





Over the past financial period, ending June 2014, Madrileña Red de Gas has consolidated its position as Spain’s leading independent natural gas distributor. Throughout our four years of operations we have dramatically increased our presence in the Madrid region, and recently have advanced further by obtaining licenses to extend our network to two new municipalities and create 20,000 new connection points. We are ready to face fresh and important challenges going forward, such as developing natural gas for automobiles and continuing to improve our service to consumers.

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Key figures

<h3>Consumers</h3> <p>MRG's main goal is to provide outstanding service to its over 800,000 consumers.</p>	<h3>Expansion</h3> <p>Madrileña Red de Gas has expanded its business from the original 38 to the current 59 municipalities in the Madrid region</p>	<h3>Network</h3> <p>Madrileña Red de Gas continues to pursue a policy of network growth, and built more than 233 km of new pipelines in the past financial period.</p>	<h3>Metering and pressure regulating stations</h3> <p>This year we set in motion an insourcing plan for monitoring and controlling our metering and pressure regulating stations, which has led to enhanced quality and reliability.</p>	<h3>Employees</h3> <p>MRG employs 166 people in-house and outsources auxiliary activities to over 300 contractors</p>	<h3>Revenue</h3> <p>Total revenue in 2014 came to €180.8 million, €4.7 million more than in 2013. 85% of this figure was accounted for by regulated remuneration for the distribution business, while the remaining 15% related to other services linked to natural gas distribution.</p>	<h3>EBIT</h3> <p>EBIT rose 3.3% year-on-year on the back of increased EBITDA.</p>	<h3>Cash flow</h3> <p>In 2014 operating cash flow totaled €97.6 million, 17% down year-on-year.</p>																																																
<p>Consumers (thousands)</p> <table><tr><td>2014</td><td>839</td></tr><tr><td>2013</td><td>835</td></tr><tr><td>2012</td><td>829</td></tr></table>	2014	839	2013	835	2012	829	<p>Municipalities</p> <table><tr><td>2014</td><td>59</td></tr><tr><td>2013</td><td>57</td></tr><tr><td>2012</td><td>49</td></tr></table>	2014	59	2013	57	2012	49	<p>Network length (Km)</p> <table><tr><td>2014</td><td>5.533</td></tr><tr><td>2013</td><td>5.300</td></tr><tr><td>2012</td><td>5.283</td></tr></table>	2014	5.533	2013	5.300	2012	5.283	<p>Metering and pressure regulating stations</p> <table><tr><td>2014</td><td>184</td></tr><tr><td>2013</td><td>181</td></tr><tr><td>2012</td><td>177</td></tr></table>	2014	184	2013	181	2012	177	<p>Employees</p> <table><tr><td>2014</td><td>166</td></tr><tr><td>2013</td><td>163</td></tr><tr><td>2012</td><td>167</td></tr></table>	2014	166	2013	163	2012	167	<p>Revenue (€M)</p> <table><tr><td>2014</td><td>180.8</td></tr><tr><td>2013</td><td>177.3</td></tr><tr><td>2012</td><td>175.9</td></tr></table>	2014	180.8	2013	177.3	2012	175.9	<p>EBIT (€M)</p> <table><tr><td>2014</td><td>114.7</td></tr><tr><td>2013</td><td>111</td></tr><tr><td>2012</td><td>100.3</td></tr></table>	2014	114.7	2013	111	2012	100.3	<p>Cash flow (€M)</p> <table><tr><td>2014</td><td>97.6</td></tr><tr><td>2013</td><td>118.2</td></tr><tr><td>2012</td><td>117.7</td></tr></table>	2014	97.6	2013	118.2	2012	117.7
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<p>839,144 consumers</p>	<p>59 municipalities</p>	<p>5,533 Km</p>	<p>184 metering and pressure regulating stations</p>	<p>166 employees</p>	<p>180.8 €M</p>	<p>114.7 €M</p>	<p>97.6 €M</p>																																																

Letter from the Chairman



Four years after Madrileña Red de Gas opened for business, we can say that we have achieved most of the goals we set ourselves when we created our new independent gas distribution company. Our goals revolve around the themes of gas as a clean, versatile energy source, a commitment to outstanding service quality to consumers, and forging ties with our host community through network expansion and ongoing in-house improvement.

As an independent gas distribution company, we must comply with our duties under the law and, furthermore, honor our commitment to serve our consumers to the promised standard. We are also accountable to our shareholders, and must meet their legitimate expectations of the company's performance.

We are aware that the role of gas in the energy mix is vital to the transition to a model that carries decreased geostrategic

risk and makes the right fit with environmental policy. Madrileña Red de Gas believes that distribution companies have a crucial part to play in extending their networks to make natural gas accessible to a wider section of the population, thus supporting this transition and helping to replace fossil fuels, which are less versatile and more pollutant. The use of gas instead of other fuels brings major savings for consumers and the domestic economy alike by bringing down the end-cost of energy usage.

Our commitment takes into consideration all these concerns and is enacted in our home territory, the Madrid region, to which we are still closely tied. In our ongoing efforts to extend our business to further municipalities, we work side-by-side with the Madrid regional government in schemes to replace energy facilities and fuels. Having opened for business in 38 municipalities originally, we now operate in 59 municipalities, and intend to extend our network still further.

Our overarching commitment is to our consumers. Madrileña's main goals are service safety and quality. This means we focus on how rapidly we can respond to emergency calls and queries, and on shortening our response times to connection requests and troubleshooting incidents. Our performance indicators have consistently improved year on year, and our aim is to maintain this trend. The feedback from our consumers suggests we are on the right track, and encourages us to continue in our efforts.

We continue to implement ongoing improvements in productivity and organizational efficiency by scrutinizing and optimizing our processes. This is not merely a conceptual or design-driven task: we keep a constant watch on both the broad issues and what might seem to be minor details, which, taken together, amount to genuine steps forward, and feed into our safety, quality and financial efficiency indicators. A good example of this is the way in which we have restructured our financing in the wake of taking over several companies: which enabled us to streamline financial expenses and achieve a very robust credit rating.

As the leading independent distribution company we can focus tightly on the pursuit of excellence. This leads to improved performance: This year, once again, we have not only met but exceeded expectations and annual budget.

Since we are the leading independent distribution company and are not vertically integrated with any other business, we can afford to focus very tightly on attaining excellence in the single thing we do. This sharp focus and the strategies outlined above have led to real progress in our performance, as shown in the following pages. This year, once more, we have not only met but exceeded expectations and the annual budget.

Our business is subject to government regulation. The central government recently introduced statutory reforms – which are already in effect – to ensure that the incipient shortfall faced by the gas system as a result of the revenue/cost mismatch is adequately contained and does not lead to serious trouble over the medium term. We trust that the reforms will maintain the conditions that have so far enabled regulated businesses, including our own, to develop in a business-friendly climate that attracts investment, constrained only by the general law and underlying regulatory principles. We are also confident that the recovery of the Spanish economy, which appears to be corroborated by an increasingly wide range of indicators, will help to drive our growth, supported by the expected upswing in demand for natural gas across all consumer segments.

Once more, it falls to me to acknowledge that this strong performance is owed to the dedication, professional competence and unflagging motivation of our people – they are the bedrock of every improvement plan, and they merit my

sincere recognition and thanks. We are counting on them to continue upon the path of ongoing growth that we are determined to follow.

To summarize our strategic vision for the future, we believe that gas is a competitive energy source which will play an ever-increasing role going forward. The business shows high growth potential in view of the low penetration in Spain compared to our neighboring countries., and we are committed to realize this potential while delivering safety and service quality to our consumers. Finally, against a background of regulatory stability over the medium and long term, we trust that our business will develop and grow to the full satisfaction of our consumers, and shareholders and institutions.

A handwritten signature in blue ink, reading 'Pedro Mielgo'.

Pedro Mielgo
Chairman



The company

In 2014 Madrileña Red de Gas focused on making natural gas accessible to the largest possible number of Madrid residents

In 2014, MRG focused on three key areas of concern: increasing the number of municipalities in the Madrid region having a gas supply, raising awareness of the benefits of natural gas as compared to more pollutant energy sources and targeting key sectors such as mobility, and devising specific solutions for energy policy.

Milestones

MRG's first bond issue on the capital market

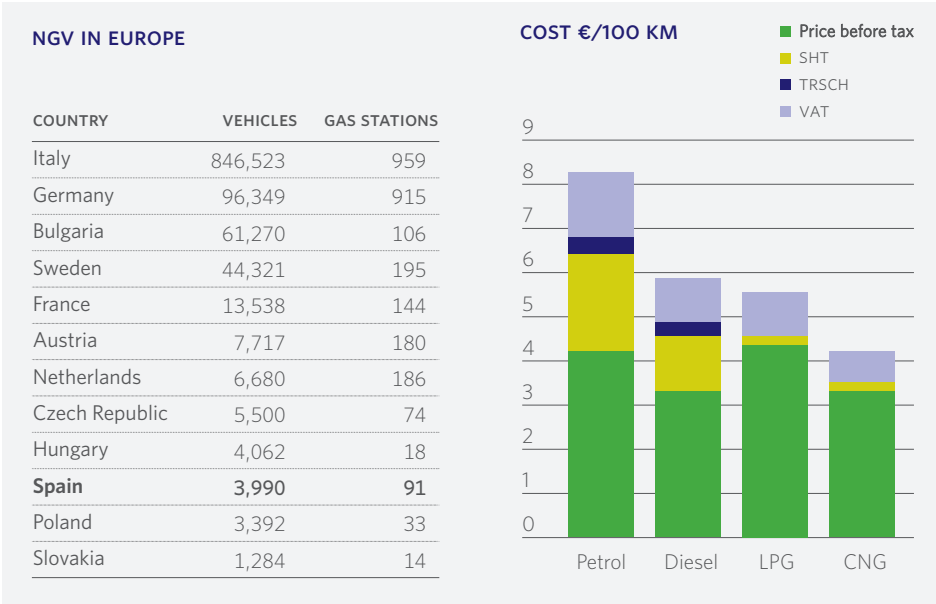
September 2013

In September 2013, and within the framework of the refinancing of its financial debt, MRG debuted in capital markets with a €500 million bond issuance maturing in September 2018. In December 2013, the company launched a second issuance for €275 of ten-year bonds. The funds obtained from the bond issuances, both rated investment grade by Standard & Poor's and Fitch, were used to prepay the outstanding bank debt facilities of MRG. These transactions have allowed a reduction of financial costs and an extension of the average tenor of the company financial debt.

