PGE Polska Grupa Energetyczna S.A.

Update

Ratings

Foreign Currency

Long-Term IDR	BBB+
Senior unsecured	BBB+

Local Currency

Long-Term IDR	BBB+
Senior unsecured	BBB+

Outlooks

Long-Term Foreign-Currency IDR	Stable
Long-Term Local-Currency IDR	Stable

Financial Data

PGE Polska Grupa Energetyczna S.A.

	31 Dec 2010	31 Dec 2009
Revenue (PLNm)	20,477	21,623
EBITDA (PLNm)	6,830	7,841
EBITDA excluding Power Purchase Agreements compensation (PLNm)	6,496	6,309
Funds from operations (PLNm)	6,063	8,386
Capital expenditure (PLNm)	-4,522	-4,022
Free cash flow (PLNm)	483	2,097
Total debt/operating EBITDA (x)	0.4	0.6
Total debt less unrestricted cash/operating EBITDA (x)	0.0	-0.3

Related Research

2012 Outlook: European Utilities (December 2011)

EMEA Utilities Sector Credit Factors Compendium (September 2011)

Rating EMEA Utilities - Sector Credit Factors (May 2010)

Fitch Downgrades 8 European Utilities' Senior Unsecured Ratings on Criteria Tightening; Affirms IDRs (August 2011)

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Key Rating Drivers

Strong Position Supports Ratings: PGE Polska Grupa Energetyczna S.A.'s (PGE S.A.) ratings reflect PGE group's (PGE, PGE S.A. and subsidiaries) vertically integrated operations in the Polish electricity market, its dominance in power generation (40% of the country's generation in 2010) and its strong position in electricity distribution and supply (26% share).

Capex to Increase Leverage: PGE has a moderate financial policy, solid liquidity and financial leverage close to 0x at end-September 2011. However, the ratings incorporate Fitch Ratings' projection of an increase in net debt/EBITDA in 2013-2015 due to a sizeable and partly debt-funded capex programme. PGE's financial policy assumes that net debt/EBITDA will not increase above 2.5x in the medium-term. This leverage is in line with the current ratings.

Energa Acquisition Uncertain: PGE's acquisition of Energa S.A., Poland's third-largest electricity distributor, will depend on the court verdict following the company's appeal against the anti-monopoly authority's decision prohibiting the transaction. Fitch believes the Energa acquisition, if eventually approved, would be credit neutral for PGE in the short to medium term.

Polkomtel Disposal: In November 2011, PGE received PLN3.3bn from the disposal of its 21.85% stake in Polish mobile operator Polkomtel S.A. This transaction is part of a wider plan to monetise non-core assets and provides additional financial headroom for PGE ahead of the capex-intensive period.

Improved Group Structure: Since 2009, PGE S.A.'s position within the group has improved in terms of cash flow and debt management, thanks to a consolidation programme and increased stakes in key operating subsidiaries. Fitch expects that new debt will be raised by PGE S.A.

CO_2 Exposure: The group's electricity generation mix is based on lignite-fired power plants, which allow strong EBITDA margins but also expose PGE to increasing carbon dioxide costs, especially after 2012 with the implementation of the EU auctioning system for CO_2 allowances.

Nuclear Investment: PGE faces substantial nuclear investment over 2015-2020; the company plans to construct the first nuclear plant in Poland together with foreign partners. Fitch will analyse the credit impact of the project once more details (including funding) become available. Currently, the project is beyond the five-year rating horizon.

Rated on Standalone Basis: PGE is 69%-owned by the Polish state ('A−'/Stable), but Fitch rates it on a standalone basis, with no state support factored in.

Rating for Unsecured Debt: The senior unsecured rating of PGE was downgraded from 'A−' to 'BBB+' and was equalised with its Long-Term IDR in August 2011 due to criteria tightening related to above-average recovery expectations upon default. For the one-notch uplift from the Long-Term IDR to be maintained, the agency expects the proportion of regulated cash flow to be dominant (at least 50% of total EBITDA), which is not the case for PGE.

What Could Trigger a Rating Action

Positive Drivers: The ratings could be positively affected by the successful implementation of long-term capex, resulting in a stronger business profile.

Negative Drivers: Financial leverage beyond the company's maximum target of 2.5x due, for example, to additional large debt-funded acquisitions or capex being substantially above the current plan, would be negative for the ratings.

