Moody's Investors Service

Credit Opinion: Gaz de France

Gaz de France

Paris, France

Ratings

Category	Moody's Rating
Outlook	Rating(s) Under Review
Issuer Rating	*Aa1
Sr Unsec Bank Credit Facility -Dom Curr	*Aa1
Senior Unsecured	*Aa1
Subordinate MTN -Dom Curr	*Aa2
Commercial Paper	P-1
Other Short Term -Dom Curr	P-1

* Placed under review for possible downgrade on February 27, 2006

Contacts

Analyst	Phone
Andrew Madge/London	44.20.7772.5454
Raffaella Altamura/London	
Stuart Lawton/London	

Key Indicators

Gaz de France

	2006	2005	2004
EBIT Margin	**11.7%**	**11.5%**	**13.7%**
RCF / Net Adjusted Debt	**70.9%**	**73.1%**	**63.3%**
FFO Interest Coverage	**15.7x**	**11.6x**	**13.5x**
RCF / Capex + Acquisitions (net of divestitures)	**126%**	**139%**	**209.0%**
Gross Adjusted Debt / Book Capitalisation	**25.3%**	**24.0%**	**29.4%**
FFO / Gross Adjusted Debt	**53.2%**	**52.3%**	**59.2%**

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Company Profile

Gaz de France ("GdF/the Company", rated Aa1, under review for downgrade) is the majority state owned owner and operator of the French high pressure gas transmission network, and of the majority of France's gas distribution network. It also owns a number of domestic electricity, and up and downstream gas investments outside France, and is France's dominant residential and wholesale gas supplier. It has the largest LNG regasification capacity in Europe and is currently increasing its vertical integration by growing its own gas and oil reserves to a target of 1000 Mboe.

Following GdF's announcement that it intended to merge with French utility Suez S.A. in February 2006, GdF's Aa1 senior unsecured and issuer rating, and Aa2 subordinated note rating, were placed under review for downgrade. At the same time, Moody's affirmed the Company's Prime-1 short term rating. The original terms of the transaction were a 1 for 1 exchange ratio, and a EUR1 per share special dividend to Suez's shareholders. In October 2006, the French Parliament approved a bill allowing the French state to reduce its ownership of GdF below 70%, which provided the legal foundation for the proposed merger. Whilst it was originally expected that the merger would be finalized by the end of 2006/early 2007, two rulings by the French establishment in November and December 2006 respectively had the effect of moving completion well into 2007; and effectively made the

transaction dependent on a decision by the new President (Nicolas Sarkozy) and government.

However, on 3 September 2007, GdF and Suez announced that revised terms for the merger has been approved by the boards of directors of both groups. These revised terms will see (i) Gaz de France SA and Suez SA merge on the basis of an exchange of 21 GdF shares for 22 Suez shares - and the absorption of Suez by GdF - and (ii) the concurrent spin-off of 65% of Suez Environnement to existing Suez shareholders. This redistribution of Suez Environnement replaces the special dividend that would have been paid to Suez's shareholders under the original terms of the merger, and acknowledges the extent to which the share prices of the two groups have diverged since the merger was originally proposed. The spin-off of 65% of Suez Environnement will be undertaken via an Initial Public Offering (IPO), with the new GDF Suez and main Suez shareholders holding 35% and 12% respectively of Suez Environnement, post completion of the IPO, and undertaking to keep their shares in Suez Environnement within the framework of a shareholder pact. (The terms of the latter have yet to be negotiated).

Moody's understands that the revised terms of the merger will require the approval of European Union competition authorities (which approved the original merger terms) and the shareholders of both companies. It also notes the comments made by GdF and Suez that these revised terms have the support of their major shareholders and that they expect to complete the transaction as early as possible in 2008.

Rating Rationale

In accordance with Moody's rating methodology for Government Related Issuers (GRI's), the Aa1 rating of GdF reflects the combination of the following inputs:

- Baseline credit assessment of 4 (equivalent to Aa3 on a scale of 1 to 21, where 1 represents Aaa, 2 Aa1, etc.)

- Aaa local currency rating of the French government

- High support

- Medium dependence

ASSESSMENT OF STATE SUPPORT

High support reflects evidence of state intervention in various unrelated cases and the important role GdF plays, both socially and economically, in the French system. Under the updated Energy law, the State will be unable to lower its stake in GdF below c.34%. The controversy associated with the recent amendment to the Energy Law (allowing a reduction in this stake from the current 79.8%), and the role played by the French government in the proposed merger, underlines Moody's belief that any further reductions will be hard to achieve, even if desired by any future government. Should the merger proceed, Moody's is likely to keep its government support assumption unchanged. Whilst the transaction would see the government's stake in GdF decline to around 36%, the intensity and nature of the public debate that has taken place over recent months, and the role played by the French government in this process, illustrate the importance of the company to the State.

ASSESSMENT OF DEPENDENCE

Medium dependence reflects the fact that France will continue to originate a large part of the Company's earnings, although the merger with Suez would enhance its international diversification. In addition, GdF remains an important French company as regards employees and customers, and performs an important security of power supply function.

ASSESSMENT OF BASELINE CREDIT ASSESSMENT

Moody's ranks the relative risk of regulated revenues by assigning a value for the "Supportiveness of the Regulatory Environment" (SRE), as set out in its rating methodology for Regulated Utilities. In the gas sector, France is ranked as an SRE 2, along with Denmark, Spain and the Netherlands. An SRE2 principally reflects a fairly supportive remuneration system where GdF's network infrastructure activities are concerned, which contribute c.60% of its operating income and thus drive its overall credit profile. Conversely, the Company's ability to pass on rising wholesale gas prices by raising consumer tariffs has been impaired by the government, which last year announced a freeze on tariffs.

