

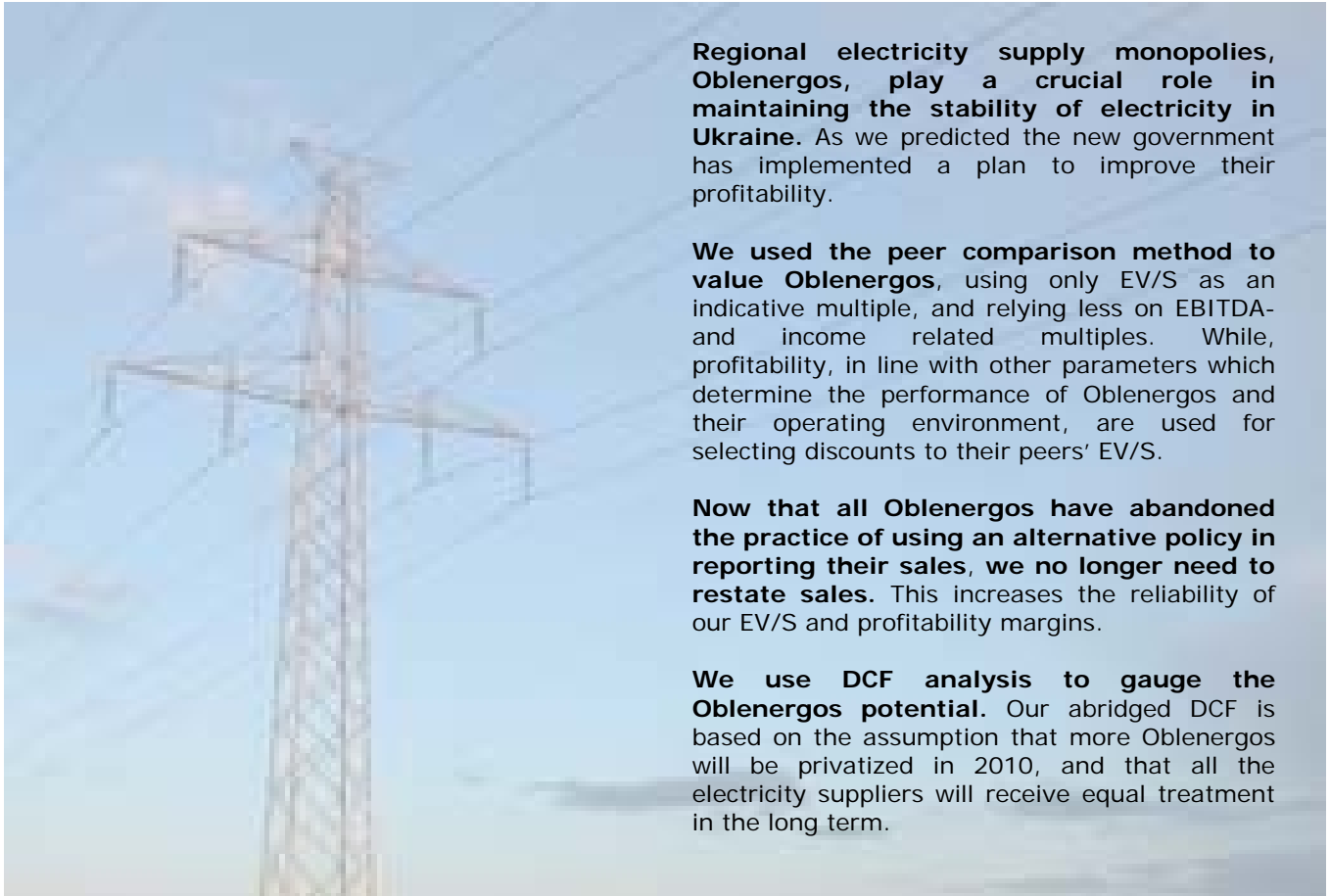


# Oblenergos

## Awakening

### Companies Covered:

Chernihivoblenergo	(CHEON)
Dniprooblenergo	(DNON)
Kharkivoblenergo	(HAON)
Khersonoblenergo	(HOEN)
Khmelnitskoblenergo	(HMON)
Kirovohradoblenergo	(KION)
Krymenergo	(KREN)
Lvivoblenergo	(LVON)
Poltavaoblenergo	(POON)
Prykarpatooblenergo	(PREN)
Sevastopolenergo	(SMEN)
Sumyoblenergo	(SOEN)
Ternopiloblenergo	(TOEN)
Vinnitsaoblenergo	(VIEN)
Volynoblenergo	(VOEN)
Zakarpatooblenergo	(ZOEN)
Zaporizhiaoblenergo	(ZAON)
Zhytomyrooblenergo	(ZHEN)



**Regional electricity supply monopolies, Oblenergos, play a crucial role in maintaining the stability of electricity in Ukraine.** As we predicted the new government has implemented a plan to improve their profitability.

**We used the peer comparison method to value Oblenergos,** using only EV/S as an indicative multiple, and relying less on EBITDA- and income related multiples. While, profitability, in line with other parameters which determine the performance of Oblenergos and their operating environment, are used for selecting discounts to their peers' EV/S.

**Now that all Oblenergos have abandoned the practice of using an alternative policy in reporting their sales, we no longer need to restate sales.** This increases the reliability of our EV/S and profitability margins.

**We use DCF analysis to gauge the Oblenergos potential.** Our abridged DCF is based on the assumption that more Oblenergos will be privatized in 2010, and that all the electricity suppliers will receive equal treatment in the long term.

#### Summary: Tradable Oblenergos

Name	Ticker	Price USD	MCap USD mln	EV USD mln	Sales USD mln	EBITDA margin	EV/S	Target USD	Upside	Rec.
Sevastopolenergo	SMEN	0.40	12.1	11.6	30.4	15%	0.38	0.73	83%	buy
Lvivoblenergo	LVON	0.17	38.8	54.7	114.9	12%	0.48	0.30	76%	buy
Volynoblenergo	VOEN	0.03	14.3	13.2	33.8	8%	0.39	0.05	67%	buy
Sumyoblenergo	SOEN	0.11	17.7	22	61.3	10%	0.36	0.16	45%	buy
Prykarpatooblenergo	PREN	0.26	20.7	32.5	75.1	16%	0.43	0.35	35%	buy
Ternopiloblenergo	TOEN	0.16	11.6	12.1	31.4	3%	0.39	0.21	31%	buy
Vinnitsaoblenergo	VIEN	7.00	9.3	10.3	63.4	6%	0.16	9.10	30%	buy
Khmelnitskoblenergo	HMON	0.20	29.6	29.8	51.6	7%	0.58	0.22	10%	buy
Kievlenergo	KIEN	1.55	162.5	192.6	310.8	6%	0.62	1.70	10%	buy
Dniiprooblenergo	DNON	37.62	219.9	218.7	721	1%	0.30	38.00	1%	hold
Poltavaoblenergo	POON	0.25	55.2	67.6	151.3	7%	0.45	0.25	0%	hold
Zhytomyrooblenergo	ZHEN	0.40	47.7	46.5	60.5	16%	0.77	0.29	-28%	sell
Kharkivoblenergo	HAON	0.30	61.6	58.7	180.9	-6%	0.32	0.21	-30%	sell
Zaporizhiaoblenergo	ZAON	1.00	107.6	105.6	276.5	2%	0.38	0.66	-34%	sell
Chernihivoblenergo	CHEON	0.40	41.8	51.3	57.3	10%	0.89	0.20	-50%	sell
Zakarpatooblenergo	ZOEN	0.24	21.2	23.2	45.5	5%	0.51	0.11	-54%	sell
Kirovohradoblenergo	KION	0.40	43	47.1	57.4	14%	0.82	0.17	-58%	sell
Krymenergo	KREN	0.60	24.2	24.8	119.8	4%	0.21	0.21	-65%	sell
Chernivtsioblenergo	CHEN	1.00	17	16.5	29.8	-5%	0.55	n/a	n/a	sell
Donestkoblenergo	DOON	0.65	65.5	67.1	269.6	-26%	0.25	n/a	n/a	sell
Khersonoblenergo	HOEN	0.15	14.2	60.3	72.6	9%	0.19	n/a	n/a	n/r

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## Summary

**Debt Problems To Become A Thing Of The Past.** The optimism we expressed in our initiating coverage report on Oblenergos in February has proven to be right on the money. In June 2005, the government passed legislation to solve the debt problem in the energy sector. This new legislation will unshackle Oblenergos from their debt problems. Since the law was adopted our scores on 24 out of 26 Oblenergos have increased.

**The NC ECU Enhances Oblenergo Profitability.** Since the creation of the National Energy Company of Ukraine (NC ECU), which has been managing all the state's stakes in Oblenergos since 3Q04, there have been noticeable improvements in reported net incomes for the state controlled Oblenergos during consequent quarters.

### **New CEO Brings Predictability To NC ECU Policy:**

- The new CEO will **lobby to resolve debt problems** for related Oblenergos. The state company is likely to stop the bankruptcy processes which are underway at some energy companies
- The NC ECU will crackdown on value-destroying spending practices by the managers of related Oblenergos by tightening control: this **will improve profitability in the segment**
- The NC ECU is **not likely to apply for higher tariffs for related Oblenergos**. Higher tariffs could become an additional income driving factor and would increase the sector's attractiveness. Low tariffs make state controlled companies potentially less attractive than those controlled by private owners, who lobby for higher tariffs

**The standardization of non-residential electricity tariffs** for all electricity distribution monopolies will lead to changes in retail electricity tariffs for all Oblenergos. However, cash flow changes from utility customers related to tariff changes **will not alter cash flows to Oblenergos**. However, tariff changes will affect electricity costs for the industrial consumers, and may cause them to change their policies regarding the use of Oblenergos as electricity suppliers.

**The low liquidity of Oblenergo stocks**, due to high share concentration and limited free float is reflected in large spreads and tends to make stock prices highly sensitive to any increment of demand. Thus, the current market prices we use are indicative in nature.

## Legislation Changes

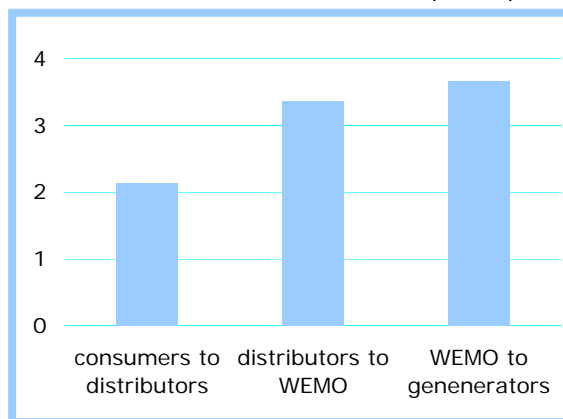
### Debt Legislation: Solving A Key Problem

#### The Debt Problem

The debt problems Ukrainian utility companies fell into, due to undisciplined payment practices during the last decade, is the most restrictive factor facing the Ukrainian energy sector. As of March 31, 2005, electricity distribution companies owed the wholesale electricity market operator (WEMO) an amount equal to 5.1% of Ukraine's GDP in 2004.

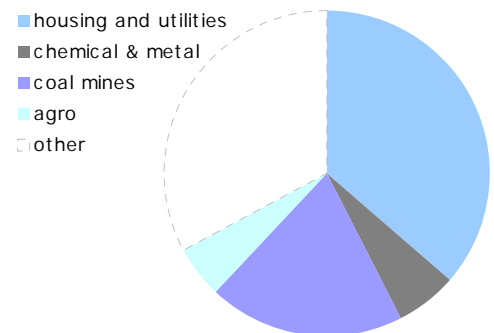
**Oblenergo debt equals about 5% of Ukraine's GDP**

Accumulated Debts As Of March 31, 2005, USD bln



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

Oblenergos Main Debtors



Oblenergo debt arrears have caused two problems:

- Some distribution companies are on the verge of bankruptcy. Bankruptcy procedures were opened for Cherkassyoblenrgo (CHON). In addition, Lunaskoblenrgo (LOEN) lost all its networks as a result of bankruptcy in 2003
- It is difficult for the companies to repay their debts due to their low profitability

**The debt problem should be solved now that the corresponding law has been adopted**

These two problems are expected to be resolved in the near future due to the adoption of the law "On Measures Directed To Ensure The Stable Work Of Fuel And Energy Sector Enterprises," in June 2005.

#### Debt Offsetting

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. Potentially, all Oblenergos could be listed.

**All Oblenergos can apply to participate in the debt offsetting process**

Any enterprise on the list of participants will have all bankruptcy procedures against it stopped for the next 9 months.

#### 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. In addition, Oblenergos will be allowed to reconcile their payables to WEMO with receivables from consumers, if the latter have debt claims to WEMO. This stage will not last more than 9 months.

**Debt write off:**

- o All payment arrears for which the period of validity has expired, must be written off, and treated as expenses, in line with Ukrainian accounting rules.
- o 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
  - are payment arrears from households that emerged before January 1, 2002

Losses from write off's of bad debt of budget and households...

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.

... and costs from payables used in restructuring will be covered by...

**Debt restructuring:** During this stage, all debts left after the reconciliation process will be restructured, with the agreement of the creditor. The restructuring period for the debts between state-controlled enterprises is 10 years. The terms for restructuring the debts between private enterprises, or private and state companies, will be determined by the mutual agreement of the parties.

...electricity consumers

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

**Possible Outcomes**

This law is good news for Oblenergos with a large amount of payables. Below we estimated the amount of debt the Oblenergos will need to have restructured after the reconciliation process.

**Debts As % of Sales 2004**

	State Own.	Debt Receivable	Debt Payable	Debt To Be Restructured
MYON	70%	43%	<b>156%</b>	<b>113%</b>
ODEN	25%	36%	<b>142%</b>	<b>105%</b>
DOON	65%	<b>191%</b>	<b>295%</b>	<b>103%</b>
VIEN	75%	36%	<b>124%</b>	87%
KREN	70%	97%	<b>181%</b>	84%
CHON	46%	18%	59%	41%
TOEN	51%	18%	50%	32%
HOEN	0%	<b>104%</b>	<b>131%</b>	27%
ZAON	60%	30%	57%	27%
DNON	75%	31%	58%	27%
HMON	70%	26%	51%	25%
HAON	65%	53%	72%	18%
ZOEN	75%	<b>111%</b>	<b>129%</b>	18%
CHEN	70%	<b>151%</b>	<b>169%</b>	18%
LVON	27%	13%	30%	17%
VOEN	75%	15%	28%	13%
KION	0%	11%	19%	7%
ZHEN	0%	15%	2%	0%
PREN	25%	2%	7%	0%
KIEN	50%	62%	20%	0%
KOEN	0%	0%	0%	0%
POON	25%	4%	1%	0%
SMEN	0%	37%	28%	0%
SOEN	0%	3%	7%	0%
CHEON	25%	0%	3%	0%
ROEN	0%	0%	1%	0%

Source: company data, Concorde Capital estimates

State Oblenergos are likely to restructure all their debts

State controlled companies are the most exposed to this problem and must rely on the NC ECU to help them get out from under the burden of their debt. The president of the

NC ECU is the head of the working group on debt offsetting therefore, we are sure that Oblenergos affiliated with this state company will be successful in solving their problems.

Odessaoblenergo (ODEN) and Khersonoblenergo (HOEN), are the only privately controlled companies with high level of debt. However, as long as the state has a stake in ODEN, it is likely that the company will also succeed in restructuring its debt.

**HOEN may face some problems when with restructuring**

With HOEN, the situation is more complicated: it is a privately owned company, and the state has little interest in helping it restructure its debt. The current government's revocation of a 17-year debt restructuring program (that had been adopted by the previous government in November 2004) show the state has no desire to help the company restructure its debts. We are optimistic HOEN will eventually solve its debt problem, but the company could face worse restructuring conditions than state controlled Oblenergos.

## Tariff Rebalance: Egalitarian Principles To Be Introduced

The Cabinet is implementing significant changes in its retail electricity tariff policy. Starting from September 2005, all tariffs which regulated suppliers (Oblenergos) use to provide electricity for industrial consumers began being set at a nation-wide level throughout Ukraine.