Peer Group

Issuer	Country
A−	
CEZ, a.s.	Czech Republic
BBB+	
PGE Polska Grupa Energetyczna S.A.	Poland
BBB	
ENEA S.A.	Poland
Slovenske elektrarne, a.s.	Slovakia
TAURON Polska Energia S.A.	Poland

Issuer Rating History

Date	LT IDR (FC)	Outlook/ Watch
12 Aug 11	BBB+	Stable
4 Aug 11	BBB+	Stable
9 Aug 10	BBB+	Stable
2 Sep 09	BBB+	Stable

Snapshot Profile: Major Issuer-Specific Rating Factors and Trends

Rating Factor	Status[a]	Trend
Operations	Average	Neutral
Market Position	Strong	Neutral
Finances	Strong	Worsening
Governance	Average	Neutral
Geography	Average	Neutral

[a] Relative to Peer Group

Related Criteria

Corporate Rating Methodology (August 2011)

Recovery Ratings and Notching Criteria for Utilities (August 2011)

Parent and Subsidiary Rating Linkage (August 2011)

Immediate Peer Group – Comparative Analysis

Sector Characteristics

Operating Risks

Vertically integrated European electric utilities are relatively stable businesses. Electricity distribution and transmission in transparent regulatory regimes benefit from high cash flow visibility and predictability. Power generation is a higher-risk and more volatile segment, due to its exposure to changes in fuel and electricity prices, and electricity demand. However, some business and financial risks in generation may be mitigated through hedging strategies.

Financial Risks

The financial profile of integrated utilities benefits from solid and stable cash flow generation. Negative free cash flow will remain common across the sector, due to large capex plans with limited short-term flexibility. Leading integrated utilities generally have good access to capital-market funding.

Business Profiles of Fitch-Rated CE Energy Utilities

	CEZ A−/Stable	PGE BBB+/Stable	Tauron BBB/Stable	SE BBB/Stable	ENEA BBB/Stable
Headroom within current rating level	Limited	Large	Medium	Medium	Large
Vertical integration	Full (from mining to supply)	Full (from mining to supply)	Full (from mining to supply)	Low	Medium (from generation to supply)
Generation mix (%)	42 nuclear, 45 lignite, 10 hard coal	67 lignite, 26 hard coal	93 hard coal	43 hydro, 32 nuclear, 25 coal	98 hard coal
Regulated business (EBITDA share) (%)	19	21	41	0	42

Source: Fitch

Key Credit Characteristics

Large utilities with solid business profiles and strong-to-medium financial profiles generally command strong investment-grade ratings. Ratings depend on business factors – including market presence, degree of vertical integration, generation mix and earnings diversification – and on financial factors, such as financial policy, leverage, profit margins, capex plans and approach to M&A activity.

Overview of Companies

CEZ, a.s. ('A−'/Stable) – 69.4%-owned by the Czech state, CEZ has a leading position and vertical integration in Czech power, and is the largest electric utility in central Europe. CEZ has a strong EBITDA margin, which is partly driven by its low-cost generation portfolio.

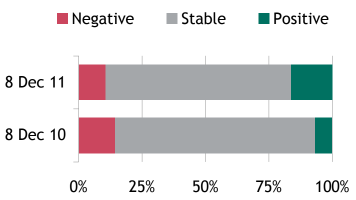
Slovenske elektrarne, a.s. (SE, 'BBB'/Stable) – the dominant power producer in Slovakia, SE is 66%-owned by Italy's Enel S.p.A. ('A−'/Stable). The company benefits from a good mix of generating sources, including nuclear (currently being expanded), hydro, gas and coal, but is less integrated than many of its peers.

TAURON Polska Energia S.A. ('BBB'/Stable) – 42%-owned by the Polish state, Tauron is the second-largest vertically integrated utility in Poland. The recent GZE acquisition improves Tauron's business profile by strengthening the company's leading position in distribution but reduces headroom within the current rating level. The company has limited generation fuel mix diversification (hard-coal-fired plants account for 93% of installed capacity).

ENEA S.A. ('BBB'/Stable) – 52.9%-owned by the Polish state and the third-largest player in the Polish electricity market. ENEA has vertically integrated operations, including a leading position in electricity distribution and supply, and a significant position in power generation.

PGE Polska Grupa Energetyczna S.A. —— Utilities Median —— Emerging BBB Cat Median ——
Source: Company data; Fitch.

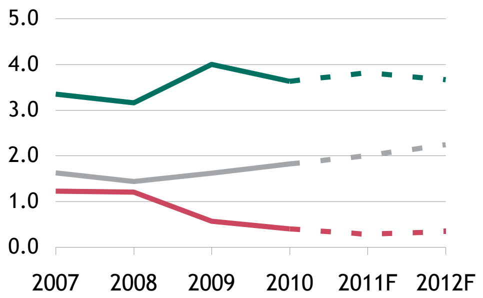
Distribution of Sector Outlooks
Directional Outlooks and Rating Watches



