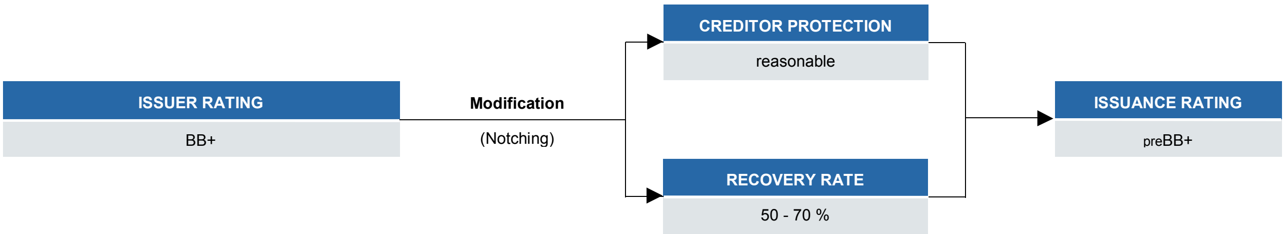
Preliminary Issuance Rating

TIGÁZ Földgázelosztó Zrt. Proposed senior unsecured bond issue (2019/2029)		03 September 2019	preBB+
		Issuance rating	
		Outlook	stable
Industry	Regulated Utility Companies	Issuance volume	HUF 34bn-50bn (target range)
		Coupon (% p.a.)	tba.



ISSUER RATING	BB+

- Low to moderate business risks due to established market regulation, distribution license and predictable operations
- Slightly increased financial risks due to rather weak credit metrics and limited financial flexibility
- No modification for operational risks or external influence

CREDITOR PROTECTION	reasonable

- Preliminary bond terms and conditions in preparation
- Reasonable, market standard terms expected, esp. with view to termination rights, covenants and negative clauses

BOND RANKING	senior unsecured

- Private placement process expected for Q4/2019
- Bond proceeds to fully replace existing senior lenders

RECOVERY	50 – 70 %

- Hypothetical default scenario based on going concern assumption
- Expected recovery rate: 50% - 70%

KEY DATA		
Listing	no	Proposed private placement (Q4/2019), secondary market listing may follow
Issuance volume	HUF 34bn – 50bn	Subject to market conditions (target range)
Fixed coupon	tba.	Subject to market conditions; based on 10y govt. bond yield + risk spread
Repayment	bullet	Full redemption / refinancing at maturity (Q4/2029)
Term to maturity	10 years	Expected maturity date in Q4/2029
Collateral	none	Senior unsecured bond

Rating rationale

Euler Hermes Rating assigns a preliminary BB+ issuance rating to TIGÁZ' proposed 2019/29 bond issue maturing in 2029 with a total expected issuance volume of between HUF 34bn and 50bn. The rating was derived from TIGÁZ' current issuer credit rating (BB+), the bond's proposed senior ranking, assumed reasonable creditor protections and adequate recovery expectations in a hypothetical bond default scenario.

Robust senior ranking within post issuance capital structure

TIGÁZ has announced that, subject to market conditions, it intends to issue HUF 34bn-50bn of unsecured fixed rate notes ("senior unsecured bonds") with a term of 10 years and governed by Hungarian law. Overall we expect the proposed bond issue to be subject of a robust senior ranking, as the net proceeds from the offering shall be used to fully replace the current providers of external senior (secured) debt financing (MKB Bank). This will bring the relative ranking of the future bond holders into the most senior position, as the proportion of higher ranking secured debt shall be zero post issuance while the second source of funding ranks subordinated (shareholder loan/facility).

Reasonable creditor protection assumed

TIGÁZ' asset base will be unpledged post issuance, representing a notable long-term borrowing base. For holders of unsecured debt it is important to mitigate the risk of becoming significantly disadvantaged in the event of additional (secured) debt issues, when permitted. For regulated utilities we generally expect lower risks, as structural protection rules often limit their ability to raise new debt by requiring a certain amount of unencumbered assets. To ensure equal rights of payment and equal seniority with potentially new debt issues, we also assume a standard set of reasonable creditor protection clauses to be included in the proposed bond terms, such as pari passu / negative pledge clauses and financial covenants.

50%-70% expected recovery rate based on hypothetical default scenario

Our recovery expectation on TIGÁZ' proposed bond issue follows a hypothetical default scenario based on a going concern assumption. At present, TIGÁZ' overall creditworthiness is driven by an already low probability of default mainly as a result of a perpetual territory-based gas distribution license, highly predictable operating cash flows and reliable market regulations, which is supportive in sustaining the typically high long-term debt levels of regulated utilities (cp. BB+ issuer rating). In a hypothetical default scenario, however, we assume a material deterioration of the issuer's overall creditworthiness as a cause of adverse market regulation leading up to depressed long-term profit prospects and stressed going concern values. We also assume that ranking and size of debt claims will usually change prior to default, and that the issuer would be forced to pledge its assets to raise new debt as its credit quality gradually deteriorates. As a consequence, loss given default usually rises disproportionately the higher the probability of default is. This is especially true for unsecured debt. Nevertheless, we still expect adequate recovery rates of between 50%-70% for the proposed unsecured senior bond of TIGÁZ', as regulated utilities have proven to maintain higher values in distressed situations due to its integral assets which provide essential, public services that cannot be easily replaced. Our assessments leads to the equalization of the bond issuance rating with the current issuer rating of TIGÁZ Földgázelosztó Zrt. (BB+).

