bought roughly 2.4TWh of electricity to cover shortages from inefficient state-owned power plants at a price of RON 198.7 (€ 46.9) per MWh in 2009.
- **Low debt but exposed to €/RON exchange rate:** Hidroelectrica has a low level of debt, with net debt-to-equity at 8.8%. Credits are mostly €-denominated (close to 70%), which leaves the company exposed to €/RON movements. On the positive side, however, the company pays a low interest rate (5.5% last year) and as a result will easily be able to access more credit for the expansion of its activities.

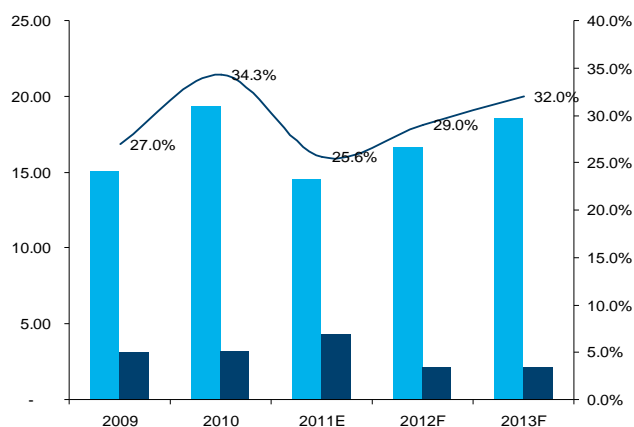
Catalysts

- The potential increase in prices with market liberalization and the cancellation of bilateral contracts should help the firm to achieve stronger margins. The firm has a high sensitivity to the price of energy sold.
- Romania is obliged to pursue EU directives for increasing green energy consumption.
- Potential for a significant increase in capacity. (Romania's estimated hydro potential is double the current capacity.)

Risks

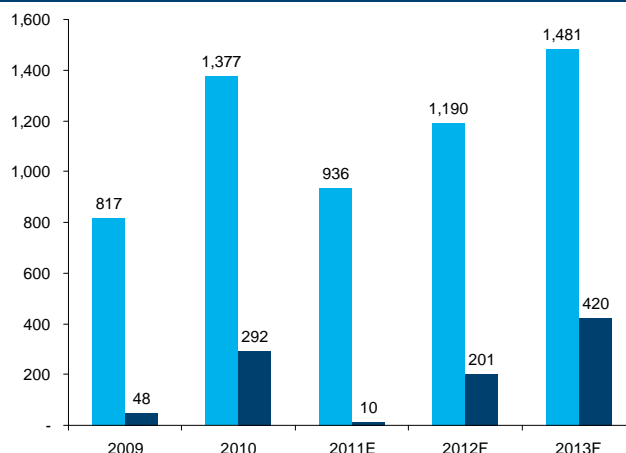
- Involvement of political power in the establishment of prices under the IMF agreement (i.e. market liberalization). Elections at the end of 2012 could lead to renewed political influence.

Hidroelectrica: Energy produced, acquired and utilization rate (RONm)



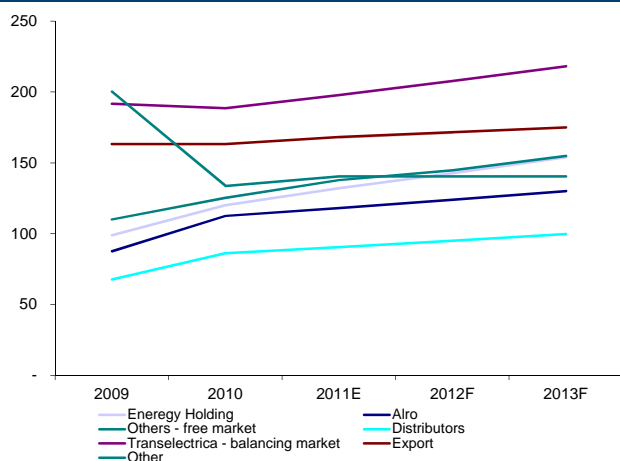
Source: company data, KBC Securities

Hidroelectrica: EBITDA and Net profit forecast (RONm)



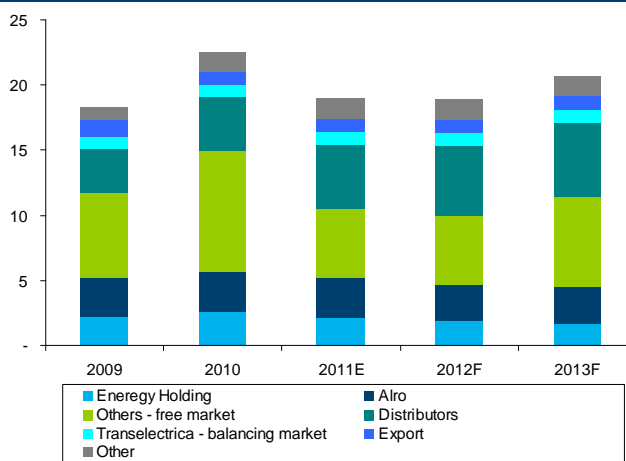
Source: company data, KBC Securities

Hidroelectrica: Prices of energy sold (RON/MWh)



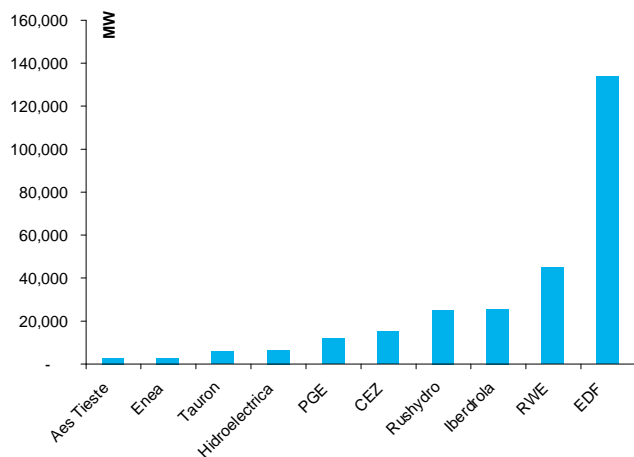
Source: company data, KBC Securities

Hidroelectrica: Structure of quantities sold (TWh)



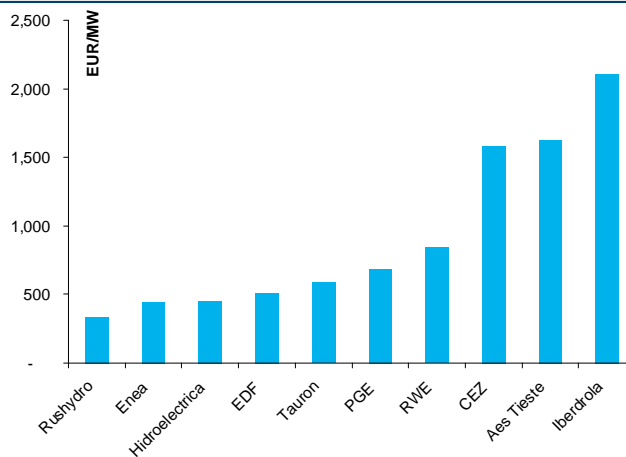
Source: company data, KBC Securities

Hidroelectrica vs Peers: Capacity (MW)



Source: company data, KBC Securities

Hidroelectrica vs Peers: Capacity (€ / MW)



Source: company data, KBC Securities

Valuation

Our discounted cash flow (DCF) model suggests a value of RON 10,357m. This puts Hidroelectrica at a 2012F EV/EBITDA of 10.7x, which implies a 118% premium to peers. We believe the premium is justified by the high growth potential resulting from rising energy prices and higher operating revenues derived from increase in production volumes.

Hidroelectrica: Two-stage FCFF valuation

RON m, unless stated otherwise	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F
EBIT	360.8	637.9	921.4	1,227.7	1,362.1	1,446.5	1,514.8	1,566.8
growth (%)	209.8%	76.8%	44.4%	33.3%	10.9%	6.2%	4.7%	3.4%
Tax on EBIT	57.7	102.1	147.4	196.4	217.9	231.4	242.4	250.7
NOPLAT	303.1	535.8	773.9	1,031.3	1,144.1	1,215.1	1,272.4	1,316.1
Depreciation	829.5	843.5	857.2	866.3	871.1	875.9	880.7	885.5
Gross Cash Flow	1,132.6	1,379.3	1,631.1	1,897.6	2,015.2	2,090.9	2,153.1	2,201.6
Change in working capital	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)
CAPEX	(1,165.7)	(1,170.8)	(1,075.9)	(981.1)	(871.1)	(875.9)	(880.7)	(885.5)
Gross investments	(1,265.7)	(1,270.8)	(1,175.9)	(1,081.1)	(971.1)	(975.9)	(980.7)	(985.5)
Free Cash Flow	(133.1)	108.5	455.2	816.5	1,044.1	1,115.1	1,172.4	1,216.1
PV of Free Cash Flow	(120.8)	89.4	340.5	554.4	643.6	623.9	595.5	560.7
Sum of PV of FCF (2012-19)	3,287.2							
PV of terminal value	8,523.5							
Enterprise value	11,810.7							
Net debt	1,452.9							
Equity value	10,357.8							

