

Ukraine:
Electricity

Sector Update

Alexander Paraschiy
ap@con-cap.com
+ 380 44 206 83 70



CONCORDE CAPITAL

Electricity Generation

Gearing Up For The Hot Season

Companies Covered:

Centrenerg (CEEN)
Dniproenerg (DNEN)
Donbasenerg (DOEN)
Zakhidenerg (ZAEN)

September 26, 2005

Content

Summary	3
Electricity Tariffs Go Up:	4
Fuel Prices Grow	4
Tariff Surcharges	4
Debt Problem To Be Solved:	6
The Debt Offsetting Process	6
Possible Outcomes	7
Pricing Methodology Change	8
The Coal Deficit	9
Competition Issues	10
Performance Analysis	11
Analysis Of Prospects	12
Valuation:	13
Peer Comparison	13
DCF Modeling	14
Profiles:	
Donbasenergo	16
Dniproenergo	17
Zakhidenergo	18
Centrenergo	19

Summary

The debt problem in the energy sector is expected to be solved in 1H06. This will end the bankruptcy threat for **CEEN** and **DNEN** who have accumulated high amounts of payables. The debt offsetting process will also be beneficial for **DOEN** as it will be able to restructure long-term liabilities.

The electricity surcharge program for CapEx support has been in effect for **ZAEN** and **CEEN** since June 2005. This will decrease the companies' costs of capital and will allow them to modernize equipment. **DOEN** has been benefiting from a similar surcharge since 2002.

A change in electricity pricing principles, which is currently only temporary, but is likely to become permanent, will allow each GenCo to be paid for its electricity at the price it applies for, instead of a uniform price. This will be especially beneficial for **ZAEN** which manages the most expensive power units, and is sensitive to gas prices.

A deficit of light coal and a surplus of anthracite coal in Ukraine required the energy sector to place operating restrictions on light coal fueled energy units. As a result of the deficit, coal supplied to all of **ZAEN's** TPPs, one of **CEEN's** TPPs and one **DNEN** TPP increased in price, making these power plants less price competitive on the local energy market.

ZAEN continues to benefit from its export exclusivity.

DOEN is increasing its capacity utilization. Its main market advantage is relatively cheap fuel.

DNEN is looking forward to the debt offsetting process which will stop financial recovery process it is currently facing.

CEEN also hopes to solve its debt problem soon. The company started reconstruction of a power unit at Zmiiv TPP which will decrease operational costs in the future.

Valuation Summary

	Bloomberg	Sales 2004 USD mln	EBITDA margin 2004	Capacity Utilization 1H05	Price USD	EV/Sales	EV/EBITDA	Target price USD	Upside	Rec.
Centrenergo	CEEN UZ	307.0	15%	17.7%	0.80	1.24	8.5	0.82	3%	HOLD
Dniproenergo	DNEN UZ	326.2	13%	17.7%	66.50	0.90	7.1	99.00	50%	BUY
Donbasenergo	DOEN UZ	169.1	15%	30.2%	4.20	1.14	7.5	6.60	57%	BUY
Zakhidenergo	ZAEN UZ	366.4	6%	35.8%	26.00	1.00	17.4	34.00	31%	BUY
Vostokenergo	Not listed	433.9	12%	44.8%						Not Traded

Electricity Tariffs Go Up

Electricity tariffs grew 32% this summer due to:

In June 2005, electricity tariffs for all the thermal generation companies increased, on average by 32% since April. This increase in TPPs tariffs happened for the following reasons:

Fuel Prices Grow

A steady increase in coal prices (by 20% during Jan-Apr 2005) caused the growth of the gas component in the GenCos' fuel mix, while GenCos did not change their electricity prices.

Share of Gas In GenCos Fuel*

	7m04	7m05
CEEN	12%	17%
DNEN	12%	19%
DOEN	10%	11%
VSEN	9%	1%
ZAEN	25%	37%

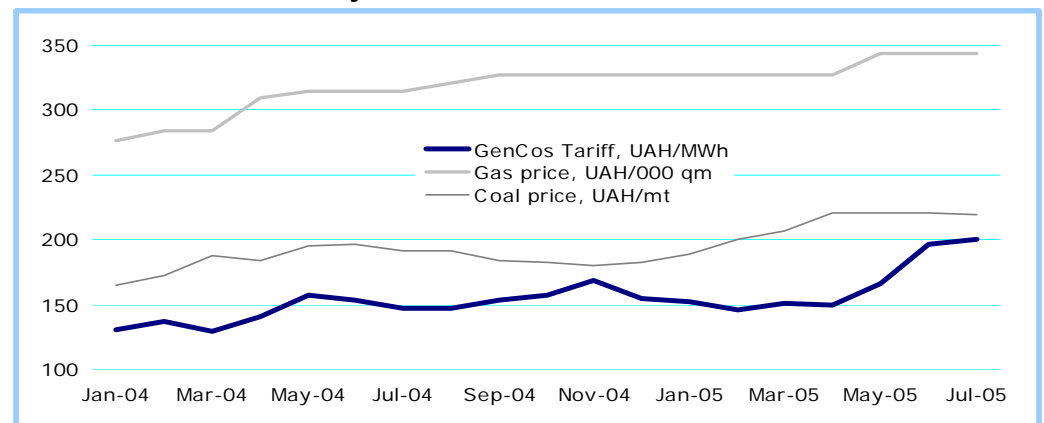
Source: Energo Business, Concorde Capital calculations
* % of gas in energy units in fuel mix of TPPs

Note that Vostokenergo (VSEN) has considerably reduced its usage of gas, as the company has a stable coal supply source from related coal mines.

the growth of fuel prices in 1H05

In May 2005, gas tariffs for GenCos increased by 5%. This caused electricity tariffs to grow for the companies that have a relatively high share of gas in their fuel mix: **CEEN** (15-20%) and **ZAEN** (35-40%). Gas prices also caused tariffs for other GenCos to go up, but this effect lagged behind gas price growth.