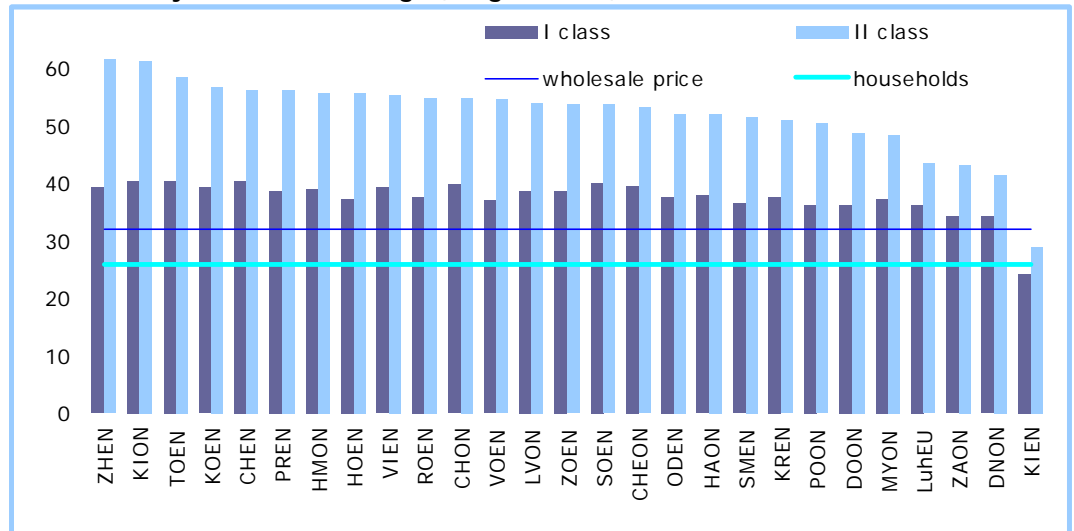
### The Current Tariff Policy

**Non-residential retail prices are different for different Oblenergos**

Currently there are different industrial tariffs for different distribution companies. While the price for households is equal and fixed across the country, non-residential electricity rates are set by each supplier individually in order to cover the costs of electricity purchases on the wholesale market, and the costs of electricity transmission and supply to end users – all the costs are agreed upon with the NERC. In addition, these tariffs must compensate for the costs of supplying electricity to households because Oblenergos provide household energy at a loss.

Tariff differentiation between Oblenergos is caused by cost differences, which depend on consumer structure and the condition of the companies' grids.

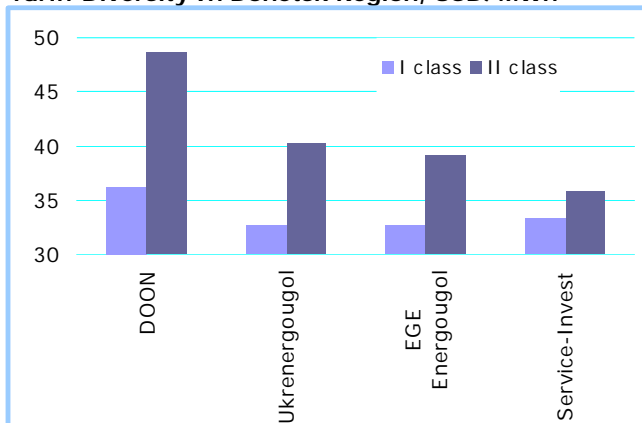
**Tariff Diversity Between Oblenergos, August 2005, USD/MWh\***



Source: Energo Business, NERC

\*The Class I tariff is for high-voltage (above 35 kV) and large consumers (about 1.2 TWh p.a), Class II is for all other of non-residential consumers

**Tariff Diversity In Donetsk Region, USD/MWh**



Source: Energo Business

Electricity in Donetsk region is supplied by four local distribution monopolies. Different industrial consumers pay different tariffs within one region.

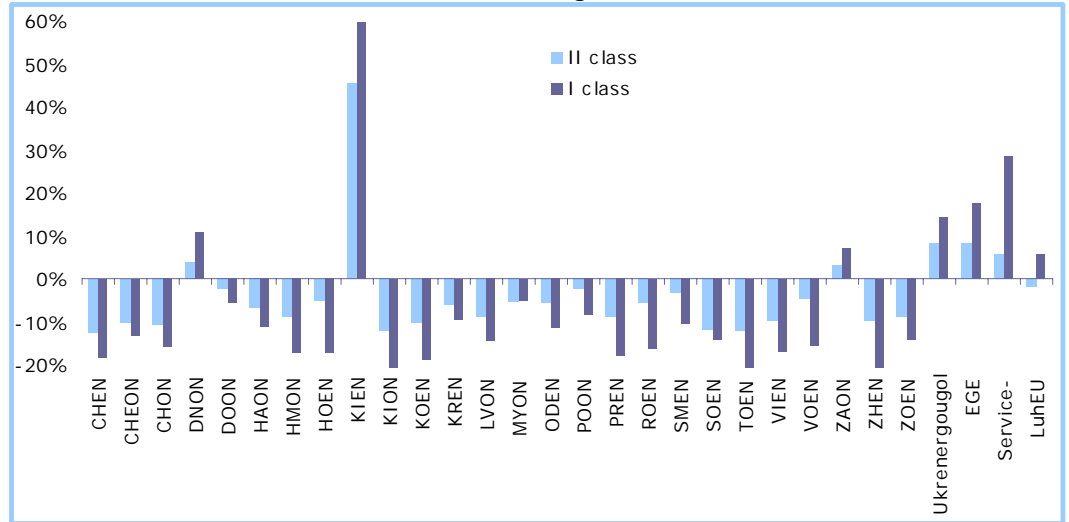


### Tariff Changes

**Non-residential retail rates will be the same across Ukraine**

According to an NERC order, starting September 2005 all retail tariffs for regulated-suppliers across the country begin to be unified. The new rates will equal the average price set by all distribution monopolies. Tariff changes will be made over 10 months, with a monthly change of no more than 5%. Thus, a homogenous non-residential rate will not be established until July 2006.

**How Current Non- Residential Tariffs Will Change To Be "Unified"**



Source: *Energ Business, Concorde Capital estimates*

**In most regions, prices will drop, while in the most industrialized regions they will grow**

As a result, non-residential rates for 23 Oblenergos will be lowered, while prices for seven large monopolistic distribution companies supplying 54% of the electricity in Ukraine will increase. Three of these companies are Oblenergos which supply the most industrially developed regions.

### Tariff Changes: The Implications

#### Cash Flow Implications:

The changing of non-residential tariffs will alter the cash flow from non-residential consumers. However, this will not alter the bottom line for Oblenergos, because a mechanism of cross subsidization will be in effect.

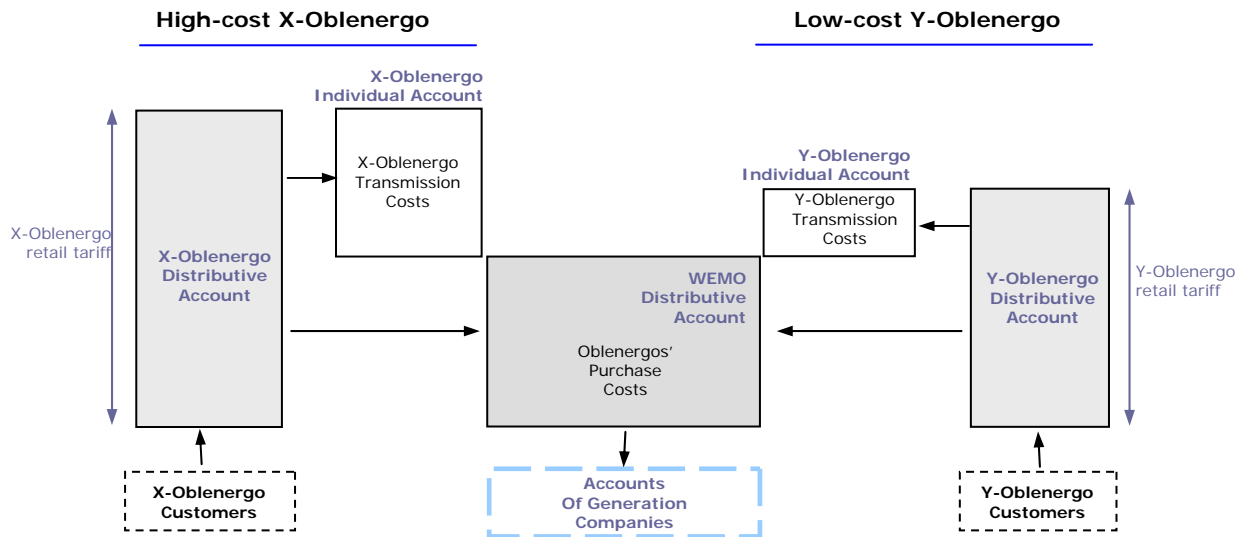
**The changing of retail tariffs for Oblenergos will not affect their bottom lines**

#### Illustration: cash flow before and after tariff changes

Currently, all the money paid to Oblenergos by their consumers is accumulated in a distributive account. Afterwards, part of the money needed to cover the cost of transmission and supply of electricity (and to allow certain profitability for private companies) is transferred to the Oblenergos' individual accounts. The rest (money for purchasing electricity) is transferred to the distributive account of the wholesale electricity market operator (WEMO) to be paid to electricity producers.

Before September, a high-cost X-Oblenergo had the same electricity purchase costs as a low-cost Y-Oblenergo, but higher costs for electricity transmission and supply. This cost difference leads to a different retail tariff for non-residential consumers.

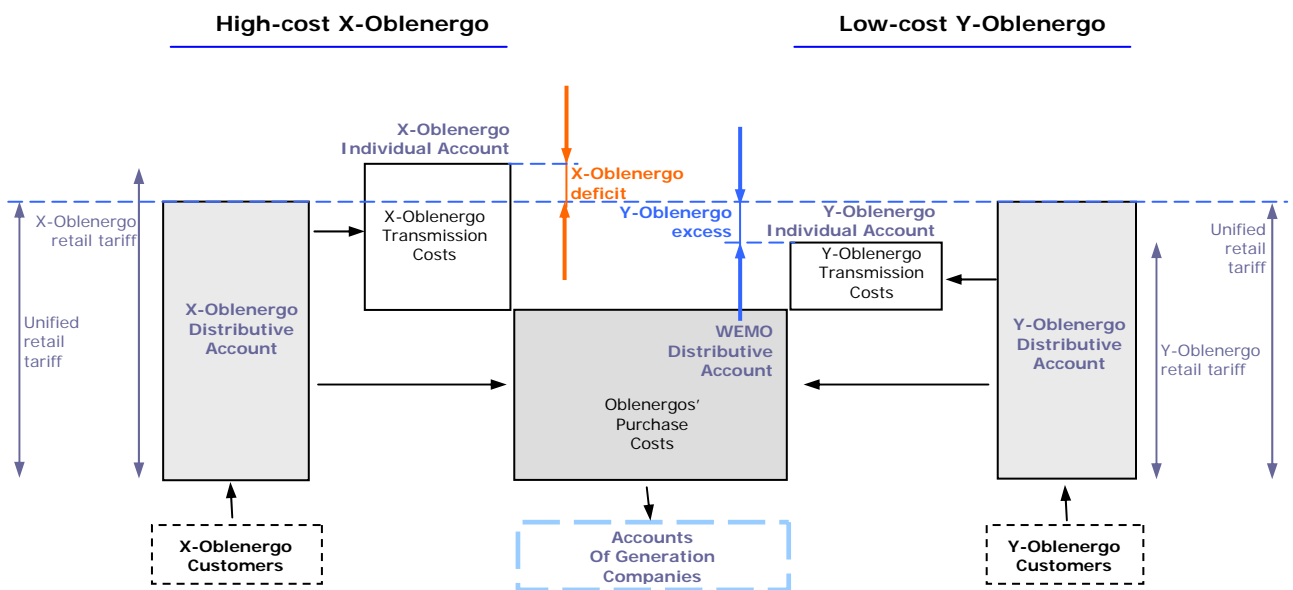
**Cash Flow To Oblenergos in August:**



When tariffs become uniform across the country:

- All similar industrial consumers will pay equal tariffs across Ukraine
- For 23 Oblenergos, money accumulated in their distributive account will not be enough to cover the costs of purchasing electricity and supply (refer to X-Oblenergo on the figure below)
- For 3 Oblenergos, as well as for the Luhansk Energy Union, EGE Energougol, Ukrenergougol and Service-Invest, money accumulated in their distributive accounts will be larger than needed to cover their costs. This excess amounts (refer to Y-Oblenergo in the figure) will be re-distributed among those companies which have cash deficits. The procedure of deficit and excess reconciliation will be developed by regulating bodies.

**Cash Flow At Unified Tariffs:**



In this way all Oblenergos will obtain the same amount of money on their own accounts, just like before the introduction of unified tariffs.

### **Some Oblenergos May Lose Their Larger Customers**

For some large industrial enterprises in eastern Ukraine it is more lucrative to supply electricity by themselves or via alternative electricity suppliers, circumventing the Oblenergos. Large enterprises can directly purchase electricity on the wholesale market (if they obtain a license) at a lower price than from an Oblenergo.

**Oblenergos may loose customers in industrial regions...**

After the unification of industrial tariffs (read: the increase of retail tariffs in industrial regions), more industrial companies may refuse service from Oblenergos, and start buying electricity directly from the wholesale market or from small alternative suppliers (whose tariffs are not regulated by the NERC).

This would reduce the eastern Oblenergos' (Dniproblenergo: DNON and Zaporizhiaoblenergo: ZAON) market sustainability.

The same is possible for Kievenergo (KIEN), whose tariffs will grow the most noticeably. However, because of the absence of large industrial consumers in this area, we do not believe there will be a major decrease in KIEN's electricity supply due to a loss of customers. Moreover, the entrance of small alternative electricity suppliers to the Kiev market could be restricted by the Kiev administration, which has a stake in KIEN.

### **Western Oblenergos Can Regain Their Market Positions**

**Small Oblenergos can regain their customer base**

As tariffs for most Oblenergos will decrease, incentives for large industrial consumers located near these Oblenergos, to buy electricity directly from the wholesale market could also decrease. Therefore we may see customers return to Oblenergos. This might increase sales for ROEN, ZHEN, KION and POON, who have all lost their major industrial consumers.

### **Ukrenergougol May Become Obsolete**

Ukrenergougol is a state owned company, created in 2003 to supply coalmines with low cost electricity, according to a pre-determined regulated tariff. This is possible because this company supplies only coal mines, and has no obligation to supply households at low tariffs. Thus Ukrenergougol's costs for electricity distribution and tariffs are lower than for Oblenergos.

**Ukrenergougol's possible redundancy may be beneficial for DOON and DNON**

This company took a significant share of the retail market in the Donetsk and Luhansk regions, and some share in the Kirovohrad, Dnipropetrovsk and Lviv regions. Now, as all industrial tariffs become unified, this industry-specific supplier is becoming unnecessary. Unless a specific tariff for the coal industry is introduced, Ukrenergougol has no future. This is positive news for DOON, DNON, KION and LVON which can return to supplying coal mines with electricity.

## Ownership Structure: No Changes

Since February all Oblenergos have maintained their ownership structure, and no significant changes in their operating control occurred. However, the last few months have been characterized by a growing corporate conflict between two rival groups who have controlling stakes in PREN, LVON, POON and CHEON.

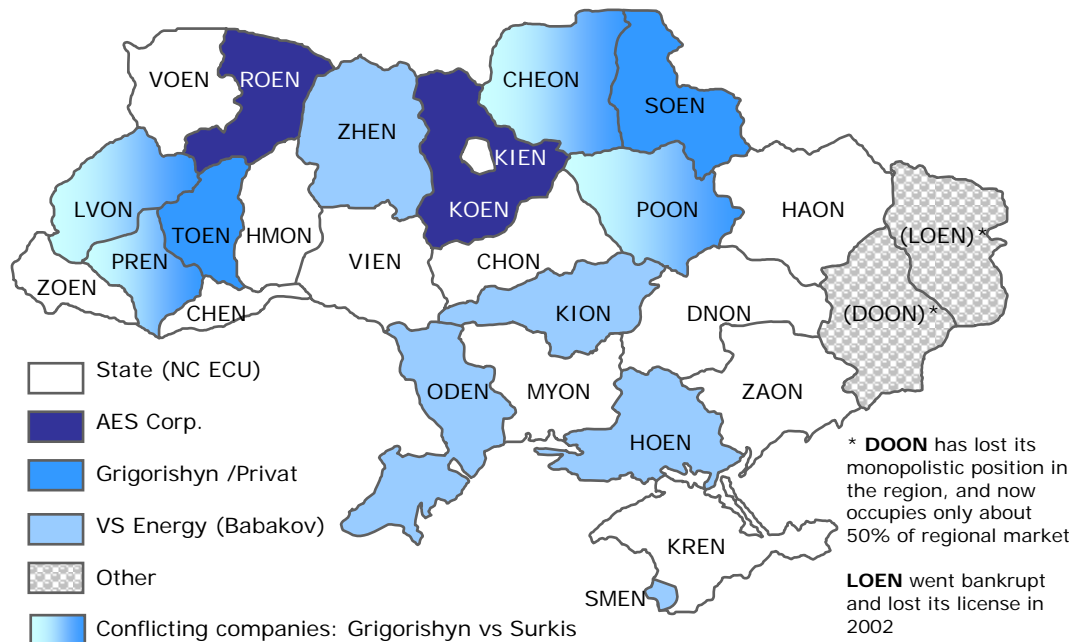
**The conflict for control of four Oblenergos is at a boil**

The management of these companies was appointed by Surkis-related shareholders in a very aggressive manner three years ago, when another shareholder, Konstantin Grigorishyn, lost control there. After the *orange revolution* we expected the situation to change rapidly in favor of Grigorishyn. However, this did not occur, mainly because the new government has not allowed Grigorishyn to use the same underhanded methods of management replacement which Surkis used. The state wants all conflict resolution to take place in the courts. In addition, Surkis's media holdings allow him the advantage of being able to keep Grigorishyn's every move in the public eye.