Source: KBC Securities estimates

Hidroelectrica: DCF assumptions

WACC calculation	For 2012-19	Term. value	Terminal value calculation	RON m	
Risk-free rate	7.0%	5.0%	FCFF/(WACC-g)	LT WACC is 7.7%, LT growth is 2.5%	23,899
Beta	100.0%	100.0%	EV/EBITDA based value	Expected average EV/EBITDA is 6.0x	12,816
Equity premium	4.5%	4.5%	P/E based value	Expected average P/E is 12.0x	16,583
Cost of equity	11.5%	9.5%	P/Bk based value	Expected average P/BV is 0.99x	20,650
Debt premium	1.0%	1.0%	PV of terminal value	Using WACC of 10.2% to discount	8,523
Cost of debt	8.0%	6.0%			
Effective tax rate	16.0%	16.0%			
WACC	10.2%	7.7%			

Source: KBC Securities estimates

Electricity producers: Multiple-based comparison

	EV/EBITDA**			P/E**			2010	
	2010	2011F	2012F	2010	2011F	2012F	EBIT margin	Leverage
RUSHYDRO	n.a.	n.a.	n.a.	8.2	8.3	9.1	12.0%	1.3
OGK 2	9.3	5.9	4.3	8.8	11.2	9.2	7.5%	1.4
MOSENERGO	3.5	2.6	2.5	12.6	6.8	7.2	5.4%	1.3
CENTRENERGO	12.8	5.5	5.1	49.4	8.8	8.1	1.8%	2.4
DNIPROENERGO	8.1	4.8	4.5	14.9	8.5	7.2	6.9%	1.9
BORALEX	14.0	8.6	9.1	110.1	n.a.	n.a.	22.1%	3.7
ENEA	3.7	3.3	3.1	11.0	9.6	9.2	9.0%	1.3
TAURON	4.8	4.4	4.0	9.6	7.3	7.7	7.9%	1.7
PGE	5.1	4.5	4.3	11.5	9.0	8.5	17.9%	1.5
CEZ	6.8	7.1	6.8	9.0	10.4	9.8	28.4%	2.6
EDF	4.1	4.6	4.3	9.2	9.1	8.5	12.7%	7.6
RWE	3.8	4.6	4.4	5.1	8.3	8.7	7.1%	5.8
IBERDROLA	7.2	6.9	6.6	8.2	8.5	8.6	14.0%	3.1
Total Average	6.9	5.2	4.9	20.6	8.8	8.5	11.7%	2.7
Hidroelectrica	10.7	12.7	11.6	35.4	1037.9	51.4	15.3%	0.1
Premium/discount vs. peers	54%	142%	136%	72%	n.m.	n.m.	30%	-96%

Source: KBC Securities, Bloomberg

**Multiples are based on IBES estimates

**Priced at 4 April 2012 closing prices

Nuclearelectrica

Company data						
Nuclear energy producer		FY Dec 31	2010	2011E	2012F	2013F
		Sales (RON m)	1,514.7	1,583.2	1,655.7	1,738.5
Capacity (MW)	1,412	EBITDA (RON m)	560.4	530.6	550.8	619.2
Energy produced in 2010 (MWh m)	11.6	margin (%)	37.0%	33.5%	33.3%	35.6%
Utilization ratio (2010)	96%	EBIT (RON m)	179.3	149.7	173.9	237.3
		Net profit (RON m)	16.1	41.0	36.4	85.5
Fair value (RON m)	3,811	margin (%)	1.1%	2.5%	2.2%	4.9%
		P/E (x)	236.9	92.5	104.6	44.6
Shareholders structure:		EV/EBITDA (x)	10.7	12.7	11.6	10.5
Economy Ministry	90.3%	P/Bk (x)	0.5	0.5	0.5	0.5
Fondul Proprietatea	9.7%	P/S (x)	2.5	2.4	2.3	2.2
		Pay-out ratio	0%	0%	80%	50%

Source: Company data, KBC Securities

Investment case

Nuclearelectrica owns the sole nuclear power plant (NPP) in Romania, operating two reactors (installed capacity 706 MW each) commissioned in 1996 and 2007 respectively. The company has its own nuclear fuel plant and supplies about 21% of Romania's total energy consumption.

- **Potential IPO this year:** The Romanian state plans to list a 10% stake in Nuclearelectrica by the end of October 2012. The listing will take place through an increase in share capital and the money will be used for the company's expansion plans (possibly the construction of two new reactors). Fondul Proprietatea will be able to subscribe in order to maintain its stake.
- **Threat of dilution of fund's stake:** Fondul Proprietatea initially held a 20% stake in Nuclearelectrica. Two capital increases through in-kind contributions (i.e. heavy water) from the state have diluted the fund's stake to 9.7%. The administrator has blocked 2.5% of the state's shares in the fund, corresponding to the stake not received in Nuclearelectrica. An additional share capital increase is possible, which would dilute the stake by a further 20% and would have a negative impact on NAV of RON 228m (this has already been provisioned in the official NAV calculation). Fondul Proprietatea has sued the state to regain its initial holdings.
- **Energy prices below market but higher than Hidroelectricita:** Nuclearelectrica sells its energy at a price of around RON 139 per MWh (€30 per MWh). This is still significantly lower than EU market prices but above the price charged by Hidroelectricita. We expect the company's electricity price to grow at a CAGR of 4.3% for 2010-2013.
- **High FX-denominated debt poses a threat:** Nuclearelectrica's financial result deteriorated significantly last year due to FX-denominated debt and RON depreciation versus €, which led to an FX loss of RON 137m in 2010. About 90% of the company's RON 2.5bn credits are FX-denominated (i.e. €, US\$ and CA\$).
- **Capacity expansion delayed until 2018:** A project company, EnergoNuclear SA, was established in 2008 for the construction of reactors 3 and 4 (each 720 MW, doubling current capacity), with Nuclearelectrica as the majority shareholder. However, the company is still looking for partners to team-up with in the construction of the reactors, with the latest deadline for submitting offers being September 2012.

Catalysts

- Nuclearelectrica's production will increase once reactors 3 and 4 have been commissioned.
- Market liberalization will lead to higher prices. In addition, planned interconnections with neighbouring countries should allow more exports.

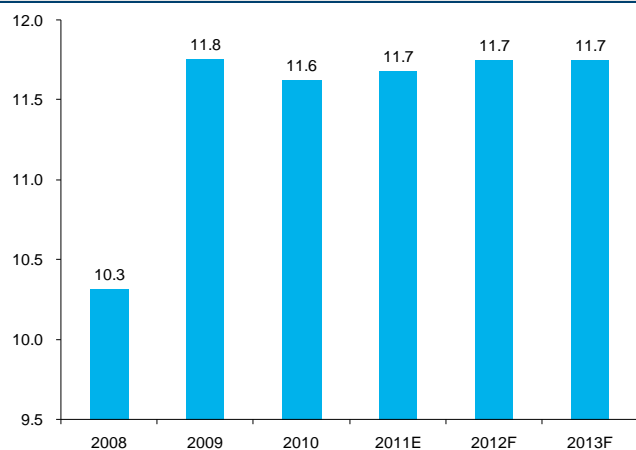
Risks

- The firm's debt burden could increase if the state maintains its 51% participation in the expansion project for the two additional reactors.
- Risks derived from exposure to FX-denominated debt.

Valuation

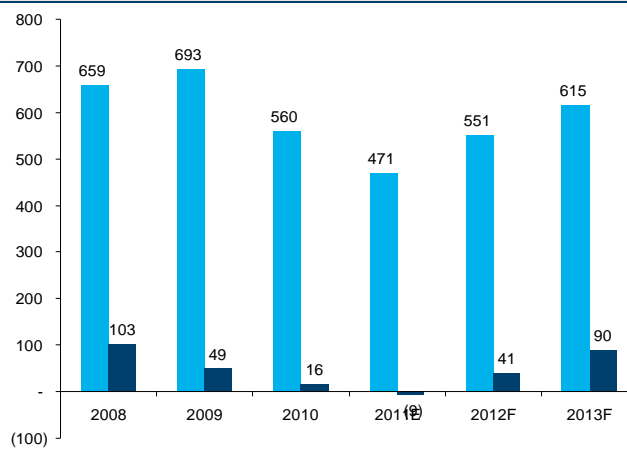
- Our discounted cash flow (DCF) model puts a value of RON 3,811m on Nuclearelectrica.

Nuclearelectrica: Electricity production (MWh)



Source: Nuclearelectrica, KBC Securities

Nuclearelectrica: EBITDA and Net profit forecast



Source: Nuclearelectrica, KBC Securities

Nuclearelectrica: Two-stage FCFF valuation

RON m, unless stated otherwise	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F
EBIT	173.9	237.3	322.7	391.1	443.1	518.6	555.6	616.2
Tax on EBIT	27.82	38.0	51.6	62.6	70.9	83.0	88.9	98.6
NOPLAT	146.0	199.3	271.1	328.5	372.2	435.6	466.7	517.6
Depreciation	377.0	381.9	385.6	388.7	390.2	390.6	391.1	391.5
Gross cash flow	523.0	581.2	656.7	717.2	762.4	826.3	857.8	909.2
Change in working capital	(80.0)	(70.0)	(60.0)	(50.0)	(40.0)	(30.0)	(30.0)	(30.0)
Capital expenditures	(480.0)	(460.0)	(450.0)	(420.0)	(400.0)	(400.0)	(400.0)	(400.0)
Free cash flow	(37.0)	51.2	146.7	247.2	322.4	396.3	427.8	479.2
PV of free cash flow	(37.0)	46.7	121.6	186.6	221.5	247.9	243.6	248.5
Sum of PV of FCF (2012-19)	1,279.5							
PV of terminal value	4,676.9							
Enterprise value	5,956.3							
Net debt	2,145.3							
Equity value	3,811.0							

