

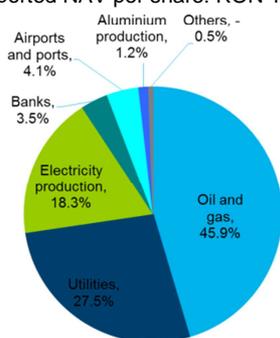
29 June 2012

Hidroelectrica enters insolvency

Financial holding

Romania

Reported NAV per share: RON 1.17



Current price*

RON 0.45

Buy

Fair value

RON 0.68

Rating maintained

Net asset value	Official NAV		Fair values	
	RON m	RON/share	RON m	RON/share
Listed shares	5,345	0.40	5,993	0.45
Unlisted shares	9,742	0.73	6,885	0.51
Cash and equivalents	471	0.04	471	0.04
Total assets	16,231	1.21	14,008	1.04
Debt (dividends payable)	-540	-0.04	-540	-0.04
Deferred taxes	-14	0.00	-14	0.00
NAV	15,678	1.17	13,454	1.00
Adjustments to NAV			-4,331	-0.32
Implied fair value			9,123	0.68
Closing price as of 28 June 2012			5,969	0.45
Upside (%)				52.85%

Source: KBC Securities

*priced at COB 28 June 2012

Fondul Proprietatea's share price has dropped 10.0% since the start of the insolvency procedure at Hidroelectrica. However, we believe the news is now fully priced-in as we do not currently attribute more than 50% probability to a complete loss of value of the fund's stake in Hidroelectrica, which accounts for 20% of the fund's NAV; thus we see the 10% drop in price as a fair reflection of the current default probability. We have also increased our fair discount to NAV for Fondul Proprietatea to reflect the risk of delays in privatizations and in listings of some companies in the portfolio. Our fair value has fallen to RON 0.68 per share, although this still implies 52.8% upside. We maintain our Buy rating.

Buy rating maintained

- **Hidroelectrica enters insolvency procedure:** On 20 June 2012, the Bucharest court approved a request from the board of Hidroelectrica for the company to enter the insolvency procedure. The reasons given for the move were that the firm had been affected by the drought at end-2011/beginning of 2012 and by fluctuations in FX rates, which led to an increase in debt and negative cash flow. The insolvency procedure aims to restructure the company's activity and increase the firm's ability to generate cash flow so that the threat of asset sales or bankruptcy is avoided.
- **Risky procedure:** In our view the procedure chosen by the state for restructuring Hidroelectrica's activity is extremely risky as it involves a lengthy court process, requires the involvement of creditors and increases credit risk (e.g. Moody's cut the rating) which could in the end lead to a "self-fulfilling prophecy". Fondul Proprietatea's administrator will have to monitor the process closely if it is to ensure that the fund's stake in Hidroelectrica is not depreciated.
- **...but there could be also positives:** However, we also see various positives if the reorganization plan is successful: the company will be able to quickly generate more profit as revenues will be boosted by changing bilateral contracts (i.e. below market prices) to market price contracts, while some unnecessary capital expenditures could be decreased.
- **Other side-effects of the process:** The insolvency procedure brings other negative influences for the fund: delays in the listing of Hidroelectrica, delays in selecting private management, provisioning requirements for banks which credited Hidroelectrica and in which the fund also owns stakes (BRD-GSG, Banca Transilvania), delays in cashing in the dividend from Hidroelectrica, a higher risk perception of the state-owned companies in the portfolio.
- **Quantifying the process:** We consider the possibility of a restructured Hidroelectrica showing full profit potential from 2014 as a best-case scenario. Under the bear-case scenario Fondul Proprietatea's stake in Hidroelectrica is valued at zero. Our base-case scenario is the average of the two.
- **Will the government continue the listing program?** The government states that it is committed to continue with the listing program but with a delay due to market conditions and an eventual restructuring of the companies before the listing. We think such a process could be more cumbersome than initially planned and could bring even more delays. For this reason we increase the fair discount to NAV applied for Fondul Proprietatea to 30%.
- **Current discount is too high:** The current market capitalization of the fund equals the value of the listed part of the portfolio and the cash. However, some of the unlisted companies are still generating hefty dividends for the fund (e.g. Romgaz) so we think a null value is not appropriate for those companies.