## The Current Ownership Structure

According to one of the main shareholders of PrivatBank, Igor Kolomoiskiy, the controversial Oblenergos are owned by Grigorishyn and PrivatBank on one side, and Surkis-related groups on the other. PrivatBank is ready to purchase Surkis's stake in these Oblenergos.

### Oblenergos: Who Controls What



The corporate conflicts surrounding four Oblenergos have not hurt their operations, despite the fact that three of these Oblenergos failed to hold their AGM's in 2005.

### AES-Related Oblenergos Stop Trading

The USA-based AES Corporation privatized two Oblenergos in 2001: Kievoblenergo (KOEN) and Rivneoblenergo (ROEN). To improve their control over the related companies, AES decided to transform these companies into closed joint-stock companies, which means there can be no free trading of the companies' stocks.

**ROEN stock is no more traded freely** Conversion to a closed joint stock company caused KOEN to be de-listed in May 2004, and in July 2005 ROEN also de-listed from the PFTS.

## NC ECU Development Implications

### “Merger” With The Ministry Of Fuel and Energy

**The head of NC ECU is also the first deputy minister of Fuel and Energy**

The appointment of an experienced energy manager Yuriy Prodan as president of the National Energy Company of Ukraine (NC ECU) has significantly strengthened the position of this structure on Ukraine’s energy market. In addition, the role of the NC ECU was further strengthened because the president of the company is now also the first deputy minister of the Fuel and Energy.

**The NC ECU head seems more prone to regulation than management**

The increased importance of the NC ECU president makes this structure the most powerful player on the market. And with changes in the top positions of the government, role of the President of NC ECU is most likely to increase. This is good for state-controlled energy companies. Now the latter can count on the NC ECU to lobby their interests in solving urgent problems. However, the combination of two different positions (manager of a corporate monopoly and the sector’s main regulator) raises the risk of drawing the NC ECU’s attention away from corporate improvement targets (which would increase the energy sector’s attractiveness for investors) and focusing it on solving the government’s short term political goals. Yuriy Prodan’s recent statements suggest he is more inclined towards the role of market regulator.

#### Who is Mr. Prodan?

Yuriy Prodan was the head of the NERC from 2001-2003. Before that, he was the director of Energorynok, a wholesale electricity market operator. With Yuriy Prodan at the helm of NERC, major changes were implemented by Yushchenko’s government in order to improve the payment and debt situation on the Ukrainian energy market in 2001-2002.

- Prodan wants to strengthen the state and NC ECU’s operating control over Oblenergos. He wants the NC ECU to gain a controlling stake in Oblenergos privatized in 1998 (CHEON, PREN, SOEN, ODEN, POON, LVON, TOEN) and wrestle operating control away from large minority shareholders.
- He is against the privatization of energy companies in Ukraine, because he believes private owners do not pay enough attention to improving them. Moreover, according to him, these companies artificially increase their costs to get higher tariffs.
- He is for strict regulation and control of costs and tariff structures in energy companies. According to him, energy company tariffs should only make the companies enough profit to re-invest in their improvement needs.

**A stronger NC ECU means:**

**.... help in solving debt problems, and a decrease in costs**

The current regulatory situation and mindset of the NC ECU management makes it unlikely that we will see Oblenergos profitability stimulated by tariff increases. Prodan, who was the head of the tariff regulation commission, is satisfied with the current tariff policy in Ukraine. However, the NC ECU will encourage income growth by increasing control of the costs reported by Oblenergos and preventing dubious cost-increasing operations by energy company management (refer to next page). In addition, the NC ECU is likely to do all it can to solve debt problems, which will increase the investment attractiveness of energy companies.

**... an increased probability of DOON and LOEN regaining their market shares**

The NC ECU management’s desire to return assets to the state could be a positive sign for the state-controlled energy companies DOON, LOEN and DOEN, which have all lost their assets due to bankruptcy procedures.

**... no privatization**

The privatization process is unlikely to be restarted next year.

**...no re-privatization**

For the Oblenergos privatized in 2001 (KION, KOEN, ROEN, HOEN, ZHEN, SMEN, which are 100% private now), there is no risk of re-privatization, as the privatization

of 2001 was successful and publicly held by a team led by the current President of Ukraine, Viktor Yushchenko.

Prodan's desire to increase the NC ECU's stake in some Oblenergos from 25-40 to 50% by purchasing shares is being treated by some investors as a re-privatization trial. However, we do not think so. This is typical activity for a corporation trying to improve its asset structure. At the moment, the company has no right to trade shares in related companies and can only do so after making corresponding changes to its charter. Therefore, it looks like it will be difficult for Prodan to achieve this goal any time soon.

### The NC ECU As An Income Driving Factor

Among the 14 state-controlled Oblenergos, most showed poor profitability during the last several years.

As can be seen from the chart below, in mid 2004, the situation started to change for the better, reported net income for 3Q04 and 2Q05 has shown significant improvement. Net income adjusted for bad debt write off's has increased on average from USD -2.2 mln in 2003 to about zero during the last four reported quarters.

**Net income increased significantly over the last year ...**

**Average Net Income Of State Controlled Oblenergos, USD mln**



Source: company data, Concorde Capital calculations

**... thanks to the establishment of the NC ECU**

It is no coincidence that these changes coincided with creation of the NC ECU. This company controls related Oblenergos more efficiently than the State Property Fund did. Once the NC ECU established control over the state Oblenergos, the management of these companies limited the use of cost-increasing activities, and the companies started to demonstrate higher profitability.

**Increased control and the resolution of the debt problem will cause net incomes to grow**

The expanding power of the NC ECU means that we can expect reported net incomes from state-controlled Oblenergos to continue to grow. Another income driving factor will be the resolution of the debt problem, the companies will be expected to write off less bad debts (part of these bad debts will be reconciled or repaid, as we mentioned in the previous section).

We believe the strengthening of the NC ECU will lead to a significant improvement in the bottom lines of state-controlled Oblenergos.

**The NC ECU often criticizes the work of private Oblenergos**

## Private Oblenergos: Why Are They Better?

There is no doubt that Oblenergos privatized in 2001 are more profitable than other energy companies. However, this does not necessarily mean that these companies perform better than their state-owned peers. The main reason for their high profitability is the “owners’ profit” included in these companies’ tariffs. According to the president of the NC ECU, the privatization of Oblenergos did not significantly improve their operating activities.

Using regression analysis, we revealed that Oblenergos which were privatized, are more successful because they were initially more inclined to success than other companies (i.e. that they were privatized because they were more successful before privatization). This partially supports the idea of Yuriy Prodan that the improvements in privatized Oblenergos are more related to these companies’ profiles (i.e. their better positioning for improvement) rather than to activity of private shareholders.

### “Selection” For Privatization

Testing the hypothesis that there existed a bias in the selection of Oblenergo’s for privatization, we chose some features from the companies which initially provided them a better position for improving their results. Among the internal factors, which could determine the company’s readiness for improvement are:

- small size (less effort for improvement needed)
- initially low excessive losses (no need to reduce losses)
- low level of debt
- initially high profitability

We used a probabilistic regression model (maximum likelihood *logit* regression) using the parameters listed above and data for 1997 and 2000 to determine the probability of choosing a certain Oblenergo for privatization. We revealed that two of the listed factors had a statistically significant (at 10%) effect on the decision to privatize a company.

#### Model Parameters:

##### Dependant Variable:

- 0 – if company is state-controlled now
- 1 – if company is not controlled by state

##### Explanatory Variables:

	Coefficient	Level of Significance
Debt in 2000 as % of sales	-3.45	0.022
Size (Sales 1997, USD mln)	-0.01	0.080
<b>Count R-squared = 0.81; Adjusted Count R-squared = 0.62</b>		



Our model estimates the probability of an Oblenergo having been privatized given the listed parameters quite accurately:

**Our model can identify the list of private Oblenergos using the pre-privatization data**

**Reality vs Model Predictions:**

**Probability That Oblenergo Is Not Now In State Control**

<b>Reality: Privatized Oblenergos:</b>		<b>Reality: Left in state control:</b>	
	Model Output (probability of being privatized):		Model Output (probability of being privatized):
ROEN	91%	VOEN	80%
CHEON	88%	HMON	74%
ZHEN	87%	ZOEN	55%
PREN	85%	CHON	42%
KOEN	82%	CHEN	29%
KION	81%	VIEN	28%
SOEN	79%	MYON	26%
ODEN	77%	KIEN	17%
POON	74%	ZAON	8%
LVON	72%	KREN	5%
SMEN	63%	HAON	5%
TOEN	45%	DNON	0%
HOEN	7%	DOON	0%

Source: Concorde Capital estimates: STATA® logit model output  
 Note: "bad" predictions are highlighted red

**Private Oblenergos are better now, because they were better positioned to be successful**

The test results support our assumption that most Oblenergos which were selected for privatization in the past were better positioned for improvements than other companies. Note that HOEN's estimated probability of privatization is only 7% (though it was privatized) is currently one of the poorest functioning companies in the group. Also, the state controlled companies which have the highest probability of having been privatized (according to our model): VOEN and HMON are the best performing state controlled companies.

Therefore, despite the fact that privatized companies have improved their results more noticeably than other Oblenergos, this improvement is due to better positioning for improvement, not efficient private owners.

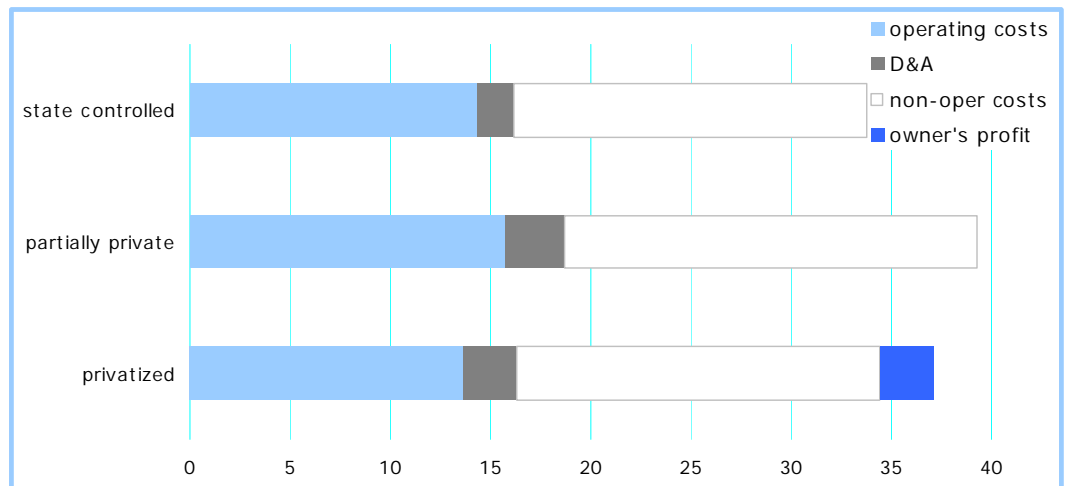
### Privatization and Cost-Increasing Behavior

According to regulators the privatization of Oblenergos failed to live up to expectations. The president of the NC ECU said that these companies are trying to increase their owner's profitability by overestimating costs (applying to the NERC for higher tariffs), and by spending money for unnecessary consulting and related services. He believes this behavior negatively affects the customers of these Oblenergos, who have to pay more for electricity compared to customers of other electricity suppliers.

All the Oblenergos privatized in 2001 can obtain additional investor profit, which is included in the company's retail electricity tariff, if the companies fulfill their debt restructuring obligations, and obey payment discipline. All the private distribution companies except Khersonoblenergo (HOEN) fulfill all the needed obligations and take advantage of this opportunity, which increases their average retail tariff by about 10%, on average. No other companies are allowed to include profit in their tariffs.

However, even with this profitability surcharge to their tariffs, fully private Oblenergos have lower average tariffs (sales per MWh of electricity) than partially privatized Oblenergos.

**Average Tariff Structure Of Oblenergos, USD/MWh**



Source: company data, Energo Business, Concorde Capital estimates

**Partially privatized Oblenergos tend to overestimate their costs to apply for higher tariffs**

This is due to the lobbying power of people related to partially privatized Oblenergos: this explanation is in line with Yuriy Prodan's (the NC ECU president) claims: refer to page 15. Despite a relatively low stake in these Oblenergos (about 25%), a Surkis-related Group has been controlling operations for most of these companies. This group lobbies for high tariffs by presenting higher costs. This behaviour might annoy the former head of the NERC, and current NC ECU president, who has already questioned the stewardship of these "minority shareholders."

However, note that difference in tariffs between the groups of Oblenergos is statistically insignificant, which can be explained either by their low numbers, or by lack of support for the claim by the NC ECU president.

## Financial Reporting: No Need To Restate Anymore

**Since 4Q04, all Oblenergos have been using a uniform revenue recognition policy**

**This improves the reliability of their sales-based ratios**

As we noted in our initiating report on February 28, some Oblenergos used an alternative revenue accounting method, which counted some sales of electricity which came to an Oblenergo's distributive account but bypassed its private account as "other operating income". This policy made their reported sales results hard to compare.

Fortunately, beginning 4Q04, all the companies started using the same revenue accounting approach, where all the proceeds obtained from sales of electricity are counted as revenue. This allows us to use the reported financials of Oblenergos for the full year of 2004 without any restatement, and improve the reliability of sale values because there is no risk of making an estimation error in the process of restatement. This improves the reliability of the sales-related indices, like EV/S multiples or EBITDA- and net margins.

## Valuation: Peer Comparison

We chose the closest two groups of peers to value Oblenergos: Czech and Hungarian regional distribution companies. Like Oblenergos, these companies purchase most of their electricity on the wholesale market from producers. In addition, they are close to Ukraine in their geographical location.