Source: KBC Securities estimates

Nuclearelectrica: DCF assumptions

WACC calculation	For 2012-19	Term. value	Terminal value calculation		RON m
Risk-free rate	7.0%	5.0%	FCFF/(WACC-g)	LT WACC is 7.9%, LT growth is 2.5%	9,018
Beta	100.0%	100.0%	<i>PV of terminal value</i>	<i>Using WACC of 9% to discount</i>	4,677
Equity premium	4.5%	4.5%			
Cost of equity	11.5%	9.5%			
Debt premium	1.0%	1.0%			
Cost of debt	8.0%	6.0%			
Effective tax rate	16.0%	16.0%			
WACC	9.8%	7.9%			

Source: KBC Securities estimates

Coal-fired power plants: Complexul Energetic Oltenia

Company data	Turceni Power Plant			Rovinari Power Plant			Craiova Power Plant		
	2008	2009	2010	2008	2009	2010	2008	2009	2010
Sales (RON m)	1,281.4	1,125.5	1,094.5	957.30	845.40	794.63	1,068.6	1,132.4	1,097.8
EBITDA (RON m)	195.2	240.9	198.4	75.50	80.30	119.13	73.6	75.5	86.2
margin (%)	15%	21%	18%	7.9%	9.5%	15.0%	6.9%	6.7%	7.9%
EBIT (RON m)	65.9	30.2	4.8	14.00	13.70	32.04	4.4	-0.7	11.2
Net profit (RON m)	20	21.3	-69.3	1.00	5.60	0.59	3.6	0.3	0.2
margin (%)	1.56%	1.89%	-6.33%	0.10%	0.70%	0.07%	0.30%	0.00%	0.02%
Fair value (RON m)	1,892			1,075			540		
P/E (x)	94.6	88.8	n.m.	n.m.	192.0	n.m.	150.0	n.m.	n.m.
EV/EBITDA (x)	10.2	8.2	12.2	16.3	15.3	12.0	7.9	7.7	8.3
P/Bk (x)	0.9	0.9	0.9	1.3	1.0	0.9	0.5	0.5	0.5
P/S (x)	1.5	1.7	1.7	1.1	1.3	1.4	0.5	0.5	0.5
Dividend pay-out	47%	0%	0%	1.40%	9.70%	90%	51%	43%	90%
Equity	2,114	2,139	2,108	854	1,065	1,230	1,081	1,097	1,095
Assets	2,712	2,790	3,207	1,303	1,632	1,984	1,393	1,581	1,602
Debt	96	154	586	133	245	425	36	137	182
Debt-to-Assets	4%	6%	18%	10%	15%	21%	3%	9%	11%
Capacity (MW)	2,640	2,640	2,640	1,320	1,320	1,320	930	930	930
Electricity produced – MWh m	7.68	6.39	5.47	5.94	4.84	5.01	4.84	4.37	4.07
Weight of revenues from regulated market		40%	53%		44%			36%	

Source: Company data, KBC Securities

Investment case

The three coal-fired power plants combined generate almost 30% of Romania's electricity output. The plants were commissioned between 1960 and 1980. The power plants are independent in terms of fuel sources, having their own coal mines with total coal reserves of 470m tonnes. Despite this, the plants need huge investments to reach EU environmental requirements, which will entail considerable efforts in the periods ahead.

- **Three coal-fired power plants to be merged with coal mine to set up Energetic Complex Oltenia:** According to a statement issued by Fondul Proprietatea in December 2011, the Romanian state intends to merge the three coal-fired power plants in the fund's portfolio together with a coal mine to set up a new company called Complexul Energetic Oltenia. The company should be ready by May 2012. Within 24 months of its incorporation (estimated to take place on 27 April) the new firm should either be listed on the stock exchange or be sold to a strategic investor. The fund will have two out of seven representatives on the supervisory board and one out of five representatives on the board of directors. The fund will be able to sell its stake according to the same conditions that apply to the state. The new board of directors and the supervisory board will have to come up with a restructuring plan to be approved by 90% of the shareholders, which means Fondul Proprietatea will have to approve it as well.

Investment case

- **Easy access to the main fuel source:** The power plants use coal from their own production (i.e. their own coal mines). The new merged company will incorporate another coal mine in this structure. This negates any risks related to coal prices, although it increases the fixed costs of the power plants and exposes them to inefficiencies in the local mining system. The coal mines in their property cover the needs of 91.5% of the Rovinari Power Plant and 74.9% of the Turceni Power Plant. Craiova Power Plant has only marginal access to coal sources. The new coal mine to be added to the merged company should provide additional access to resources and the largest clients of the company are already the three power plants. However, the mine is a lossmaker (RON 63m loss posted in 2010) and could put an additional burden on the financials of the three power plants.
- **Most expensive producers:** All three entities sell to local distributors at regulated prices but an important part of their production – 55% on average as of 2010 – is sold on the free market, i.e. on the Bilateral Contracts Market, the Day-Ahead Market or the Balancing Market. While market liberalization could help to raise prices, we do not envisage any major improvements at the three companies: the three power plants are the most expensive producers in terms of selling prices. Turceni Power Plant sells energy at RON 181 (€42) per MWh, Rovinari Power Plant at RON 157 (€36) per MWh and Craiova Power Plant at RON 247 (€ 57) per MWh.
- **Large investments needed to meet EU standards:** The three entities started the investment programs necessary to meet EU standards in 2007. Total required investments stand at €1.2bn and investments will continue for another three years. In the last 10 years, only 10% of installed power capacity at traditional plants has been modernized in Romania. By the time the environment-related capacities are in place, the companies will have to buy CO₂ certificates from the market, which adds to costs and makes production more expensive.
- **2011 preliminary results:** Production at the three power plants was boosted by the decrease in hydro production in Romania in 2011. Total production of electricity at coal-fired power plants in Romania increased by 21% in 2011. This boosted the production of coal and created economies of scale for the mines (which are inefficient) as well as for the three power plants and led to significant profits for all of them.

Catalysts

- Modernization and rehabilitation could increase the energy efficiency of the plants.
- Grid operator Transelectrica plans to develop more interconnection lines for Romania's energy system, thereby creating export opportunities.

Risks

- Regulated tariffs in the energy production sector.
- Outdated equipment needs high investments.
- Coal is not an environment-friendly fuel and the three power plants need to make large investments to bring their facilities in line with EU environmental legislation.

Valuation

We valued the three power plants using a sum-of-the-parts (SOTP) valuation, which takes into account the rebuild cost of each generator. Our SOTP valuation includes the investments needed to comply with EU standards. Our valuations imply an average EV/EBITDA of 11x and average P/B of 0.9x for 2010.

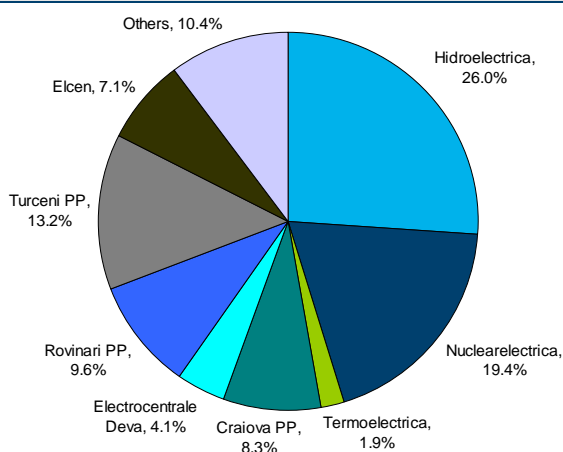
Coal-fired power plants: SOTP valuation

Company	Asset	Amount	Price per unit (US\$ m)	Value (US\$ m)	Total EV (US\$ m)	Net debt* (US\$ m)	Fair value of equity (US\$ m)	(RON m)
Turceni PP	Power generator	1.65 GW	0.50	833	833			
	Coal reserves	287mt	2.50	718	718			
	Total			1,551	1,551	-978	573	1,892
Rovinari PP	Power generator	1.32 GW	0.45	594	594			
	Coal reserves	324mt	1.11	360	360			
	Total			954	954	-628	326	1,075
Craiova PP	Power generator	0.93 GW	0.45	417	417			
	Coal reserves	7.5 mt	2.00	15	15			
	Total			432	432	-269	164	540

Source: KBC Securities estimates, Company data

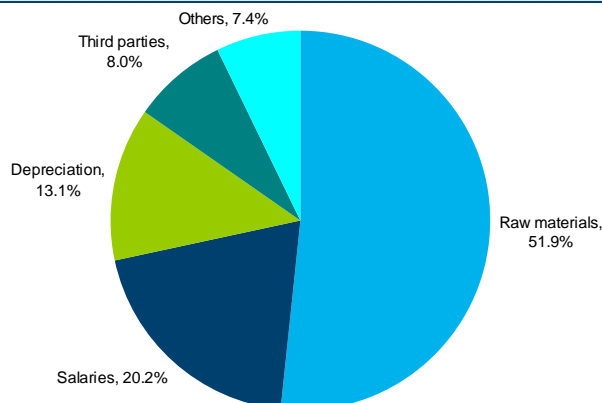
*including amounts to be spent for future investments