Prices for Fuel and Electricity



Source: Ministry of Fuel and Energy, Energo Business, Concorde Capital

Note: Tariffs are presented in local currency, not in USD, to avoid the effect of UAH appreciation by 6% in April 2005. The current UAH/USD rate is 5.05

An Increase Of Surcharges To Electricity Tariffs

investment surcharge growth

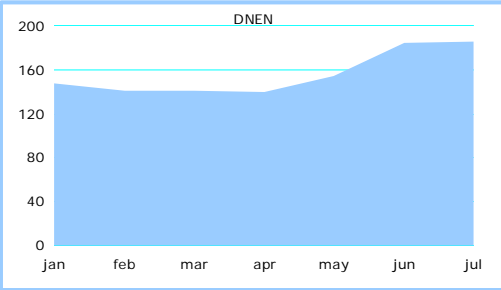
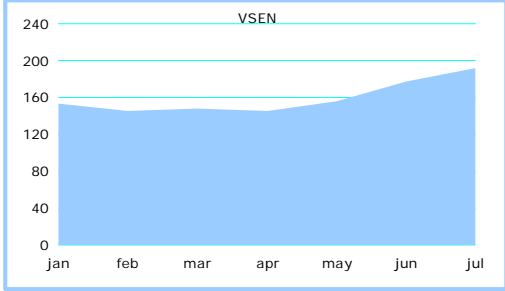
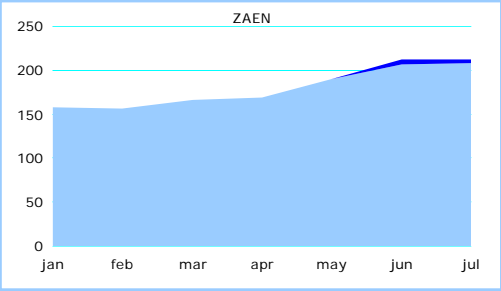
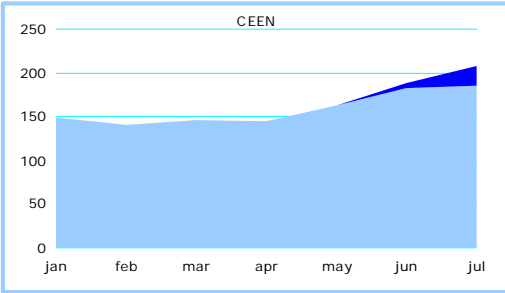
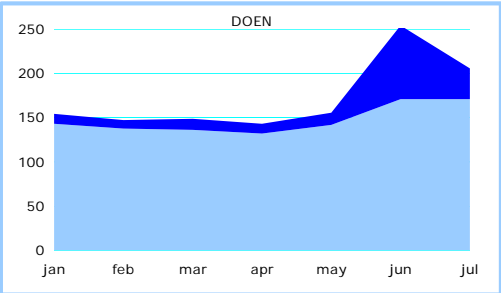
In June 2005, the previous government's decree to support GenCos' CapEx programs (described in GenCos initiating coverage) started to take effect. The NERC introduced special CapEx-oriented surcharges to the electricity tariffs of **ZAEN** and **CEEN** (this surcharge has been active for **DOEN** since 2002).

the introduction of dividend surcharges

In addition to the surcharge to support equipment upgrades, the NERC started to execute the new government's decree according to which, GenCos must pay out dividends for the state's stake from 1999-2003 (note that minority shareholders' rights for dividends are ignored here). This initiative is meant to increase the state budget. Unsurprisingly, the government found the most reliable source for dividend payouts: from the special electricity surcharge.

Both these surcharges considerably increased electricity tariffs for **DOEN**, **CEEN** and **ZAEN** in June-Aug 2005. Surcharges to **DNEN** tariffs are not applied.

Tariffs For GenCos, UAH/MWh



■ Tariff w/o CapEx and Dividend surcharges
■ CapEx and Dividend surcharges

Source: NERC, Energo Business, Concorde Capital estimations

Debt Problem To Be Solved

The poor past payment discipline by electricity consumers caused GenCos to accumulate a large amount of payables. This lack of capital, pushed some companies to the verge of the bankruptcy. **DOEN's** bankruptcy in 2002 forced the company to divest three TPPs out of five. **DNEN** is facing financial recovery procedures and **CEEN** is close to declaring bankruptcy.

Debt Accounts (July 2005) As % Of Sales 2004*

	A/P	A/R	Bad Debt Provision
CEEN	48%	88%	0%
DNEN	70%	31%	131%
DOEN	23%	84%	98%
VSEN	3%	16%	0%
ZAEN	13%	34%	0%

Source: company data, Concorde Capital calculations

* Note that **DNEN** and **DOEN** have cleared their accounts receivable by writing off considerable part of A/R as bad debt. **CEEN** did not so. But, we expect, **CEEN** will write off about 1/2 of its A/R as bad debt provision. **DOEN** transferred large amounts of payables to Other Long Term Liabilities (53% of sales 2004).

Legislation adopted in June to eliminate the debt problem

In June 2005, the Vekhovna Rada adopted the law *On Measures Directed To Ensure The Stable Work Of Fuel And Energy Sector Enterprises*, this legislation was designed to eradicate the debt problem.

According to the law, all the fuel and energy companies with outstanding debts on their accounts can participate in the procedure to have their debts reconciled and restructured. To be eligible companies must register to be included on a special list, which will then be approved by the Cabinet. All the GenCos which have high level of debts are very likely to be listed.

Any enterprise on the list of participants will have all bankruptcy procedures against it stopped for the next 9 months: this is especially important for **DNEN**, which financial recovery process cannot be completed during the last couple of years, and for **CEEN** which is almost bankrupt.

The Debt Offsetting Process

The process consists of three stages:

Debt reconciliation: During the first stage, energy companies will reconcile all debts and receivables with other parties. The energy companies will then mutually write off an equal amount of debts and receivables. The mutual reconciliation of debts will be held via debt offsetting accounts, controlled by energy sector regulators. The NERC will be responsible for managing these accounts. This stage will not last more than 9 months.

Debt write off:

The rest of the payment arrears are written off if they:

- emerged due to the liquidation of state or municipal enterprises
- emerged because of an insufficient amount of budget financing

Losses from writing off the listed payment arrears are to be compensated by special surcharges to electricity tariffs. The amount of compensation and the terms are to be approved by the government and NERC. Thus, the burden of writing off the debts for state companies will be shifted to electricity consumers.

The other debts must be written off according to Ukrainian legislation. This is especially important for **CEEN**, which has accumulated a high amount of A/R, most of which (about 1/2) can be written off without compensation.