### Oblenergos vs Eastern European Peers

	Sales USD mln	EBITDA margin	Net margin	El. Supplied TWh	El. Losses
CHEN	30	-5%	-8%	0.90	32%
CHEON	57	10%	-2%	1.37	15%
CHON	58	-3%	-12%	1.57	14%
DNON	721	1%	-2%	25.87	8%
DOON	270	-26%	-30%	8.38	31%
HAON	181	-6%	-11%	4.71	18%
HMON	52	7%	0%	1.52	23%
HOEN	73	9%	-3%	1.80	21%
KIEN	311	6%	0%	6.93	15%
KION	57	14%	-3%	1.60	17%
KOEN	120	18%	10%	3.17	18%
KREN	120	4%	-6%	3.63	18%
LVON	115	12%	5%	3.28	18%
MYON	64	-17%	-34%	2.02	28%
ODEN	147	-1%	-19%	4.41	25%
POON	151	7%	-3%	3.31	8%
PREN	75	16%	5%	1.71	13%
ROEN	66	14%	8%	1.99	15%
SMEN	30	15%	9%	0.77	19%
SOEN	61	10%	0%	1.54	13%
TOEN	31	3%	-6%	0.89	21%
VIEN	63	6%	0%	1.84	23%
VOEN	34	8%	2%	0.97	21%
ZAON	276	2%	0%	10.15	10%
ZHEN	60	16%	6%	1.67	18%
ZOEN	45	5%	-1%	1.47	31%

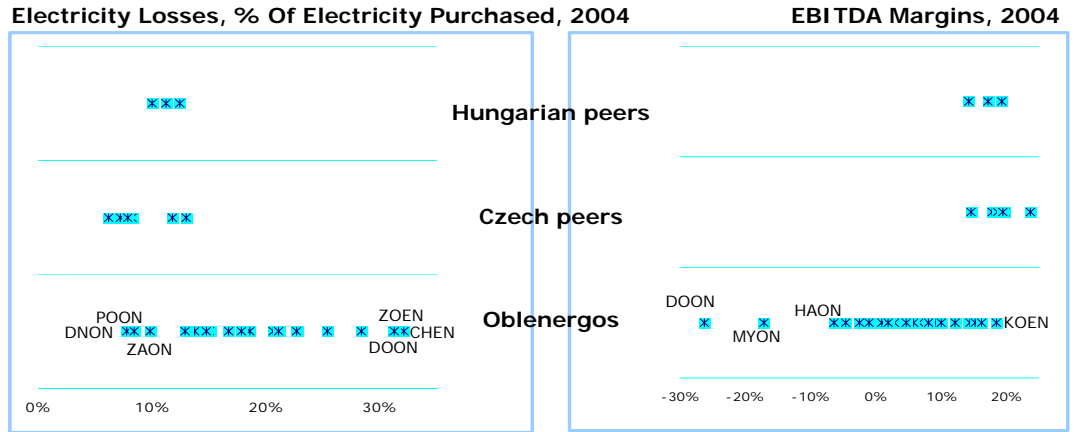
### Hungarian Distributors

Demasz RT	391	19%	6%	3.83	10%
Emasz RT	445	14%	4%	3.27	12%
ELMU RT	978	17%	8%	8.35	11%

### Czech Distributors

Prazska Energetika	457	18%	9%	5.34	8%
Vychodoceska Energetika	455	n/a	6%	6.20	8%
Severoceska Energetika	500	20%	9%	6.44	7%
Severomoravska Energetika	612	19%	4%	8.30	8%
Stredooceska Energeticka	481	15%	6%	6.21	12%
Zapadooceska Energetika	412	24%	11%	4.40	6%
Jihomoravska Energetika	631	20%	9%	8.02	13%

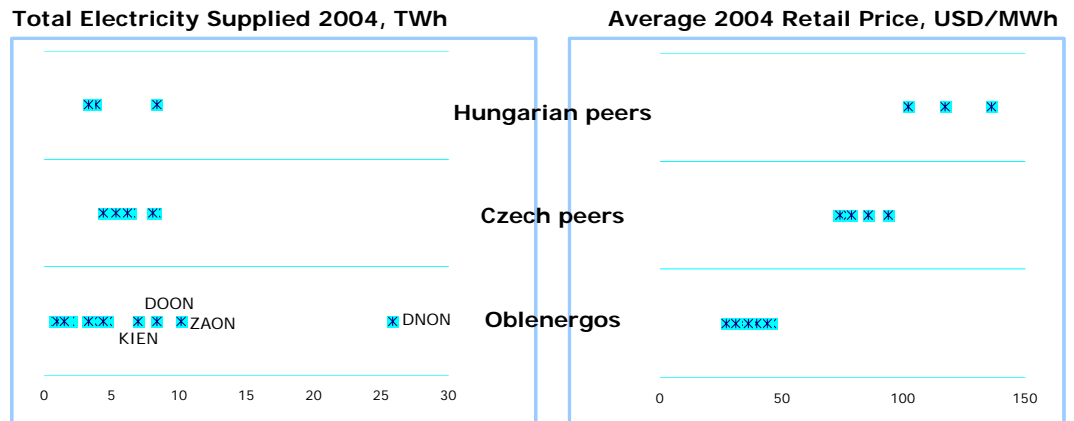
International peers are more efficient in terms of electricity transmission losses, and have higher EBITDA margins than Oblenergos on average. We believe that only the best performing Oblenergos can be compared to their international peers without any discount.



Source: company data, Concorde Capital calculations

As electricity prices are not unified in the countries used in the study, we cannot value the companies accurately using the companies' physical parameters of supply. However, we see significant potential locked in Oblenergos, as Ukraine's electricity prices are expected to reach the level of its western neighbors in the long term.

In addition, we are cautious in valuing Oblenergos by their profitability parameters, as Oblenergos have very unstable bottom lines, which depend on their level of bad debt (this will be unimportant in the future). Therefore, as in the previous report, we will rely more on EV/S multiples, while technical and profitability parameters will be utilized in identifying the discount to the Oblenergos' target price compared to their peers.



Source: company data, Concorde Capital calculations

Therefore, as before, we used a multistage valuation method, with different discounts to the international peers' averages, depending on the Oblenergos' performance.

## Scoring

Compared to the previous scoring methodology, we have excluded a parameter, which has become insignificant with the adoption of the law on debt restructuring: the debt factor. The new law, described above, lessens the importance of the Oblenergos' high payables on their operational stability and future cash flows (as the companies will repay their outstanding debts with the special surcharge to their electricity tariffs, not from their profit).

We also modified our *NERC algorithm* (% of money transferred from the distributive to personal accounts of Oblenergos) scoring. We score Oblenergo as a five if it obtains 100% of the cash flow from its distributive account, and a four otherwise. With increasing payment levels for electricity from Oblenergo customers, we see no reason to score companies less than four by this factor.

The remaining score-determining factors are the same as in our February report.

### Ranking Summary

	Avg. Score	Supply Change			EBITDA Margin 2004		Avg. NERC Algorithm, 9m05, %		Excessive El. Losses, % of El. Purchase			Payment Level 1H05		Mkt. Position Sustainability		Score Change Since Feb.05
		04/03	1H05/1H04					2004	5m05							
KOEN	4.8	5%	6%	5	18.4%	5	51	4	1.2	-1.9	5	106%	5	high	5	+0.1
LVON	4.8	3%	4%	5	12.1%	5	30	4	0.3	-2.0	5	105%	5	high	5	+0.7
PREN	4.8	12%	14%	5	15.6%	5	37	4	-0.8	-1.9	5	103%	5	high	5	+0.7
SMEN	4.8	1%	5%	5	15.3%	5	100	5	3.0	0.2	4	115%	5	high	5	+0.4
SOEN	4.8	10%	14%	5	10.0%	5	32	4	-3.1	-4.6	5	103%	5	high	5	+0.8
ZHEN	4.8	1%	4%	5	16.2%	5	100	5	0.6	-0.2	5	108%	5	medium	4	+0.4
CHEON	4.5	2%	3%	5	9.7%	4	35	4	-0.9	-1.8	5	100%	5	medium	4	+0.6
HMON	4.5	4%	6%	5	6.6%	4	37	4	5.0	0.1	4	105%	5	high	5	+0.5
VOEN	4.5	6%	5%	5	8.1%	4	32	4	4.9	0.1	4	101%	5	high	5	+0.5
POON	4.3	5%	4%	5	6.6%	4	53	4	-2.2	-2.8	5	105%	5	low	3	+0.6
ROEN	4.3	7%	-2%	4	14.4%	5	36	4	0.8	0.7	4	103%	5	medium	4	0.0
TOEN	4.3	-1%	-1%	4	2.8%	3	39	4	0.0	-2.0	5	105%	5	high	5	+0.3
HOEN	4.2	-8%	2%	4	9.2%	4	34	4	3.4	0.2	4	104%	5	medium	4	+1.0
KIEN	4.2	5%	2%	5	6.2%	4	100	5	4.5	2.0	3	n/a	4	medium	4	0.0
KION	4.2	-11%	-26%	1	14.3%	5	100	5	-0.3	-2.4	5	116%	5	medium	4	0.0
VION	4.0	7%	-4%	4	5.8%	4	37	4	7.4	6.1	2	100%	5	high	5	+0.7
ZAON	4.0	-6%	5%	4	1.9%	3	7	4	0.6	-0.3	5	105%	5	low	3	+1.0
HAON	3.8	-1%	4%	5	-6.3%	2	27	4	2.0	0.3	4	101%	5	low	3	+1.0
KREN	3.8	14%	-1%	4	4.3%	4	26	4	1.9	2.8	3	96%	4	medium	4	+0.7
CHON	3.7	-5%	-5%	3	-2.5%	2	36	4	-0.5	-2.3	5	109%	5	low	3	+0.4
DNON	3.7	16%	0%	5	1.0%	3	9	4	2.5	1.6	3	97%	4	low	3	+0.4
ODEN	3.7	4%	1%	5	-1.0%	2	27	4	10.3	6.0	2	97%	4	high	5	+1.4
ZOEN	3.7	7%	7%	5	4.7%	4	30	4	9.1	5.9	2	82%	2	high	5	+0.5
MYON	2.8	-3%	4%	4	-17.2%	0	20	4	14.0	10.3	1	87%	3	high	5	+1.1
CHEN	2.3	-3%	-19%	2	-4.6%	2	28	4	10.7	17.0	0	76%	2	medium	4	-0.8
DOON	2.3	-16%	7%	4	-26.3%	0	15	4	14.7	11.6	1	81%	2	low	3	+1.8

Most of the companies have improved their scores since our February ranking. The companies with highest upgrade are those who have large debts: with the debt problem expected to be solved, these companies are becoming more attractive.

ODEN's increased profitability helped it to improve its results significantly.

CHEN's position has worsened because of its poor operating results: a jump in its electricity losses on the grid caused a drop in profitability. CHEN's performance reflects the significant problems inside the company. Thus, we will not treat this stock as an investment opportunity now.

Despite increasing its score, DOON remains an unattractive stock. Poor operating results and a possible market share reduction due to the existence of several alternative powerful suppliers in the Donetsk region still plague the company. On the other hand, as we noted above, DOEN has a chance to increase its market share in the Donetsk region, if Ukrenergogol is liquidated.

**We divided the Oblenergos into four groups depending on their performance and operating environment:**

**The First Group:** the best performing, exemplary companies (scored 4.5 and higher)

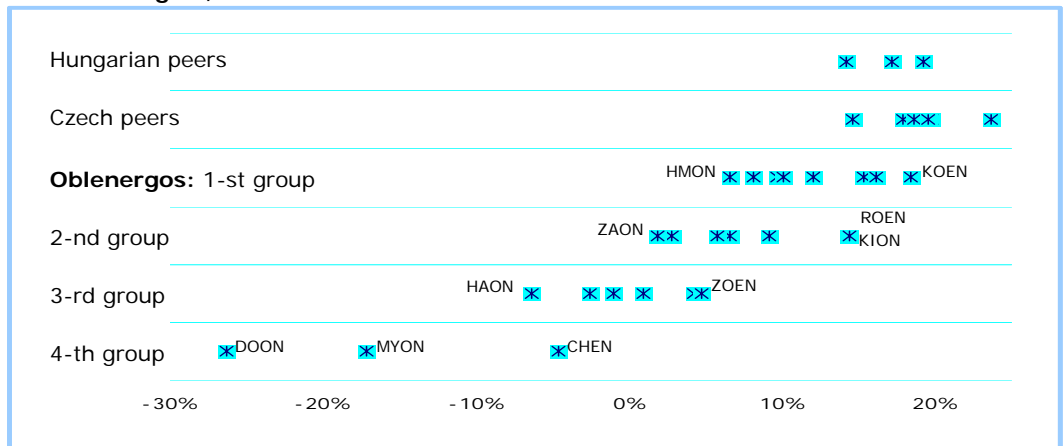
**Second:** companies who perform well (scored 4.0-4.49)

**Third:** companies of relatively poor performance (scored 3.5-3.99)

**Fourth:** companies that perform the worst (below 3.5)

The exemplary Oblenergos are close in profitability to their international peers. We applied no discount to the best performing Oblenergos when comparing them to their peers.

#### EBITDA Margins, 2004



Source: company data, Concorde Capital calculations

We used a 25% discount with the second group of Oblenergos, and a 50% discount with the third group. The three worst performing Oblenergos are not considered investment opportunities.

#### Valuation

##### Peer Multiples Summary

	MCap USD mln	EV USD mln	EV/S	EV/EBITDA	P/E	EV/EI. Supply USD/MWh	EV/Lines USD/m
Demasz RT	294.1	354.0	<b>0.91</b>	4.71	12.1	92	11.5
Emasz RT	166.4	292.6	<b>0.66</b>	4.63	9.6	89	13.3
ELMU RT	908.0	955.6	<b>0.98</b>	5.67	11.6	115	44.5
Prazska	396.1	407.5	<b>0.89</b>	5.00	10.0	76	37.0
Vychodoceska	214.2	220.7	<b>0.48</b>	n/a	8.2	36	6.9
Severoceska	284.7	266.3	<b>0.53</b>	2.69	6.0	41	10.6
Severomoravska	353.6	329.3	<b>0.54</b>	2.89	13.0	40	9.2
Stredoceska	262.0	271.4	<b>0.56</b>	3.86	9.6	44	7.2
Zapadoceska	289.3	253.2	<b>0.61</b>	2.60	6.1	58	11.6
Jihomoravska	336.6	364.1	<b>0.58</b>	2.95	5.6	45	9.0
average			<b>0.67</b>	3.89	9.2	64	16.1
median			<b>0.60</b>	3.86	9.6	52	11.1
<b>Oblenergos</b>			<b>0.55</b>	9.98	113.5	20	2.5
median			<b>0.52</b>	7.13	12.4	18	1.2

Source: IBES, Bloomberg, company data, Concorde Capital calculations  
 Note: capital city suppliers are highlighted grey

Note that companies which supply capital cities (Prazska En. and ELMU) are valued higher than other distributors.

In choosing our EV/S target for Oblenergos, we do not take capital city utilities into consideration. But, in valuing KIEN we will rely on Prazska and ELMU signals.

Based on this consideration, we will choose average EV/S of peripheral peers (0.61) as a discount-less target for peripheral Oblenergos, and average EV/S for ELMU and Prazska (0.93) as a discount-less target for KIEN.

### Valuation Summary

	Price USD	MCap USD mln	EV USD mln	EV/S	EV/ EBITDA	P/E	EV/EL	Implied Upsides			
								EV/S	EV/ EBITDA	P/E	EV/EL
CHEN	0.30	17.0	16.5	<b>0.55</b>	neg	neg	18	n/a	n/a	n/a	n/a
CHEON	0.35	41.8	51.3	<b>0.89</b>	9.2	neg	37	-39%	-82%	n/a	1%
CHON	0.42*	62.3	61.3	<b>1.06</b>	neg	neg	39	-70%	-107%	n/a	-35%
DNON	36.70	219.9	218.7	<b>0.30</b>	31.7	neg	8	1%	-89%	n/a	195%
DOON	1.00	65.5	67.1	<b>0.25</b>	neg	neg	8	N/a	n/a	n/a	n/a
HAON	0.24	61.6	58.7	<b>0.32</b>	neg	neg	12	-6%	n/a	n/a	96%
HMON	0.22	29.6	29.8	<b>0.58</b>	8.7	279	20	6%	-62%	-97%	92%
HOEN	0.20	14.2	13.7	<b>0.19</b>	2.1	neg	8	137%	68%	n/a	378%
KIEN	1.50	162.5	192.6	<b>0.62</b>	10.0	133	28	15%	-64%	-92%	137%
KION	0.36	43.0	47.1	<b>0.82</b>	5.8	neg	29	-48%	-50%	n/a	30%
KOEN	0.05*	52.0	47.7	<b>0.40</b>	2.2	4	15	49%	66%	n/a	213%
KREN	0.14	24.2	24.8	<b>0.21</b>	4.9	neg	7	49%	-32%	n/a	272%
LVON	0.12	38.8	54.7	<b>0.48</b>	3.9	7	17	40%	-43%	27%	282%
MYON	0.13*	20.6	21.9	<b>0.34</b>	neg	neg	11	n/a	n/a	n/a	n/a
ODEN	0.08*	16.7	48.9	<b>0.33</b>	neg	neg	11	-24%	-176%	n/a	368%
POON	0.25	55.2	67.6	<b>0.45</b>	6.8	neg	20	3%	-68%	n/a	103%
PREN	0.20	20.7	32.5	<b>0.43</b>	2.8	6	19	65%	-13%	46%	256%
ROEN	0.40*	34.1	32.1	<b>0.49</b>	3.4	7	16	-5%	7%	35%	125%
SMEN	0.16	12.1	11.6	<b>0.38</b>	2.5	4	15	57%	40%	110%	222%
SOEN	0.10	17.7	22.0	<b>0.36</b>	3.6	205	14	87%	-25%	-96%	310%
TOEN	0.19	11.6	12.1	<b>0.39</b>	13.6	neg	14	19%	-79%	n/a	183%
VIEN	3.00	9.3	10.3	<b>0.16</b>	2.8	neg	6	202%	13%	n/a	385%
VOEN	0.03	14.3	13.2	<b>0.39</b>	4.8	25	14	52%	-21%	-65%	163%
ZAON	0.60	107.6	105.6	<b>0.38</b>	20.3	300	10	19%	-81%	-97%	138%
ZHEN	0.39	47.7	46.5	<b>0.77</b>	4.8	12	28	-20%	-26%	-29%	78%
ZOEN	0.17	21.2	23.2	<b>0.51</b>	10.9	neg	16	-44%	-77%	n/a	64%

\* companies are not listed on PFTS and not traded, the price listed is the price of last transaction



## Abridged DCF Valuation

To test our peer valuation results and gauge them with the companies' potential, we used a DCF model. The energy supply market is over-regulated in Ukraine, and all the Oblenergos' potential depends on regulation changes. Our basic assumption in our DCF modeling is that the regulator will treat all the companies equally, so that there will be no discrimination between Oblenergos in long term.