Electricity producers: 2010 market shares



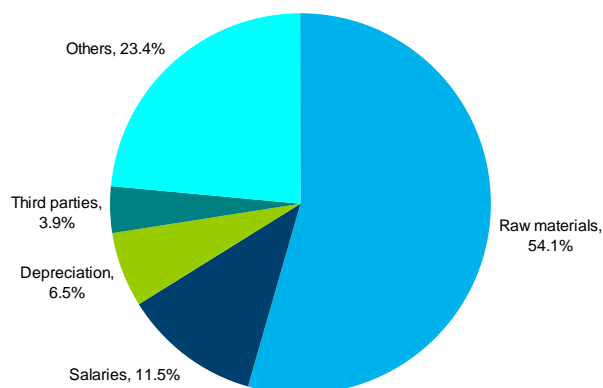
Source: Company data, KBC Securities

Turceni PP: Structure of production costs 2010



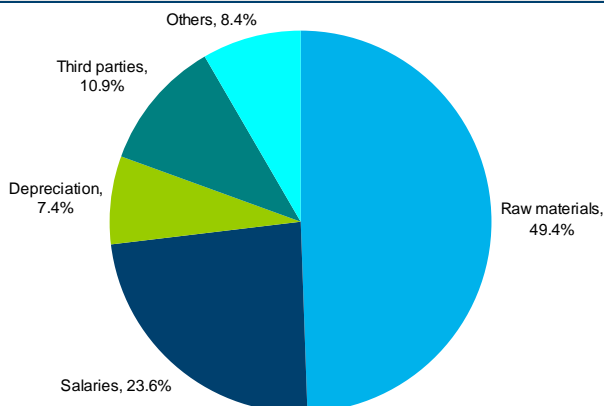
Source: Company data, KBC Securities

Craiova PP: Structure of production costs 2010



Source: Company data, KBC Securities

Rovinari PP: Structure of production costs 2010



Source: Company data, KBC Securities

C. Electricity and gas transmission

Transelectrica

Company data							
National Power Grid Operator			FY Dec 31	2010	2011F	2012F	2013F
Quantity of electricity transported in 2011	56.1	Sales (RON m)		2,683	3,148	2,825	2,940
		EBITDA (RON m)		456	502	507	548
		margin (%)		17.0%	15.9%	18.0%	18.6%
Fair value (RON m)	1,503	EBIT (RON m)		188	211	195	211
		Net profit (RON m)		104	138	151	146
Shareholders structure:		margin (%)		3.9%	4.4%	5.3%	5.0%
	Economy Ministry	58.70%	P/E (x)*	10.8	8.1	7.4	7.6
Fondul Proprietatea	13.50%	EV/EBITDA (x)*	4.67	4.30	4.51	4.65	
Free float	27.80%	P/Bk (x)*	0.3	0.3	0.3	0.2	
		P/S (x)*	0.4	0.4	0.4	0.4	
		Dividend pay-out (%)		90%	89%	80%	50%

Source: Company data, KBC Securities

*priced at COB 04 April 2012

Investment case

Romania's Transelectrica is the state-owned power grid operator. The company has its tariffs regulated by ANRE in accordance with the revenue cap methodology. The profit of the company is established by using the formula Profit = RAB (Regulated Asset Base) x RR (Regulated rate of return).

- **Successful placement of a 15% stake:** The state successfully sold an additional 15% stake in Transelectrica at an SPO on 27 March 2012, at an average price of RON 15.0 per share. We see as positive the increase in the firm's free float as this should improve the liquidity on the market and make the company more visible. The SPO also proves the current market price is a strong reference price for the company.
- **Potential increase in electricity volumes:** We expect electricity volumes in Romania to increase in the medium term as more producers enter the market. (CEZ with a 600 MW wind generator at end-2011, Petrom with an 860 MW gas-fired power plant in 2H12.) In addition, hydro electricity production, disrupted by a severe drought last year, should resume its full potential in 2012. Overall we expect to see a 2.5% increase in volumes this year.
- **Dividend yield at 7.1%:** Transelectrica will pay a dividend of RON 1.1 per share, implying a dividend yield of 7.1%. The ex-dividend date is 11 May 2012. The dividend pay-out stands at 89.3% for 2011 and this high rate will be maintained in 2012, resulting in a dividend yield of 10.4%.
- **Faster tariff adjustments by an independent regulator:** Revenue cap methodology implies, roughly, that $EBIT = RAB \times RoR$. However, the tariff decisions of regulator ANRE have not fully followed this formula so far. A new law to be passed by the Romanian parliament stipulates an independent ANRE, which should help the faster adjustment of the tariff and could lead to the company's profit coming closer to that implied by the methodology.

- **ANRE to establish new five-year characteristics:** ANRE should decide by the end of the year on the characteristics of the next five-year regulatory period (2013-2018). A new RoR should be established while a revaluation of assets is also likely to take place, which should lift the RAB value.
- **Management reshuffle:** A recent Ordinance obliges each major state-owned company to elect a board of administrators, comprised of "professional members" selected by an international HR firm, who will have to reach profit targets according to an employment contract. Only two board members can be state employees. The CEO will be selected by the board. Transelectrica held an AGM on 29 February 2012 to start the process of board selection.
- **CPT costs under control:** Transelectrica has to buy energy to cover grid losses (roughly 0.9TWh per year). Starting this year, the firm is able to buy this energy from the market rather than ANRE, which usually set the price above that of the market. The new methodology should allow the firm to decrease its CPT costs.
- **Trading at a discount:** On a 2012F EV/EBITDA of 4.5x, Transelectrica trades 47.5% below the median of peer companies. We see part of the discount as justified given the higher cost of capital in Romania although we believe the current discount is too high given our estimates for improved operating profit in the years ahead.

Catalysts

- Revenues and profitability to be boosted by improved consumption in 2012 and subsequent years.
- Increased exports to help boost the firm's margins.
- Potential increase in regulated rate of return.

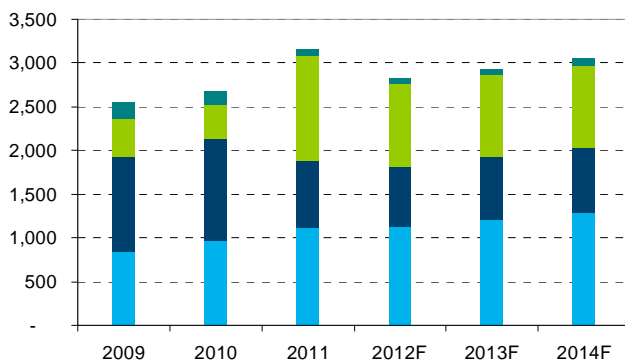
Risks

- The company is exposed to regulatory risk as its tariffs are set by ANRE.
- A potential drop in consumption could lead to lower profitability.

Valuation

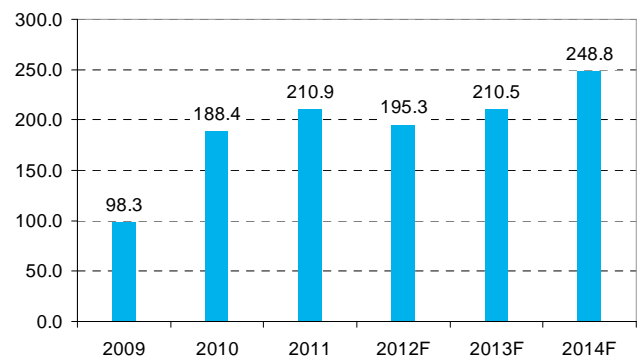
- Our DCF valuation model puts the fair value of the company at RON 21.4 per share while our DDM valuation model results in a value of RON 19.7 per share. Our fair value is calculated as an average of the two, respectively RON 20.5 per share.

Transelectrica: Revenues breakdown (RON m)



Source: Transelectrica, KBC Securities estimates

Transelectrica: EBIT forecast (RON m)



Source: Transelectrica, KBC Securities estimates

Consensus versus KBC forecasts

(RON m)	2012F			2013F			2014F		
	Consensus	KBC	Difference (%)	Consensus	KBC	Difference (%)	Consensus	KBC	Difference (%)
Total revenues	2,574.9	2,824.7	9.7%	2,655.0	2,939.6	10.7%	2,825.5	3,281.4	16.1%
EBITDA	482.3	507.3	5.2%	519.2	547.8	5.5%	521.3	682.6	31.0%
EBIT	169.7	195.3	15.1%	188.5	210.5	11.7%	199.8	247.8	24.0%
Net result	115.6	150.9	30.5%	128.2	146.4	14.3%	144.0	173.9	20.8%

Source: KBC Securities estimates; Bloomberg

Electricity producers: Multiple-based comparison

	EV/EBITDA**			P/E**			P/B**		
	2011E	2012F	2013F	2011E	2012F	2013F	2011E	2012F	2013F
FLUXYS-D	9.2	9.1	9.6	18.9	18.9	19.5	1.7	1.7	1.7
ENAGAS SA	7.9	7.2	6.7	9.3	8.9	8.3	1.8	1.7	1.6
SNAM RETE GAS	9.2	8.8	8.4	12.6	12.4	12.1	2.1	2.0	2.0
ELIA SYSTEM OPERATOR	9.7	9.5	9.1	15.9	15.6	14.1	1.0	0.9	0.9
TERNA SPA	9.9	9.1	8.6	15.5	14.5	13.9	2.2	2.1	2.1
RED ELECTRICA CORPORACION	8.4	7.8	7.3	9.9	8.9	8.1	2.5	2.2	2.0
Total Average	9.1	8.6	8.3	13.7	13.2	12.7	1.9	1.8	1.7
Transelectrica	4.3	4.5	4.6	8.1	7.4	7.6	0.3	0.3	0.2
Premium/discount vs. peers	-52.6%	-47.5%	-43.8%	-40.6%	-43.9%	-39.7%	-86.3%	-85.8%	-85.7%

