



Analyst's Notebook

Ukraine/Energy
 January 25, 2006

****Editor's Note:** In order to keep our coverage of the Ukrainian market as up to date as possible Concorde Capital is launching a new product – Analyst's Notebook. Unlike our more in-depth desk notes and reports, Analyst's Notebook provides rapid feedback on breaking news in the Ukrainian market. Analyst's Notebook gives you our analysts' first impressions of a situation and may set the table for further investigation. Our analysts will use their experience in their sectors to take a look at the situation and provide insight or speculate on possible scenarios. We want to emphasize however, this product consists mostly of the analyst's intuition and may require further analysis.

CEZ To Enter The Ukrainian Electricity Market?

In a nutshell: CEZ officials have confirmed that they are targeting Ukrainian Oblenergos controlled by VS Energy:

94.0% in Kirovogradoblenergo (**KION: HOLD**) 90.5% in Khersonoblenergo (**HOEN: SELL**)
 55.4% in Odessaoblenergo (**ODEN: N/R**) 95.2% in Sevastopolenergo (**SMEN: HOLD**)
 91.6% in Zhytomiroblenergo (**ZHEN: BUY**)

A CEZ representative confirmed that VSE had agreed to sell the blocks, for the right price.

How Much CEZ Is Going To Pay?

We estimate the fair value of these stakes at about USD 250 mln, while VSE is rumored to want twice this amount. Clearly a sweet deal for VSE, which bought controlling blocks in **KION**, **HOEN**, **SMEN** and **ZHEN** for only about USD 92 mln in 2001.

We gauge the price CEZ may pay for the stakes in the five Oblenergos by looking at CEZ's latest deals in Central and Eastern Europe (CEE):

CEZ Acquisitions Of Distribution Companies In CEE

		Oltenia (Romania)	Pleven, Sofia, Sofia Oblast (Bulgaria)
Price	EUR mln	151	281.5
Stake		51%	67%
Sales 04	EUR mln	399	361
El. Supply 04	TWh	6.8	7.7
EBITDA 04	EUR mln	70	35
P/S		0.74	1.16
P/EBITDA		4.2	12.0
P/El. Suppl	USD/MWh	52.7	66.3

Source: CEZ, Concorde Capital estimates

Possible Price For Stakes In Five Oblenergos, USD mln

	Implied By Oltenia	Implied By Bulgarian Three
P/S	254.9	399.3
P/Electricity	413.3	520.0

Source: CEZ, Concorde Capital estimates

However, these implied prices do not reflect adjustments needed to account for the companies' net debt. **HOEN's** debt to the energy market is USD 75 mln (which may be compensated by USD 71 mln in receivables from consumers), and **ODEN's** debt is USD 206 mln (net receivables USD 22 mln). If the debts are restructured (as it is stipulated by the new law on debt restructuring for energy companies adopted in June 2005) CEZ will offer the price implied by its other CEE acquisitions.

What's With AES-Ukraine?

AES, which controls Kievoblenergo (**KOEN: N/R**) and Rivneoblenergo (**ROEN: N/R**), also has plans to buy blocks in five of VSE's Oblenergos, and is going to participate in future Oblenergo privatizations. CEZ, on the other hand, has expressed interest in buying two companies owned by AES.

If CEZ enters the Ukrainian market by purchasing five Oblenergos, we believe it will be hard for AES to compete with CEZ when other Ukrainian generation and distribution companies are privatized. Despite the fact that AES has been operating for five years in Ukraine, we believe the management of CEZ would be more efficient at privatization, as they know the rules of the Eastern European game better, and would learn faster than AES. Thus, CEZ is likely to acquire the most attractive companies when they are privatized, leaving the rest for AES.

If AES sells its networks to VSE, this would mean they share our concerns. However, we do not believe AES will do it: they seem set on some very ambitious plans. AES believes it will be able to create adequate competition for CEZ in Ukrainian privatization.

What's With VSE's Minority Holdings?

VSE also has minority stakes in several Oblenergos:

- About 22% in Chernivtsioblenergo (**CHEN: N/R**)
- About 12% in Khmelnikoblenergo (**HMON: SELL**)
- About 24% in Mykolaivoblenergo (**MYON: N/R**)

It is doubtful CEZ is interested in these stakes, as they do not give any access to the companies' management. **WATCH:** these stocks are likely to become available to portfolio investors.

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