Hidroelectrica: Influences of the insolvency procedure

	Possibility of a thorough reorganization of Hidroelectrica, which will allow the firm to emerge in better shape.
Positive	The Romanian government is the initiator of the plan and sees it as the best option for the company. The possibility of the cancellation of some unprofitable contracts. Other aspects of activity such as CAPEX or OPEX can be checked.
	Higher risk as creditors are involved in the reorganization plan. Parties (e.g. beneficiaries of bilateral contracts) may file claims. Lengthy court process creates uncertainties and risks. Delay in the listing of the company (now expected in 2013).
Negative	Delays in establishing professional management. Dividends from Hidroelectrica payable to Fondul Proprietatea are delayed (estimated RON 46.9m). Dividends that Fondul Proprietatea will pay next year are uncertain as NAV is now below nominal value (the fund's manager said the situation should be resolved by year-end). Increased risk for other IPOs and SPOs that are due to take place this year due to negative image.
Neutral	The dividend that Fondul Proprietatea intends to pay this year will be paid as scheduled (starting 29 June). Buy-back program is unaffected. A buy-back program could also be started next year despite NAV being below nominal Technical listing in Warsaw is not affected (the decision for the listing was taken at the EGM on 27 June). The link between depositaries necessary for the listing to take place is still missing.

Source: KBC Securities estimates

Hidroelectrica: Calendar of the insolvency procedure

Step	Estimated date*
1. Opening the insolvency procedure	20-Jun-12
2. Company forwards within 10 days an initial list of documents including the list of creditors	30-Jun-12
3. Judicial administrator writes a report to decide if liquidation is needed	10-Jul-12
4. Administrator writes a report on the causes of the insolvency and measure taken	15-Jul-12
5. Deadline for including debt in the list	04-Aug-12
6. Deadline for verifying the list of debt and making a preliminary list of debts	24-Aug-12
7. First creditors meeting: discuss the report of the administrator regarding the necessity of bankruptcy, selects a committee of three to five creditors, confirms maintaining the judicial administrator	29-Aug-12
8. The company or administrator puts forward a reorganization plan	31-Aug-12
9. Deadline for contesting the list, final list is published	08-Sep-12
10. Creditors' meeting votes on the plan	31-Sep-12
11. The judge adopts the plan, decides on the continuation of insolvency or the resumption of normal	12-Dec-12
12. Insolvency procedure ends	When all debts assumed in the plan have been paid

Source: All dates are estimated by KBC Securities using the Bucharest Court decision regarding the opening of the procedure and the provisions of the Insolvency law in Romania but are only indicative and are subject to delays