Debt restructuring: During this stage, all debts left after the reconciliation process will be restructured, with the agreement of the debtor. The restructuring period for the debts between state-controlled enterprises (which is the case for all the GenCos which are listed on stock market) is 10 years.

Costs of debt restructuring to be shouldered by consumers

Again the funds for repayment will not come from the companies' profits, but from a special surcharge to electricity tariffs. Such tariff surcharges will be adopted by the regulators.

Possible Outcomes

The main outcome will be the release of GenCos from the burden of debt and thus, the companies will no longer be on the verge of bankruptcy.

CEEN and DNEN will enjoy 1-4% restructuring surcharge in tariffs

We believe after the debt reconciliation process and debt write off, **CEEN** will have payable amounts equal to 10% on annual sales on its account, and **DNEN** will have about 40% of its restructured debt in sales. This debt is expected to be restructured during the next 10 years, which will increase the average electricity tariff for **CEEN** by 1% and for **DNEN** by 4% during this period.

Pricing Methodology Change

The NERC has been testing a new methodology for GenCo electricity pricing, since late June 2005, which also made an impact on GenCos electricity tariff growth.

Old Electricity Pricing Methodology

All the power units which were ready for work, had to submit their electricity prices to the dispatcher each morning, and the dispatcher selected about 60% of the power units (the cheapest ones) to produce electricity. We call this process *Capacity Tender*. It works perfectly, because Ukraine has an excess supply of electric capacities.

All electricity produced at TPPs was priced equally until June 2005

The price *all* power units were paid for the electricity they supplied was the price of the most expensive maneuverable unit working (the so-called *marginal price of a generator's system*).

This pricing methodology has two important drawbacks:

This created incentives for GenCos to understate costs

- It created incentives to underestimate the electricity prices generated by the units of power plants in order to remain in work: if a power unit showed a lower price, it would remain in work, while it will be paid the *marginal price*, which is higher than the price it applied for.

To prevent such behavior, the regulator calculated the costs of electricity production by each energy unit itself, and punished the units which asked for a lower price. This process demanded additional effort from the regulators, which means additional costs.

- For **ZAEN** it was hard to regulate its price for electricity. Two out of three of **ZAEN's** power plants (Burshtyn and Dobrotvir), which supply electricity to UCTE countries, have some of the highest costs for electricity generation. However, their electricity price cannot be set as a *marginal price*, as they do not directly participate in the capacity tender. As a result, these power plants may be paid less than is needed to cover their costs.

To solve this problem, the NERC has a system of special surcharges for electricity prices, so that all the GenCos obtain about 20% more than the marginal price of the system. **ZAEN** gets special treatment here, as there are special electricity surcharges for those power plants which are working for UCTE.

The old pricing model made ZAEN's profits sensitive to cost of gas

Still, often these surcharges were not enough to allow **ZAEN** the same level of profitability that other GenCos have. This is most noticeable when gas prices go up, as **ZAEN** is the most sensitive to gas prices due to the high share of gas in its fuel mix.

Pricing Changes

In new pricing model, TPPs will get the prices they applied for

According to the NERC experiment, which started in late June, all the power units are paid according to the price they applied for, instead of the *marginal price*. This automatically prevents "dumping" due to the under-estimation of power unit costs, and makes payments for electricity more in line with each power unit's cost structure. New methodology is especially beneficial for **ZAEN's** power plants: now their profitability will be less dependent on gas prices fluctuations.

We expect the NERC's experiment to succeed, and in the future all the TPPs will be paid according to their applied price.

The Coal Deficit

The light coal deficit made the operation of 7 TPPs problematic

In the summer of 2005 Ukraine faced a light coal deficit, and had an excess supply of anthracite coal. TPP equipment is only designed for the consumption of one type of coal, and therefore, those power units which consume light coal, had a bad summer.

Coal Types Used By Thermal Power Plants

	Coal-fueled Capacity, GW	Coal Type		Coal-fueled Capacity, GW	Coal Type
CEEN			VSEN		
Zmiiv	2.15	anthracite	Zuiv	1.20	light
Uglegorsk*	1.20	light	Kurakhov	1.46	light
Trypillia	1.20	anthracite	Luhansk	1.40	anthracite
DNEN			ZAEN		
Kryvyi Rih	2.82	anthracite	Ladyzhyn*	1.80	light
Prydniprovsk	1.74	anthracite	Burshtyn	2.30	light
Zaporizhia*	1.20	light	Dobrotvir	0.50	light
DOEN					
Slaviansk	1.75	anthracite			
Starobeshev	0.72	anthracite			

Source: *Energo Business, Concorde Capital calculations*

* These power plants could become less price – competitive

In order to solve the problem, electricity market regulators decided to limit the work of power units working on light coal, and increase the use of TPPs working on anthracite over the summer. This allows them to correct the supply/demand disproportion between the two types of coal and increase the stock of light coal at the TPPs. This allows them to be better prepared for the hot season, the winter months, when demand for energy skyrockets.

The work of 5 TPPs was restricted by the coal deficit

As a result, the work of Zaporizhia TPP (**DNEN**), Dobrotvir TPP (**ZAEN**), Zuiv and Kurakhov TPPs (**VSEN**) and Uglegorsk TPP (**CEEN**) was limited to their lowest level: not more than two power units at each TPP, working at their minimum possible capacity. Note there was no limit placed on two of **ZAEN**'s power plants: Burshtyn and Dobrotvir, as these two TPPs have special exporter status.

Light-coal fueled TPPs may become less price competitive

The limitation on TPPs has not considerably changed their working schedule, as most of TPPs work at minimum capacity in summer. However, the biggest drawback for light coal-fueled TPPs is that their main fuel has become more expensive than coal for other TPPs, so that these power plants may become less price competitive. Note that this will not be the case for TPPs operated by Vostokenergo, as these TPPs have related companies which supply them with relatively cheap coal.

Competition Issues

Commissioning Of Dnister PSPP Postponed

Currently TPPs, which supply the most expensive electricity to Ukraine's wholesale electricity market, have no competitors in their market segment: the supply of maneuverable capacity. The only competitors to TPPs are hydro power stations which are able to work in a changeable mode. However, HPPs can supply only about 30% of the needed maneuverable capacity in Ukraine, the rest of the changeable capacity must be supplied by TPPs. Thus, the ability to change their capacity fast is the main competitive advantage for TPPs in Ukraine.