Second Convention on Natural Gas for Mobility

October 2013

For the past two years MRG has had a representative on the board of the Spanish Association of Natural Gas for Mobility (GASNAM). Transportation is the most fossil fuel-intensive sector of the economy, and hence the largest producer of emissions. Compared to the steps taken in the industrial and domestic sectors, almost nothing has been done in this domain. So in the coming years the transportation sector must face this reality head-on to decrease energy



Source: NGVA-2013 / EDP NATURGAS ENERGÍA

intensity, particularly in major cities such as Madrid. The difficulties are wide-ranging – a lack of natural gas-powered vehicles, reluctance from oil companies , a slow rate of licensing for natural gas service stations, lack of awareness, political apathy, and an absence of incentives, particularly when compared to alternative energy sources. Yet again, Spain is behind its European peers in terms of adoption of natural gas for transportation purposes (see *table*), and is burdened by high natural gas pricing (see *chart*). The reality is the market is not working and energy policymakers need to come up with fresh answers.

Madrileña has set in motion a new initiative: building six natural gas service

stations in the Madrid region. We have replaced a large proportion of the natural gas vehicle fleet and will continue to drive development in this area, which we believe is vital to bringing down atmospheric emissions and the energy bill.

Corporate restructuring

December 2013

During the fiscal year ending on June 30, 2014, the company completed its corporate reorganization that started during the acquisition processes of both MRG and MRG II. As the final step, on December 17, 2013 the merger of Madrileña Red de Gas, S.A.U. (merging

company) and Madrileña Red de Gas II, S.A.U. (merged company) was registered in the Madrid Mercantile Registry.

The merger was concluded with minimal impact on end consumers and supply companies – after a three-month long systems project, and a review of contracts and purchase orders with our suppliers.

The merger allowed for administrative synergies in the operational areas of the company, and specifically for shorter timeframes for work completion certification, billing and regulatory reporting.

New website

February 2014

In our bid to reach out more effectively to end users, we launched the new Madrileña Red de Gas website, tailored to consumer needs. The new, fresh design makes it easier for users to find the information they want. They can access the online office to view meter readings, usage statistics, and the state of progress of queries and complaints, all in real time. We have also updated our written content to explain our processes clearly and concisely.

We cross-publicized the launch of our new website through all our existing channels (call center, inspection notices



and meter reading reports) and monthly traffic has gone up by 33%.

The website now also includes an investor relations section providing relevant financial data.

Fourth anniversary of Madrileña Red de Gas

February 2014

2014 is MRG's fourth year of operation. It is time to mark the emergence of a new distribution company, and celebrate its

having grown to become the country's third-largest distributor overall, and the leading independent distributor. Over this period, we have grown our business from 38 municipalities to 59. We have increased our distribution network by 233 km and installed 4,000 new connection points. In addition, we supply two natural gas service stations.

The figures show we are delivering on our commitment to the Madrid region, and we shall continue our growth policy by making natural gas available throughout the territory in support of enhanced industrial competitiveness

and replacing costlier and more pollutant energy sources, such as liquefied petroleum gas, diesel and electricity.

Our successes over the past four years have been aided by our installation partners and their business association, Asefosam. We have also been supported by our partners and suppliers, and the Madrid region's Department of Industry and Mining, which has provided ongoing guidance and monitoring. The Madrileña team is grateful for all this support, and is firmly committed to achieving its targets in the near future.

Gas balance and allocation
March 2014

The Resolution of February 7 2013 of the Directorate General of Energy Policy and Mining, amending the technical management standards NGTS-06 Allocation and NGTS-07 Balance, and Protocol PD-02 Allocation Procedure at Transportation-Distribution Connection Points, prompted us to review all our procedures for gas balance and allocation in new municipalities and bring them in-house. This step required us to train our people and implement new software applications.

Since the changes were introduced, MRG has achieved 99% compliance



with the daily protocol. We are now ready to adopt these procedures across the entire network by January 1, 2015, the date of the split between the Gas Natural Fenosa and Madrileña Red de Gas networks.

Article 14 of Order IET/2446/2013 establishing tolls and fees for third-party access to gas facilities and the remuneration of regulated activities provides that the distributor must calculate metering differences at transportation/distribution and distribution/distribution connection points. The introduction of this statutory instrument has required MRG to change the way it calculates definitive allocations and measurement differences throughout its entire distribution zone from the former area-based method to the transportation/distribution connection point approach. This development

has prompted a review to ensure that all our network connection points are correctly located, and the updating of our IT applications.

Agreement with the Parque Azul residential development in Colmenarejo
March 2014

Our signed agreement with the Parque Azul development lays the groundwork for installing facilities to make natural gas available to the largest residential estate in Colmenarejo – 388 households will now use natural gas as their primary energy source. We have made a related investment of over €450,000 in network and other facilities to replace the old liquefied petroleum gas infrastructure.

Extension of our partnership deal with the Asefosam association of installers
2013 – 2014

Madrileña Red de Gas has extended its partnership deal with Asefosam, originally signed in March 2013, to boost the marketing effort arising from our public offering for signing new connection points in the fields of vertical saturation and the retail market. New measures have been introduced to encourage Asefosam installer members to market new natural gas connection points. 420 installation firms are now publicly offering the natural gas option, making for an 8% increase year-on-year.

Cooperation deals with municipal authorities
2013 – 2014

In line with our natural gas promotion policy, Madrileña Red de Gas has signed an agreement with Parla City Council and energy service companies. As a result, throughout 2013 we have provided natural gas supply to 25 schools, arts centers and sports facilities managed by Parla City Council.

We have also entered into cooperation agreements with the municipal authorities of Alcalá de Henares,



Móstoles, and Collado-Villalba, and energy service companies.

In addition, as a result of Madrileña's determined marketing efforts this year, infrastructure is being put in place to make natural gas available to the public buildings of the El Molar and Torrelozones municipal authorities.

Moreover, a tender has been put out for the gasification of all the centers and facilities under the control of San Lorenzo de El Escorial City Council, and a plan is underway to build 2,000 m of network piping to supply natural gas to the Felipe II residential estate in that municipality. MRG is building a new supply antenna for the Quijorna municipality, projected to start in February 2015.

Cooperation agreement to implement the Madrid region's subsidized equipment replacement scheme
2013 – 2014

As an initiative to improve equipment safety and energy efficiency by the gradual replacement of collective boilers and gas-fired industrial machinery, MRG has extended the lifetime of its cooperation agreement originally signed in 2012 to implement the Madrid region's subsidized equipment replacement scheme. Madrileña has accordingly invested €420,000 to provide installation discounts. This initiative encourages efficient energy use.



Key achievements and growth

Efficient operation and productivity

With the goal of providing end users with outstanding service, we have put in place the necessary quality metrics for meter readings, periodic inspections, contract terminations, reconnections, complaints and emergencies. All these activities undergo continuous development and improvement in order to optimize consumer satisfaction.

Madrid: Full Marks

The gasification of the trade fair facilities within Madrid’s Casa de Campo woodland reserve was a long-standing project which was finally completed this year.

The starting point was the implementation of gas supply to the PIPA pavilion and to the planned “Safety City.” This led to a project for gasification of this area of the Casa de Campo reserve, driven by Madrileña Red de Gas in partnership with various entities. The construction of more than 2,000 m of pipework will make natural gas available to 18 miscellaneous buildings: eight restaurants, a high school, municipal swimming pools, a SAMUR emergency response base, and various public facilities. The switch to natural gas will bring significant savings (these buildings consume over