Hidroelectrica: Sequence of events and official statements

18 June 2012	<p>According to a statement published by Fondul Proprietatea and several Romanian newspapers, Hidroelectrica, the fund's largest holding, has filed for insolvency. The official reasons given by company representatives are:</p> <ul style="list-style-type: none"> - the severe drought at the end of 2011, which led to a 10% decrease in turnover; - a 27% reduction in cash flow in the first months of 2012; - an increase in overdue payables to RON 470m; - financial losses due to an adverse €/RON exchange rate. <p>The press speculates that the insolvency procedure could be an attempt to cancel the bilateral contracts which oblige Hidroelectrica to sell electricity at below-market prices and which have been undergoing renegotiations in recent months.</p>
18 June 2012	<p>According to a communiqué from Franklin Templeton, if the request made by the Board of Administrators is approved (first court hearing on 20 June) the regulations require that the fund registers its shares in Hidroelectrica at a nil value. This would decrease the fund's NAV by 21.0%.</p>
20 June	<p>Mr Remus Vulpescu, the head of Romania's Privatization Office and president of the board of Hidroelectrica, has been quoted in several newspapers as stating the following regarding the insolvency procedure started by the company:</p> <ul style="list-style-type: none"> - The insolvency procedure started by Hidroelectrica relates to the reorganization of the company. Bankruptcy is not part of the plan. - One reason for insolvency is the company's lack of cash to pay its liabilities in the short term; another reason is that the company needs complete reorganization if it is to become more profitable. - The current activity of the company will not be affected in any way: Hidroelectrica will continue to supply electricity and the scope of activity will not be decreased in any way. - According to Mr Vulpescu, the bilateral contracts are affecting the activity of the company but the problems date from a long time ago and were generated by mismanagement. - Hidroelectrica's IPO will be delayed and the reorganization process could take a maximum of 16-18 months. - The restructuring plan will be made public and will have to be agreed with the firm's creditors and the special administrator appointed by the court. It is planned that the current administration will stay in place but under the supervision of the court-named administrator.
20 June	<p>According to a statement published by Fondul Proprietatea, the Bucharest court has approved the insolvency procedure for Hidroelectrica. The court has named Euro Insol SPRL as the administrator of the company. The administrator will have to present a reorganization plan for the company, including the renegotiation of the contracts currently held by the company. The first meeting with creditors is due on 29 August and the administrator needs to present to the court the measures taken on 12 December. Fondul Proprietatea's NAV will be significantly affected by the process as the shares have to be registered at a nil value. The fund manager does not expect the process to have a material impact on the fund's activities.</p>
20 June	<p>Moody's has cut its rating on Hidroelectrica from Ba1 to B2. Moody's says the four-notch downgrade is justified as the insolvency procedure might lead to Hidroelectrica being unable to pay its debts. New loans would also be harder to obtain, according to the Moody's report.</p>
25 June	<p>According to Ziarul Financiar quoting Mr Nicolae Aurariu, the general secretary of Hidroelectrica's labour union 'Hidrosind', the organization has signed an agreement with Romania's Ministry of Economy and with Hidroelectrica for maintaining the company operationally and not selling assets or firing employees. According to the interview, the reorganization plan will primarily target the company's contracts and expenses incurred by the company. In the same article, Mr Remus Borza, director of Euro Insol SPRL, the company appointed as judicial administrator of Hidroelectrica, states that Hidroelectrica's bilateral contracts and high expenses are the problems confronting the company that need to be solved.</p>
26 June	<p>According to ZF daily, Prime Minister Victor Ponta and the vice governor of the National Bank of Romania met yesterday with representatives of banks with exposure to Hidroelectrica in an attempt to assure them that the insolvency will not affect the company's credits. According to participants, Romanian officials have stated that the insolvency action by Hidroelectrica has the backing of both the EU and IMF. Among the banks that have credited Hidroelectrica are BRD (RON 400m) and Banca Transilvania (RON 100m).</p>
27 June	<p>According to Ziarul Financiar daily quoting Mr Remus Borza, representative of Hidroelectrica's judicial administrator, the company's first bilateral contract has been terminated. The contract with Euro PEC provided 0.3 TWh of electricity per year at a price of RON 141 per MWh. The contract is rather small and was the first to be terminated as the energy supplied to Euro PEC had not been paid for in the last six months, which facilitated the termination. According to the administrator, the bigger contracts will also be discussed in the month ahead. According to Jurnalul daily, some of Hidroelectrica's construction and investment contracts might also be terminated.</p>
28 June	<p>According to Mediafax news agency, the rating of Hidroelectrica has been cut again by Moody's, after the court has approved the insolvency procedure. Thus rating has been cut from B2 to Caa1 with negative perspective.</p>
29 June	<p>According to Ziarul Financiar newspaper, a shareholders meeting of Hidroelectrica has empowered Mr. Remus Vulpescu, Head of the Privatization office, as the special administrator of Hidroelectrica, to put together in 2 months the reorganization plan of the company. According to Ziarul Financiar, quoting the AGM documents, the plan should include a complete termination of all bilateral contracts and selling the entire energy on the OPCOM market, in contracts no longer than one year and with quarterly indexation of the price to market prices. The reorganization plan should be finalized and made public by 31 August while an interim report should be published by 15 July.</p>