PSPPs will be significant competitors to TPPs

The commissioning of hydro pump storage plants is expected to partially crowd out TPPs from the segment of maneuverable electric capacity (**DOEN** report of July 4). According to our estimates, the commissioning of 900 MW Dnister PSPP and 300 MW capacity at Tashlyk PSPP could substitute three TPPs in the maneuverable segment. Thus, commissioning pump storage capacities (expected in late 2005 - mid 2006) can negatively affect demand for electricity generated at TPPs.

But not until 2008

However, according to the latest information announced by the Minister of Fuel and Energy, the first units of Dnister PSPP (325 MW) will not be operational until 2008. The date of Tashlyk PSPP's launch is also unknown. Thus, TPPs will remain the most important source for maneuverable electricity in Ukraine for at least the next three years.

Export Changes: Less East, More West

Export to Russia halted in June 2005

Since the NERC forbid Energoatom (the nuclear power plant operator) to sell electricity at low tariffs to Russia in July 2005, export has stopped. This has reduced the electricity generation of Energoatom, but has not affected other electricity generators. However, if exports do not resume shortly, Energoatom could potentially crowd out GenCos from the market of fixed (base load) capacity in the winter period, so that GenCos will work in the base load mode only at the level which will allow them produce the needed level of changeable capacity.

ZAEN is increasing its export to UCTE

Again, **ZAEN** is unlikely to be affected by export crisis, as most of its capacities are working isolated from Ukrainian energy system. Moreover, the company is increasing its exporting capacity from 500 MW to 520 during the second half of August and 550 during September. This will allow ZAEN to additionally produce about 50 GWh of electricity for export during August-September.

The Commissioning Of DOEN's New Unit Postponed

Cost related to fire at Starobeshev TPP must be paid by the installing contractor

The reconstructed energy unit at Starobeshev TPP, which is to become the first energy unit using efficient, cheap and environment-friendly CFB technology will be commissioned in mid 2006, instead of September 2005. The main reason for the postponement was a fire which damaged the CFB boiler when it was being tested.

DOEN is unlikely to suffer seriously because of the fire, as all the repair costs will be paid by the company that installed the equipment. However, the postponement of the new cheap energy unit will result in higher costs for electricity production in 2H05-1H06. Still, **DOEN's** power plants which use relatively cheap anthracite coal, will remain among the best positioned for price competition.

Performance Analysis

Centrenerg	1H03	2H03	1H04	2H04	1H05
Equip. Utilization	25.6%	23.4%	18.8%	19.4%	17.7%
Sales USD mln	211.0	204.8	170.9	197.5	194.0
EBITDA margin	3%	9%	8%	12%	7%
Net margin	-9%	2%	0%	-3%	1%

Dniproenergo	1H03	2H03	1H04	2H04	1H05
Equip. Utilization	21.4%	22.0%	18.6%	18.1%	17.7%
Sales USD mln	161.6	173.8	154.9	171.3	171.5
EBITDA margin	1%	81%	9%	21%	12%
Net margin	-12%	53%	-4%	1%	0%

Donbasenergo	1H03	2H03	1H04	2H04	1H05
Equip. Utilization	36.6%	41.5%	29.0%	30.0%	30.2%
Sales USD mln	101.9	101.1	84.9	84.2	93.7
EBITDA margin	30%	-23%	11%	18%	15%
Net margin	13%	-39%	0%	0%	7%

Vostokenergo	1H03	2H03	1H04	2H04	1H05
Equip. Utilization	41.3%	43.9%	34.6%	39.0%	44.8%
Sales USD mln	200.1	196.0	155.4	276.1	224.8
EBITDA margin	5%	0%	7%	15%	17%
Net margin	5%	-3%	7%	11%	12%

Zakhidenergo	1H03	2H03	1H04	2H04	1H05
Equip. Utilization	31.8%	31.7%	33.3%	32.9%	35.8%
Sales USD mln	200.1	196.0	155.4	276.1	224.8
EBITDA margin	11%	13%	9%	3%	7%
Net margin	2%	-1%	6%	1%	1%

Source: company data, Energo Business, Concorde Capital calculations

VSEN and **ZAEN** are the leaders in capacity utilization. **VSEN** supplies electricity at the lowest price, so its power plants are utilized more. **ZAEN** is head and shoulders above the competition when it comes to access to internal electricity market, because of its export-oriented capacities. It is the most stable company for electricity output and capacity utilization. **DOEN** is recovering after a 2004 drop in production. It also is able to supply relatively cheap electricity to the market. **DNEN** and **CEEN** are becoming less competitive.

According to **CEEN** management, the company is accumulating fuel to increase its electricity output in winter 2005-2006. But, at the moment we do not see significant competitive advantages for **CEEN** compared to other GenCos, which might allow the company to improve its situation.

Due to relatively low fuel costs, **VSEN** and **DOEN** have the highest EBITDA margins among GenCos.

The high fuel costs of **ZAEN** and **CEEN** make their EBITDA margin the lowest in the sector. We expect that change in pricing policy (described on page 8) will slightly increase the profitability of these companies in 2H05.

GenCos Prospect Analysis

	CEEN	DNEN	DOEN	VSEN	ZAEN
Competitive Advantages:					
Fuel Costs	-		+	++	--
Exclusive Advantages			+		++
Equipment Utilization	-	-		+	+
Other issues:					
Production Costs	-		+	+	-
Repair and Development		-	+	+	+
Debt/Bankruptcy		?			
Risks Of TPPs Expropriation				-	
Long-term market position sustainability		-	+	+	
Overall Rank	-	-	+	++	+

Despite the fact that **CEEN** and **DNEN** have become more attractive for investment since our initiating report, as their debt problem is likely to be solved, the companies still have problems with equipment utilization. Moreover, **DNEN** is the least suitably positioned among GenCos in terms of reconstruction: its current CapEx is the lowest, and its future CapEx is expected to be the same. In addition, despite debt restructuring on the horizon, **DNEN's** high level of accumulated payable debts still makes bankruptcy a realistic threat.

The most promising company in the sector is Vostokenergo (**VSEN**). Its main advantages are access to cheap coal and high level of planned equipment upgrades in the near future. Unfortunately, **Vostokenergo** is a fully private company and is not traded on the stock market.