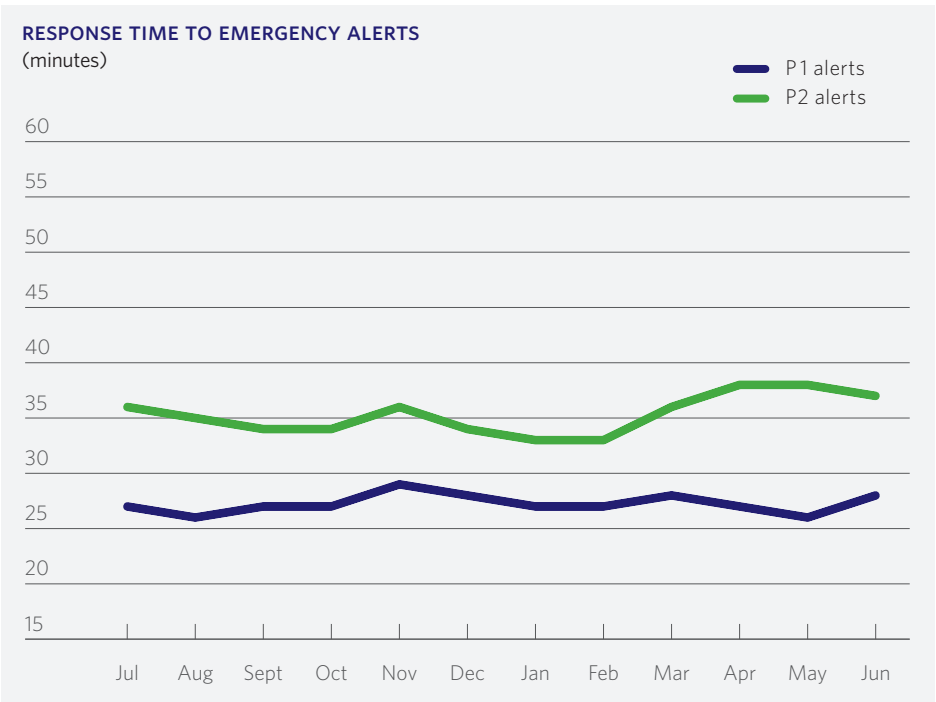
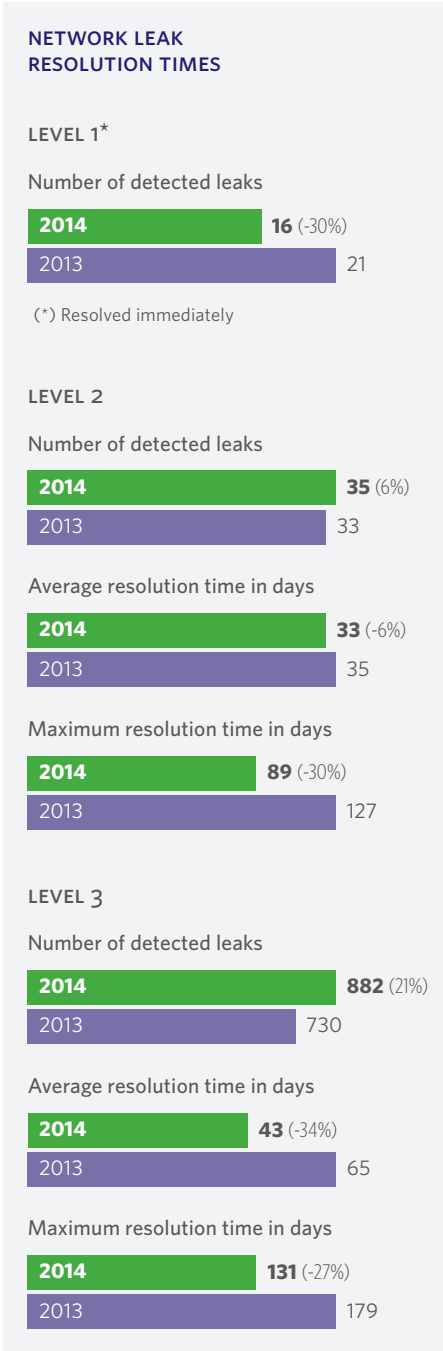
7 GWh per annum) and a decrease in carbon emissions of over 600 metric tons per annum.

Insourcing of key activities

Industry regulations require that at two-year intervals a thorough review be conducted throughout the entire distribution network to detect any gas leaks. In the course of this process Madrileña uses special equipment to detect methane emissions above the paved surface covering the natural gas pipework. Any detected gas emission is classified by severity: urgent action required (level 1), scheduled action required (level 2) and monitoring required (level 3). This classification reflects the following factors: operating pressure, concentration, and proximity to buildings or other pipelines.

Leaks calling for urgent action are addressed immediately by our emergency team, while level 2 and level 3 incidents are dealt with on a scheduled basis by the network maintenance team. We later conduct a review in the course of which the results are compared to earlier events so as to resolve incidents and make any required improvements to the network.

In support of this process Madrileña employs 31 specialist technicians who



are able to respond 24 hours a day, 365 days a year, through both emergency action and scheduled preventive maintenance. Scheduled maintenance has now been brought entirely in-house, thus enhancing efficiency and optimizing the working time available to emergency technicians.

100% of service supervision is performed by our emergency technicians, thus optimizing travel distances. Leak reclassification is also conducted entirely through our own staff, raising quality and safety.

Emergency response
We highlight that MRG has achieved excellent response times to emergency alerts. Madrileña is now an industry leader in this metric, thanks to its day-to-day efforts to shorten the time within which it addresses potential risk situations at consumers’ premises and/or within the natural gas distribution system.

MRG’s average emergency response time is well under the statutory limit. While the statutory response time for a level 1 alert is one hour, Madrileña’s average stands at 30 minutes. For

level 2 alerts, service is provided within 60 minutes on average, as compared to the statutory two hours.

We achieved our target to ensure that level 1 response times exceeding the hour limit is under 4% of all alerts annually – during the period, level 1 alerts dealt with in less than one hour came to 99,4% of the total.

Network maintenance
Madrileña’s maintenance plan specifies all the preventive maintenance actions to be taken on all assets within the distribution system in terms of scope, frequency, and other features. The plan is monitored using an SAP-PM module which optimises maintenance management.

Madrileña employs 10 technicians for network operation activities, including maintenance of metering and pressure regulating stations (MPRSs): we have brought all preventive maintenance and 80% of corrective maintenance in-house. By optimizing its maintenance plan, Madrileña has significantly raised the quality and reliability of MPRS functionality.

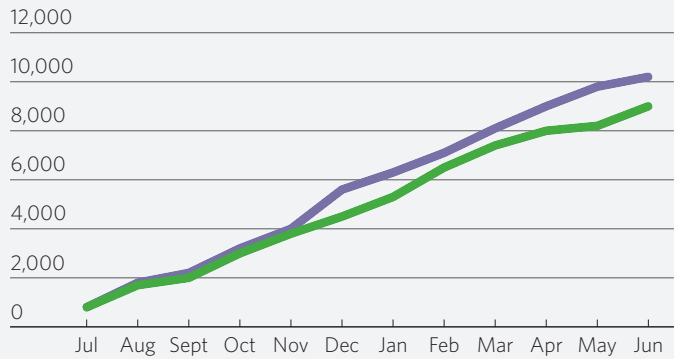
We also conduct cathodic protection maintenance largely in-house – 90% of corrective maintenance and 20% of preventive. This enables MRG specialists to perform directly in the field instead of merely overseeing contractors’ work. This step further safeguards the quality of MRG’s operations.

MAINTENANCE PLAN OUTCOMES

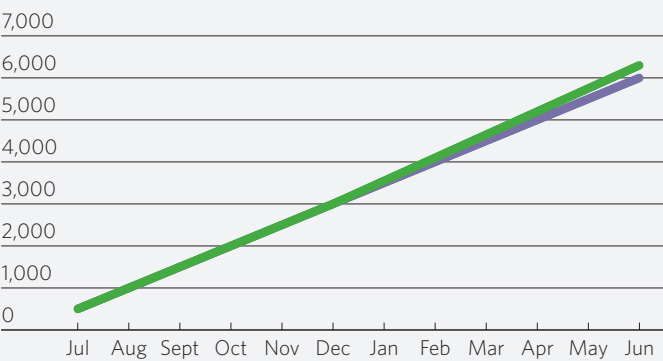
Progress and results of documentation
The implementation of the maintenance plan is outlined by the following charts. Implementation was completed in the course of the reporting period:

- Planned
- Completed

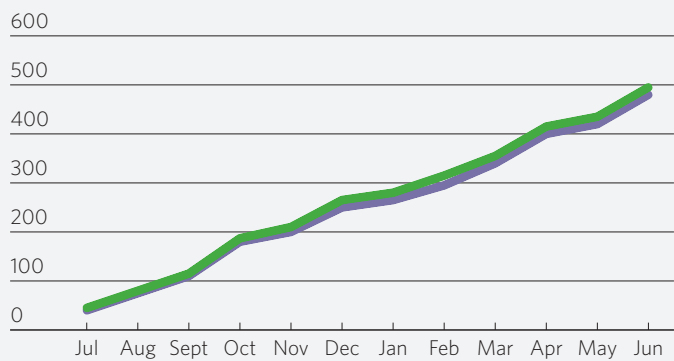
NUMBER OF ALERTS (P1, P2, P3 AND P4)



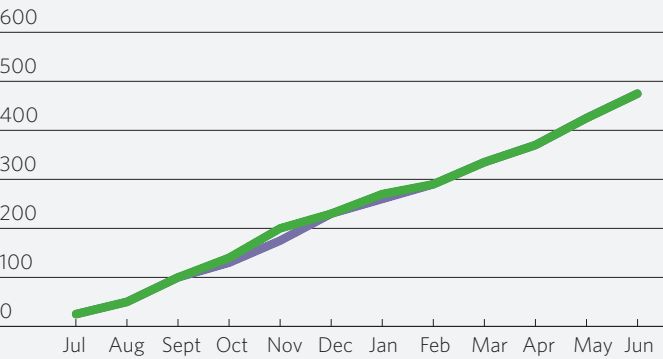
A-TYPE MONITORING (Km)



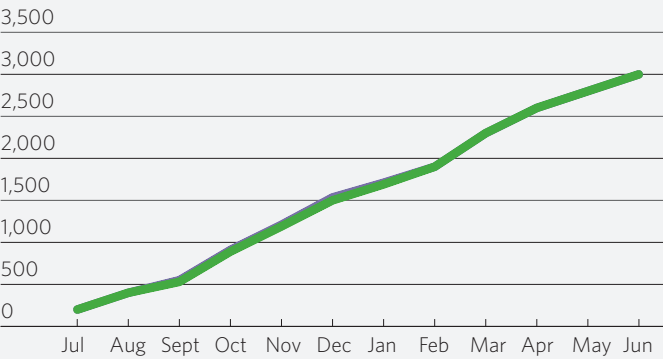
B-TYPE MONITORING (Km)