### Key Assumptions

**Constant growth rate : 2%**

***Oblenergo operating incomes are close to current EBIT, but they will be corrected In the long run by:***

- **Commercial (excessive) electricity losses:**

The NERC includes certain allowance for electricity losses on Oblenergos' tariffs. If the company loses more electricity, these excessive losses are covered by the company's profit. If the company has a lower level of losses than is included into the tariff, it obtains additional profit (short-term) from economies. In the long-run, actual and allowed losses of electricity must converge, so that no company will lose/gain from this. Thus, we correct our long-term EBIT by these losses/profits.

- **Bad debt write offs:**

As payment discipline is improving, in the long run the companies will not write off their bad receivables, and will not lose on this.

We expect these income corrections to be made by 2010.

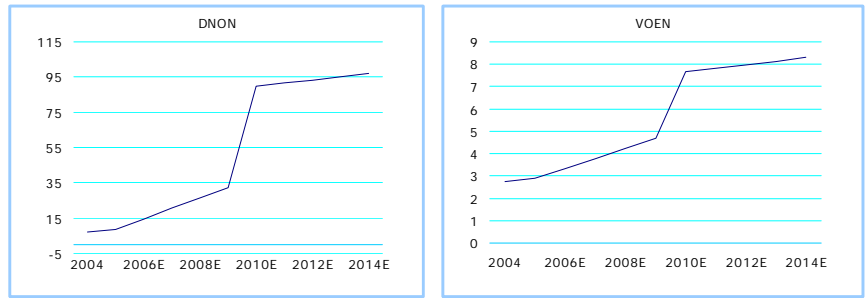
- **Investor profit:**

Fully private Oblenergos (except HOEN) obtain annual investor profit which is equal to privatization MCap multiplied by 17%. By 2009, they will obtain "not less than 11%" (according to legislation). So, we assume, they all will see a drop in investment profit to 11% starting in 2009.

We believe that the companies, which are now under state control, will be privatized in 2010, and will obtain investor profit according to the same conditions as those which are 100% private: 11% from MCap at privatization. We select this MCap as 0.65 to sales, which is average for those companies privatized in 2001. This investor profit for current state companies looks like a strong assumption, but we are sure that the investor profit (*de jure*, the only allowed net income source for Oblenergos) will be applied equally to all the companies in the long term.

The investor profit assumption affects the companies' EBITDA significantly. It will considerably increase EBITDA forecasts for those non-privatized companies, which would have the largest privatization MCap, i.e. the largest level of sales. For the state controlled companies with low sales, the EBITDA change in 2010 will be less noticeable.

**Illustration: EBITDA forecasts (USD mln) for a large company (DNON) and a small company (VOEN):**



On the other hand, for those companies which obtain owner profit now, this profit is expected to decrease in 2009 from 17% of MCap to 11%, reducing these companies' profitability.

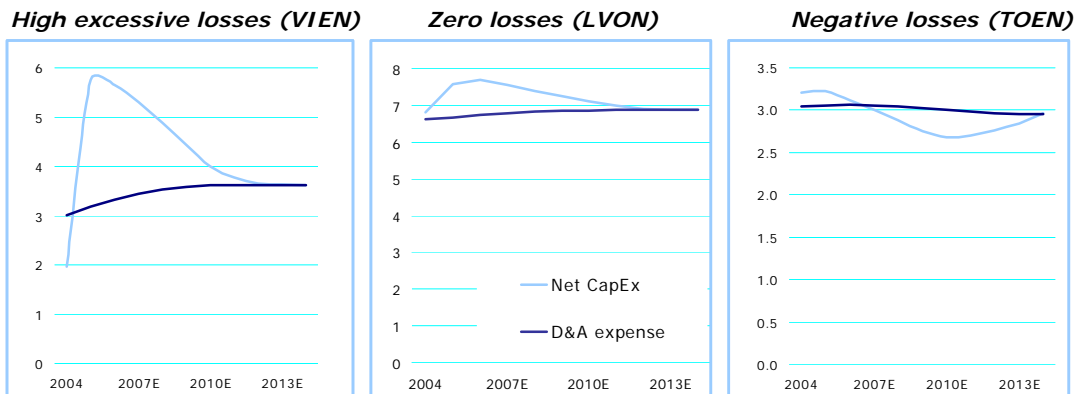
**Illustration: EBITDA forecasts (USD mln) for 100% private companies:**



**CapEx and D&A Assumptions**

Those companies, that have a high level of excessive losses, are expected to invest more to improve their grids. For such companies, net capital expenditures will be larger than their depreciation costs in the mid-term, while for those companies, which have no excessive electricity losses, net capital expenditures will be lower than their D&A expenses in the midterm.

**Illustration: Net CapEx and D&A forecasts (USD mln) for Oblenergos with:**



**Companies are modeled to increase their working capital proportionally to their sales growth**

---

**WACC assumptions:**

WACC is equal to cost of equity, as most of Oblenergos do not use bank loans:

**Cost of equity calculation:**

Ukr Eurobonds YTM	6.0%
Corp. bond premium	7.5%
Equity premium	5.5%
Company-specific Premium/Discount	

A **company-specific premium** will adjust our model to the uncertainties related to the company's operating environment and future stability. We believe this premium will depend on the companies scoring (from the page 22):

- Those companies which are scored 4.6+ have 0% premium to their equity cost
- Companies that scored 4.0-4.5 have 1% premium
- A 2% premium is added to Oblenergos that scored 3.0-3.9

We have not employed a DCF model for those companies, that we do not treat as investment opportunities (scored below 3.0).

WACC to perpetuity is assumed to be 13%.

## Valuation Summary

In general, a multiple-based valuation represents the target price of the stock taking into account its current performance, and operating environment. The DCF-based target represents the stock's potential (especially for those companies that were not privatized in 2001) assuming they improve their operating results, and assuming equal treatment to all the Oblenergos in long term.

### Valuation Summary, USD

		Current price	Target by EV/S	DCF-Based Value	Target	Upside	Recom.
Sevastopolenergo	SMEN	0.40	0.71	0.81	0.73	83%	<b>buy</b>
Lvivoblenergo	LVON	0.17	0.28	0.41	0.3	76%	<b>buy</b>
Volynoblenergo	VOEN	0.03	0.05	0.05	0.05	67%	<b>buy</b>
Sumyoblenergo	SOEN	0.11	0.19	0.12	0.16	45%	<b>buy</b>
Prykarpatooblenergo	PREN	0.26	0.33	0.52	0.35	35%	<b>buy</b>
Ternopiloblenergo	TOEN	0.16	0.23	0.15	0.21	31%	<b>buy</b>
Vinnitsaoblenergo	VIEN	7.00	9.06	11.99	9.1	30%	<b>buy</b>
Khmel'nitskoblenergo	HMON	0.20	0.23	0.18	0.22	10%	<b>buy</b>
Kievlenergo	KIEN	1.55	1.72	1.69	1.7	10%	<b>buy</b>
Dniprooblenergo	DNON	37.62	36.9	53.98	38	1%	hold
Poltavaoblenergo	POON	0.25	0.26	0.06	0.25	0%	hold
Zhytomyrooblenergo	ZHEN	0.40	0.31	0.21	0.29	-28%	sell
Kharkivoblenergo	HAON	0.30	0.23	0.09	0.21	-30%	sell
Zaporizhiaoblenergo	ZAON	1.00	0.72	0.46	0.66	-34%	sell
Chernihivoblenergo	CHEON	0.40	0.21	0.16	0.2	-50%	sell
Zakarpatooblenergo	ZOEN	0.24	0.1	0.16	0.11	-54%	sell
Kirovohradoblenergo	KION	0.40	0.19	0.12	0.17	-58%	sell
Krymenergo	KREN	0.60	0.21	0.23	0.21	-65%	sell
Khersonoblenergo	HOEN	0.15	0.35	0.35		-100%	(n/r)*

\* HOEN has problems with debts restructuring now, and it is not clear that the problem will be solved in short term.

Detailed information on the reasoning for our recommendation can be found in the profiles below. To refer to the profile of **Kievlenergo (KIEN)**, see our KIEN's August 15 report.

**We recommend SELL**, without a target:

**Chernivtsioblenergo (CHEN)**, and  
**Donetskoblenergo (DOEN)**: the companies are among the worst performing

**Luhanskoblenergo (LOEN)**: the company has lost its license to supply electricity in Lunahsk region, and also has lost all networks in the process of bankruptcy.

**We do not rate** Oblenergos, which do not have free float or which shares are not allowed to trade freely:

**Cherkassyoblenergo (CHON)**  
**Kievlenergo (KOEN)**  
**Mykolaivoblenergo (MYON)**  
**Odessaoblenergo (ODEN)**  
**Rivneoblenergo (ROEN)**

## Profiles

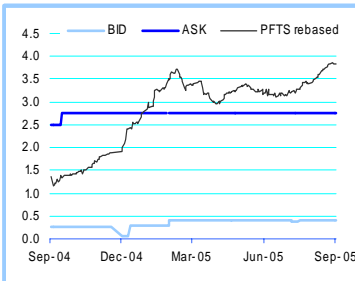
Chernihivoblenergo	30
Dniprooblenergo	31
Kharkivoblenergo	32
Khersonoblenergo	33
Khmelnitskoblenergo	34
Kirovohradoblenergo	35
Krymenergo	36
Lvivoblenergo	37
Poltavaoblenergo	38
Prikarpatoblenergo	39
Sevastopolenergo	40
Sumyoblenergo	41
Ternopiloblenergo	42
Vinnitsaoblenergo	43
Volynoblenergo	44
Zakarpatooblenergo	45
Zaporizhiaoblenergo	46
Zhytomiroblenergo	47

## SELL

Current price      Target price

**0.40**                      **0.20**

### CHEON Quotes, UAH



### Market Information

Number of shares, mln	119.32
MCap, USD mln	47.7
Free float, %	3.79

### Stock Ownership

State (NC ECU)	25%+1
Surkis	25.1%
Grigorishyn	40.0%
Other	9.9%

## ChernihivOblenergo

The company remains in the middle of our rankings due to its stable operating results. The on going conflict between two minority shareholders has not hurt company operations.

In 2005 the company failed to hold an AGM because of corporate conflicts. This will not hurt shareholder dividends, as the company did not post a positive net income in 2004. A new AGM has been scheduled for September, 16.

CHEON was recently fined USD 1 mln - for signing dubious insurance contracts in 2004.

Poor liquidity and very limited free float have caused the stock to be overpriced.

Peer valuation suggests a downside for CHEON, and our DCF model supports this result. We have downgraded the stock to SELL.

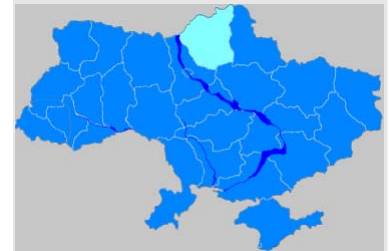
### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	57.3	5.6	1.0
2005E	69.8	6.9	2.2
2006E	73.3	7.1	2.4

### Key Ratios

	EV/S	EV/EBITDA
2004	1.00	10.3
2005E	0.82	8.3
2006E	0.78	8.1

Region: **Chernihiv**  
 Population: 1.23 mln  
 Area: 31,900 km<sup>2</sup>



Grid length, '000 km      41.0

Transformer capacity, MVA      3172

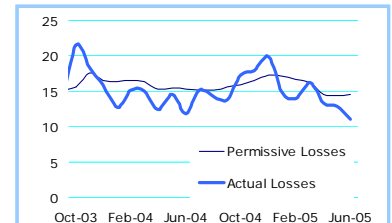
### Electricity supply, TWh

2003	1.35
2004	1.38
2005E	1.39

### Tariff change

I class	-10%
II class	-13%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	5.58	6.90	7.10	7.31	7.51	7.72	11.14	11.36	11.59	11.82	12.05
EBIT	USD mln	0.95	2.21	2.37	2.55	2.75	2.95	6.36	6.58	6.81	7.04	7.27
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	0.71	1.65	1.78	1.92	2.06	2.21	4.77	4.93	5.10	5.28	5.46
D&A	USD mln	4.63	4.69	4.73	4.75	4.76	4.77	4.78	4.78	4.78	4.78	4.78
Net CapEx	USD mln	(4.30)	(5.72)	(5.36)	(5.11)	(4.94)	(4.90)	(4.85)	(4.80)	(4.80)	(4.78)	(4.78)
WACC		20.0%	19.3%	18.6%	17.9%	17.2%	16.5%	15.8%	15.1%	14.4%	13.7%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

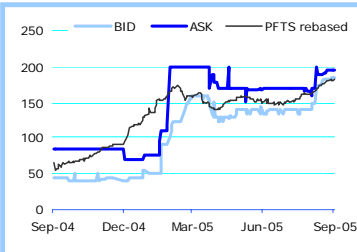
DCF-based price	<b>0.16</b>
EV/S-based target	<b>0.21</b>
Target	<b>0.20</b>

## HOLD

Current price      Target price

**37.62**                      **38.00**

### DNON Quotes, UAH



### Market Information

Number of shares, mln	5.99
MCap, USD mln	225.4
Free float, %	9.11

### Stock Ownership

State (NC ECU)	75%
Grigorishyn	15.9%
Other	9.1%

## DniproOblenergo

When retail electricity prices are raised DNON may lose its largest customers, industrial enterprises, as the latter will most likely begin to buy directly from the wholesale market in the midterm.

A slowdown in metallurgical industry growth (DNON's main consumer) and a reduction of market power sustainability may cause the company's power supply growth to slowdown in 2005.

The company remains the largest electricity supplier in Ukraine and the most liquid stock among Oblenergos.

DNON's management was prosecuted for misuse of power in Mar-Sept 2004, which caused a cash outflow of USD 12 mln. Assuming that this was a fact, we adjust future profits by this sum in our DCF valuation. This prompts a significant upside for DNON by our DCF.

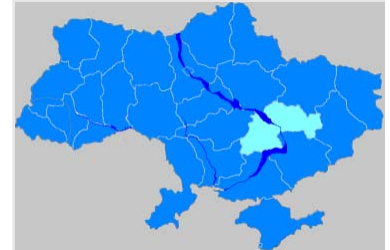
Still, in our valuation we rely more on a multiple-based target, as the company risks losing sales in the long-run, which we do not account directly in our DCF. We confirm our HOLD recommendation.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	721.0	6.9	-3.2
2005E	865.0	20.7	9.5
2006E	908.3	26.9	14.6

### Key Ratios

	EV/S	EV/EBITDA
2004	0.31	32.5
2005E	0.26	10.8
2006E	0.25	8.3

**Region: Dnipropetrovsk**
**Population:** 3.53 mln  
**Area:** 31,900 km<sup>2</sup>


Grid length, '000 km      63.5

Transformer capacity, GVA      10.9

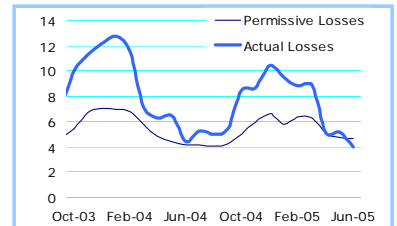
### Electricity supply, TWh

2003	22.30
2004	25.87
2005E	27.00

### Tariff change

I class	+4%
II class	+11%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	6.89	20.70	26.89	33.08	39.27	45.46	103.33	105.40	107.51	109.66	111.85
EBIT	USD mln	(3.22)	9.48	14.64	19.92	25.43	31.11	88.62	90.46	92.45	94.59	96.79
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	(3.22)	7.11	10.98	14.94	19.08	23.33	66.46	67.84	69.34	70.95	72.59
D&A	USD mln	10.11	11.21	12.25	13.15	13.84	14.35	14.71	14.94	15.05	15.06	15.06
Net CapEx	USD mln	(9.41)	(28.55)	(28.40)	(27.40)	(24.50)	(22.45)	(20.40)	(18.45)	(16.85)	(15.20)	(15.06)
WACC		21.0%	20.2%	19.4%	18.6%	17.8%	17.0%	16.2%	15.4%	14.6%	13.8%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

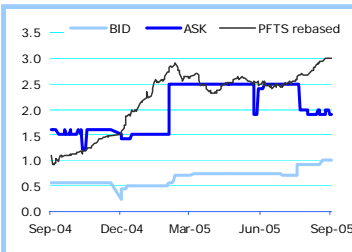
DCF-based price	<b>53.98</b>
EV/S-based target	<b>36.90</b>
Target	<b>38.00</b>

## SELL

Current price      Target price

**0.30**                      **0.21**

### HAON Quotes, UAH



### Market Information

Number of shares, mln	256.54
MCap, USD mln	77.0
Free float, %	6.18

### Stock Ownership

State (NC ECU)	65%
Grigorishyn	28.8%
Other	6.2%

## KharkivOblenergo

Even though it is the fourth largest Oblenergo and is located in an industrial region, HAON has a relatively low amount of industrial consumers. It is unlikely the company will see any customers depart due to the tariff rebalance as its tariff will decrease in short run.