Source: KBC Securities, Bloomberg

*Multiples are based on IBES estimates

**Priced at 04 April 2012 closing prices

Transgaz

Company data		FY Dec 31	2010	2011E	2012F	2013F
Operator of the gas network in Romania						
Quantity of gas transported in 2011	544.0	Operating revenues (RONm)	1,337.7	1,348.3	1,396.0	1,408.3
		EBITDA (RONm)	573.3	605.9	523.6	514.3
		margin (%)	42.9%	44.9%	37.5%	36.5%
Fair value (RON m)	3,135	EBIT (RONm)	430.3	442.6	353.1	334.1
		Net profit (RONm)	367.4	379.6	287.3	286.5
		margin (%)	27.5%	12.1%	20.6%	20.3%
Shareholders structure:		P/E (x)*	7.5	7.2	9.5	9.6
Economy Ministry	73.5%	EV/EBITDA (x)*	4.6	4.9	5.2	5.4
Fondul Proprietatea	15.0%	P/Bk (x)*	0.9	0.8	0.8	0.8
Others	11.5%	P/S (x)*	2.0	2.0	2.0	1.9
		Dividends paid-out (RONm)	338.7	350.4	313.2	171.9
		Pay-out ratio (%)	92.2%	92.3%	109.0%	60.0%

Source: Company data, KBC Securities

*priced at COB 04 April 2012

Investment case

Transgaz is the operator of Romania's national gas transmission system as well as the operator of transit pipelines. For the transmission side of the business, Transgaz's revenues are regulated by ANRE, which establishes tariffs based on a formula that divides revenues according to the quantity of electricity estimated to have been transported during the year. For the transit side of the business, revenues are established through direct negotiations with clients (i.e. Gazprom and Bulgargaz).

- **State to sell shares in 2012:** The sale of an additional 15% stake in Transgaz is scheduled to take place within the next three months. The placement should improve the firm's liquidity and increase its attractiveness for investors. However, the price is currently unknown, which leaves the risk of a share overhang.
- **Dividend play:** As a state-owned company, Transgaz is obliged to pay at least 50% of net income as dividends. The state has required a 90% dividend pay-out in the last two years, which implies the firm will pay a dividend of RON 29.8 per share from 2011 profit, implying a dividend yield of 12.4%. We believe the high dividend pay-out is also likely to be maintained next year, when we expect the dividend yield at 11.0%.
- **Tariff increase possible in 2012:** With the start of a new regulatory period in July 2012, we would expect Transgaz to negotiate a small increase in the transport tariff with ANRE. The tariff currently stands at RON 7.5 per MWh, with no adjustment in the past two years. We believe the current regulatory vectors (RoR of 7.8%, efficiency gain of 0.91%) are also likely to be adjusted, but there is no indication so far on the outcome of the negotiations with ANRE.
- **We forecast lower gas consumption:** We expect gas consumption growth to slow down in 2012 after 2.8% y/y growth in 2011. We expect volumes to be negatively affected by hikes in natural gas prices: prices for industrial consumers were up 18% in 2011, while the price of gas from Russia rose to a record high US\$ 545 per 1,000 cubic metres in 4Q11. The EU is pushing for additional price increases for end-consumers. In addition, Petrom will start converting some of its gas production into electricity in 2H12 (about 5% of total gas consumption per year), thus we expect transported quantities to decrease by 1.0% in 2011-2012 before rising 1% in 2012-2013 and 2% in 2013-2014.

- **Low debt profile compared to peers:** Transgaz is much less indebted than foreign peers. This should allow the company to further expand its investment program and boost its profitability. The firm had a net debt-to-EBITDA level of 0.34x in 2011.
- **Maintenance costs might erode profitability slightly:** The value of maintenance works has been below the budgeted numbers so far this year. We believe additional maintenance expenses might emerge in 2012. However, one of the reasons we forecast a higher EBIT than the consensus is our below-consensus estimate for maintenance.
- **Transit revenues helped by stronger US\$ versus RON:** Transit revenues (i.e. from gas transited through Romania from Russia to Bulgaria) are likely to increase in 2012 as we expect further RON depreciation versus US\$. Transit contracts are US\$-denominated while quantities are essentially fixed, thus US\$/RON changes have the biggest impact on these revenues. Costs also tend to be fixed on this side of the business, which means all increases in transit revenues are reflected in Transgaz's profits.
- **Trading at a discount to peers:** On a 2011 EV/EBITDA of 5.2x, the company trades at a 39.8% discount to foreign peers. While some of the discount is justified by Transgaz's higher risk profile related to the possibility of ANRE cutting costs, we view the current discount as too high.

Catalysts

- Potential increase in tariffs in July 2012.
- Investments to lead to lower costs.
- Eventual start of the Nabucco project or alternative project.

Risks

- Regulatory risk as ANRE has several times postponed a sufficient increase in tariffs e.g. to cover costs.
- Uncertainty regarding dividends this year.

Valuation

- Our fair value of RON 266.3 per share is the average of our DCF model result (RON 263.1 per share) and DDM model result (RON 269.5 per share).

Electricity producers: Multiple-based comparison

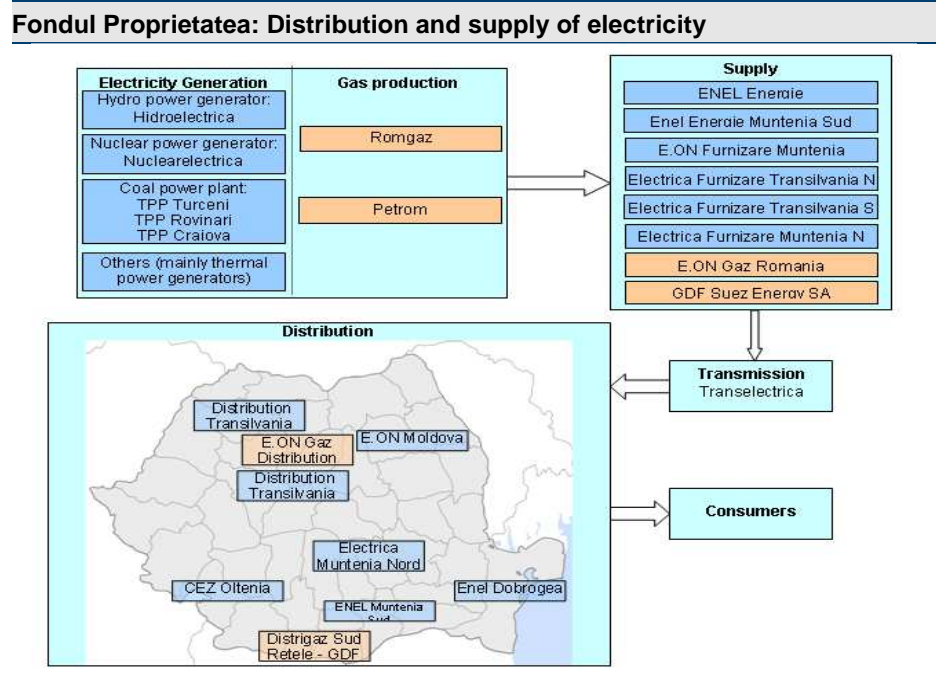
	EV/EBITDA**			P/E**			P/B**		
	2009	2010E	2011F	2009	2010E	2011F	2009	2010E	2011F
FLUXYS-D	9.2	9.1	9.6	18.9	18.9	19.5	1.7	1.7	1.7
ENAGAS SA	7.9	7.2	6.7	9.3	8.9	8.3	1.8	1.7	1.6
SNAM RETE GAS	9.2	8.8	8.4	12.6	12.4	12.1	2.1	2.0	2.0
ELIA SYSTEM OPERATOR	9.7	9.5	9.1	15.9	15.6	14.1	1.0	0.9	0.9
TERNA SPA	9.9	9.1	8.6	15.5	14.5	13.9	2.2	2.1	2.1
RED ELECTRICA CORPORACION	8.4	7.8	7.3	9.9	8.9	8.1	2.5	2.2	2.0
Total Average	9.07	8.58	8.27	13.67	13.22	12.68	1.85	1.78	1.72
Transgaz	4.86	5.17	5.40	7.22	9.54	9.57	0.81	0.81	0.78
Premium/discount vs. peers	-46.4%	-39.8%	-34.8%	-47.2%	-27.8%	-24.5%	-56.0%	-54.6%	-54.7%

Source: KBC Securities, Bloomberg

**Multiples are based on IBES estimates

**Priced at 04 April 2012 closing prices

D. Electricity and gas distributors and suppliers



Source: Fondul Proprietatea, KBC Securities

Investment case

Five of Romania's eight electricity distributors and suppliers and both gas distributors and suppliers were privatized in 2004-2008 (see table on the following page). The buyers were E.ON, Enel, CEZ and GDF Suez. In recent years, distribution has been separated from supply, which has led to the formation of additional companies, though the shareholders remain the same.

- **Potential sale of assets:** Fondul Proprietatea has announced plans to sell its stakes in the electricity and gas distribution and supply companies and has appointed an investment bank to try to sell these assets. According to the book value, these companies are worth €530m. The latest sale the fund undertook was the disposal of a 30% stake in CEZ Romania for €230m (2.3x above book value) in 2009.
- **Eventual sale hard to accomplish but positive:** We would see a potential decrease in the fund's exposure to this sector as positive, as most of the companies are highly regulated, offer low growth and do not have clear dividend policies. However, it could be difficult for the fund to sell these stakes. Enel's official position, for example, is that they are not interested in buying out the minority stake. Additional options for a potential sale could be seen either where the state has a Put option (as was the case with CEZ), though it is unclear if the fund will benefit from the same option; or where there are more minority shareholders who could act together to put the majority shareholder under pressure to sell. The state is present in the shareholding structure of all the privatized companies.