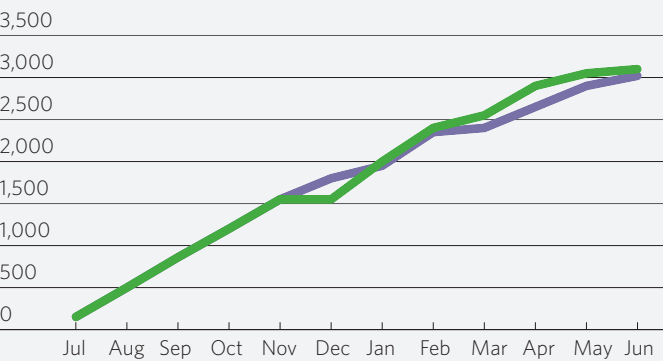
METERING AND PRESSURE REGULATING STATIONS (unit)



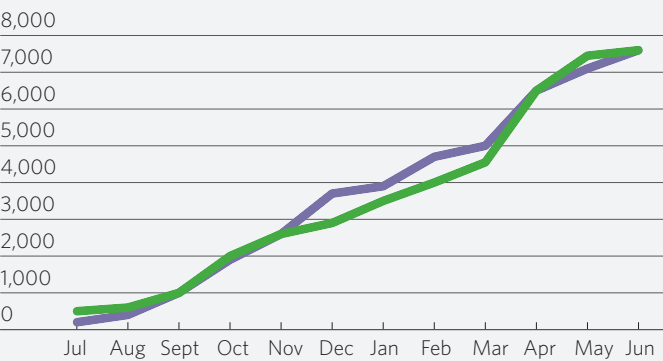
CATHODIC PROTECTION (unit)



NETWORK SURVEILLANCE ROUTES (Km)



VALVES (unit)



Cooperation with supply companies

Madrileña Red de Gas has displayed the ability to react and adapt effectively to the needs of supply companies in its territory. This has translated into a 400% increase in operational responses in payment default shutoff campaigns launched by suppliers for debt recovery purposes. MRG is an industry leader in creating proprietary methods, which have raised fieldwork success by 60%. Highlights include our vertical working (climbing) techniques because at least half of households

have no accessible meter. These new methods, among others, raised operational costs by 100%, but the effort considerably increased the number of reconnections within the regulatory time frame of 48 hours.

The development of natural gas vehicle adoption in Madrid

At present, MRG has commissioned a service station for the waste collection truck fleet operated by the Boadilla del Monte municipal authority, and a new public service station at Alcorcón.

In the coming months, a new public service station is scheduled to open at Aravaca, and several municipal authorities – including Madrid – are expected to put out tenders for the construction of new public refueling sites. The groundwork has been laid for the introduction of NGV buses operated by new intercity transport companies.

Updating our vehicle fleet

As part of our natural gas development policy, Madrileña Red de Gas is a front

runner in promoting the use of NGVs. The use of natural gas for transportation purposes brings both environmental benefits and economic savings as compared to other fuels. Natural gas-fired engines are cheaper to maintain and have a longer useful life than engines powered by liquid fuels.

MRG will replace its entire fleet – about 60 vehicles – with Natural Gas Vehicles (NGVs). We have acquired new Fiat Dobló vans to equip our network operation units, and four Seat and Volkswagen cars for technical and sales managers. We are in the process of acquiring more Seat units and

Volkswagen Caddy vans for network operation management officers.

Driving the development of natural gas

Although the gas industry is regulated, the development of natural gas is one of the key factors of Madrileña Red de Gas' mission. We are committed to publicizing its benefits and raising awareness of its suitability as a replacement for costlier and more pollutant fossil fuels. The shift toward natural gas produces savings in the country's energy bill, lowering energy

Natural Gas Vehicle (NGV)

PRICE ADVANTAGES:

- Compared to gasoline: > 50%
- Compared to diesel: > 30%
- Compared to LPG: > 20%

ENVIRONMENTAL BENEFITS:

Global footprint (carbon dioxide)

- Compared to gasoline: 30%
- Compared to diesel: 20%
- Compared to LPG: 12%

Local footprint

- Nitrogen oxides (NO_x): 75-95%
- Particulate matter (PM): 95%
- Carbon monoxide (CO): 20-25%
- Sulfur dioxide (SO₂): 100%
- Noise: 50%

costs for end consumers and cutting down atmospheric emissions with no additional cost to public funds or private resources.

MRG is accordingly promoting and taking part in efforts to implement new NGV service stations. A number of trends strongly suggest that the present transportation model is unsustainable over the medium term. Almost 100% of energy sources are petroleum byproducts: world reserves are limited, and are concentrated in geo-politically problematic regions. Fuel prices are both volatile and follow a historically upward path. Given the economic and environmental advantages, the rise of NGVs in Spain's mobility system offers an attractive opportunity for consumers and opens up new product perspectives for the domestic automobile industry.

Engaging in new regulation

In recently developed domains that have not yet been covered by specific regulations – such as NGVs – Madrileña Red de Gas has supported policy-making by providing comparative studies of relevant legislation across Europe. Highlights of this process include parking natural gas vehicles in spaces reserved for the Madrid Transport Consortium and conversion of gasoline-powered vehicles to natural gas.

Marketing strategy

Automobile industry

MRG has been active in marketing to industrial estates in 12 municipalities in the Madrid region, having conducted more than 300 visits and filed 147 studies on energy savings and conversion proposals. After conducting a range of visits and producing specific studies, we have offers to 15 members of the AMDA association of vehicle dealers, achieving a number of agreements with them. In addition, MRG has carried out actions in coordination with the vehicle repair garage associations ASETRA and GANVAM to promote the energy efficiency and savings that gas provides.

Taxicab sector

In partnership with the devolved regional government of Madrid and the two leading taxicab associations, Madrileña Red de Gas is working to increase the number of natural gas vehicles among the region's 16,000 licensed taxicabs. To encourage the emergence of a standard taxicab, Madrileña is in contact with various car manufacturers: Volkswagen, Mercedes, Seat, Toyota, Peugeot and Fiat.

At present, the regional government of Madrid has allocated €1 million to the gradual replacement of the taxicab fleet. If 2,000 taxicabs were to switch to natural gas, annual savings in

atmospheric emissions would come to 1,000 metric tons of carbon dioxide and 24 metric tons of nitrogen oxides.

Madrileña Red de Gas is also working with the ONCE Foundation (Spain's charity for blind and disabled people) to develop a compressed natural gas-driven taxicab model capable of accommodating the needs of people with disabilities.

MRG also supports switching to natural gas as a fuel for gasoline/electric hybrid cars. MRG is in the process of signing agreements with car dealership associations.

LNG plants in several municipalities

Madrileña is well on the way to achieving one of its main goals: making natural gas available in the Manzanares Upper Basin. This milestone will come about through planning, research and other work conducted in aid of natural gas distribution via liquefied natural gas (LNG) plants to be installed in the municipalities of Talamanca del Jarama, Valdetorres del Jarama, Guadalix de la Sierra, Miraflores, Torrelaguna, Zarzalejo and El Vellón. The relevant licenses were obtained in 2012.

At El Vellón, where an LNG plant was intended to be built, it was finally

decided that the quickest and most effective solution was to create a connection to the distribution network in the neighboring municipality of Pedrezuela.

A further highlight was the replacement of the liquefied petroleum gas plant at Valdemorillo with a new 4,500 meter antenna which supplies the Parque Infantas residential development.

Home Service operations: streamlining of contractors

This year we reorganized home service operations by signing new contracts and producing new field protocols. This represents a shift from having to deal with many specialist firms, each having heterogeneous capabilities, to consolidating tasks with four companies that have widened their scope of action to embrace all the specific operations formerly covered by many different firms.

The reorganization drive has achieved improved consistency in fieldwork procedures, more effective supervision of contractors, and an average 21% reduction in the unit cost of operations. Fieldwork success rates are also on the rise: 90% in user-requested shutoffs and 75% in payment default shutoffs, all within one year, and with an 8% increase



in fieldwork operations with respect to the previous period.

Service improvements

Madrileña Red de Gas works closely with regional authorities, holding monthly meetings at which the company reports on its present actions and future projects to improve service, and receives suggestions and proposals. Another major step forward was the creation of an online customer service

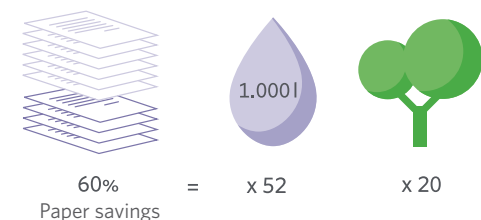
office providing consumers with full visibility of the steps taken in relation to their installations. Users can view information on the status of their complaints, meter reading histories, status of scheduled inspections, etc., using their computer, tablet or smartphone. In the next few months, user notifications via e-mail and text messaging will be implemented.

To speed up the management of fieldwork requests and cancellations, we have also implemented mobility and request-overlap solutions for retail suppliers.

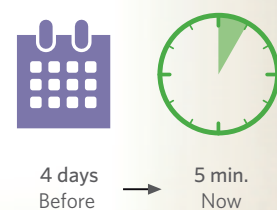
The new mobile apps significantly reduce environmental impact and shorten work order notification times

BENEFITS OF MOBILE APPS

Environmental savings



Job notification times



Mobile app

99% of our home service operations, scheduled inspections and gas supply connection procedures take place in mobility scenarios – this has cut our paper usage by 60%. The reduction in environmental impact is equivalent to 52,000 liters of water and 20 trees. We have also considerably shortened work order notification timeframes: from four days to five minutes. These steps forward have made MRG highly agile in its response to reconnections, order cancellations, etc.

Since the introduction of the app in July 2013 it has supported over 300,000 transactions. This lightens the administrative burden surrounding the process and provides a rich complement of information captured in the field, including photographs, GPS coordinates and real-time delivery of work order records.

Today, all our contractors work with Android devices and portable printers, which means they do not need to visit the office to receive and download work orders.