ZAEN's exclusive export status to UCTE is the main advantage the company has. It will keep this exclusive status for the next 5 years. Then the energy system of Ukraine will be connected to the UCTE, and all the other power plants in Ukraine will be able to supply their electricity to the west, and all **ZAEN's** power plants will be forced to compete to supply its energy in line with other Ukrainian TPPs. **ZAEN's** connection to UCTE gives it another important advantage, as these TPPs are the first targets for equipment improvements in order to be closer to European Union standards.

DOEN has completely recovered from its bankruptcy, and now is increasing its equipment utilization. The operation of only one unit at Slaviansk TPP makes this power plant unique, as its work cannot be stopped by the dispatcher. Relatively low fuel costs due to the usage of a cheap type of coal and a small share of gas gives the company good future prospects.

Valuation

Peer Comparison

The closest peers for Ukrainian GenCos are Russian thermal power plants (GRESs). Compared to Russian GRESs, Ukrainian GenCos look significantly undervalued. However, we will treat the comparison of GenCos with GRESs cautiously, as stock values for Russian peers were highly volatile during the last half of the year.

Change In GRESs' Market Prices

	Growth Since May 13, 2005*	1M Growth
Cherepets GRES	46%	39%
Kostroma GRES	68%	39%
Stavropol GRES	25%	5%
Pechorsk GRES	84%	41%
Konakovo GRES	69%	53%

Source: RTS

* the date of last GenCos valuation by GRES (initiating coverage)

GenCos vs Russian GRESs

	Sales USD mln		EBITDA margin		Capacity Utiliz.
	2004	1H05*	2004	1H05	2004
Cherepets GRES	70.0	79.9	6.9%	7.4%	19%
Kostroma GRES	199.0	275.6	11.2%	9.4%	58%
Stavropol GRES	164.6	206.4	9.9%	10.8%	44%
Pechorsk GRES	54.2	64.2	11.4%	14.6%	56%
Konakovo GRES	137.1	130.7	5.1%	13.3%	30%
CEEN	307.0	388.0	14.7%	7.4%	19%
DNEN	326.0	343.2	12.6%	11.6%	18%
DOEN	169.1	187.4	15.2%	14.8%	30%
ZAEN	366.0	449.6	5.7%	6.9%	33%

Source: company data, Concorde Capital estimates

* annualized data

While Russian TPPs are more utilized than GenCos, they have lower profitability because of their lower electricity tariffs. In general, Russian and Ukrainian power generators should be valued similarly by the market. However, because of the significant growth of market capitalization for Russian peers, which we do not believe to be justified, we treat the potential upsides of GenCos compared to GRESs cautiously.

Valuation Summary

	Price	MCap	EV	EV/S		EV/EBITDA	
	USD	USD mln	USD mln	2004	1H05*	2004	1H05*
Cherepets GRES	168.00	84.9	88.6	1.27	1.11	18.3	15.1
Kostroma GRES	0.25	687.2	708.6	3.56	2.57	31.9	27.3
Stavropol GRES	205.00	278.5	298.4	1.81	1.45	18.3	13.4
Pechorsk GRES	0.14	139.9	146.0	2.69	2.27	23.7	15.6
Konakovo GRES	1.00	404.0	410.4	2.99	3.14	58.8	23.6
average				2.47	2.11	30.2	19.0
median				2.69	2.27	23.7	15.6
CEEN	0.8	277.1	380.6	1.24	0.98	8.5	13.3
DNEN	66.5	260.9	294.7	0.90	0.86	7.1	7.4
DOEN	4.2	115.9	192.7	1.14	1.03	7.5	6.9
ZAEN	26.0	332.6	365.7	1.00	0.81	17.4	11.8
average				1.07	0.92	10.1	9.8
median				1.07	0.92	8.0	9.6
Implied GenCos' Upsides:							
To average				130%	129%	198%	93%
To median				152%	147%	197%	62%

Source: RTS, company data, Concorde Capital estimates

Thus, we will rely more on our DCF model valuing GenCos.

DCF Modeling

Key Assumptions:

Our electricity output forecast for GenCos is in line with their competitive advantages and market sustainability. **DOEN** and **ZAEN** will increase their electricity production level more rapidly compared to **CEEN** and **DNEN** during the next couple of years. In the long term, GenCo cash flows will grow at a 2.0% rate.

As the government's program giving investment-oriented surcharges to GenCos electricity tariffs starts to be implemented, these surcharges will significantly decrease the costs of capital for GenCos. The electricity surcharge program (refer to GenCos initiating coverage of May 13 for more details) will cover 44-64% of the costs for GenCos to repair equipment during 2005-2010. In an analytical sense, these surcharges must be treated as a loan with a zero interest rate, or as additional equity with zero cost. This zero costs component in capital structure (we attribute them as investment obligations, part of equity) will reduce WACC to 6.6-7.6% by 2014. WACC to perpetuity is 12%.

In order to reflect correctly working capital changes to GenCos, we re-classified as long-term liabilities part of the accounts payable for **DOEN**, **DNEN** and **CEEN** which reflect delayed payments for electricity.

More detailed information and DCF models for each company can be found in the profiles below.

Profiles

Current Price

Target Price

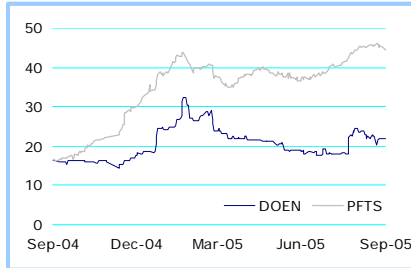
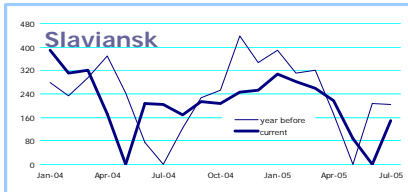
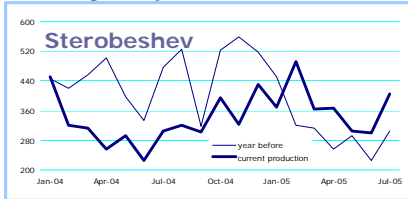
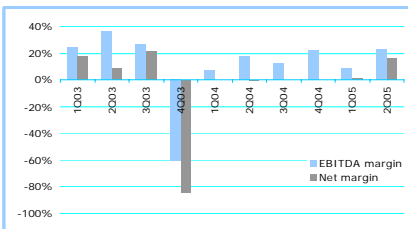
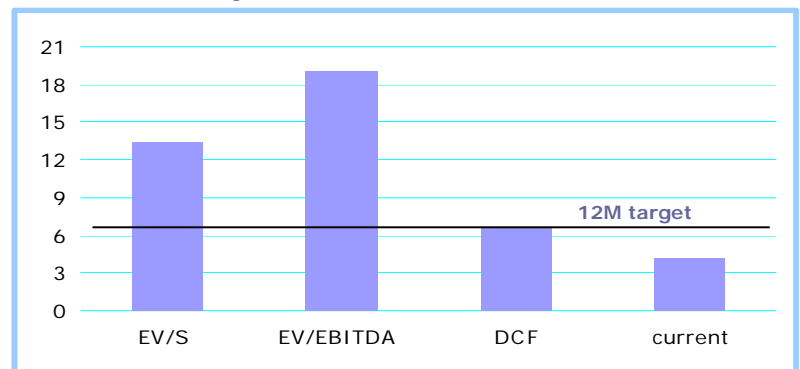
USD 4.2**USD 6.6****Donbasenergo (DOEN): BUY**