In recent quarterly results the company's bottom line is improving.

Multiple valuation suggests HAON's stock is slightly overvalued, and our simplified DCF analysis prompts significant downside in the long term. We downgrade the stock SELL.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	180.9	-11.5	-21.0
2005E	222.0	0.1	-9.5
2006E	233.1	1.6	-8.1

### Key Ratios

	EV/S	EV/EBITDA
2004	0.41	-6.5
2005E	0.33	721.6
2006E	0.32	47.0

**Region:**                      **Kharkiv**
**Population:**                      2.89 mln  
**Area:**                                      31,400 km<sup>2</sup>


Grid length, '000 km                      42.0

Transformer capacity, MVA                      7.3

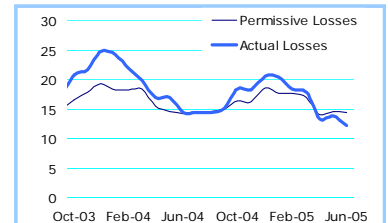
### Electricity supply, TWh

2003	4.75
2004	4.71
2005E	4.84

### Tariff change

I class	-7%
II class	-11%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	(11.46)	0.10	1.58	3.05	4.53	6.00	20.72	21.13	21.56	21.99	22.43
EBIT	USD mln	(21.01)	(9.52)	(8.09)	(6.63)	(5.16)	(3.68)	11.03	11.45	11.87	12.30	12.74
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	(21.01)	(9.52)	(8.09)	(6.63)	(5.16)	(3.68)	8.27	8.58	8.90	9.22	9.55
D&A	USD mln	9.55	9.62	9.67	9.68	9.69	9.69	9.69	9.69	9.69	9.69	9.69
Net CapEx	USD mln	(5.11)	(10.76)	(10.45)	(9.90)	(9.75)	(9.64)	(9.70)	(9.70)	(9.70)	(9.69)	(9.69)
WACC		21.0%	20.2%	19.4%	18.6%	17.8%	17.0%	16.2%	15.4%	14.6%	13.8%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.09</b>
EV/S-based target	<b>0.23</b>
<b>Target</b>	<b>0.21</b>

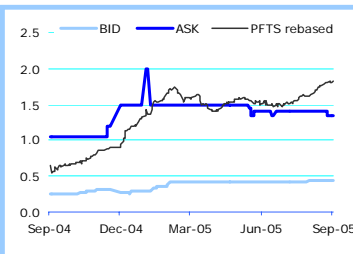


## N/R

Current price      Target price

**0.15**                      **(0.35)**

### HOEN Quotes, UAH



### Market Information

Number of shares, mln	94.98
New Issuance, 2005E	83.92
MCap (w/o new shares), USD mln	14.2
Free float, %	9.49

### Stock Ownership

VS Energy (Babakov)	90.5%
Other	9.5%

## Kherson Oblenergo

This is the worst performing company among those privatized in 2001, and the only private company whose tariff has no included investor profit.

HOEN's new debt restructuring program, adopted in October 2004 and set to last 17 years, was abolished by new government in February 2005. Now the company can only count on the newly adopted law to solve its debt problem and avoid bankruptcy.

The charter fund is expected to increase soon by 88% due to the issuance of additional shares. Results of the additional share issue will be adopted at an EGM on September 14. The money raised may partially solve the company's debt problem.

In our net debt calculation for EV estimation, we do not account for a current portion of LT debt, as this part represents outstanding payables, but not the company's current debt. This makes our restated net debt USD -0.5 mln, while reported net debt stands at USD 46.1 mln.

Our target price might suggest a buy recommendation, but as this company has a large level of debt and is on the verge of bankruptcy, we do not recommend buying the stock before it is clear that debt will be successfully restructured. Thus, we will NOT RATE the company.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	72.6	6.7	0.9
2005E	87.9	6.8	1.0
2006E	92.3	7.4	1.5

### Key Ratios

	EV/S	EV/EBITDA
2004	0.19	2.1
2005E	0.16	2.0
2006E	0.15	1.8

Region:                      Kherson

Population:                1.16 mln  
Area:                        28,500 km<sup>2</sup>



Grid length, '000 km                      33.3

Transformer capacity, GVA                4.5

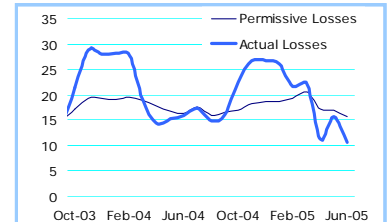
### Electricity supply, TWh

2003	1.96
2004	1.80
2005E	1.84

### Tariff change

I class	-5%
II class	-17%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	6.65	6.79	7.44	8.09	8.74	9.39	15.52	15.83	16.14	16.47	16.80
EBIT	USD mln	0.87	1.02	1.53	2.06	2.61	3.21	9.33	9.64	9.95	10.27	10.60
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	0.65	0.77	1.15	1.54	1.95	2.41	7.00	7.23	7.46	7.70	7.95
D&A	USD mln	5.78	5.76	5.90	6.03	6.13	6.17	6.19	6.19	6.19	6.19	6.19
Net CapEx	USD mln	(1.79)	(5.52)	(8.07)	(8.02)	(7.70)	(6.87)	(6.38)	(6.25)	(6.22)	(6.20)	(6.19)
WACC		20.0%	19.3%	18.6%	17.9%	17.2%	16.5%	15.8%	15.1%	14.4%	13.7%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

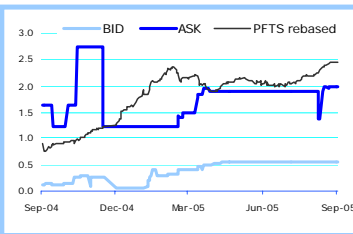
DCF-based price	<b>0.35</b>
EV/S-based target	<b>0.35</b>

## HOLD

Current price      Target price

**0.22**                      **0.22**

### HMON Quotes, UAH



### Market Information

Number of shares, mln	134.55
MCap, USD mln	26.9
Free float, %	18.22

### Stock Ownership

State (NC ECU)	70%
VS Energy (Babakov)	11.8%
Other	18.2%

## Khmelnytsk Oblenergo

The company remains the best performing among state-controlled Oblenergos (together with VOEN). Its consumer structure and expected non-residential tariff decrease guarantee the stability of the company's market share.

The company paid USD 44,600 in dividends in 2005, the dividend yield is 0.15%.

HMON is currently fairly priced by the market, as both our valuation methods suggest. So we support our HOLD recommendation on this stock.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	51.6	3.4	0.3
2005E	64.0	3.8	0.2
2006E	67.2	4.4	0.7

### Key Ratios

	EV/S	EV/EBITDA
2004	0.53	7.9
2005E	0.42	7.2
2006E	0.40	6.1

Region:                      Khmelnytskiy

 Population:                      1.41 mln  
 Area:                                      20,600 km<sup>2</sup>


Grid length, '000 km                      36.1

Transformer capacity, GVA                      3.0

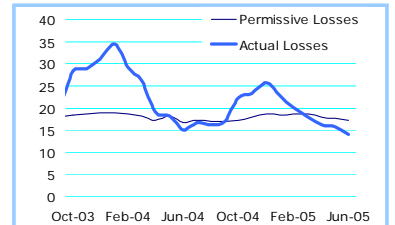
### Electricity supply, TWh

2003	1.46
2004	1.52
2005E	1.61

### Tariff change

I class	-9%
II class	-17%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

	2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	
EBITDA	USD mln	3.42	3.77	4.44	5.10	5.76	6.42	10.74	10.96	11.18	11.40	11.63
EBIT	USD mln	0.26	0.21	0.72	1.29	1.91	2.55	6.86	7.07	7.28	7.51	7.74
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	0.20	0.16	0.54	0.97	1.43	1.91	5.15	5.30	5.46	5.63	5.80
D&A	USD mln	3.16	3.56	3.72	3.80	3.85	3.87	3.88	3.89	3.89	3.89	3.89
Net CapEx	USD mln	(4.76)	(9.93)	(6.12)	(5.12)	(4.55)	(4.24)	(4.10)	(4.00)	(3.95)	(3.90)	(3.89)
WACC		20.0%	19.3%	18.6%	17.9%	17.2%	16.5%	15.8%	15.1%	14.4%	13.7%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

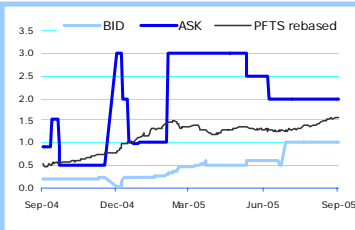
DCF-based price	<b>0.18</b>
EV/S-based target	<b>0.23</b>
Target	<b>0.22</b>

## SELL

Current price      Target price

**0.40**                      **0.17**

### KION Quotes, UAH



### Market Information

Number of shares, mln	119.38
MCap, USD mln	47.8
Free float, %	6.00

### Stock Ownership

VS Energy (Babakov)	94.0%
Other	6.0%

## KirovohradOblenergo

The company has noticeably reduced electricity losses in its grid, which helps its short term profits.

The defection of Pobuzk Ferronickel, a major client, has severely crippled the company's sales.

A significant decrease in retail electricity tariffs for industrial consumers, expected in the next six months, is likely to attract Pobuzsk Ferronickel back to the company. In addition, the drop in prices could stimulate electricity consumption in Kirovohrad region and KION revenue.

A large percentage of fixed assets compared to sales cause KION's D&A expenses to be quite high. These expenses destroy KION's profits and value.

Our multiple comparison suggests a significant downside for the stock, and this is supported by our DCF. We downgrade the stock to SELL.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	57.4	8.2	-1.7
2005E	58.3	8.3	-1.1
2006E	61.2	8.3	-0.8

### Key Ratios

	EV/S	EV/EBITDA
2004	0.90	6.3
2005E	0.89	6.2
2006E	0.85	6.3

**Region:**                      Kirovohrad

**Population:**                      1.12 mln  
**Area:**                                      24,600 km<sup>2</sup>


Grid length, '000 km                      34.0

Transformer capacity, GVA                      3.4

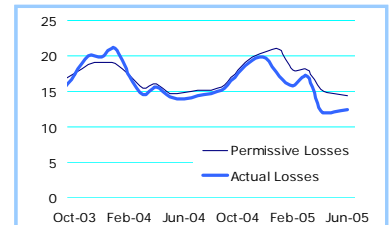
### Electricity supply, TWh

2003	1.80
2004	1.60
2005E	1.46

### Tariff change

I class	-12%
II class	-25%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	8.18	8.35	8.29	8.24	8.18	5.55	5.66	5.77	5.89	6.00	6.12
EBIT	USD mln	(1.68)	(1.12)	(0.80)	(0.51)	(0.24)	(2.57)	(2.18)	(1.80)	(1.45)	(1.10)	(0.77)
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	(1.68)	(1.12)	(0.80)	(0.51)	(0.24)	(2.57)	(2.18)	(1.80)	(1.45)	(1.10)	(0.77)
D&A	USD mln	9.86	9.47	9.09	8.74	8.42	8.12	7.84	7.57	7.33	7.10	6.89
Net CapEx	USD mln	(4.10)	(4.27)	(4.10)	(4.10)	(4.10)	(4.10)	(4.10)	(4.10)	(4.10)	(4.10)	(4.10)
WACC		20.0%	19.3%	18.6%	17.9%	17.2%	16.5%	15.8%	15.1%	14.4%	13.7%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

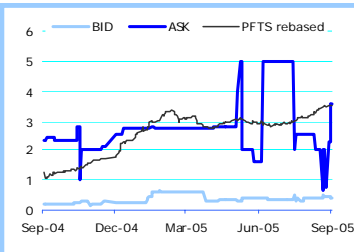
DCF-based price	<b>0.12</b>
EV/S-based target	<b>0.19</b>
<b>Target</b>	<b>0.17</b>

## SELL

Current price      Target price

**0.60**                      **0.21**

### KREN Quotes, UAH



### Market Information

Number of shares, mln	172.97
MCap, USD mln	103.8
Free float, %	30.00

### Stock Ownership

State (NC ECU)	70.0%
Other	30.0%

## Krymenergo

The company cut its excessive electricity losses by 16% of electricity purchased during 2003-2004. With the current level of excessive losses at about 0, the company started to post positive net income in the last two quarters.

With the company's debt problem expected to be solved in the near future, KREN could be a good investment opportunity.

The company has very little risk of losing its market share, and therefore its future looks stable.

Both simplified DCF and peer valuation methods suggest that the market overvalues the company. We support our SELL recommendation.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	119.8	5.1	-0.1
2005E	143.1	5.2	0.0
2006E	147.7	5.9	0.7

### Key Ratios

	EV/S	EV/EBITDA
2004	0.87	20.5
2005E	0.73	20.1
2006E	0.71	17.6

**Region:**                      **Crimea Rep.**
**Population:**                      2.13 mln  
**Area:**                                      26,100 km<sup>2</sup>


Grid length, '000 km                      35.8

Transformer capacity, GVA                      5.9

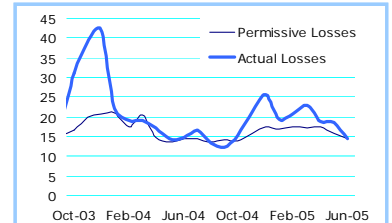
### Electricity supply, TWh

2003	3.17
2004	3.63
2005E	3.64

### Tariff change

I class	-6%
II class	-10%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
<b>EBITDA</b>	USD mln	5.10	5.20	5.93	6.67	7.41	8.14	17.39	17.73	18.09	18.45	18.82
<b>EBIT</b>	USD mln	(0.06)	(0.02)	0.67	1.37	2.08	2.80	12.03	12.37	12.72	13.08	13.45
<b>Tax Rate</b>		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
<b>Taxed EBI</b>	USD mln	(0.06)	(0.02)	0.50	1.03	1.56	2.10	9.02	9.28	9.54	9.81	10.09
<b>D&amp;A</b>	USD mln	5.16	5.22	5.26	5.30	5.33	5.35	5.36	5.36	5.37	5.37	5.37
<b>Net CapEx</b>	USD mln	(6.00)	(6.12)	(6.00)	(5.89)	(5.75)	(5.66)	(5.54)	(5.46)	(5.39)	(5.37)	(5.37)
<b>WACC</b>		21.0%	20.2%	19.4%	18.6%	17.8%	17.0%	16.2%	15.4%	14.6%	13.8%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.23</b>
EV/S-based target	<b>0.21</b>
<b>Target</b>	<b>0.21</b>

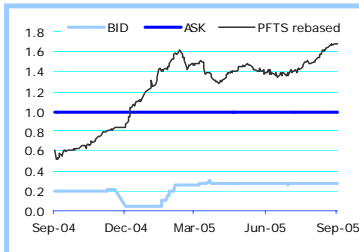
## BUY

Current price

Target price

**0.17**
**0.30**

### LVON Quotes, UAH



### Market Information

Number of shares, mln	193.97
MCap, USD mln	33.0
Free float, %	21.08

### Stock Ownership

State (NC ECU)	27.0%
Surkis	13.3%
Grigorishyn	38.7%
Other	21.0%

## LvivOblenergo

The company failed twice to hold its AGM in March 2005, because of the conflict between the main minority shareholders.

For this reason the shareholders were unable to obtain dividends for 2004, which could yield 1.5% (if dividend payoff were 10%, as it was for a related company PREN) to 6% (if div. payoff were 40% - a common level for state-controlled companies). We expect these dividends to be paid off in the future.

The conflict did not affect the company's operating results for 2005. The company remains one of the best performing in the sector.