Sustainable solutions for information systems

We have also made changes to our infrastructure management and storage contracts. MRG undertook market research to identify and establish suitable comparisons with a view to negotiating with the companies now providing these services. By renegotiating service contracts on the basis of this research, we achieved an annual cost saving of 35%. In addition, we increased our installed infrastructure base to cover our new SCADA software tool for distribution network monitoring.

With the new SCADA system, Madrileña Red de Gas has completed the implementation of software tools for its core activities. When it becomes operational, SCADA will provide real-time data supplied by all the metering and pressure regulating stations throughout our distribution network, so enabling monitoring and management 24 hours a day, 365 days a year, via a video wall in the new control center at our headquarters. The culmination of this project has in-sourced a service so far provided by Gas Natural Fenosa. By supporting end to end management of emergency responses and network monitoring by a single team of people, this change enhances consistent and coordinated action.

Efficient capex

MRG's marketing model is based on executing efficient infrastructure for consumers applying for connections to the Madrileña network, and on an optimized, sustainable layout of the distribution network.

Madrileña Red de Gas builds a trunk network in the main artery of the municipality and lays down feeders to connection points at the same time as executing pipework. Our parallel work approach optimizes waiting times for supplying natural gas to new connection points.

MRG's efforts have ensured that 50% of all pipework can be laid using far narrower trenches than the conventional width. We have used state of the art machinery, such as the machine known as La Zanjadora ("trench-digger"), which considerably reduces the inconvenience of digging trenches in municipalities by cleanly cutting through rock, frozen ground, pavements, etc., without damaging the surrounding terrain, obstructing traffic or creating noise or waste.

Corporate governance

Madrileña Red de Gas’ mission is to distribute natural gas and promote its adoption. Our approach is to carry out rigorous and transparent management of our capital for the benefit of our shareholders, employees and the broader community. We continuously strive to achieve excellence both within our business and elsewhere. To achieve this Madrileña follows stringent principles of corporate responsibility and good governance.

The board and the management committee are both committed to the good governance ethic, and in this respect each member of those bodies undertakes to use his or her best endeavors in furtherance of Madrileña’s corporate integrity.

We are aware that the proper use of our assets is vital to the success of the company, and accordingly take it upon ourselves to deal with those assets honestly, effectively and responsibly. Our approach in this domain is to follow policies that safeguard control and accountability in key decision-making areas, such as procurement and investment, appointments, remuneration, and the laying down of procedures, which must be completely transparent, verifiable and auditable.

MRG’s supreme decision-making body is the Board of Directors. Its rules of action are guided by principles of transparency – these being essential to

foster trust and confidence in prospective investors, employees, customers and the wider community – and are designed to ensure compliance with best practices in corporate governance. All members of the board are highly qualified professionals characterized by integrity, independence of opinion, and a robust track record in the field of finance.

The board of Madrileña Red de Gas, comprising seven members with extensive experience in the industry, regularly receives progress reports produced by the various divisions of the organization. The management committee creates the company’s action plans and takes considered decisions with a view to achieving the intended objectives, while supervising and managing the running of the company in all respects. The committee endeavors to follow a course of effective decision-making in alignment with approved budgets and strategy.

Board of Directors

- Pedro Mielgo**
Chairman
- Gordon Hunt**
Deputy Chairman
- Markus Hottenrott**
Director
- John Watt**
Director
- Thomas Gray**
Director
- Yacine Saidji**
Director
- Luis Isasi**
Director
- Hugo Aramburu**
Director

Management Committee

- Alejandro Lafarga**
Chief Executive Officer
- Rafael Fuentes**
Head of Legal Affairs
- Javier Contreras**
Chief Financial Officer
- Félix Gómez**
Business Development Director
- Félix Blasco**
Head of Network Operations
- Glen Lancaster**
Head of Systems and Operations
- Ramón Rodríguez**
Head of Human Resources



Members of the Management Committee
(from left to right, seated): Félix Blasco, Rafael Fuentes and Javier Contreras. Standing: Félix Gómez, Alejandro Lafarga, Glen Lancaster and Ramón Rodríguez

Madrileña Red de Gas management

Madrileña's management approach aims to be responsible with our people, the environment and the broader community

Madrileña invests in its employees by implementing a training program. Its goal is to extend the adoption of natural gas with a view to energy savings and environmental improvement, and to create and develop technologies and processes to ensure high quality service to end users.

Madrileña Red de Gas engages in philanthropic projects in partnership with a range of nonprofit entities and sponsors sports initiatives aimed at young people.

Human resources

Training

Madrileña Red de Gas is committed to ongoing improvement of our people’s skills and professional development. We believe training initiatives are crucial to the growth of the company. Every year, we plan a range of training courses that effectively cater to Madrileña’s real needs. Our training programs are tailored to the emerging needs that arise in MRG’s employees’ jobs and commitments so as to support the professional growth of our people on an individualized basis. Training goals are aligned with the organization’s strategy so as to create real value within the business.

The benefits of our training drives include enhanced productivity and competitiveness through acquiring and improving our employees’ skills, heightened awareness of our policies, and adaptation to technological and organizational change.

The key factor guiding our training plans is customer orientation and satisfaction, which is the sustaining force of the company. Our commitment to users is the mainstay of the planning and implementation of the courses we offer to our employees, in a bid to provide them with the best training within our reach.

This year, 70% of our employees undertook at least one training action,



rigorously developed and implemented by MRG’s training unit. 2,700 hours of training were provided across 25 different courses. Over 1,700 hours of training revolves around direct business concerns: cathodic protection, gas-driven climate control projects, energy efficiency, regulatory matters, etc.

500 hours of training were devoted to skills upgrading (leadership and

communication skills), and a further 500 hours to office IT skills (Access, Excel, GiS-GDO, Microstation, etc).

Creating jobs

Madrileña Red de Gas employs 166 people in-company and outsources auxiliary activities to over 300

contractors. Requirements as to training, qualifications, and occupational health and safety are standard for both in-house employees and for contractors.

In addition, our business indirectly supports a further 600 jobs at other companies: installers, boiler manufacturers, distributors, retail suppliers, etc.

Maximum safety

In partnership with Gas Natural Distribución, MRG developed an Emergency Protocol, which sets out a procedure for mutual support in serious emergencies that might compromise gas supply continuity or safety. We undertake ongoing occupational risk prevention efforts, including an exhaustive training plan for all staff involved in maintenance and emergency response work. We also equip our people with the gear needed to do their jobs to the highest standards of safety.

We have the necessary resources to monitor and follow up our contractors’ compliance with safety requirements via firms specializing in risk prevention.

The fact that Madrileña has not experienced any serious incident this year bears out the effectiveness of the measures taken.



Lower occupational accident rate

One of the key goals Madrileña Red de Gas has achieved over its four-year lifetime is a significant decrease in the number of occupational accidents.

This achievement was based on:

- A robust and consistent drive to raise employee awareness of occupational

risk and train our staff in prevention activities.

- Comprehensive investigation of occupational accidents and adoption of preventive measures.

Risk management

With a view to achieving our business objectives Madrileña Red de Gas has laid down an end to end business risk management policy. The underlying principles and commitments of the policy address the concerns of a wide range of stakeholders, support strategic flexibility and optimization, and bolster efficiency and minimizing costs.

Business risk is monitored by systematically documenting all our actions so as to produce a risk map in accordance with the widely recognized COSO II standard. The conclusions are as follows:

- 100 identified risks, 10 of which qualify as key risks.
- Nine distinct risk categories: finance, safety, regulatory affairs and compliance, operations, reputation, strategy, contractors and suppliers, information and reporting, and structure.
- 158 identified high-level controls.

Environment



Replacing other fuels

Significant savings were made in the past year through replacing other fuels: €3.1 million in the residential market and €3.2 million in the large consumer market. The figures translate into a total €6.3 million of savings in the proprietary distribution zone (our own calculation based on annual growth and the energy mix handled by us in the residential and large consumer markets).

The energy mix of fuels we have displaced is made up of 65% propane and butane, 20% diesel and 15% electricity.

Regarding carbon emissions, the savings achieved in 2013 translate into: 4,500 metric tons in the residential market and 7,200 metric tons in the large consumer market, making for a total of 11,700 metric tons per annum of emission savings in the Madrid region. A key fact to bear in mind: a propane-fuelled household emits 420 kg per annum of carbon dioxide more than if it were fuelled by natural gas.

Energy efficiency study

With condensing boilers, which utilize the latent heat of condensation gases and reduce natural gas usage, MRG has achieved efficiency figures in excess of 110%. This makes for energy savings of more than 25%. In addition, emissions of carbon dioxide and nitrogen oxides are up to 20% less than for a conventional low-consumption boiler, which only achieves NO_x emission savings of 6%. Furthermore, maintenance costs are considerably lower.

Innovation

MRG’s information systems are the industry benchmark

Madrileña Red de Gas’ operating information systems are highly sustainable in terms of maintenance costs. MRG is known for implementing solutions fast: six months for field mobility solutions. This enables us to troubleshoot end-user issues in real time. Madrileña’s approach, which involves implementing field mobility terminals, lets our technicians manage issues more effectively, shortens response times and provides real-time access to graphical documentation and on-site visit records.