The company finished an intensive CapEx program for the reconstruction of Sterebeshev TPPs' unit #4, but currently cannot use the benefits of this reconstruction because of a fire during the unit's testing. However, according to the management, the fire has not changed the company's plans for electricity production in 2005. DOEN plans to start reconstruction of Slaviansk TPPs' unit #3.

DOEN has no units consuming deficit types of coal, which makes it better positioned in the price competition between TPPs.

The company re-classified its payables as long-term liabilities in 2003-2004. It is now beyond the threat of bankruptcy. Participation in the program of debt offsetting will allow it to successfully reduce its long term debt (which is 53% of sales 2004) via reconciliation and restructuring.

DCF and peer comparison show a significant upside for DOEN's stock. We confirm our BUY recommendation on DOEN, increasing the 12m target price to USD 6.6 (implying a 57% upside).

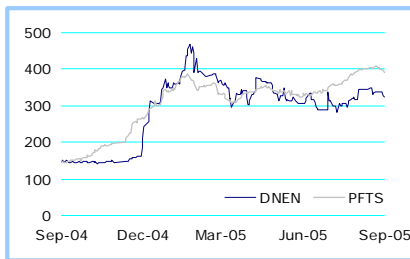
DOEN Mid Market, UAH**Monthly Output Per Plant, GWh****Profitability****Valuation Summary, USD****DCF Summary**Valuation date **26-Sep-06**

For the purposes of forecasting local currency is used (mln)

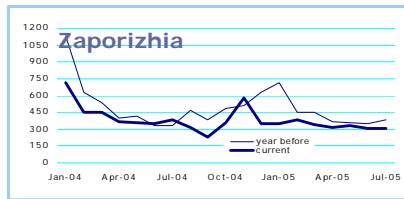
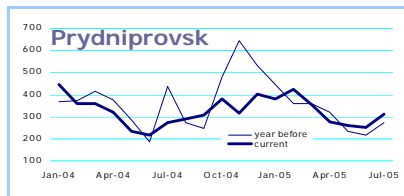
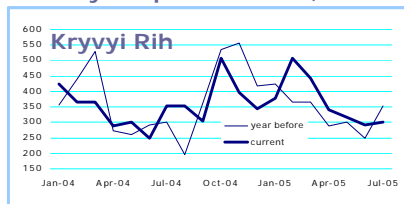
	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	
EBITDA	149	184	226	277	302	316	326	315	328	337	
EBIT	52	69	103	150	168	179	184	171	182	189	
Tax Rate	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	
Taxed EBIT	39	51	78	113	126	134	138	129	137	142	
Plus D&A	97	116	122	127	134	137	141	144	146	148	
Less CapEx	(150)	(157)	(162)	(180)	(185)	(192)	(170)	(155)	(150)	(150)	
Less change in OWC	(11)	(1)	(1)	(1)	(0)	(13)	(2)	(7)	(7)	(1)	
FCFF	(25)	9	37	59	75	67	108	110	125	138	
WACC	12.6%	12.7%	12.5%	11.5%	10.4%	9.1%	8.4%	7.5%	6.6%	6.6%	
WACC To Perpetuity										12%	
Terminal Value										1 412	
Firm Value		1 094								Portion Due To TV	62.5%
Less Net Debt		302								Perpetuity Growth Rate	2.0%
Equity Value		793								Implied exit EBITDA multiple	4.2x
DCF - based 12m price		6.57									
Current stock price		4.20									
Upside		56%									

Current Price Target Price
USD 66.5 **USD 99.0**

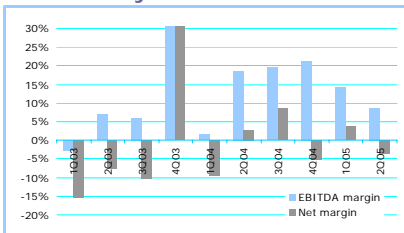
DNEN Mid Market, UAH



Monthly Output Per Plant, GWh



Profitability



Dniproenergo (DNEN): BUY

We believe the company will be able to reconcile, restructure its debts, and complete the financial recovery process in the near future.

Unlike other GenCos, DNEN still does not obtain surcharges for its power units. Mass reconstruction is expected to start in 2008.

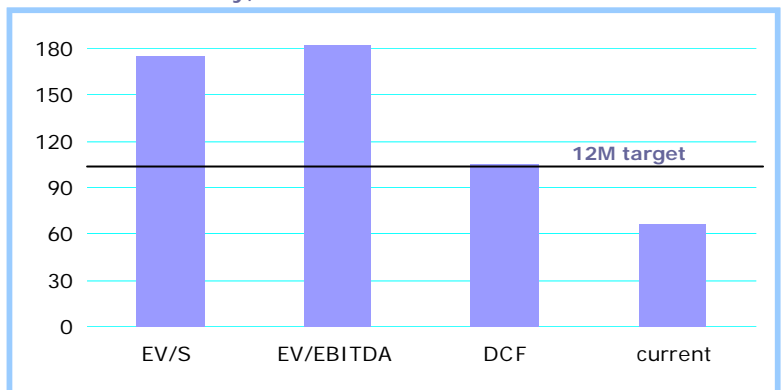
The company has seen a steady decrease of its capacity utilization over the last several years. In 2005 utilization will stabilize, and start growing from 2009.