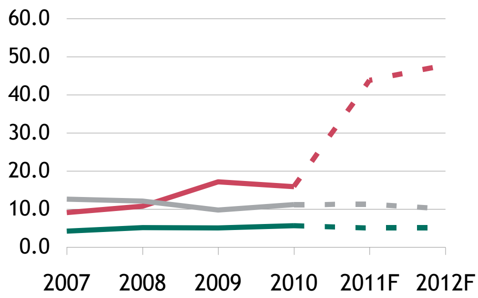
Fitch's expectations are based on the agency's internally produced, conservative rating case forecasts. They do not represent the forecasts of rated issuers individually or in aggregate. Key Fitch forecast assumptions include:

- improved FFO and EBITDA from Q311 thanks to the commissioning of a new 858MW unit in Bełchatów;
- an increase in annual capex in 2012 compared with 2011;
- the Energa acquisition is not included in the projections given the pending court case.

Leverage
including Fitch expectations



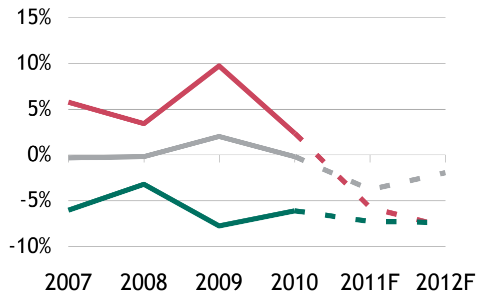
Interest Cover
including Fitch expectations



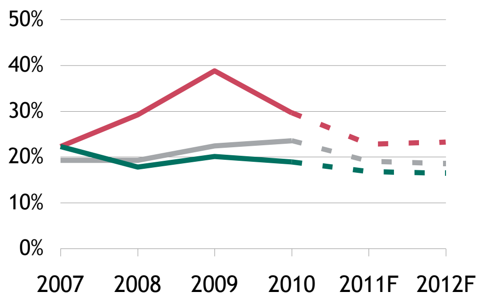
Debt Maturities and Liquidity at end-Sep 2011

Debt maturities	(PLNm)
Up to 12 months	883
Long term	1,489
Unrestricted cash and equivalents	2,185
Undrawn committed long-term facilities	2,300

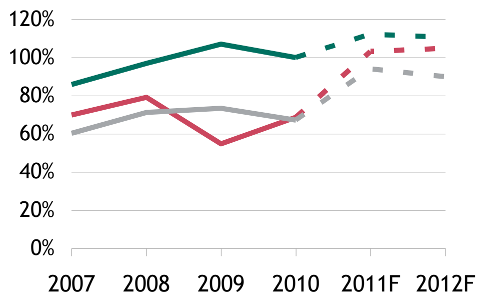
FCF/Revenues
including Fitch expectations



FFO Profitability
including Fitch expectations



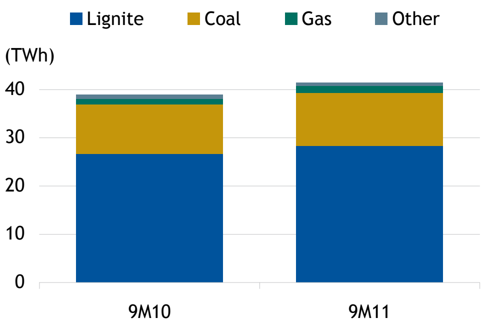
Capex/CFO
including Fitch expectations



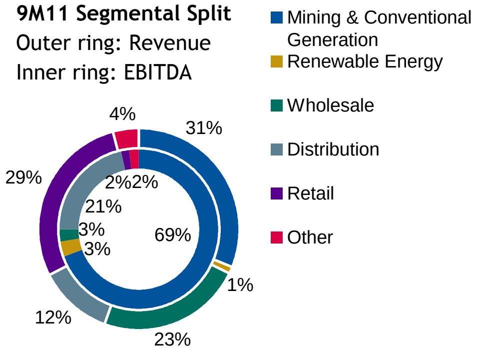
Definitions

- Leverage: Gross debt plus lease adjustment minus equity credit for hybrid instruments plus preferred stock divided by FFO plus gross interest paid plus preferred dividends plus rental expense.
- Interest cover: FFO plus gross interest paid plus preferred dividends divided by gross interest paid plus preferred dividends.
- FCF/revenue: FCF after dividends divided by revenue.
- FFO profitability: FFO divided by revenue.
- For further discussion of the interpretation of the tables and graphs in this report, see Fitch's "*Interpreting the New EMEA and Asia-Pacific Credit Update Format*", dated 25 November 2009 and available at www.fitchratings.com.