GdF has a dominant position as a fully integrated player in the domestic distribution and gas supply market, and is expected to retain this over the medium term, largely due to the comparatively slower pace of market liberalization and relatively benign and flexible regulation. In 2006, 63% of Group EBITDA stemmed from its "Infrastructures" segment, the assets of which are predominantly regulated. At the same time, Moody's factors into GdF's ratings its ongoing diversification outside France, as well as its upstream activities, and a gradual erosion of its domestic supply market share.

In Moody's view, these developments will gradually increase GdF's business risk. Going forward, Moody's

anticipates that GdF will continue to have meaningful investment needs and may expand through debt financed acquisitions. However, Moody's believes that GdF will remain a robust, stable and highly cash generative gas utility, with a dominant position in France over the medium term.

In terms of the business risk associated with a GdF/Suez combination, Moody's believes that this would increase, compared to that of GdF, given the greater contribution from competitive businesses such as power generation. Although the regulated Infrastructure segment currently contributes more than 60% of GdF's EBITDA, that share would fall to around 25 - 30% for the enlarged group. Whilst Moody's recognises that the combined group would be one of Europe's largest integrated power companies, with strong positions in pipeline and liquid gas as well as power generation, the nature of many of its businesses would be more commensurate with a medium to low business risk profile, albeit still supported by a large transmission and distribution business. Accordingly, the new entity would be very much comparable with similar fully integrated and large scale companies such as E.ON and Enel.

GdF's financial profile is characterised by strong debt coverage. The Company exhibited strong cash flow metrics in 2006, with retained cash flow (RCF) / Net Adjusted Debt of 70.9% and funds from operations (FFO) interest coverage of 15.7x, which is comparable with similarly rated peers such as Gasunie. These ratios reflect the substantial cash flow produced by the company's Infrastructure business, and its relatively low debt burden.

Liquidity

The cornerstone of GdF's liquidity position is the significant cash and marketable securities it holds, and the committed bank facilities it has in place. As at 30 June 2007, GdF reported approximately EUR3.7 billion of cash and marketable securities, and EUR3 billion of undrawn MAC and covenant-free, committed syndicated bank lines, which mature in 2012.

GdF's main uses of cash include capital expenditure, debt service costs, working capital, acquisitions, dividends and tax payments. The group's planned investment spend for 2005 - 2008 was EUR17.5 billion, of which it had invested EUR6.9 billion at the end of 2006, based on projects completed in 2005 and 2006. When announcing the group's 2006 results in March 2007, management also announced, for the first time, their commitment to a dividend payout based policy of at least 50% of earnings, going forward. Not only will this improve visibility in terms of shareholder returns, but it will also bring GdF more in line with its utility peers. They also stated that the EUR17.5 billion investment plan for 2005 - 2008, announced at the time of the IPO, now looks overly ambitious, and that the actual investment spend could well be EUR4.6 billion lower than that planned. Consequently, there is a possibility that some of this financial flexibility will be used to make returns to shareholders, and the company has said that a decision on a special dividend will be taken in 2008.

Of total group gross debt of EUR5 billion as at 30 June 2007, approximately EUR1.1 billion is due to mature by the end of June 2008.

GdF has a EUR1.25 billion French Billet de Tresorerie programme in place, of which approximately EUR0.25 billion was outstanding as at 30 June 2007, and a USD1 billion US commercial paper programme, which is currently undrawn. The group accesses the CP market on a regular basis and targets to cover a high proportion of its short term debt, including CP outstanding at any one time, with its un-drawn committed bank lines and cash. CP usage is expected to remain low during the next 12 months.

Recent Developments

GdF announced its H107 results on 29 August. Revenues showed a decline of 11% on the prior year period at EUR13.8 billion (H106 - EUR15.4 billion), and EBITDA declined by 4.9% to EUR3.1 bn (H106 - EUR3.3 billion). Operating income was down 8.7% at EUR2.3 billion (H106 - EUR2.5 billion). These results reflected the negative impact of a very difficult environment in H107, characterized by exceptionally mild climate conditions and unfavourable market conditions, which in turn, were reflected in the low gas prices on the markets. GdF has, however, announced that it is maintaining its financial target for 2007, with full year EBITDA expected to be in line with that for 2006. This assumes average climate conditions during H207.

Rating Outlook

The ratings remain on review for downgrade, reflecting the pending merger with Suez.

What Could Change the Rating - Down

If the merger with Suez proceeds, it is likely that GdF's ratings will be downgraded. The extent of any downgrade will depend on (1) the final terms of the merger, (2) the capital structure to be adopted by the new group, and (3) the final strategy and financial policy of the combined group, and potential structural subordination within it. At this stage, there is insufficient clarity/visibility for Moody's to fully assess the potential impact of the required disposals on the business risk assessment of the combined entity. However, it would seem unlikely to be material, given the likelihood that Suez and GdF will look to exchange, rather than sell, the assets they will need to dispose of, and thereby limit the negative impact on the enlarged group's business risk profile.

What Could Change the Rating - Up

Given the commitment of both GdF and Suez to the merger, Moody's does not see any pressure for an upgrade in the short term. If the merger with Suez fails to complete, GdF's current ratings will likely be affirmed at the current level.

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