Zaporizhia TPP of DNEN cannot utilize its three gas-fueled units of total capacity 2.4 GW because of the relatively high gas price and low demand for base load capacity supplied by these units. In addition, the coal-fueled units of Zaporizhia TPP could be price uncompetitive because it uses light coal.

The company is traded with a significant discount to its Russian and Ukrainian peers.

We factored higher risks explicitly in our DCF model, increasing DNEN's company-specific risk to 5% in 2005. Still, our model suggests a substantial upside for the stock. We confirm our BUY recommendation and upgrade the target price to USD 99, which implies a 50% upside.

Valuation Summary, USD



DCF Summary

Valuation date **26-Sep-06**

For the purposes of forecasting local currency is used (mln)

	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	293	348	372	503	525	549	454	461	465	466
EBIT	117	172	197	319	330	350	251	255	258	259
Tax Rate	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBIT	87	129	148	239	248	262	188	192	193	194
Plus D&A	176	175	175	185	194	199	204	206	207	208
Less CapEx	(108)	(160)	(208)	(302)	(310)	(308)	(241)	(231)	(218)	(208)
Less change in OWC	(0)	(2)	(5)	(5)	(3)	(5)	(6)	(6)	(5)	(6)
FCFF	155	142	109	117	130	149	145	161	177	188
WACC	17.6%	15.6%	13.5%	10.0%	8.5%	7.7%	7.3%	7.2%	7.2%	7.0%
WACC To Perpetuity										12%
Terminal Value										1,919
Firm Value		2,036								47.7%
Less Net Debt		41								2.0%
Equity Value		1,995								4.1x
DCF-based 12m price		99.68								
Current stock price		66.50								
Upside		50%								

Current Price

USD 26

Target Price

USD 34

Zakhidenergo (ZAEN): BUY

Two of the company's TPPs are insulated from competition on the local market and remain the most stable power plants in Ukraine. Another TPP (Ladyzhyn) which uses a deficit type of coal, is likely to decrease its output slightly.

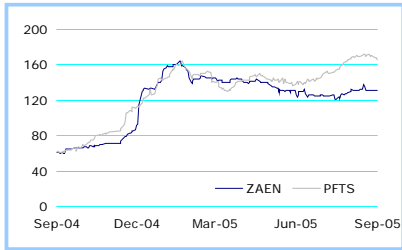
Burshtyn power plant increased its export capacity during August-September 2005, so that its forecasted electricity output grew this year.

The company can increase profitability due to changes in pricing methodology: now electricity generated at ZAEN's power plants will be priced independently from the other power plants in Ukraine.

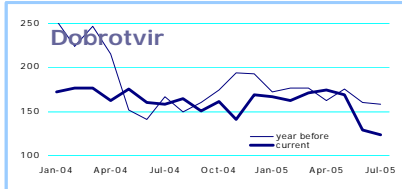
Since June 2005 ZAEN has started obtaining a special investment surcharge which will partially compensate its costs of construction and reconstruction of power units.

The company is undervalued by the market, as our valuation suggests. We increase ZAEN's target price to USD 34, (which implies a 31% upside) and reiterate our BUY recommendation.

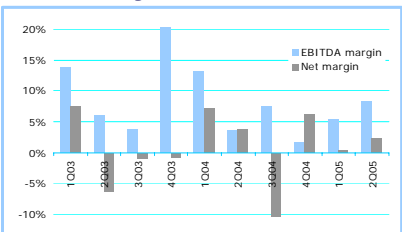
ZAEN Mid Market, UAH



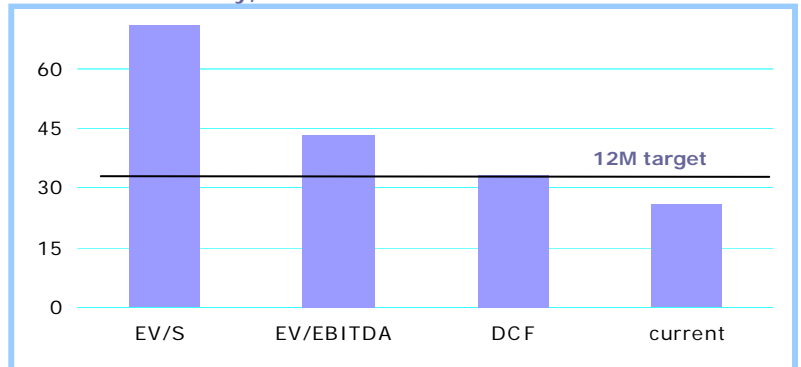
Monthly Output Per Plant, GWh



Profitability



Valuation Summary, USD



DCF Summary

Valuation date **26-Sep-06**

For the purposes of forecasting local currency is used (mln)

	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	229	501	611	636	609	577	552	549	566	584
EBIT	135	395	486	491	446	397	356	341	348	355
Tax Rate	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBIT	101	296	364	368	334	298	267	256	261	267
Plus D&A	94	106	125	145	164	181	196	208	218	228
Less CapEx	(107)	(280)	(391)	(394)	(372)	(335)	(276)	(253)	(232)	(228)
Less change in OWC	(11)	(3)	(1)	(8)	(5)	(4)	(2)	1	(1)	(1)
FCFF	76	118	98	111	122	140	185	212	246	266
WACC	17.1%	14.9%	12.8%	11.3%	10.3%	9.4%	9.0%	8.4%	7.5%	7.3%
WACC to Perpetuity										12%
Terminal Value										2,713
Firm Value		2,310								55.7%
Less Net Debt		164								2.0%
Equity Value		2,146								4.6x
DCF-based 12m price, USD		33.23								
Current stock price, USD		26.00								
Upside		28%								