Natural Gas Vehicles (NGVs)

MRG continuously encourages the adoption of natural gas vehicles within its area of influence by taking the following actions:

- visits to the main municipal governments with a view to converting their waste collection vehicle fleets;
- installation over the next two years of eight new public natural gas service stations within our distribution zone;
- joint capex effort with suppliers to interconnect our high-pressure infrastructure;

SYSTEMS MAP

CUSTOM SOFTWARE

GAS QUANTITY REPORTS	Calculation of daily deliveries of distributed gas	
OPERATING MOBILITY	Fieldwork order management	
REMOTE METERING	Management of remote metering for customers consuming >5 GwH	
ON-SITE METER READING MOBILITY	Management of on-site meter reading orders and routes	
EMERGENCIES	Acceptance and processing of emergency calls	
POTENTIAL MARKET	Identification of prospects based on data cross-references and zone assignment to sales reps	
TECHNICAL DRAWING MGMT.	Quality control and review of drawings and integration with the geographical information system	

STANDARD APPLICATIONS

TDCS	Transportation and Distribution Communication Systems	
GDO	Gas Distribution Office	
WINFLOW	Network load simulator	
BUSINESS WAREHOUSE	Reporting	
FOR UTILITIES	Reporting Finance Maintenance and Operations Projects Meter Readings - Billing - Collections Third-Party Network Access	
SCADA & DISPATCHING	Real-time monitoring of metering and regulating stations (currently under implementation)	

PROVIDED AS A SERVICE

PAYROLL	Calculation of MRG employee pay	
CORPORATE EMAIL	Corporate e-mail platform based on the Google docs solution	

- infrastructure investment so that large bus companies and waste collection fleets can have natural gas stations available at their depots. Partnered firms include Transportes Ruiz and FCC;
- support for producing the technical report commissioned from the regional government of Madrid's Energy Foundation on the introduction of natural gas refueling facilities at long-distance coach stations;
- active membership of the Spanish Association of Natural Gas for Mobility (GASNAM); and
- approaching vehicle fleet operators (SEUR, COFARES, etc.).

Liquefied Natural Gas (LNG)

Six of our distribution licenses in the Madrid region relate to locations not covered by the MRG distribution network, so we have installed liquefied natural gas facilities.

Registered industrial design

The ongoing economic downturn has driven up the rate of payment default shutoffs and fraudulent usage in the gas market, and Madrileña Red de Gas has been fast to react. Plastic devices for locking shutoff valves have proved inadequate to prevent unauthorized reconnections, with the safety issues that this involves. So, within a record time frame of just two months, the MRG research and development team designed a tamper-proof metal device that can be fitted to a shutoff valve to ensure it stays locked and so avoid unauthorized or fraudulent gas usage. We have also developed tamper-proof screws – and their corresponding keys – for fixing the locking device to the valve. About 10,000 units are now in place. This new locking mechanism has brought down unauthorized reconnection incidents by 80%. Since the locking devices are harder to destroy, their reuse rate has improved by 100%, providing significant material cost savings.



Quality



Internal review, improvement of meter reading procedures

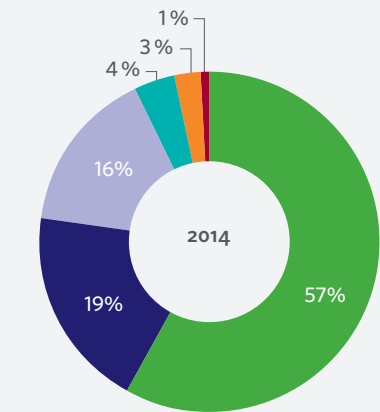
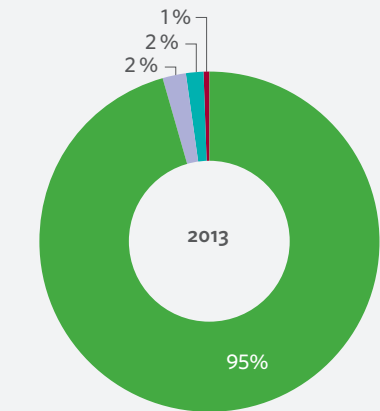
In the first quarter of 2014, MRG implemented a project to improve meter reading and data capture procedures in the field based on a case study analysis embracing the whole of 2013. Involving all customer-facing operations, the project was designed to fulfill the following goals:

- Increasing the use of real field-based readings additional to the predetermined meter reading routes.
- Shortening timeframes for adjustments to end consumers' real usage.

- Making best use of readings provided by end-consumers and retail suppliers.
- Triggering early warning alerts for end-consumer usage anomalies.

The utilization of readings provided by third parties rose by 20%, and improvements were made in the identification and resolution of outstanding issues with reconciling billed usage to real usage. This process took place within the framework of cooperation with the Directorate General of Industry, with whom we agreed upon the principles guiding the use of real meter-readings, billing adjustments, and campaigns for capturing readings from inaccessible

PROCESSING CHANNELS FOR METER READINGS AND REQUESTS
Fourth quarter (April and June)



- Line 902 (Customer Service)
- Line 900 (Meter readings)
- Photographic readings
- Electronic mailbox
- madrilena.es (Online Office)
- Written case files

meters from which real readings had not been taken for over one year.

New meter-reading channels

During this period MRG has created two free-of-charge communication channels to enable users to provide their meter readings direct to our call center or send photographs of their meters to our electronic mailbox. The new channels will increase the number of real meter-readings and therefore reduce the number of estimated readings. This is significant because in our distribution area 40% of metering devices are located within households, which means readings cannot be taken if the occupant is absent.

Campaign to retrieve overdue Inspections

Even in a period of economic difficulty Madrileña achieved its best performance so far in terms of successfully completed inspections.

One of the statutory duties of a natural gas distributor is to ensure the safety of consumers' facilities by conducting the regulatory inspections. In coordination with the Directorate General of Industry, MRG undertook a campaign to retrieve inspections due on connection points overdue and outside the five-year

regulatory limit by arranging individual visits. To date, the success rate is 39%. Over 8,000 inspections have been conducted on connection points that were formerly in default of the statutory inspection timing. In addition, we successfully performed 154,178 scheduled inspections, representing 94.85% of all consumers due for planned inspections.

This performance was driven by exhaustive follow-up in the field and an increase in the information sent to consumers regarding their obligations.

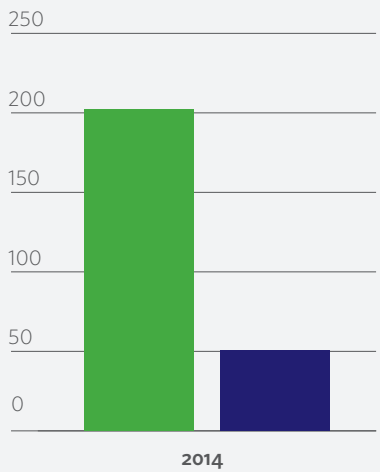
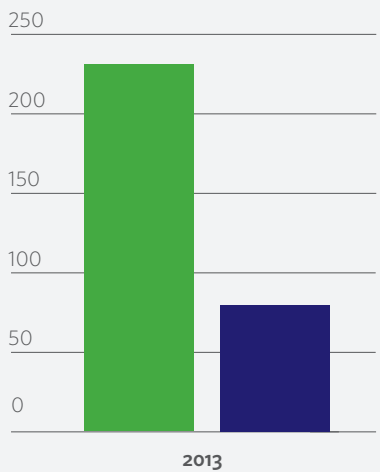
Improved complaint management

In 2014, Madrileña Red de Gas consolidated its customer service and emergency response platforms, which are now operated by multidisciplined agents who can attend calls from either service.

We have also created a back-office dedicated exclusively to meter readings. This unit receives readings from consumers via the two new channels – telephone and photographs sent by email.

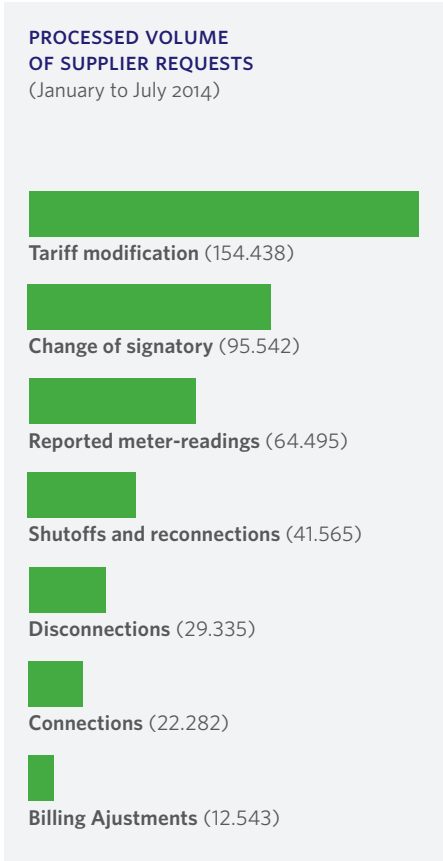
The online office on MRG's website has seen a significant rise in registered users and a rising proportion of complaints are now processed over the Internet.

VOLUME OF CALLS TAKEN BY MRG SERVICE UNITS
(Thousands of calls)



- Customer service
- Emergency response

Commitment to the community



Outstanding service to consumers

In our 305,000 field visits and 2.4 million meter readings conducted this year Madrileña has shown its pursuit of service excellence: real meter-readings and user-provided photographic readings have both risen, and we have achieved high success

rates in home service operations. We performed 112,000 home service operations, with a 90% success rate, and 193,000 periodic inspections, with a 94.85% success rate.

MRG has centralized all customer service and complaint handling functions in a dedicated unit in charge of detecting needs and implementing preventive initiatives. Because we

operate as an independent distributor, we have no direct contractual relationship with consumers. Therefore we proactively have to find ways to contact with consumers, manage absences and carry out scheduled but overdue visits. These efforts extend to retail suppliers, with whom we are working more closely to manage the wide range of requests involved.

Willingness to invest

Thanks to its focus on performance and transparency, Madrileña has helped bolster the reputation of the natural gas industry in Spain, which has begun to attract foreign investors. MRG plays an active role in the potential development projects emerging within its field of action, and offers new property and industrial developers a range of benefits linked to the use of natural gas for their own projects-

This recognition is reflected in the makeup of the company's shareholder structure and in the success of our recent corporate debt success in capital markets.