PGE Generation by Fuel



9M11 Segmental Split
Outer ring: Revenue
Inner ring: EBITDA



PGE Polska Grupa Energetyczna S.A.
FINANCIAL SUMMARY

	31 Dec 2010 PLNm Original	31 Dec 2009 PLNm Original	31 Dec 2008 PLNm Original	31 Dec 2007 PLNm Original	31 Dec 2006 PLNm Original
Profitability					
Revenue	20,477	21,623	19,409	23,091	24,344
Revenue Growth (%)	(5.30)	11.41	(15.95)	(5.15)	43.20
Operating EBIT	4,182	5,203	2,718	1,975	2,196
Operating EBITDA	6,830	7,841	5,302	4,583	4,786
Operating EBITDA Margin (%)	33.40	36.26	27.32	19.85	19.66
FFO Return on Adjusted Capital (%)	16.00	20.29	16.57	15.82	12.73
Free Cash Flow Margin (%)	2.40	9.70	3.41	5.77	3.80
Coverages (x)					
FFO Gross Interest Coverage	38.50	24.90	15.43	7.75	9.56
Operating EBITDA/Gross Interest Expense	16.80	15.13	9.11	7.21	7.28
FFO Fixed Charge Coverage (inc. Rents)	38.40	24.86	15.39	7.74	9.56
FCF Debt-Service Coverage	0.60	1.85	0.31	1.00	0.68
Cash Flow from Operations/Capital Expenditures	1.50	1.83	1.26	1.43	1.39
Debt Leverage of Cash Flow (x)					
Total Debt with Equity Credit/Operating EBITDA	0.40	0.64	1.42	1.54	1.78
Total Debt Less Unrestricted Cash/Operating EBITDA	0.00	(0.33)	1.03	0.96	1.10
Debt Leverage Including Rentals (x)					
Rental Expense	1	1	1	1	0
Gross Lease Adjusted Debt/Operating EBITDAR	0.40	0.64	1.42	1.54	1.78
Gross Lease Adjusted Debt/FFO+Int+Rentals	0.40	0.58	1.24	1.20	1.57
FCF/Lease Adjusted Debt (%)	17.60	41.67	8.80	18.82	10.85
Debt Leverage Including Leases and Pension Adjustment (x)					
Pension and Lease Adjusted Debt /EBITDAR + Pension Cost	0.40	0.65	1.44	1.55	1.79
Liquidity					
(Free Cash Flow+Available Cash+Committed Facils)/(ST Debt + Interest) (%)	1,053.80	749.64	91.54	191.44	190.46
Balance Sheet Summary					
Cash and Equivalents (Unrestricted)	2,630	7,607	2,071	2,675	3,271
Restricted Cash and Equivalents	101	106	70	51	40
Short-Term Debt	919	971	3,039	1,331	1,636
Long-Term Senior Debt	1,811	4,057	4,472	5,743	6,878
Subordinated Debt	0	0	0	0	0
Equity Credit	0	0	0	0	0
Total Debt with Equity Credit	2,730	5,028	7,512	7,074	8,514
Off-Balance-Sheet Debt	5	4	9	5	0
Lease-Adjusted Debt	2,735	5,032	7,520	7,079	8,514
Fitch- identified Pension Deficit	111	185	317	205	208
Pension Adjusted Debt	2,846	5,217	7,837	7,284	8,721
Cash Flow Summary					
Operating EBITDA	6,830	7,841	5,302	4,583	4,786
Gross Cash Interest Expense	(162)	(351)	(393)	(762)	(566)
Cash Tax	(852)	(491)	(574)	(592)	(358)
Associate Dividends	135	385	171	237	388
Other Items before FFO (incl. interest receivable)	112	1,002	1,158	1,674	597
Funds from Operations	**6,063**	**8,386**	**5,664**	**5,140**	**4,847**
Change in Working Capital	522	(1,040)	(454)	58	(121)
Cash Flow from Operations	**6,585**	**7,346**	**5,210**	**5,197**	**4,726**
Total Non-Operating/Non-Recurring Cash Flow	0	0	0	0	0
Capital Expenditures	(4,522)	(4,022)	(4,124)	(3,635)	(3,406)
Dividends Paid	(1,580)	(1,227)	(424)	(230)	(396)
Free Cash Flow	**483**	**2,097**	**662**	**1,332**	**924**
Net (Acquisitions)/Divestitures	(3,109)	(265)	(1,933)	0	0
Net Equity Proceeds/(Buyback)	(1)	5,918	0	0	0
Other Cash Flow Items	(52)	270	230	(488)	(5,567)
Total Change in Net Debt	(2,679)	8,020	(1,041)	844	(4,643)
Working Capital					
Accounts Receivable Days	37.00	34.76	33.71	36.91	36.04
Inventory Days	37.70	41.84	35.47	17.75	14.94
Accounts Payable Days	33.10	35.64	31.82	34.52	32.70

The ratings above were solicited by, or on behalf of, the issuer, and therefore,
Fitch has been compensated for the provision of the ratings.