Source: Fondul Proprietatea

Hidroelectrica: Bilateral contracts

Company	2011 Quantity (MWh)	Value (RONm)	RON per MWh
Alro	2,494,572	322.5	129.3
Luxten	260,429	36.7	141.1
Elsid Titu	172,587	17.8	103.0
Energy Holding	2,155,802	280.3	130.0
Europec	320,876	45.3	141.2
Electromagnetica	891,105	125.0	140.2
Electrocarbon	156,412	16.1	103.0
Arcelor Mittal Galati	1,424,126	185.5	130.2
ALPIQ Romindustries	999,988	130.0	130.0
EFT Romania	1,043,408	136.7	131.0
Electrica	398,300	51.8	130.0
ALPIQ RomEnergie	1,571,913	204.3	130.0
CNH Petrosani	141,869	22.7	160.2
CLMB - Patinoar Brasov	1,240	0.2	139.5
Societatea Nationala a Sarii	20,561	2.9	140.4
OMV Petrom (test)	22,105	3.2	142.5
TOTAL	12,075,293	1,580.8	130.9

Source: Company data

Hidroelectrica: Financial overview

FY 31 Dec. (RONm)	2009	2010	2011		2009	2010	2011
Fixed assets	22,602.0	19,667.2	20,339.1	Turnover	2,420.8	3,273.7	3,020.6
Current assets	387.3	476.5	611.9	Other revenues	45.4	13.4	26.5
o/w cash	28.1	99.9	77.2	Total operating revenues	2,466.2	3,287.1	3,047.1
Deferred Expenditures	0.6	0.6	11.4	EBITDA	816.8	1377.0	894.5
TOTAL ASSETS	22,989.9	20,144.3	20,962.3	EBITDA margin	33.1%	41.9%	29.4%
Short term bank loans	677.0	701.1	1,099.0	Depreciation	654.9	874.2	733.3
Short term other liabilities	1,118.6	1,027.9	1,540.1	EBIT	161.9	502.8	161.2
Long term bank loans	804.0	1,200.3	1,418.9	Operational margin	6.6%	15.3%	5.3%
Long term others	3,581.0	79.7	88.7	Net financial result	(96.5)	(112.5)	(121.5)
Provisions	254.6	313.1	286.6	Net result	48.4	292.4	6.4
Equity	1,452.9	1,801.5	2,440.8				
TOTAL EQUIT AND DEBT	22,989.9	20,144.5	20,962.3				

Source: Company data

Hidroelectrica: Short term debt

(RONm)	2010	2011
Payables	888.1	1,126.0
Pre-payments from clients	8.6	38.1
Dividends payable	0.0	258.6
Other debt	131.2	117.5
Current portion of long term credits	284.9	346.2
Interest on long term credits	5.9	15.0
Comissions on credits	1.1	1.4
Short term credit lines	409.2	736.4
Total short term debt	1,729.0	2,639.1