LVON is unlikely to lose its market share; it is more likely that it will regain lost consumers: coal mines supplied by Ukrenergougol are likely to return to LVON, as this company's existence is in peril.

The company's stock has growth potential, as our analyses suggest. We upgrade our recommendation to BUY.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	114.9	13.9	7.3
2005E	140.7	17.5	10.8
2006E	146.0	18.2	11.4

### Key Ratios

	EV/S	EV/EBITDA
2004	0.43	3.5
2005E	0.35	2.8
2006E	0.33	2.7

Region:

**Lviv**

Population:

2.61 mln

Area:

 21,800 km<sup>2</sup>


Grid length, '000 km

39.2

Transformer capacity, GVA

4.5

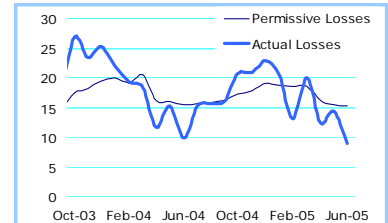
### Electricity supply, TWh

2003	3.20
2004	3.28
2005E	3.37

### Tariff change

I class	-9%
II class	-15%

### Electricity Losses, % Of Purchased El.



### DCF Valuation Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	13.89	17.45	18.17	18.88	19.59	20.30	26.84	27.38	27.93	28.49	29.06
EBIT	USD mln	7.26	10.77	11.42	12.09	12.76	13.45	19.98	20.51	21.05	21.61	22.18
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	5.45	8.08	8.57	9.06	9.57	10.09	14.98	15.38	15.79	16.21	16.63
D&A	USD mln	6.62	6.68	6.74	6.79	6.83	6.85	6.87	6.88	6.88	6.88	6.88
Net CapEx	USD mln	(6.81)	(7.57)	(7.70)	(7.55)	(7.39)	(7.25)	(7.11)	(7.00)	(6.91)	(6.89)	(6.89)
WACC		19.0%	18.4%	17.8%	17.2%	16.6%	16.0%	15.4%	14.8%	14.2%	13.6%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

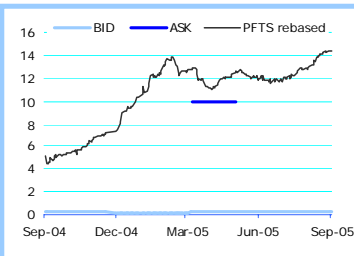
DCF-based price	<b>0.41</b>
EV/S-based target	<b>0.28</b>
<b>Target</b>	<b>0.30</b>

## HOLD

Current price      Target price

**0.25**                      **0.25**

### POON Quotes, UAH



### Market Information

Number of shares, mln	220.96
MCap, USD mln	55.2
Free float, %	1.00

### Stock Ownership

State (NC ECU)	25%+1
Surkis	34.0%
Grigorishyn	40.0%
Other	1.0%

## PoltavaOblenergo

The company failed twice to held its AGM in March 2005, because of the conflict between its main minority shareholders. This kept the shareholders from receiving dividends for 2004. Dividends could yield 1% (if dividend payoff were 10%, as it was for related company: PREN) to 4% (if div. payoff were 40% - a common level for state-controlled companies). The decision to pay the dividends might be adopted at the next AGM scheduled for September 14, if its held.

The company was fined in 2005 USD 12.3 mln for breaking the rules of its tender in 2004.

The company has almost zero free float, with an extremely low supply of shares on the OTC. This makes POON's current share price rather unstable.

The operations of Kremenchug CHPP make the company different from other regional distributors: POON is a both producer and supplier of electricity (producing about 35% of its needs). In addition, its high share of industrial consumers make POON's future hard to predict. Therefore, we will not rely on our DCF model designed to value Oblenergos, and rely solely on a multiple-based target. We support our previous HOLD recommendation.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	151.3	9.9	-3.1
2005E	186.3	-0.2	-13.2
2006E	195.6	13.2	0.2

### Key Ratios

	EV/S	EV/EBITDA
2004	0.45	6.8
2005E	0.36	neg.
2006E	0.35	5.1

**Region:**                      **Poltava**
**Population:**                      1.61 mln  
**Area:**                                      28,800 km<sup>2</sup>


Grid length, '000 km                      48.9

Transformer capacity, GVA                      4.0

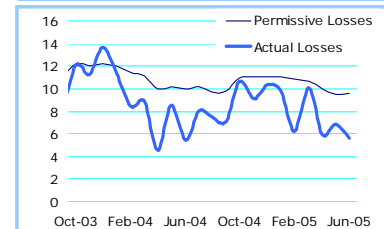
### Electricity supply, TWh

2003	3.17
2004	3.31
2005E	3.43

### Tariff change

I class	-2%
II class	-8%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	9.94	(0.18)	13.16	13.31	13.45	13.59	20.38	20.78	21.20	21.62	22.06
EBIT	USD mln	(3.05)	(13.18)	0.16	0.29	0.42	0.56	7.34	7.74	8.16	8.58	9.01
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	(3.05)	(13.18)	0.12	0.21	0.32	0.42	5.51	5.81	6.12	6.44	6.76
D&A	USD mln	13.00	13.00	13.01	13.02	13.03	13.03	13.04	13.04	13.04	13.04	13.04
Net CapEx	USD mln	(12.02)	(13.00)	(13.12)	(13.25)	(13.15)	(13.10)	(13.10)	(13.09)	(13.07)	(13.04)	(13.04)
WACC		20.0%	19.3%	18.6%	17.9%	17.2%	16.5%	15.8%	15.1%	14.4%	13.7%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.06</b>
EV/S-based target	<b>0.26</b>
<b>Target</b>	<b>0.25</b>

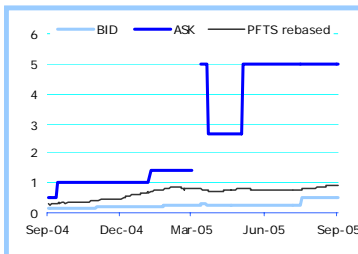
## BUY

Current price

Target price

**0.26**
**0.35**

### PREN Quotes, UAH



### Market Information

Number of shares, mln	103.64
MCap, USD mln	26.9
Free float, %	13.68

### Stock Ownership

State (NC ECU)	25.02%
Surkis	27.56%
Grigorishyn	33.64%
Other	13.68%

## PrikarpatOblenergo

This is the only company involved in the conflict between its minority shareholders, which managed to hold its AGM. The results of this AGM, however, were only satisfactory for Surkis's group: the state and Grigorishyn have lost most of their places on the supervisory board. PREN dividend payoff was the lowest among Oblenergos in 2005: only 10%. Dividend yield is 1.7%.

The results of the AGM are in question, as the Grigorishyn group is questioning the AGM's validity. The conflict is continuing, but it hasn't affected the company's operating results. Moreover it could even be beneficial for the company, as it increases the supervisory control of shareholders over all the moves of PREN's management.

The company is among the best performing Oblenergos, and there is no reason for this to change.

Our upgrade to BUY is supported by both DCF and peer valuation methods.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	75.1	11.7	7.7
2005E	97.5	13.4	9.3
2006E	102.3	13.7	9.6

### Key Ratios

	EV/S	EV/EBITDA
2004	0.51	3.3
2005E	0.40	2.9
2006E	0.38	2.8

**Region: Ivano-Frankivsk**
**Population:** 1.40 mln  
**Area:** 13,900 km<sup>2</sup>


Grid length, '000 km 25.3

Transformer capacity, GVA 2.8

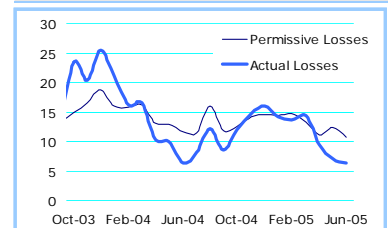
### Electricity supply, TWh

2003	1.53
2004	1.71
2005E	1.87

### Tariff change

I class	-9%
II class	-18%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	11.71	13.42	13.74	14.05	14.37	14.69	17.16	17.51	17.86	18.22	18.58
EBIT	USD mln	7.68	9.30	9.56	9.83	10.11	10.41	12.88	13.22	13.57	13.93	14.29
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	5.76	6.98	7.17	7.37	7.59	7.81	9.66	9.91	10.18	10.44	10.72
D&A	USD mln	4.03	4.12	4.18	4.23	4.26	4.27	4.28	4.29	4.29	4.29	4.29
Net CapEx	USD mln	(3.42)	(5.56)	(5.16)	(4.92)	(4.75)	(4.55)	(4.42)	(4.37)	(4.30)	(4.29)	(4.29)
WACC		19.0%	18.4%	17.8%	17.2%	16.6%	16.0%	15.4%	14.8%	14.2%	13.6%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

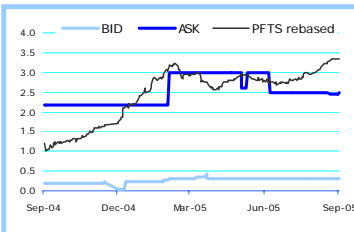
DCF-based price	<b>0.52</b>
EV/S-based target	<b>0.33</b>
<b>Target</b>	<b>0.35</b>

## BUY

Current price      Target price

**0.40**                      **0.73**

### SMEN Quotes, UAH



### Market Information

Number of shares, mln	26.89
MCap, USD mln	10.8
Free float, %	4.82

### Stock Ownership

VS Energy (Babakov)	95.18%
Other	4.82%

## SevastopolEenergo

Due to its size, SMEN is the smallest Oblenergo, it is one of the best performing companies.

The company paid USD 0.45 mln in dividends this year, which yielded 3.7%.

Limited free float makes the stock a doubtful investment opportunity as SMEN's price is rather unstable.

Our peer comparison valuation and simplified DCF show that the company has upside potential at the current price. Thus, we upgrade SMEN to BUY.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	30.4	4.7	4.1
2005E	37.6	4.7	4.1
2006E	39.5	4.9	4.2

### Key Ratios

	EV/S	EV/EBITDA
2004	0.34	2.2
2005E	0.27	2.2
2006E	0.26	2.1

Region: Sevastopol city

Population: 0.38 mln  
Area: 900 km<sup>2</sup>



Grid length, '000 km      1.2

Transformer capacity, GVA      0.9

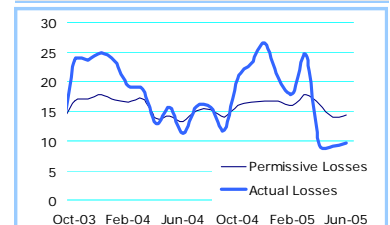
### Electricity supply, TWh

2003	0.76
2004	0.77
2005E	0.80

### Tariff change

I class	-3%
II class	-11%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	4.66	4.75	4.87	5.00	5.12	4.12	4.25	4.33	4.42	4.51	4.60
EBIT	USD mln	4.05	4.12	4.23	4.35	4.47	3.47	3.59	3.67	3.76	3.85	3.94
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBIT	USD mln	3.04	3.09	3.18	3.26	3.35	2.60	2.69	2.76	2.82	2.89	2.95
D&A	USD mln	0.60	0.63	0.64	0.64	0.65	0.65	0.65	0.66	0.66	0.66	0.66
Net CapEx	USD mln	(1.15)	(0.97)	(0.82)	(0.74)	(0.71)	(0.71)	(0.70)	(0.68)	(0.67)	(0.66)	(0.66)
WACC		19.0%	18.4%	17.8%	17.2%	16.6%	16.0%	15.4%	14.8%	14.2%	13.6%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.81</b>
EV/S-based target	<b>0.71</b>
<b>Target</b>	<b>0.73</b>



## BUY

Current price	Target price
<b>0.11</b>	<b>0.16</b>

## SumyOblenergo

Even though two rival groups, Surkis and Grigorishyn, have stakes in this company, no noticeable corporate conflicts have taken place. However, the company's AGM was not held this year, due to a court ruling. This did not affect minority shareholders, as the company was not expected to pay off large dividends: its EPS of USD 0.01 does not imply a dividend yield higher than 0.2%. The next AGM is scheduled for September 21.

The company has the lowest (negative) level of excessive electricity losses, which gives SOEN additional short term profits.

The company was fined USD 2.14 mln by the regulator for using money inappropriately in 2004. This fine will be taken out in equal monthly amounts for the next two years. This fine decreases our DCF target by USD 0.01.

The company is not listed on the PFTS, however, its shares are available for investors. DCF and peer valuation suggest an upside to the current price. We support our BUY recommendation on this stock.

<b>Region:</b>	<b>Sumy</b>
<b>Population:</b>	1.28 mln
<b>Area:</b>	23,800 km <sup>2</sup>



Grid length, '000 km	33.3
----------------------	------

Transformer capacity, GVA	3.5
---------------------------	-----

### Electricity supply, TWh

2003	1.41
2004	1.54
2005E	1.68

### Market Information

Number of shares, mln	177.13
MCap, USD mln	19.5
Free float, %	19.66

### Stock Ownership

State (NC ECU)	25%+1
Surkis	15.39%
Grigorishyn	39.95%
Other	19.66%

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	61.3	6.2	0.9
2005E	79.7	7.5	2.1
2006E	83.7	6.5	1.1

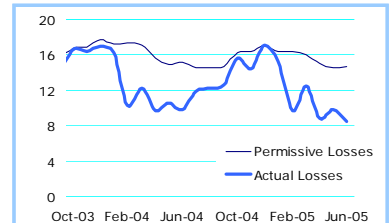
### Key Ratios

	EV/S	EV/EBITDA
2004	0.39	3.9
2005E	0.30	3.2
2006E	0.28	3.7

### Tariff change

I class	-12%
II class	-14%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
<b>EBITDA</b>	USD mln	6.16	7.47	6.49	6.51	7.53	7.56	11.72	11.95	12.19	12.43	12.68
<b>EBIT</b>	USD mln	0.89	2.15	1.14	1.14	2.14	2.16	6.32	6.55	6.78	7.03	7.28
<b>Tax Rate</b>		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
<b>Taxed EBI</b>	USD mln	0.67	1.61	0.85	0.85	1.61	1.62	4.74	4.91	5.09	5.27	5.46
<b>D&amp;A</b>	USD mln	5.28	5.32	5.36	5.38	5.39	5.40	5.40	5.40	5.41	5.41	5.41
<b>Net CapEx</b>	USD mln	(2.33)	(6.06)	(5.87)	(5.70)	(5.64)	(5.50)	(5.44)	(5.44)	(5.44)	(5.41)	(5.41)
<b>WACC</b>		19.0%	18.4%	17.8%	17.2%	16.6%	16.0%	15.4%	14.8%	14.2%	13.6%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

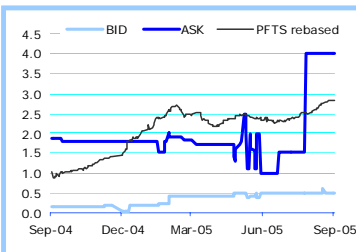
DCF-based price	<b>0.12</b>
EV/S-based target	<b>0.19</b>
<b>Target</b>	<b>0.16</b>

## BUY

Current price      Target price

**0.16**                      **0.21**

### TOEN Quotes, UAH



### Market Information

Number of shares, mln	61.09
MCap, USD mln	9.8
Free float, %	8.93

### Stock Ownership

State (NC ECU)	50.99%
Grigorishyn	40.08%
Other	8.93%

## TernopilOblenergo

This is the only company privatized in 1998, in which the state has a controlling stake. The company is one of the Oblenergos involved in the Surkis-Grigorishyn conflict. Like the others it twice failed to hold its AGM in March 2005.

The company's industrial consumers will see the largest decrease in retail electricity tariffs, which may stimulate electricity consumption in the region.

The company managed to reduce its electricity losses during 2003-2004, which, however, did not increase TOEN's net income in 2005.