Investment case

- **Regulated versus free market activities:** Romania's electricity and gas distribution companies are natural monopolies in charge of the distribution grids. They are regulated using a methodology which allows them to recover total costs for grid maintenance plus a pre-established rate of return. Distributors are likely to remain regulated in the future, in line with EU norms. On the other hand, while suppliers are still regulated, they should slowly become unregulated and be able to sell their energy at market prices.
- **Next regulatory period starts in 2013:** The current regulatory period allows distributors a rate of return of 7% for state-owned distributors and 10.0% for private distributors. Gas distributors have a regulated rate of return of 8.6%. The suppliers have a margin of 2.5% allowed over electricity purchasing costs for the part of the electricity that they sell to household consumers, while there is no restriction on the remainder. We expect the new regulatory period starting in 2012 to show an improvement in the level of profitability, albeit to a limited degree.
- **Cash rich companies:** The privatization methodology (roughly the same for all companies) involved selling a 25% stake from the state to a private investor and a cash subscription by the private investor to reach a 51% stake. As a result, some of the distributors are cash rich. For example, Enel Distribution Muntenia Sud had a negative net debt of RON 1.85bn, Enel Distribution Banat had a negative net debt of RON 0.4bn and Enel Distribution Dobrogea had a negative net debt of RON 0.18bn as of 2009. Suppliers were created after privatization when they were separated from distribution, thus they have no debt but also no cash position.
- **Reference market transaction at EV/EBITDA of 8.0x:** The stake held by Fondul Proprietatea in CEZ's distribution and supply companies was sold for €230m in 2009, at a P/B of 1.3x, an EV/EBITDA of 8.0x and 2.3x higher than the value at which the stake was registered in Fondul Proprietatea's portfolio.

Shareholders structure

Company	Shareholders
Distribution	
Enel Distributie Muntenia S	Enel Investment Holding - 64.4%, Electrica SA - 23.6%, Fondul Proprietatea 12%
Electrica Distributie Transilvania N	Electrica SA - 78%, Fondul Proprietatea - 22%
Enel Distributie Banat	Enel investment Holdings - 51.0%, Electrica - 24.9%, Fondul Proprietatea - 24.1%
Electrica Distributie Muntenia N	Electrica SA - 78%, Fondul Proprietatea - 22%
Electrica Distributie Transilvania S	Electrica SA - 78%, Fondul Proprietatea - 22%
Enel Distributie Dobrogea	Enel investment Holdings - 51.0%, Electrica - 24.9%, Fondul Proprietatea - 24.1%
E.ON Distributie Moldova	E.ON Energie Romania - 51%, Electrica - 27%, Fondul Proprietatea - 22%
GDF Suez Energy SA (Distrigaz Sud)	Romania Gas Holding - 51%, Ministry of Economy - 37%, Fondul Proprietatea - 12% (EBRD and IFC each own 10% in Romania Gas Holding)
E.ON Gaz Distributie SA	E.ON Ruhrgas International - 51%, OPSPI - 37%, Fondul Proprietatea - 12%
Supply	
Enel Energie Muntenia S	ENEL - 64.4%, Electrica - 23.6%, Fondul Proprietatea - 12%
Electrica Furnizare Transilvania N	Electrica - 78%, Fondul Proprietatea - 22%
Electrica Furnizare Transilvania S	Electrica - 78%, Fondul Proprietatea - 22%
Electrica Furnizare Muntenia N	Electrica - 78%, Fondul Proprietatea - 22%
E.ON Furnizare Moldova	E.ON Romania - 51%, Electrica - 27%, Fondul Proprietatea - 22% (EBRD owns 9.8% on E.ON Romania)
Enel Energie	Enel Distribuzione - 51%, Electrica - 37%, Fondul Proprietatea - 12%
E.ON Gaz Romania SA	E.ON Romania - 51%, Min of Economy - 31.8%, Fondul Proprietatea - 13.4%, Electrica 3.8% (EBRD owns 9.8% on E.ON Romania)

Source: Company data, KBC Securities

*Tariff methodology:
Distributors*

- The revenues of distributors are established by ANRE by adding normal operating expenses to a pre-established profitability. The profitability is calculated by using the formula: regulated profit = regulated asset base (RAB) x regulated rate of return (RoR). A certain cost efficiency target is imposed.
- For distributors, the regulated revenue cap methodology means that the companies act in a similar way to a bond. Besides the regulated profit (RAB x RoR), additional profits or losses could be incurred if the companies manage to reduce costs below the normalized regulated costs or costs are above this level.
- Current RoR is set at 10% for privatized distributors and 7% for state-owned electricity distributors. The RoR is set at 8.6% for gas distributors.

Tariff methodology: Suppliers

- Electricity suppliers have their prices regulated for the energy supplied to end consumers (with a 2% profit margin allowed), while they can freely negotiate the price with industrial consumers. While an end-user is allowed to switch from regulated supply prices to negotiated prices, in practice this situation does not occur as the regulated margin is low and consumers cannot obtain a better price from the supplier.

Catalysts

- Increase in profit due to higher Regulated Assets Base (RAB).
- Increase in electricity consumption.
- Decline in costs after investments.
- Market liberalization to help profitability of the supply business.

Risks

- Regulatory risk as ANRE might not adjust the tariffs fast enough on the regulated side of the business.
- Investments still required to keep the networks operational in standard conditions

Valuation

- We value distribution companies as bond instruments because of the price-cap revenue methodology applied. We treat them as perpetual bonds with cash flow represented by regulated EBIT discounted at current WACC. Supply companies are valued using a target EBITDA based on the regulated profit margin (2.5%) and a target EV/EBITDA based on a peer comparison.

Electricity & gas utilities companies: Acquisition price (RON m)

Company	Buyer	Date of acquisition	Ownership	Equivalent of 100% (€ m)	Cash infusion (€m)	Total acquisition value	
						(€m)	RONm
Electrica Moldova	E.ON	2005	51.0%	127.5	68.6	196	830
Electrica Banat	Enel	2004	51.0%	73.2	38.0	111	470
Electrica Oltenia	CEZ	2005	51.0%	192.5	103.6	296	1,253
Electrica Muntenia Sud	Enel	2007	67.0%	790.0	593.0	1383	5,850
Electrica Dobrogea	Enel	2004	51.0%	73.2	38.0	111	470
Distrigaz Nord	E.ON	2005	51.0%	416.7	178.0	595	2,515
Distrigaz Sud	GDF Suez	2005	51.0%	426.7	183.0	610	2,579

Source: company data, KBC Securities estimates

Electricity & gas distribution companies: Valuation according to price-cap methodology (RON m)

Company	Regulated Asset Base as of 2010	Rate of Return	Implied operating result (RABxRoR)	WACC	Enterprise Value	Estimated equity value
Electrica Distributie Muntenia Nord	1,354.3	7.0%	95	10.7%	886	1,012
Enel Distributie Banat	1,052.7	10.0%	105	10.7%	984	1,446
Enel Distributie Dobrogea	1,079.4	10.0%	108	10.7%	1009	1,275
Enel Distributie Muntenia Sud	1,777.2	10.0%	178	10.7%	1661	3,520
Electrica Distributie Transilvania Nord	1,320.4	7.0%	92	10.5%	880	860
Electrica Distributie Transilvania Sud	1,365.1	7.0%	96	10.7%	893	897
E.ON Moldova Distributie	1,273.3	10.0%	127	10.5%	1213	1,213
E.On Gaz Distributie	1,183.4	8.6%	102	10.3%	988	977
GDF Suez (Distrigaz Sud)	2,649.0	8.6%	228	9.8%	2325	2,325

Source: company data, ANRE, KBC Securities estimates

Electricity & gas distribution companies: WACC Calculation

	Electrica Distributie Muntenia Nord	Enel Distributie Banat	Enel Distributie Dobrogea	Enel Distributie Muntenia Sud	Electrica Distributie Transilvania Nord	Electrica Distributie Transilvania Sud	E.ON Moldova Distributie	E.On Gaz Distributie	GDF Suez (Distrigaz Sud)
Risk free rate	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%	6.2%
Beta	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Equity premium	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%
Cost of equity	10.7%	10.7%	10.7%	10.7%	10.7%	10.7%	10.7%	10.7%	10.7%
Debt premium	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%
Cost of debt	7.2%	7.2%	7.2%	7.2%	7.2%	7.2%	7.2%	7.2%	7.2%
Effective tax rate	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%
Debt	0.0%	0.0%	0.0%	0.0%	1.4%	0.0%	2.3%	8.3%	17.3%
Equity	100.0%	100.0%	100.0%	100.0%	98.0%	100.0%	97.7%	91.7%	82.7%
WACC	10.7%	10.7%	10.7%	10.7%	10.5%	10.7%	10.5%	10.3%	9.8%

Source: KBC Securities estimates, Company data

Electricity supply companies: Valuation according to EV/EBITDA multiple

Company	EBITDA 2010	Target EBITDA	Target EV/EBITDA	Enterprise value (RON m)	Estimated equity value (RON m)
ELECTRICA FURNIZARE TRANSILVANIA SUD	17.8	34.3	7.7	264.0	277.2
ELECTRICA FURNIZARE TRANSILVANIA NORD	-24.8	29.2	7.7	224.7	193.1
ELECTRICA FURNIZARE MUNTENIA NORD	11.6	32.4	7.7	249.8	247.1
ENEL ENERGIE SA	-5.9	48.0	7.7	369.2	581.8
E.ON MOLDOVA FURNIZARE SA	-0.8	45.9	7.7	353.1	697.3
E.ON GAZ ROMANIA SA	-21.2	36.4	7.7	280.4	294.8