Source: Company data

Fair value NAV

Fondul Proprietatea: NAV calculation (our fair values)				
	% owned	RON m	% of NAV	RON per share
Total cash and equivalents		471	3.5%	0.035
Share portfolio		12,877	95.9%	0.960
Listed		5,993	44.6%	0.447
Petrom	20.1%	4,443	33.1%	0.331
Transgaz	15.0%	470	3.5%	0.035
Transelectrica Bucuresti	13.5%	203	1.5%	0.015
Alro Slatina	10.2%	160	1.2%	0.012
Oil Terminal	8.5%	6	0.0%	0.000
Azomures Targu Mures	11.1%	117	0.9%	0.009
BRD - Groupe Societe Generale	3.6%	213	1.6%	0.016
Erste Group Bank AG	0.3%	73	0.5%	0.005
Raiffeisen Bank International AV	0.6%	113	0.8%	0.008
Others		195	1.5%	0.015
Unlisted		6,885	51.2%	0.513
Hidroelectrica	19.9%	1,136	8.5%	0.085
Romgaz	15.0%	1,468	10.9%	0.109
Nuclearelectrica	9.7%	371	2.8%	0.028
Complexul Energetic Craiova	21.5%	854	6.4%	0.064
CN Aeroporturi Bucuresti	20.0%	396	2.9%	0.030
GDF Suez	12.0%	317	2.4%	0.024
E.ON Gaz Distributie	12.0%	117	0.9%	0.009
E.ON Moldova Distributie	22.0%	267	2.0%	0.020
E.ON Energie	13.4%	68	0.5%	0.005
ENEL Electrica Dobrogea Distributie	24.1%	307	2.3%	0.023
Electrica Transilvania Sud Distributie	22.0%	197	1.5%	0.015
ENEL Electrica Banat Distributie	24.1%	349	2.6%	0.026
Electrica Muntenia Nord Distributie	22.0%	222	1.7%	0.017
Electrica Transilvania Nord Distributie	22.0%	189	1.4%	0.014
Enel Distributie Muntenia SA	12.0%	422	3.1%	0.031
Posta Romana	25.0%	203	1.5%	0.015
Total assets		14,008	100.0%	1.004
Debt (dividends payable)		-540	-4.0%	-0.040
Deferred taxes (RON m)		-14	-0.1%	(0.001)
Estimated NAV (RON m)		13,454	100.0%	1.003

Source: KBC Securities estimates, company data

Fondul Proprietatea: Valuation summary (RON m)	
Portfolio value	13,536.2
- Fair discount applied	-4,060.9
+ Cash	471.4
- Potential negative effect of dilution at Nuclearelectrica	-270.0
- Debt	-539.6
- Deferred taxes	-14.2
Implied fair value	9,123.0
Number of shares (m)	13,412.6
Implied fair value per share (RON)	0.68
Closing price as of 28 June (RON)	0.4450
Upside (%)	52.8%

Source: KBC Securities

*priced at COB 27 June 2012

Annex 1 – Official NAV calculation

Fondul Proprietatea: Official NAV calculation – May 2012

	RON m	% of NAV	RON per share
Official NAV (RONm)	15,678	100.0%	1.169
Split of NAV by type			
Listed shares	5,345	34.1%	0.398
Unlisted shares	9,742	62.1%	0.726
Cash, equivalents	471	3.0%	0.035
Receivables net of debt	119	0.8%	
Split of NAV by sector			
Cash, equivalents and receivables net of debt	591	3.8%	0.044
Electricity production	4,862	31.0%	0.362
Oil&Gas	5,489	35.0%	0.409
Electricity distribution and transport	3,228	20.6%	0.241
Banks	466	3.0%	0.035
Infrastructure	447	2.9%	0.033
Aluminium	166	1.1%	0.012
Heavy industry	277	1.8%	0.021
Postal services	96	0.6%	0.007
Others	56	0.4%	0.004
Top holdings			
OMV Petrom SA	3,965	25.3%	0.296
Hidroelectrica SA	3,289	21.0%	0.245
Romgaz SA	1,438	9.2%	0.107
Nuclearelectrica SA	497	3.2%	0.037
Complexul Energetic Oltenia SA	1,075	6.9%	0.080
Transgaz SA	342	2.2%	0.025
GDF Suez Energy Romania	340	2.2%	0.025
Enel Distributie Muntenia SA	343	2.2%	0.026
E.ON Moldova Distributie SA	400	2.6%	0.030
ENEL Distributie Banat SA	445	2.8%	0.033
Others	3,543	22.6%	0.264
Current trading price	6,124		0.445
Discount of current trading price vs NAV			-62.0%

Source: Fondul Proprietatea

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