Ukraine / Utilities

Energougol

An Oblenergo with Donetsk Muscle

BUY

September 20, 2006	**3.6 USD**
12m Target	**5.1 USD**

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Company name:
Power Grid Company (PGC) Energougol

Alternative name:
PGC Enerhovuhillya

Abbreviation (Unofficial):
ENUG

Market Information	
Not listed	
No of Shares, mln	**5.49**
Market price, USD (Indicative)	3.6
Target Price, USD	5.1
Upside	**42%**
Target MCap, USD mln	28.1
Free Float, %	**16%**

Stock Ownership	
Embrol Ukraine	11.79%
SCM	15.34%
ARS	24.98%
Servis-Invest	20.46%
Total SCM-related	**72.57%**
Other	**27.43%**

Ratios 2006E	
EBITDA Margin	7.3%
EBIT Margin	6.0%
Net Margin	4.7%
Net Debt/Equity	0.01

We are initiating coverage of the electric power distributor Energougol, a supplier of electricity to coal mines in the Donetsk region, which is similar in its business structure and regulatory environment to an Oblenergo. The company's main shareholder, SCM, has airtight ties to the new government, and with former SCM managers now in key state positions controlling the energy sector, Energougol is likely to enjoy favorable treatment. The stock is currently traded only over the counter, but our indicative price suggests a 42% upside.

Power Grid Company Energougol (ENUG) is similar to Ukraine's regional electricity distributors or Oblenergos: it transmits electricity through its own energy networks to its customers. The main thing separating ENUG from Oblenergos is that it specializes in supplying energy to coal mines.

Energougol is poised to reap greater profits in the midterm thanks to expected changes in tariff policies for energy distribution companies and the backing of SCM, the government and the main ruling party, the Party of Regions.

The revival underway of Ukraine's coal sector guarantees stable growth in demand for the company's energy supplies. On top of that, SCM's unrivalled lobbying power puts Energougol in a good position to snatch market share from another, state-owned supplier of energy to coal mines, which currently operates parallel to ENUG.

Like other energy companies Energougol has high debts, but they are due to be restructured according to a law designed to resolve energy sector companies' debts. ENUG is likely to mutually reconcile its debts, as its creditors are indirect debtors of its main debtors.

The main risk associated with Energougol is SCM's disregard for minority shareholders, which the company displayed with its recent dilutive share issue at Azovstal earlier this year and its plans to approve a similar, more dilutive share issue at ZaporizhCoke. On the other hand, SCM's recent moves to increase business transparency and form good relations on global capital markets suggest SCM will be more investor friendly as it takes a dominant role in the energy sector.

ENUG is not listed on any stock exchange, but it has a free float of about 16%, much of which is still held by individuals who received shares through mass privatization. Our peer valuation suggests a 42% upside to ENUG's indicative price. We initiate coverage with a BUY recommendation.

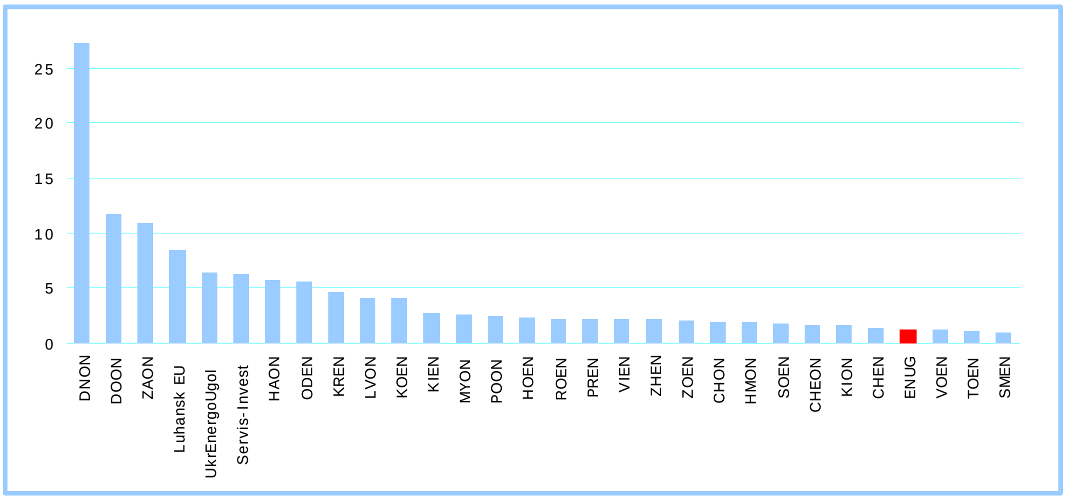
Key Financials, USD mln

	Sales	EBITDA	Margin	Net Income	Margin
2003	39.0	2.8	7.1%	1.4	3.5%
2004	39.4	2.6	6.5%	1.3	3.4%
2005	44.6	2.8	6.2%	1.7	3.7%
2006E	55.8	4.1	7.3%	2.6	4.7%

Energougol: Like a Small Oblenergo

EnergoUgol (referred to as ENUG) is an electricity distribution company operating in the Donetsk region, in the same regulatory environment as regional energy distribution companies (Oblenergos). In terms of the volume of electricity it supplies it can be compared to the smaller Oblenergos.