Source: KBC Securities estimates, ANRE, Company data

E. Airports

	Henri Coanda Airport			Aurel Vlaicu Airport			CN Aeroporturi Bucuresti		
	2007	2008	2009	2007	2008	2009	2009	2010	2011b
Operating revenues (RON m)	282.1	318.9	328.6	39.6	77.1	103.9	396.5	460.1	546.6
EBITDA (RON m)	160.3	156.9	142.3	17.8	37.1	43.1	n.a.	164.8	222.4
margin (%)	104.9	78.9	57.8	16.1	22.8	24.7	82.5	54.2	111.9
EBIT (RON m)	37.19%	24.74%	17.59%	40.66%	29.57%	23.77%	20.81%	11.78%	20.47%
Net profit (RON m)	103.1	103.1	59.5	-10.8	-0.1	14.6	74.1	52.8	99.2
margin (%)	36.60%	32.30%	18.10%	-27.30%	-0.10%	14.00%	18.69%	11.48%	18.15%
Fair value (RON m)							1,981.50		
EV/EBITDA (x)	8.3	8.4	9.2	33.4	15.8	13.1		12.4	8.9
P/Bk (x)	1.46	1.36	1.22	16.3	0.2	0.1	26.7	37.5	20.0
Number of passengers (m)	4.98	5.06	4.48	0.97	1.72	1.97		7.1	7.5

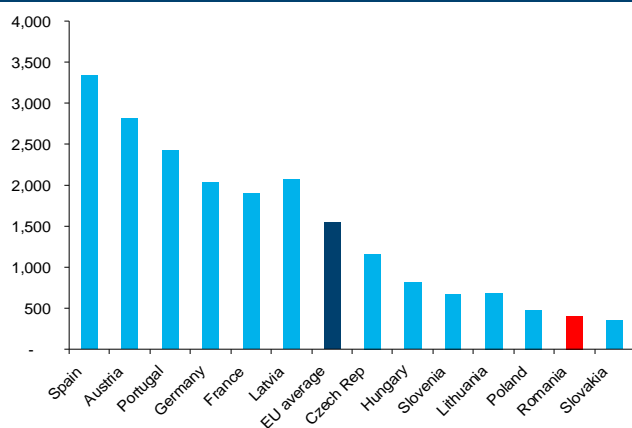
Source: Company data, KBC Securities

Investment case

Of Romania's 17 airports, four are part of Fondul Proprietatea's portfolio, the two biggest being the Bucharest-based airports Henri Coanda and Aurel Vlaicu. In 2009, the two airports in Bucharest – Henri Coanda and Aurel Vlaicu – merged into Compania Nationala Aeroporturi SA. The total traffic for the two airports reached 7.5m passengers in 2011, an increase of 5.9% versus 2010. This represents about 70% of the total passenger traffic in Romania.

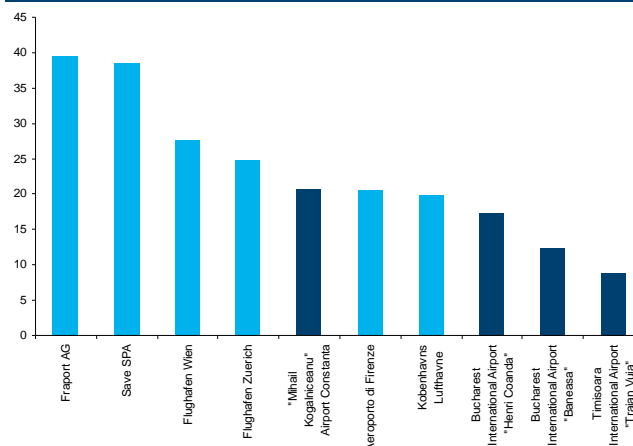
- **Number of passengers set to increase:** Romania currently has one of the lowest ratios of air passengers per inhabitant in the EU, with an average of 412 passengers/1,000 inhabitants in 2010 versus the EU average of 1,550 passengers/1,000 inhabitants.
- **Shift of traffic among the two airports could boost revenues:** Starting in March 2012, the low-cost traffic from Aurel Vlaicu airport will be shifted to Henri Coanda while Aurel Vlaicu will be changed into a business airport. This move will increase the traffic at Henri Coanda Airport by almost 50%. Although the two airports report financial data together, we believe the move might actually lead to an increase in overall revenues despite the total traffic being the same, as the taxes at Henri Coanda Airport are higher and the other services provided (e.g. shopping areas) are much larger than at Aurel Vlaicu.
- **Extension and new terminal at Henri Coanda Airport:** Investments of €150m in the third phase of development should boost capacity to more than 6m passengers per year. A first extension was opened in March 2011 and the new terminal should become fully operational in August 2012. The new terminal is expected to boost revenues from air traffic and extra services.
- **Revenues per passenger should also increase:** The two main airports in Romania have a low level of operating revenues per passenger. Besides the expected increase in air traffic, we believe the two Bucharest airports could derive additional revenues from connected services, which should leave the ratio of revenues per passenger more in line with the average of peers. This should create economies of scale and improve the profitability margins of the two airports.

Number of passengers per 1,000 inhabitants



Source: Eurostat

Turnover per passenger at peer airports (€/pax)



Source: Bloomberg, KBC Securities

Catalysts

- Increase in air traffic in Romania as living standards increase.
- Higher revenues per passenger at the airports.
- Extension of airports through the construction of new terminals.
- Improved infrastructure for access to the airports.

Risks

- Decline in aviation industry at the global level due to the economic crisis.
- Costs of expansion and modernization of the airports.

Valuation

In order to value airports we employed a multiple-based approach by using an EV/no. of passengers ratio. This method values CN Aeroporturi Bucuresti at RON 1,981.5m. This implies a 2011b P/E of 20.0x and an EV/EBITDA of 12.4x.

Airports: Valuation based on EV/Number of passengers

Company	No of passengers(m)	Target EV/No of passengers (€/pax)	Resulting EV (€ m)	Resulting EV (RON m)	Net debt (RON m)	Fair value (RON m)
CN Aeroporturi Bucuresti	7.50	59.52	446.40	1,919.50	(62.00)	1,981.50
Timisoara International Airport "Traian Vuia"	0.89	59.52	52.97	224.07	4.31	219.76
"Mihail Kogalniceanu" Airport Constanta	0.09	59.52	5.54	23.41	(0.74)	24.15

Source: KBC Securities estimates

Airports: Valuation based on EV/Number of passengers

Company	EV/No of passengers (€/pax)	Revenues / passenger (€/pax)	EBITDA margin (%)	EV/EBITDA
Fraport AG	96.0	39.5	28.8%	11.1
Aeroporto di Firenze	51.7	20.5	28.8%	11.5
Flughafen Wien	68.4	27.7	33.3%	9.2
Flughafen Zuerich	94.2	24.8	49.1%	8.3
Kobenhavns Lufthavne	86.5	19.9	52.0%	9.8
Save SPA	49.6	38.4	17.7%	8.0
Average	74.4	28.5	34.9%	9.7
CN Aeroporturi Bucuresti	59.5	17.3	46.7%	12.4
Timisoara International Airport "Traian Vuia"	59.5	8.8	29.7%	20.6
"Mihail Kogalniceanu" Airport Constanta	59.5	20.6	20.4%	9.14

Premium/Discount to peers

CN Aeroporturi Bucuresti	-20.0%	-39.4%	33.7%	27.8%
Timisoara International Airport "Traian Vuia"	-20.0%	-68.9%	-14.9%	113.5%
"Mihail Kogalniceanu" Airport Constanta	-20.0%	-27.5%	-41.5%	-5.3%

Source: KBC Securities estimates

Annex 3 – Market news

Date	Event
April 2012	<p>The EGM on 4 April 2012 approved the listing of the fund on Warsaw Stock Exchange and the modification of the Constitutive Act to allow the cancellation of shares with lower quorum requirements. The EGM also approved the proposal for a higher fee for fund administrator Templeton in the event of cash being returned to shareholders from asset disposals. Finally, new members were selected for the board of nominees. The new members are Mr Julian Rupert Francis Healy (candidate nominated by City of London), Mr Steven van Groningen and Mr Piotr Rymaszewski (nominated by Manchester Securities). In addition, Mr Cristian Busu and Mr Sorin Mihai Mindrutescu were re-elected. The request to decrease share capital via the cancellation of shares that have been bought back so far was not approved because the minimum quorum requirement of 50% was not met (45.2% of the shareholders voted at this EGM). This point will be discussed again at the EGM on 25 April 2012, with the new quorum conditions as approved at the recent EGM.</p>
March 2012	<p>According to a statement published by Fondul Proprietatea, one of the company's shareholders (with a more than 5% stake) has asked for an amendment to the agenda for the General Shareholders' Meeting on 25 April 2012. The amendment aims to reconfirm all past shareholder meeting decisions since 2010, when Templeton was named administrator. The amendment aims to avoid any further potential trials started by minority shareholders, such as the numerous actions started by Mrs Ioana Siraiala</p>
March 2012	<p>Fondul Proprietatea is calling an EGM and AGM for 25 April in order to vote on the approval of the annual statements for 2011, the approval of a dividend of RON 0.03854 per share and the approval of a share buy-back program with the purpose of cancellation for 1.1bn shares (8% of the share capital). The buy-back should be done at a price between RON 0.2 per share and RON 1.5 per share, for an 18 months period and will depend on the available cash resources. The cancellation of the shares will be decided by shareholders at a later stage in another EGM.</p>
January 2012	<p>The EGM on 6 September 2010, appointing Franklin Templeton as manager, is being contested in court by a minority shareholder. Franklin Templeton representatives consider the action in court as non-material as the role of Templeton as asset manager has been reapproved in several other shareholders meetings which made changes to the constitutive act which includes the appointment of Franklin Templeton as manager.</p>
November 2011	<p>According to a statement published by Fondul Proprietatea, the state has further decreased its shareholding in the fund to 1.53%, down from 36.8% in January. The state has thus used the entire shares to be transferred to individuals entitled to receiving them.</p>
November 2011	<p>An EGM that took place on 23 November at Fondul Proprietatea has approved the lifting of any voting restrictions in Fondul Proprietatea. Additional items on the agenda were the changes in the bylaws which allow administrator Franklin Templeton to decide regarding potential disposals and investments up to 20% of the assets, decrease in the share capital, voting for the budget and naming new auditor.</p>
November 2011	<p>According to a statement issued by Fondul Proprietatea, quoting a draft of Emergency Government Ordinance, the state wants to increase participation in the share capital of Nuclearelectrica (majority state owned nuclear power plant) with an amount of RON 1,442.5m which has been allocated from the state budget in the previous years for buying heavy water from Regia Autonoma pentru Activitati Nuclear, a state controlled company that produces this substance. According to Franklin Templeton, the administrator of the fund, this operation would lead to a dilution of the stake held by Fondul Proprietatea by RON 266m or a decrease of 1.8% in the NAV. According to the statement, Templeton will take legal actions to stop this process.</p>