MRG supports the community

Madrileña Red de Gas has set in motion a range of changes designed to raise the service quality we provide to users and enhance the functioning of the system. The changes relate to terminations and shutoffs, reconnections, fraud control, new connections, supplier switches, licenses, natural gas expansion, replacement of more expensive forms of energy, safety and natural gas vehicles, among other topics. Most of these measures are already in place, while the rest will be implemented in the next few months.

Support for Madrid regional government plans

In relation to the subsidized replacement plan for individual boilers, Madrileña processed 9,964 applications and contributed financial support worth €163,000.

As to the subsidized replacement plan for central heating boilers and the industrial market, MRG processed 183 applications and made an economic contribution of €21,197.

Partnerships with community stakeholders

Since April 29 in El Molar and May 25 in Pedrezuela, Madrileña Red de Gas is distributing natural gas to residents of these municipalities in the north of the Madrid region. We have also improved our medium and long-term growth prospects by obtaining local government licenses to distribute natural gas in the municipalities of Los Molinos and Soto del Real.

Madrileña's commitment to the community has involved the execution of more than 1,000 m of network pipework and 20 connections to supply the municipal centers in Parla, supporting usage in excess of 8 GW (23 centers). At Alcalá de Henares,

MRG overhauled eight municipal centers. At Valdemoro, Collado-Villalba and Móstoles, we have plans in place to switch municipal centers to gas supply and conduct feasibility studies for conversion to natural gas of 178 secondary schools.

Highlights include our partnership with Saint Gobain group on a pilot energy efficiency project at public secondary schools, and our cooperation with the Fundación de la Energía for the gasification of industrial estates. The first trials were conducted at Alcalá de Henares, where we have made 218 visits.

Supporting sport and youth communities

Soccer is undisputedly the leading sport in the Madrid region and is the game of choice for our children, who are our future. Madrileña is making a modest but heartfelt contribution by funding a soccer team which now competes with the region's finest. We are proud to serve the community and help our boys and girls to nurture their team spirit through their committed pursuit of soccer. The 34 teams within the Adarve sports association comprise a total 748 children and young people.

Financial analysis

The 2014 financial period has been shaped by stable operating earnings and the impact of the refinancing debt process

2014 is the third year running in which our scope of consolidation remains unchanged after the acquisition from Gas Natural Fenosa in April 2010 and June 2011 of its natural gas distribution operations in various municipalities of the Madrid region.

There were two exceptional milestones in the financial period: the refinancing and restructuring of our financial debt, and the completion of the corporate reorganization of the Group following the acquisitions from Gas Natural in 2010 and 2011.

Performance overview

PROFIT AND LOSSES		
€M	2013	2014
Remuneration	152.0	153.4
Other revenues	25.3	27.4
EBITDA	146.4	149.2
EBIT	111.0	114.7
Net profit	30.7	10.3

The financial period ended June 30, 2014 is the third period running in which our scope of consolidation remains unchanged after the acquisition from Gas Natural Fenosa in April 2010 and June 2011 of its natural gas distribution operations in various municipalities of the Madrid region.

There were two exceptional milestones in the financial period: the restructuring of our financial debt, and the completion of the corporate restructuring prompted by our acquisitions from Gas Natural.

In 2014, MRG recorded net earnings of €10.3 million, 46.7% down year-on-year. This should be viewed against the background of the impact of various non-recurring financial expenses arising

from the bank loan refinancing process completed in the second half of 2013.

In 2014, MRG continued to grow its distribution network by connecting new consumers within its existing territory and expanding into new adjacent municipal districts, laying the foundation for sustainable growth in the coming years.

In line with this approach, this year we obtained local government licenses to distribute natural gas in the municipalities of Los Molinos and Soto del Real, both being located in the Madrid region.

At the end of the financial period, the company was operating in 59 municipalities and supplying a total 839,144 connection points.

Operating earnings

Earnings before interest, tax, depreciation and amortization (EBITDA) grew 2% year-on-year.

In this period the main sources of growth were regulated remuneration, periodic inspections and reconnection fees.

Requests for terminations, shutoffs, reconnections and metering device removals continued to grow, but at a slower rate (17% in 2014 as against 70% in 2013). This high volume slowed down the growth of the company customer base and impacted variable costs for the year.

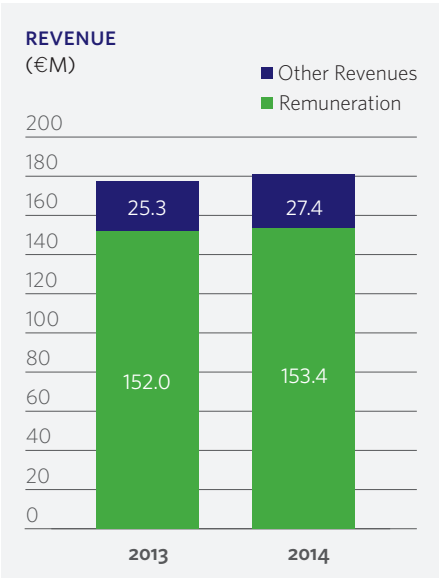
Gross capture of new connection points increased by more than 9% year-on-year, driven largely by the extension of distribution networks into new municipalities.

We continued to implement and consolidate improvements in operating processes with the aid of technological resources and/or internal processes.

Revenue

Total revenue in 2014 came to €180.8 million. Approximately 85% of this figure was accounted for by regulated remuneration for the distribution activity under Order 2812/2012 of the Ministry of Industry, Tourism and Trade, published in Boletín Oficial del Estado (Official Journal of Spanish Central Government) No 314, December 31, 2012, and Order 2446/2013, published in Boletín Oficial del Estado No 312, December 30, 2013. The remaining 15% arose from the provision of services relating to natural gas distribution, most being regulated activities as well. Highlights include revenue from meter rental, periodic inspections, and other services to consumers

Remuneration for the distribution business is calculated in accordance with the provisions of the regulatory framework prevailing in the given financial period, using a parameter-based formula whose main vectors of review are (i) inflation (as given by the Spanish hydrocarbons price index “IPH”), (ii) growth in terms of new



connection points, and (iii) growth in the volume of distributed natural gas.

Although the IPH index declined in 2013, the company's regulated remuneration revenue increased 1% year-on-year as a result of the rise in connection points and distributed gas volume.

Total revenue in 2014 came to €180.8 million

Financial position and balance sheet

BALANCE		
€M	2013	2014
Gas distribution licences	713.4	713.4
Net tangible fixed assets	385.5	374.3
Total Network Fixed Assets	1,098.9	1,087.7
Goodwill	57.4	57.4
Deferred tax asset	30.8	32.3
Other non-current assets	4.2	3.4
Current assets	40.0	41.0
Cash	33.4	55.4
Total Assets	1,264.6	1,277.2
Equity	230.5	436.7
Subordinated shareholders loan	194.0	–
Long term debt	726.3	769.0
Deferred tax liability	23.5	27.8
Other non-current liabilities	1.3	2.0
Current liabilities	89.0	41.7
Total Liabilities & Shareholders equity	1,264.6	1,277.2

The changes on the liabilities side of the balance sheet reflect the restructuring of debt completed in the first half of the period

Operating cash flow

FREE CASH FLOW		
€M	2013	2014
EBITDA	146.4	149.2
Income tax paid	(9.2)	(14.7)
Working capital	2.0	(19.8)
Capex	(21.1)	(17.1)
Free cash flow	118.2	97.6

In 2014 operating cash flow totaled €97.6 million, 17% down year-on-year.

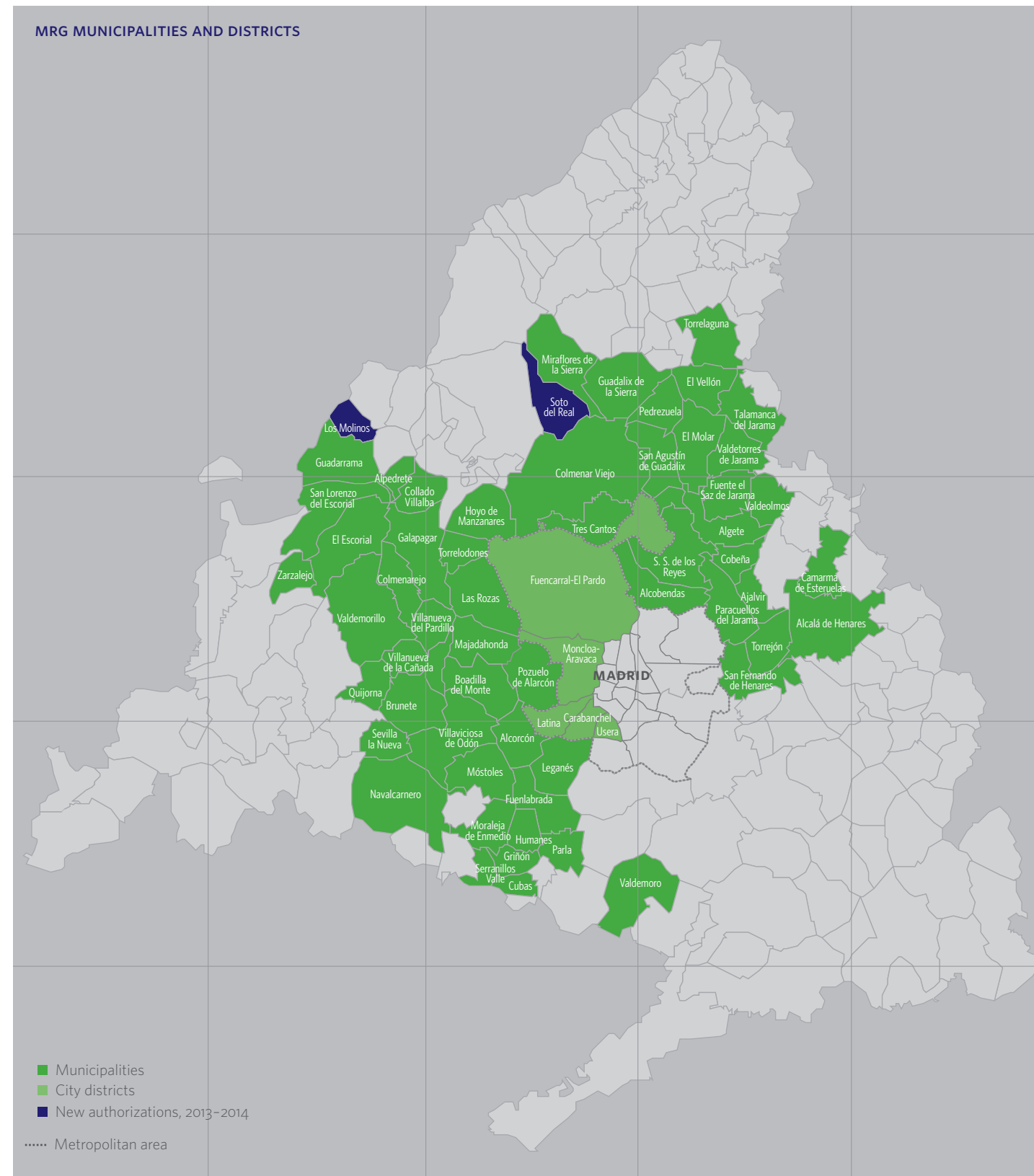
The main factors driving down cash flow in this period were:

- Increase in working capital. This temporary fact is chiefly due to outflows in the first quarter of the present period in respect of
- A larger corporate income tax payment owing to the impact throughout the financial period of the temporary measures adopted in 2012.

investments undertaken in the previous period and to a decrease in total invoicing in the second quarter of 2014, given higher temperatures than in the same period last year.

The temporary rise in working capital and the changes in the corporate income tax figure were the main impacts on cash flow in this financial period

MRG MUNICIPALITIES AND DISTRICTS



Capital expenditure

MRG's capital expenditure on projects undertaken throughout the period came to €17.1 million. This 19% year-on-year decrease was due to a lower investment in network sectorization projects.

The key points of Madrileña's capital expenditure outlays in 2014 are classifiable into three main areas:

Expansion

MRG's strategy focuses on growing its distribution network by connecting new consumers within its existing territory and expanding into adjoining municipal districts.

In line with this approach, MRG invested a total of €14.5 million in expanding its distribution networks, 18% up year-on-year.

In addition to sustained expansion in the company's consolidated territories, we made a significant capex effort to create new distribution networks in neighboring municipalities such as El Molar, Villanueva de la Cañada, San Lorenzo del Escorial and Griñón, enabling us to establish a robust platform to capture new connection points in future financial periods.



Network Sectorization

This project, designed to achieve technical separation between MRG's distribution networks from Gas Natural Fenosa's and connection to primary transport networks, accounted for capital expenditure of €1.1 million during the period.

Other projects

Other highlights included our investments in projects to develop information systems and technical improvements in the company's other areas.

Refinancing

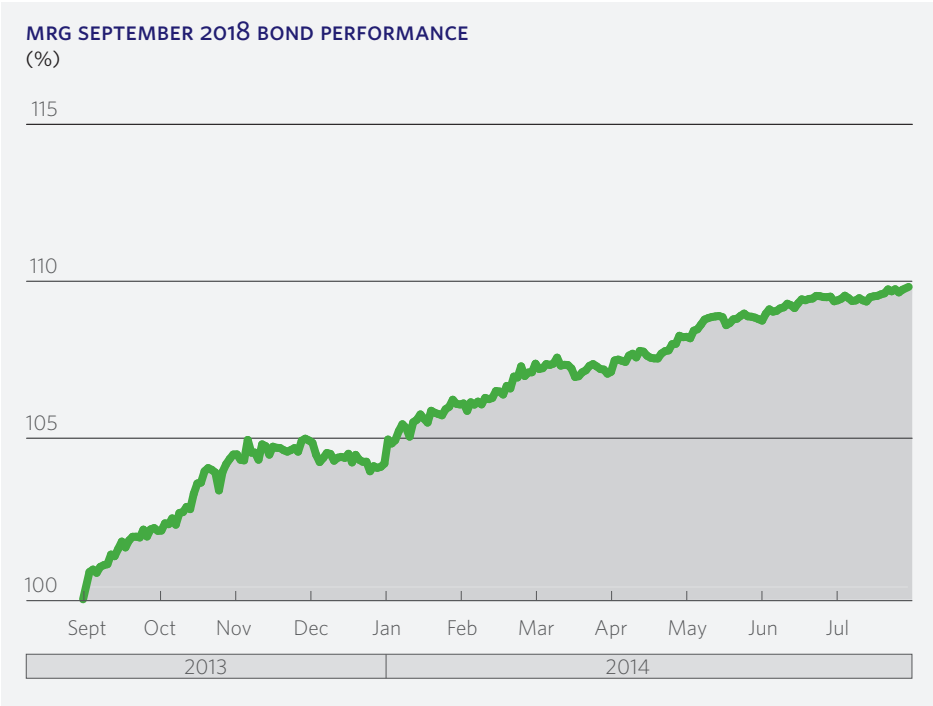
In the first half of the period we restructured and refinanced our corporate debt.

First, the company made early repayment of the two syndicated loans which had funded the acquisitions of Madrileña Red de Gas and Madrileña Red de Gas II in 2010 and 2011, respectively. The interest rate hedges linked to this financing to above were also terminated.

Secondly, to secure funds for early repayment of the two bank loans and termination of the hedging instruments, we launched bond issues to a value of €500 million and €275 million, maturing in September 2018 and December 2023, respectively.

The bonds, issued by Madrileña Red de Gas Finance BV, a Dutch-registered company wholly owned by the sole shareholder of MRG, are guaranteed by Madrileña Red de Gas and were given effect under a Euro Medium Term Notes (EMTN) programme registered with the Luxembourg Stock Exchange on 1 August 2013.

In addition, as part of the drive to restructure the company’s financial, the subordinated loans granted by MSIP Goldfinch BV to finance the acquisitions referred to above were paid off by means of a capital increase funded by the offset of accounts the outstanding debt , fully allotted to the sole shareholder of the company MSIP Violin BV.



Favorably received in capital markets

In the second half of 2013, Madrileña Red de Gas made its debut on the European capital markets with two bond issuances, to a value of €500 million and €275 million, maturing in 2018 and 2023, respectively. The robustness of the company’s creditworthiness is borne out by the fact that both issuances qualified for investment-grade ratings from two international credit rating agencies, Standard & Poor’s and Fitch. The

bondholders, including financial institutions that manage the assets and pensions of thousands of European savers – some of which are based in Spain – have become long-term partners of MRG, sharing in the company’s earnings. The proceeds of the bond issues help finance sustained growth for the benefit of present and future generations.



This version of our report is a free translation of the original, which was prepared in Spanish. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.

AUDIT REPORT ON THE ANNUAL ACCOUNTS

To the Sole Shareholder of Madrileña Red de Gas, S.A.U.:

1. We have audited the annual accounts of Madrileña Red de Gas, S.A.U. consisting of the balance sheet at 30 June 2014, the income statement, the statement of changes in equity, the cash flow statement and the related notes for the year then ended. The Company's Directors are responsible for the preparation of these annual accounts in accordance with the financial reporting framework applicable to the entity (as identified in Note 3 to the accompanying annual accounts), and in particular, with the accounting principles and criteria included therein. Our responsibility is to express an opinion on the annual accounts taken as a whole, based on the work performed in accordance with legislation governing the audit practice in Spain, which requires the examination, on a test basis, of evidence supporting the annual accounts and an evaluation of whether their overall presentation, the accounting principles and criteria applied and the estimates made are in accordance with the applicable financial reporting framework.
2. As stated in the Spanish Companies Act and in the Spanish Accounting Standards, the Company must disclose in the accompanying notes to the accounts the salaries, per diems and remuneration of any type as well as any advances, loans or guarantees given or obligations made in the area of pensions and life insurance policies to the Senior Management of the Company during the year. Given the small number of persons receiving these benefits and the confidential nature of the latter, the Company has not disclosed this information in the accompanying notes to the annual accounts. Also, our audit opinion on the 2013 annual accounts contained a qualification for this matter.
3. In our opinion, except for the qualification set out in paragraph above, the accompanying annual accounts for 2014 present fairly, in all material respects, the equity and financial position of Madrileña Red de Gas, S.A.U. at 30 June 2014 and the results of its operations and cash flows for the year then ended in accordance with the applicable financial reporting framework, and in particular, with the accounting principles and criteria included therein.
4. The accompanying Directors' Report for 2014 contains the explanations which the Directors consider appropriate regarding the Company's situation, the development of its business and other matters and does not form an integral part of the annual accounts. We have verified that the accounting information contained in the Directors' Report is in agreement with that of the annual accounts for 2014. Our work as auditors is limited to checking the Directors' Report in accordance with the scope mentioned in this paragraph and does not include a review of information other than that obtained from the Company's accounting records.

PricewaterhouseCoopers Auditores, S.L.

Originally signed by Juan Manuel Anguita Amate
Audit Partner

July 23, 2014

PricewaterhouseCoopers Auditores, S.L., Torre PwC, Pº de la Castellana 239 B, 28046 Madrid, España
Tel.: +34 915 684 400 / +34 902 021 111, Fax: +34 913 083 566, www.pwc.com/es

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Calle Virgilio, 2-B
28223 - Pozuelo de Alarcón
Madrid, Spain
T (+34) 902 330 150

www.madrilena.es