As our multiple-based target suggests significant upside for TOEN, we support our BUY recommendation.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	31.4	0.9	-2.2
2005E	37.5	2.7	-0.3
2006E	39.4	2.9	-0.2

### Key Ratios

	EV/S	EV/EBITDA
2004	0.33	11.6
2005E	0.27	3.8
2006E	0.26	3.6

**Region:**                      **Ternopil**
**Population:**                      1.13 mln  
**Area:**                                      13,800 km<sup>2</sup>


Grid length, '000 km                      24.6

Transformer capacity, GVA                      2.1

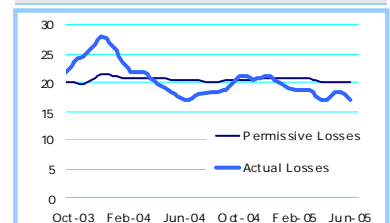
### Electricity supply, TWh

2003	0.90
2004	0.89
2005E	0.89

### Tariff change

I class	-12%
II class	-21%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

	2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	
EBITDA	USD mln	0.89	2.72	2.90	3.08	3.26	3.45	5.47	5.58	5.69	5.80	5.92
EBIT	USD mln	(2.16)	(0.34)	(0.16)	0.02	0.22	0.42	2.47	2.60	2.72	2.85	2.96
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	(2.16)	(0.34)	(0.16)	0.02	0.16	0.32	1.85	1.95	2.04	2.13	2.22
D&A	USD mln	3.05	3.06	3.06	3.06	3.05	3.02	3.00	2.98	2.96	2.96	2.96
Net CapEx	USD mln	(3.21)	(3.22)	(3.12)	(3.00)	(2.88)	(2.75)	(2.68)	(2.70)	(2.76)	(2.84)	(2.96)
WACC		20.0%	19.3%	18.6%	17.9%	17.2%	16.5%	15.8%	15.1%	14.4%	13.7%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.15</b>
EV/S-based target	<b>0.23</b>
<b>Target</b>	<b>0.21</b>

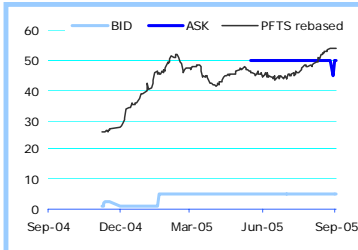
## BUY

Current price

Target price

**7.00**
**9.10**

### VIEN Quotes, UAH



### Market Information

Number of shares, mln	3.10
MCap, USD mln	9.3
Free float, %	4.85

### Stock Ownership

State (NC ECU)	75.00%
VS Energy (Babakov)	9.89%
Grigorishyn	10.26%
Other	4.85%

## VinnitsaOblenergo

The company is not in the pool of companies which are performing well because of poor profitability and a high level of excessive electricity losses.

Its high excessive electricity losses are related to the region profile: VIEN has many agricultural consumers with poor payment discipline, and its lines are often damaged by severe weather. In addition, VIEN's grid is in poor condition. The company is planning to spend USD 2.1 mln to reduce excessive electricity losses in 2005.

The debt offsetting process should alleviate VIEN's debt to the wholesale operator.

Almost all VIEN's shares are distributed among its three main shareholders. Limited free float makes VIEN's share price rather sensitive to demand for the shares.

Despite VIEN's relatively poor performance, our analysis shows that the stock has an upside potential. Thus, we recommend BUY.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	63.4	3.7	0.7
2005E	74.2	4.1	0.9
2006E	78.0	5.3	2.0

### Key Ratios

	EV/S	EV/EBITDA
2004	0.16	2.8
2005E	0.14	2.5
2006E	0.13	1.9

Region:

**Vinnitsa**

Population:

1.75 mln

Area:

 26,500 km<sup>2</sup>


Grid length, '000 km

48.4

Transformer capacity, GVA

3.7

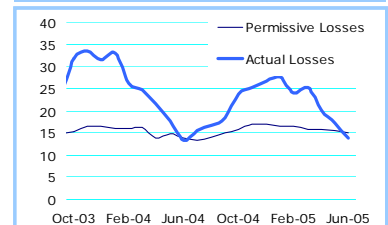
### Electricity supply, TWh

2003	1.72
2004	1.84
2005E	1.80

### Tariff change

I class	-10%
II class	-17%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
<b>EBITDA</b>	USD mln	3.69	4.08	5.33	6.58	7.83	9.08	14.76	15.06	15.36	15.66	15.98
<b>EBIT</b>	USD mln	0.67	0.90	2.00	3.13	4.30	5.49	11.15	11.43	11.73	12.04	12.35
<b>Tax Rate</b>		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
<b>Taxed EBI</b>	USD mln	0.51	0.67	1.50	2.35	3.22	4.12	8.36	8.58	8.80	9.03	9.27
<b>D&amp;A</b>	USD mln	3.01	3.18	3.33	3.45	3.53	3.59	3.61	3.62	3.62	3.62	3.62
<b>Net CapEx</b>	USD mln	(1.97)	(5.76)	(5.65)	(5.31)	(4.88)	(4.44)	(4.00)	(3.77)	(3.65)	(3.63)	(3.62)
<b>WACC</b>		21.0%	20.2%	19.4%	18.6%	17.8%	17.0%	16.2%	15.4%	14.6%	13.8%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>11.99</b>
EV/S-based target	<b>9.06</b>
<b>Target</b>	<b>9.10</b>

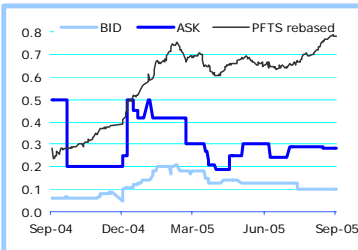
## BUY

Current price

Target price

**0.03**
**0.05**

### VOEN Quotes, UAH



### Market Information

Number of shares, mln	477.28
MCap, USD mln	14.3
Free float, %	14.7

### Stock Ownership

State (NC ECU)	75.0%
Grigorishyn	10.3%
Other	14.7%

## VolynOblenergo

Together with HMON, this is the best performing state-controlled Oblenergo, and the company, which is positioned good for further improvements.

The company reduced its excessive electricity losses last year. Its low share of industrial consumers suggests no threat of market share reduction in the long term.

The company paid USD 0.23 mln in 2005, which yielded 1.65% per share.

Both our valuation methods suggest significant upside at current VOEN's price. Thus, we upgrade our recommendation to BUY.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	33.8	2.7	1.2
2005E	41.6	2.9	1.3
2006E	43.7	3.3	1.7

### Key Ratios

	EV/S	EV/EBITDA
2004	0.39	4.8
2005E	0.32	4.6
2006E	0.30	4.0

**Region: Volyn (Lutsk)**
**Population:** 1.05 mln  
**Area:** 20,200 km<sup>2</sup>


Grid length, '000 km 25.6

Transformer capacity, GVA 2.1

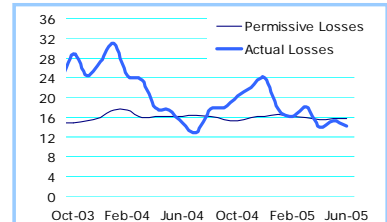
### Electricity supply, TWh

2003	0.92
2004	0.97
2005E	1.01

### Tariff change

I class	-5%
II class	-16%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	2.74	2.88	3.33	3.78	4.23	4.68	7.67	7.82	7.98	8.14	8.30
EBIT	USD mln	1.24	1.30	1.68	2.07	2.49	2.91	5.89	6.04	6.20	6.36	6.52
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	0.93	0.98	1.26	1.55	1.86	2.19	4.42	4.53	4.65	4.77	4.89
D&A	USD mln	1.50	1.58	1.65	1.71	1.74	1.77	1.78	1.78	1.78	1.78	1.78
Net CapEx	USD mln	(0.76)	(2.77)	(2.84)	(2.54)	(2.33)	(2.11)	(1.96)	(1.84)	(1.80)	(1.78)	(1.78)
WACC		20.0%	19.3%	18.6%	17.9%	17.2%	16.5%	15.8%	15.1%	14.4%	13.7%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.05</b>
EV/S-based target	<b>0.05</b>
<b>Target</b>	<b>0.05</b>

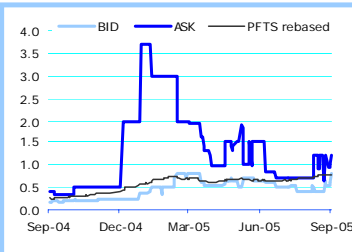
## SELL

Current price

Target price

**0.24**
**0.11**

### ZOEN Quotes, UAH



### Market Information

Number of shares, mln	124.60
MCap, USD mln	29.9
Free float, %	14.48

### Stock Ownership

State (NC ECU)	75.00%
VS Energy (Babakov)	10.52%
Other	14.48%

## ZakarpatoBlenergo

The company has the fourth largest level of excessive electricity losses among all the Oblenergos, and there is no visible improvement in this area.

Theft and harsh weather are the main reasons for the company's excessive electricity losses.

Despite high electricity losses (part of which are still compensated by electricity tariffs), the company managed to post a positive net income in 1Q05 and 2Q05.

Our peer comparison method based on current performance suggests a considerable downside to the current price, and the DCF based price supports this result. We are sticking with our SELL recommendation.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	45.5	2.1	-0.3
2005E	56.8	2.2	-0.4
2006E	59.6	3.2	0.5

### Key Ratios

	EV/S	EV/EBITDA
2004	0.70	14.9
2005E	0.56	14.6
2006E	0.54	9.8

Region: **Transcarpathian (Uzhgorod)**

Population: 1.25 mln  
Area: 12,800 km<sup>2</sup>



Grid length, '000 km 17.4

Transformer capacity, GVA 2.3

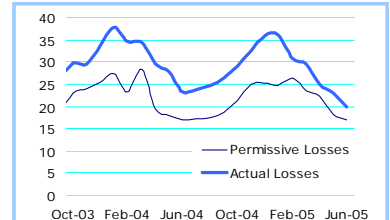
### Electricity supply, TWh

2003	1.37
2004	1.47
2005E	1.57

### Tariff change

I class	-9%
II class	-14%

### Electricity Losses, % Of Purchased El.



### DCF Model Summary\*

		2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E
EBITDA	USD mln	2.14	2.18	3.25	4.32	5.39	6.46	10.56	10.77	10.98	11.20	11.43
EBIT	USD mln	(0.30)	(0.41)	0.51	1.44	2.39	3.40	7.46	7.65	7.86	8.08	8.30
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	(0.30)	(0.41)	0.38	1.08	1.80	2.55	5.59	5.74	5.89	6.06	6.23
D&A	USD mln	2.44	2.59	2.74	2.88	3.00	3.06	3.10	3.12	3.13	3.13	3.13
Net CapEx	USD mln	(2.03)	(4.97)	(5.07)	(5.06)	(4.88)	(4.12)	(3.70)	(3.41)	(3.21)	(3.13)	(3.13)
WACC		21.0%	20.2%	19.4%	18.6%	17.8%	17.0%	16.2%	15.4%	14.6%	13.8%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

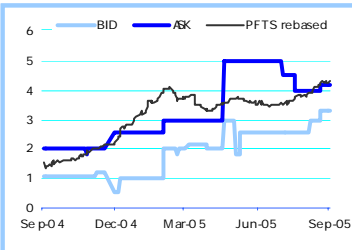
DCF-based price	<b>0.16</b>
EV/S-based target	<b>0.10</b>
<b>Target</b>	<b>0.11</b>

## SELL

Current price      Target price

**1.00**                      **0.66**

### ZAON Quotes, UAH



### Market Information

Number of shares, mln	179.36
MCap, USD mln	179.4
Free float, %	10.95

### Stock Ownership

State (NC ECU)	60.24%
Surkis	10.14%
Grigorishyn	18.67%
Other	10.95%

## Zaporizhia Oblenergo

The company succeeded in reducing its excessive electricity losses, and over the last two reported quarters the company started showing a positive net income.

ZAON's future rate of revenues and market position are uncertain due to the company's over regulation and dependence on industrial consumers.

The increase to ZAON's retail tariff for industrial consumers may increase the market share of alternative, non-regulated, electricity suppliers in Zaporizhia region.

In June 2005 ZAON's former CEO was accused of misappropriating USD 1.4 mln during the previous year. This suggests that ZAON's profitability is intentionally reduced, and leaves room for optimism.

Still, both our valuation methods showed that ZAON is overpriced. We support our SELL recommendation.

### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	276.5	5.2	-0.2
2005E	341.2	5.4	-0.1
2006E	358.2	6.4	0.9

### Key Ratios

	EV/S	EV/EBITDA
2004	0.64	34.1
2005E	0.52	33.1
2006E	0.50	27.9

**Region:**                      Zaporizhia

**Population:**                      1.91 mln  
**Area:**                                      27,200 km<sup>2</sup>


Grid length, '000 km                      41.0

Transformer capacity, GVA                      9.3

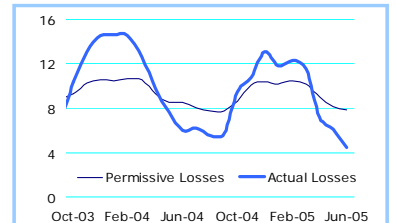
### Electricity supply, TWh

2003	10.77
2004	10.15
2005E	10.63

### Tariff change

I class	3%
II class	7%

### Electricity Losses, % Of Purchased EI.



### DCF Model Summary\*

	2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	
EBITDA	USD mln	5.20	5.37	6.37	7.36	8.36	9.36	30.35	30.95	31.57	32.21	32.85
EBIT	USD mln	(0.25)	(0.10)	0.85	1.81	2.80	3.80	24.78	25.39	26.00	26.64	27.28
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	(0.25)	(0.10)	0.64	1.36	2.10	2.85	18.59	19.04	19.50	19.98	20.46
D&A	USD mln	5.45	5.46	5.51	5.55	5.56	5.57	5.57	5.57	5.57	5.57	5.57
Net CapEx	USD mln	(10.83)	(5.73)	(6.29)	(6.12)	(5.70)	(5.65)	(5.60)	(5.60)	(5.60)	(5.57)	(5.57)
WACC		21.0%	20.2%	19.4%	18.6%	17.8%	17.0%	16.2%	15.4%	14.6%	13.8%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.46</b>
EV/S-based target	<b>0.72</b>
<b>Target</b>	<b>0.66</b>

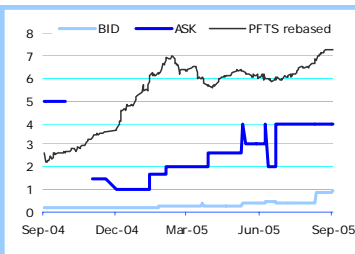
## SELL

Current price

Target price

**0.40**
**0.29**

### KION Quotes, UAH



### Market Information

Number of shares, mln	122.40
MCap, USD mln	49.0
Free float, %	8.4

### Stock Ownership

VS Energy (Babakov)	91.6%
Other	8.4%

## Zhytomir Oblenergo

This is one of the top three Oblenergos with excellent overall results.

The company has potential for sales growth, because its retail tariff will decrease significantly during the next 10 months. This may stimulate electricity consumption in the region, which would be a boost for ZHEN.

However, our analysis showed that the stock is overvalued. In addition, most of the stock is concentrated in one hand, which considerably limits its liquidity and makes the stock price rather unstable. We downgrade ZHEN to SELL.

**Region:** Zhytomir

**Population:** 1.37 mln  
**Area:** 29,900 km<sup>2</sup>


Grid length, '000 km 37.9

Transformer capacity, GVA 3.3

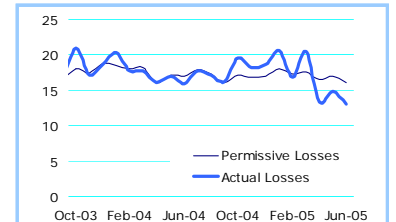
### Electricity supply, TWh

2003	1.66
2004	1.67
2005E	1.72

### Tariff change

I class	-10%
II class	-25%

### Electricity Losses, % Of Purchased EI.



### Key Financial Data, USD mln

	Net revenue	EBITDA	EBIT
2004	60.5	9.8	5.7
2005E	74.3	10.5	6.3
2006E	78.0	10.5	6.3

### Key Ratios

	EV/S	EV/EBITDA
2004	0.79	4.9
2005E	0.64	4.6
2006E	0.61	4.5

### DCF Model Summary\*

	2004	2005E	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	
EBITDA	USD mln	9.77	10.47	10.50	10.53	10.56	7.75	7.78	7.93	8.09	8.25	8.42
EBIT	USD mln	5.66	6.30	6.28	6.29	6.31	3.49	3.52	3.68	3.83	4.00	4.16
Tax Rate		25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBI	USD mln	4.24	4.73	4.71	4.72	4.73	2.62	2.64	2.76	2.88	3.00	3.12
D&A	USD mln	4.11	4.16	4.21	4.24	4.25	4.25	4.25	4.26	4.26	4.26	4.26
Net CapEx	USD mln	(5.57)	(5.01)	(5.00)	(4.62)	(4.39)	(4.35)	(4.28)	(4.28)	(4.26)	(4.26)	(4.26)
WACC		19.0%	18.4%	17.8%	17.2%	16.6%	16.0%	15.4%	14.8%	14.2%	13.6%	13.0%

\* Basic assumptions about DCF model are listed on pages 25-27

### Valuation Summary, USD

DCF-based price	<b>0.21</b>
EV/S-based target	<b>0.31</b>
Target	<b>0.29</b>

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