Current Price

Target Price

USD 0.80

USD 0.82

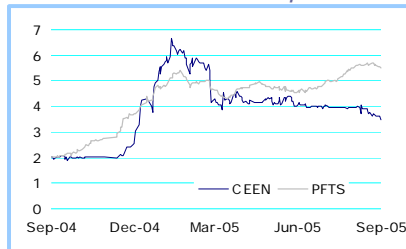
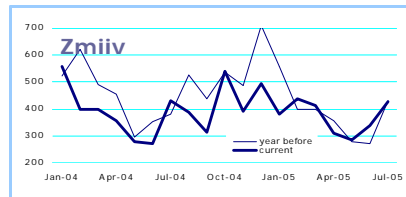
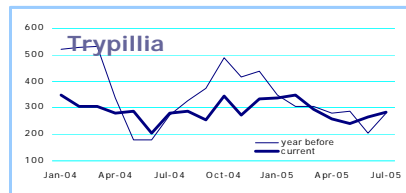
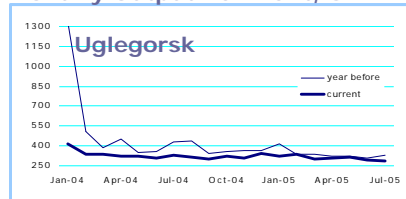
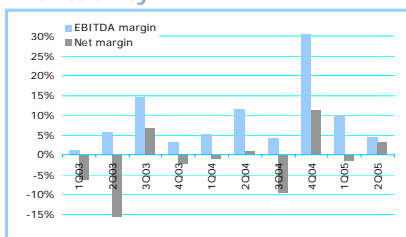
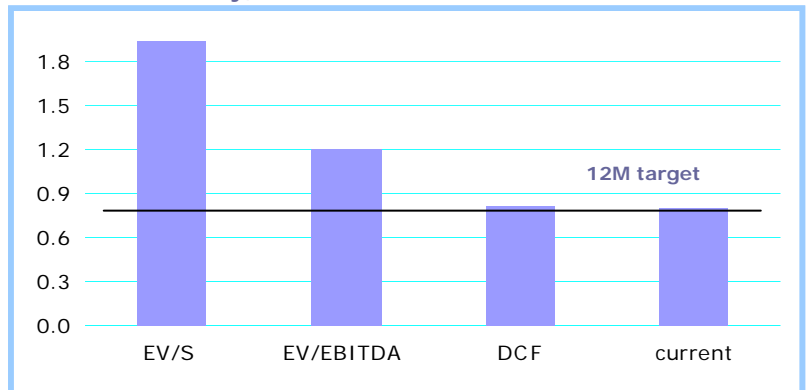
Centrenergó (CEEN): HOLD

The possibility of CEEN facing bankruptcy has significantly decreased since the adoption of the law on debt offsetting.

The company possesses 3 GW of idle capacities: 0.6 GW of gas-fueled capacities at Trypillia TPP (they are price uncompetitive to coal-fueled power units) and 2.4 GW of base-load power units at Ulegorsk TPP. Note that Ulegorsk TPP has been working near its minimum level for the last two years. The reason for this is limited supply of coal and the high costs of electricity production at the power plant. CEEN's power plants lack of competitiveness is the main reason for the decreased capacity utilization.

The company started obtaining surcharges aimed at partially compensating for the costs of the reconstruction of Zmiiv TPP's power unit #8. Reconstruction will increase the competitiveness and stability of the power plant in the midterm.

While peer multiple valuation suggests an upside for CEEN stock, our DCF shows that the company is valued fairly by the market. We have increased CEEN's target price to USD 0.84, and reiterate our HOLD recommendation.

CEEN market Quotes, UAH**Monthly Output Per Plant, GWh****Profitability****Valuation Summary, USD****DCF Summary**Valuation date **26-Sep-06***For the purposes of forecasting local currency is used (mn)*

	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	288	552	607	641	731	751	519	457	465	473
EBIT	154	394	437	447	516	520	274	201	197	194
Tax Rate	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBIT	115	296	328	335	387	390	206	151	148	146
Plus D&A	134	158	170	194	214	231	245	256	268	278
Less CapEx	(132)	(304)	(377)	(385)	(416)	(391)	(296)	(283)	(284)	(276)
Less change in OWC	(1)	(4)	(6)	(3)	(2)	(4)	(6)	(5)	(1)	(2)
FCFF	116	146	115	141	184	226	149	119	131	146
WACC	16.5%	15.2%	13.3%	11.7%	10.4%	9.3%	8.9%	8.1%	7.7%	7.6%
WACC To Perpetuity										12%
Terminal Value										1 487
Firm Value		1 727								40.1%
Less Net Debt		192								Perpetuity Growth Rate
Equity Value		1 535								2.0%
DCF-based 12m price, USD		0.81								Implied exit EBITDA multiple
Current stock price, USD		0.80								3.1x
Upside		1%								

Concorde Capital
72 Chervonoarmiyska St.
2nd entry, 6th floor
Kiev 03150, UKRAINE

Tel: +380 44 206 8370
Fax: +380 44 206 8366
www.concorde.com.ua
office@con-cap.com

CEO

Igor Mazepa

im@con-cap.com

Chief Operating Officer

John David Suggitt

js@con-cap.com

Director, International Equity Sales

Peter Bobrinsky

pb@con-cap.com

Equity Sales

Marina Martirosyan

Lucas Romriell

Alexis Stenbock-Fermor

mm@con-cap.com

lr@con-cap.com

asf@con-cap.com

Director of Research

Konstantin Fisun, CFA

kf@con-cap.com

Utilities (Telecom, Energy)

Alexander Paraschiy

ap@con-cap.com

Oil & Gas, Pipes, Non-Ferrous Metals

Andriy Gostik

ag@con-cap.com

Ferrous Metals

Viktor Koval

vk@con-cap.com

Machine Building, Chemicals

Olga Pankiv

op@con-cap.com

Banking & Macroeconomics

Alexander Viktorov

av@con-cap.com

Editor

Nick Piazza

np@con-cap.com

Disclaimer

This report has been prepared by Concorde Capital investment bank for informational purposes only. Concorde Capital does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that Concorde Capital may have a conflict of interest that could affect the objectivity of this report.

Concorde Capital, its directors and employees or clients may have or have had interests or long or short positions in the securities referred to herein, and may at any time make purchases and/or sales in them as principal or agent. Concorde Capital may act or have acted as market-maker in the securities discussed in this report. The research analysts, and/or corporate banking associates principally responsible for the preparation of this report receive compensations based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors, firm revenues and investment banking revenues.

The information contained herein is based on sources which we believe to be reliable but is not guaranteed by us as being accurate and does not purport to be a complete statement or summary of the available data. Any opinions expressed herein are statements of our judgments as of the date of publication and are subject to change without notice. Reproduction without prior permission is prohibited. © 2005 Concorde Capital