Rating History

	03 September 2019
Issuer rating	BB+
Issuance rating	preBB+
Outlook	stable

Upgrade / Downgrade Factors

Factors that could lead to an Upgrade

- Upgrade of TIGÁZ' issuer credit rating
- Lasting improvement of the bond's expected recovery rate

Factors that could lead to a Downgrade

- Downgrade of TIGÁZ' issuer credit rating
- Lasting deterioration of the bond's expected recovery rate

Issuance

HUF 34bn – 50bn issue to refinance existing financial debt

TIGÁZ has announced that, subject to market conditions, it intends to issue HUF 34bn-50bn of unsecured fixed rate notes ("senior unsecured bonds") with a term of 10 years and governed by Hungarian law. The net proceeds from the proposed offering shall be used to refinance existing financial debt of the company. As of 30.06.2019 the company's capital structure contained secured long-term loans provided by MKB Bank (HUF 34bn) and subordinated loans provided by the shareholders (HUF 25bn). Depending on the final issuance volume, a fractional amount of between HUF 25bn and HUF 9bn of shareholder loans shall remain post issuance.

Private placement and market sounding process announced for Q3/Q4 2019

TIGÁZ aims to raise the funds via a private placement process involving the Central Bank of Hungary (MNB) and four additional institutional investors. Therefore, TIGÁZ applied for MNB's "Bond Funding for Growth Scheme" (BGS) and intends to initiate a bond roadshow and market sounding process during Q3/2019. At a later stage, a secondary market listing of the notes at the corporate bond market in Hungary remains an option. We expect further announcements to be made upon pricing of the offering. The coupon rate shall be based on the market conditions for the 10 year government bond yield of Hungary (02/09/19: 1.96% p.a.; 52 week range: 1.55% - 3.99%) plus a credit risk spread relative to the final issuance volume and the issuer rating of TIGÁZ.

Preliminary issuance rating assigned

During our assessment the actual bond terms and conditions were still in preparation. However, based on current proposals we made assumptions and assigned a preliminary issuance rating to the proposed issue at this stage. Assigning a final issuance rating depends on the provision of the terms and conditions for the proposed bond issue.

Appendix 1: Execution

Notice

This report represents a supplement to the issuer rating report from 14 August 2019. The issuance rating is derived from the current issuer rating. The full rationale for the issuer rating notation can be found in the issuer rating report.

Analysts

- Matthias Peetz, Senior Analyst / Project Lead
- István Braun, Senior Analyst

Rating committee

- Dörte Mählmann, Director
- Holger Ludewig, Director

Principal sources of information

- Preliminary information on the envisaged bond structure
- Use of the proceeds - Scenario analysis provided by the issuer
- Management interview

Rating methodology

- Euler Hermes Rating GmbH Issue Rating Methodology of December 2014 (formally amended on 14 November 2017) (https://www.ehrg.de/seiten/Methodology_Issue%20Rating_20171114.pdf)

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Appendix 2: Rating categories

Category	Explanation
AAA	In the opinion of EHR, AAA rated obligations demonstrate an excellent credit quality and the lowest default risk.
AA	In the opinion of EHR, AA rated obligations demonstrate a very high credit quality with a very low default risk.
A	In the opinion of EHR, A rated obligations demonstrate a high credit quality with a low default risk.
BBB	In the opinion of EHR, BBB rated obligations demonstrate a medium credit quality with a moderate default risk.
BB	In the opinion of EHR, BB rated obligations demonstrate a medium-low credit quality with a slightly increased default risk.
B	In the opinion of EHR, B rated obligations demonstrate a low credit quality with an increased default risk.
CCC	In the opinion of EHR, CCC rated obligations demonstrate a very low credit quality with a high default risk.
CC	In the opinion of EHR, CC rated obligations demonstrate a very low credit quality, an event of default is very likely.
C	In the opinion of EHR, C rated obligations demonstrate a very low credit quality, an event of default is imminent.
D	D rated obligations have defaulted, as defined by the rating agency.
PLUS (+) **MINUS (–)**	Rating categories from AA to CCC are modified by a PLUS (+) or MINUS (-), where required, in order to show their relative position within the rating category.

Disclaimer

Magyar Nemzeti Bank (client) engaged Euler Hermes Rating GmbH to conduct a rating of the envisaged bond issuance (rated obligation) of TIGÁZ Földgázelosztó Zrt. (issuer) on 18 June 2019. An interview with the issuer was conducted on 26 July 2019.

The Rating Committee of Euler Hermes Rating GmbH reviewed the rating process, issued the rating notation and approved the rating report in its current form on 03 September 2019. This rating report was given to the client on 03 September 2019, thereby concluding the rating process.

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The issuer is solely and exclusively liable for any errors and omissions in the documents and information openly and willingly provided to us in response to our requests for information. The issuer has reviewed the rating report and certified that all the information considered in the rating report is accurate and complete in all significant respects, no significant aspects have been concealed and any forward-looking statements are based on plausible, verifiable and current data and were prepared by the issuer exercising reasonable and commercial care. The issuer's representatives have issued a written certification of completeness to Euler Hermes Rating GmbH. However, the issuer cannot be held liable if actual results differ from the forward-looking statements presented in this document, particularly the projections. Forward-looking statements and projections may be adversely affected by unforeseeable events and changes in the economic environment. Euler Hermes Rating GmbH assumes no liability for the accuracy of the information it considers when issuing a rating and extends no guarantee whatsoever that the information is explicitly or implicitly correct, timely, complete, suitable for the market or fit for any particular purpose.

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Hamburg, 03 September 2019