- November 2011** According to Ziarul Financiar daily, quoting an official document released by the Ministry of Economy, the Romanian government held talks with IMF representatives regarding the state of Hidroelectrica's below-market-price contracts and regarding the sale of minority stakes in state-owned companies. According to the statement, Hidroelectrica should cancel all of its contracts signed below-market at the first possible term. This represents more than 66% of the entire energy produced by Hidroelectrica. In addition, the government will accelerate the sale of minority stakes in state-owned companies in Fondul Proprietatea's portfolio (i.e. Romgaz, Transelectrica, Transgaz, Hidroelectrica, Nuclearelectrica) and start the privatization of Olchim and the remaining state-owned electricity distributors.
- August 2011** According to a statement issued by Fondul Proprietatea, Franklin Templeton, the administrator of the fund, has decided to decrease the paid share capital of the fund from RON 13.78bn to RON 13.40bn. This is due to the fact that the state has not contributed to the share capital with shares worth RON 340.8m for Nuclearelectrica, RON 20.0m for Romarm and RON 11.7m for Electromecanica Ploiesti. The not-paid shares will be registered as "Subscribed unpaid share capital" and will be blocked until the situation is cleared. These shares represent approximately 2.7% of the fund shares.
- April 2011** The requests of the Ministry of Finance regarding hiking the dividend from RON 0.01569/share to RON 0.03141/share as well as the election of a new member to the committee of representatives (the equivalent of a BoD in the fund's governance structure) have been approved in the AGM on 27 April 2011.
- April 2011** The EU Commission asked Romania to bring its national legislation on regulated end-user energy prices in line with EU rules, according to Mediafax news agency and a Bloomberg report. EU rules state prices are set primarily by supply and demand. The Commission will send "reasoned opinions" to Romanian authorities and if compliance with the legal obligations does not occur within two months, the Commission may take the case to the Court of Justice. The EU Commission targets both the electricity and the natural gas market in Romania.
- March 2011** According to a communiqué published by the Index Committee of the Bucharest Stock Exchange, the shares of Fondul Proprietatea (FP) will be included in four exchange indices from 21 March 2011: the blue-chip BET and BET-XT indices, the composite BET-C index and the financial sector index BET-FI (alongside SIFs).
- January 2011** According to daily Ziarul Financiar, Fondul Proprietatea convened an EGM for the shareholders of natural gas producer Romgaz on 17 January 2011. The purpose of the EGM was to dismiss and take legal action against those board members who voted in favour of a RON 400m (€93m) donation to the state budget in November. Fondul Proprietatea lost some RON 60m (€14m) because the state chose to oblige Romgaz to make a donation instead of distributing a special dividend. Of the five members on Romgaz's board, three are state representatives. Franklin Templeton representatives said they are extremely concerned as the transfer has already occurred and they intend to make efforts to recover the funds.
- January 2011** Franklin Templeton officials have stated their discontent about Hidroelectrica's decision to sell 1.7m MWh (10% of production) to ArcelorMittal Galati at a price of RON 130/MWh. Fondul Proprietatea's manager says this price is significantly lower than the average price of RON 170/MWh established on the OPCOM market. Templeton said it would take all necessary measures to protect minority rights in the case. The administrator believes this quantity should have been sold on the open market. Hidroelectrica's former CEO Mihai David said the Romanian state decided to sell this quantity to ArcelorMittal Galati as it wants to support Romania's metallurgical industry.
- December 2010** According to a statement published on 16 December 2010, Fondul Proprietatea's NAV stood at RON 15.9bn (€ 3.7bn) in December, or RON 1.1541/share. The value is up 18% m/m but is not directly comparable to historical values as it was calculated according to a new National Securities Commission regulation issued in November. The new regulation stipulates that listed securities and money market instruments are valued at exchange closing prices as opposed to the 90-day weighted average price of the old regulation. Another important change is that shares that have not been traded during the last 30 days (as well as unlisted shares) can be valued using either shareholders' equity from the latest financial statements or by using valuation methods in accordance with International Valuation Standards (i.e. fair value).

December 2010	<p>According to Ziarul Financiar, shareholders of state-controlled gas producer Romgaz approved the controversial RON 400m (€ 93m) donation to the state budget at an EGM on 30 November 2010. The funds are likely to come from Romgaz's cash holdings, which totalled RON 773m (€ 179m) as of December 2009. Fondul Proprietatea is a minority shareholder in Romgaz with 15% of shares, while Romania's Ministry of Economy holds 85% of shares. Through manager Franklin Templeton, the fund voted against the proposal at the EGM and asked instead for the cash to be distributed as a special dividend to all entitled shareholders. After the vote, Fondul Proprietatea announced its intention to challenge the EGM decision in court, as it did not represent the equal treatment of minority shareholders. Fondul Proprietatea could have received some RON 60m (€ 14m) from the special dividend, which would have boosted the fund's budgeted dividend revenues by 29% for 2011.</p>
September 2010	<p>Fondul Proprietatea published its official NAV calculated in accordance with the Romanian National Securities Commission's regulation 4/2010. NAV per share came in at RON 1.0283 for July, RON 1.0423 for June and RON 1.0442 for May 2010. NAV was calculated by KPMG.</p> <p>According to a communiqué issued on 5 August 2010, Fondul Proprietatea scheduled an EGM for 6 September 2010. The agenda of the EGM includes: approval of the fund's bylaws and the appointment of Franklin Templeton Investment Management as the sole manager of the fund; approval of the fund's listing on the Bucharest Stock Exchange and other international exchanges (within 90 days of the fund's registration with the National Securities Commission); and the authorization of the fund to perform a share buyback amounting to a maximum of 1,375,759,258 shares (10% of total share capital). The EGM will decide upon replacing the existing governing bodies of the fund (namely the supervisory board and the directorate) with a new structure called the committee of representatives. The EGM will also vote on a proposal to distribute a gross dividend worth RON 0.0822/share from both 2008 and 2009 profit, which implies a 94% cumulative distribution rate. Calculated at an OTC price of RON 0.47/share the dividend yield would be 17.5%.</p>
August 2010	<p>According to a communiqué issued by Fondul Proprietatea, the Chamber of Deputies approved amendments to Government Ordinance 81/2007 at the plenary session held on 23 June 2010. This will allow the cancellation of the state's unpaid shares (482m shares) and the distribution of dividends from 2008 and 2009 profit.</p>
June 2010	<p>According to daily Ziarul Financiar, utility companies E.ON and Enel could acquire the remaining minority shares in Romanian electricity distribution and supply entities from the state. E.ON and Enel already acquired the majority stakes in two distribution and supply companies in the privatization process organized by state-owned monopoly Electrica SA several years ago. The state currently holds 27% in E.ON Moldova (distribution and supply), 23.6% in Enel Muntenia Sud (distribution) and 37% in Enel Energie Muntenia SA (supply), while Fondul Proprietatea holds 22% in E.ON Moldova (distribution and supply) and another 12% in ENEL Energie Muntenia SA (both distribution and supply). The sale should take place in accordance with Put/Call options in the privatization contracts. According to the article, the E.ON Moldova stake purchase is conditional on the payment of debt by the National Railway Company to E.ON Moldova.</p>
June 2010	<p>Fondul Proprietatea announced it has filed all the necessary documents with Romania's National Securities Commission (NSC) to register as "Other Collective Investment Undertakings". The NSC has yet to issue an official resolution, after which the official NAV of the fund (calculated according to Regulation no. 4/03.03.2010) will be published.</p>
May 2010	<p>The National Securities Commission issued Regulation no. 4 covering the registration, functioning and rules for the calculation of net asset value (NAV) for Fondul Proprietatea.</p>
March 2010	<p>Romania's National Securities Commission (NSC) approved the contract assigning Franklin Templeton as administrator of Fondul Proprietatea. The NSC reiterated that its approval of the administration contract is conditional on the fund's current management registering the entity within 45 days. The NSC designated Fondul Proprietatea a closed-end fund under the 'Other Collective Investment Undertakings' category (i.e. non-UCITS): as such, the fund's representatives must complete a series of documents before the administration contract can come into effect.</p>
February 2010	

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