Volumes of Electricity Distributors (TWh Bought Wholesale, 2005)

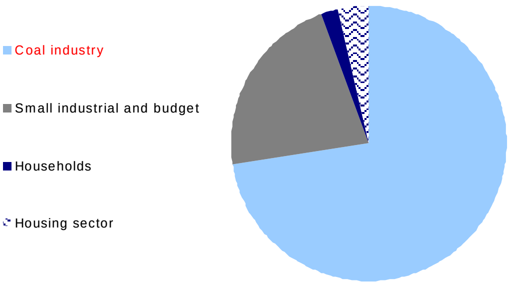


Source: EnergoBiznes

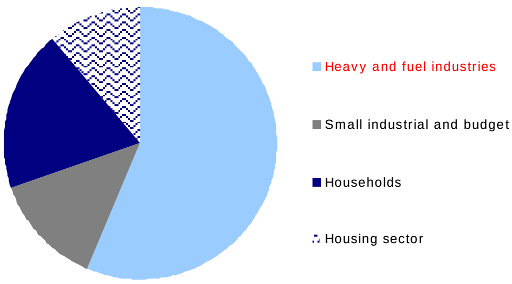
Specialization in the Coal Industry

Energougol's main activity is the transmission of electricity from its power grids and the supply of electricity to consumers. The company was created specifically to supply electricity to coal mines in the Donetsk region, and the coal industry accounts for about three-quarters of the company's market.

Energougol Consumer Breakdown

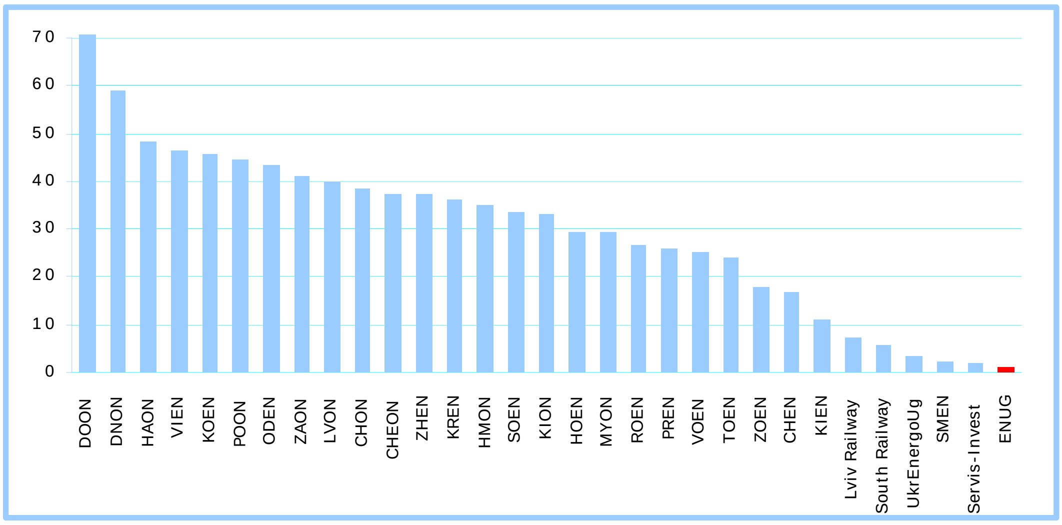


Average Oblenergo Consumer Breakdown



Source: Company data, Fuel and Energy Ministry, Concorde Capital

Power Grids of Ukrainian Companies, ths km



Source: NERC, company data

Because of its specialization, Energougol's grid is much smaller than Oblenergos.

A Privately Owned Public Company, With Existing Free Float

ENUG is a public company (an open joint-stock company), owned by SCM, whose affiliates control 72.5% of the shares. It is managed by the Donbass Fuel and Energy Company (DFEC), SCM's vehicle for consolidating its assets in the power sector.

ENUG's estimated free float is 16%, much of which is still held by individuals who received shares through mass privatization. ENUG is not listed on any stock exchange and its shares have no trading history.

A Stable Market

Energougol's history is rooted in Soviet times: it was created in 1989 as a structural unit of the regional coal holding, and was responsible for the operation of coal mine power grids, and grids in mining settlements. ENUG was privatized in 1995, but otherwise the company and its business have been remarkably stable for the past 27 years.

The Donetsk Retail Energy Market

Four companies own and operate their own power grids in the Donetsk region:

DonetskOblenergo (DOON) – used to be the monopoly supplier of electricity in Donetsk region, excluding coal industry enterprises.

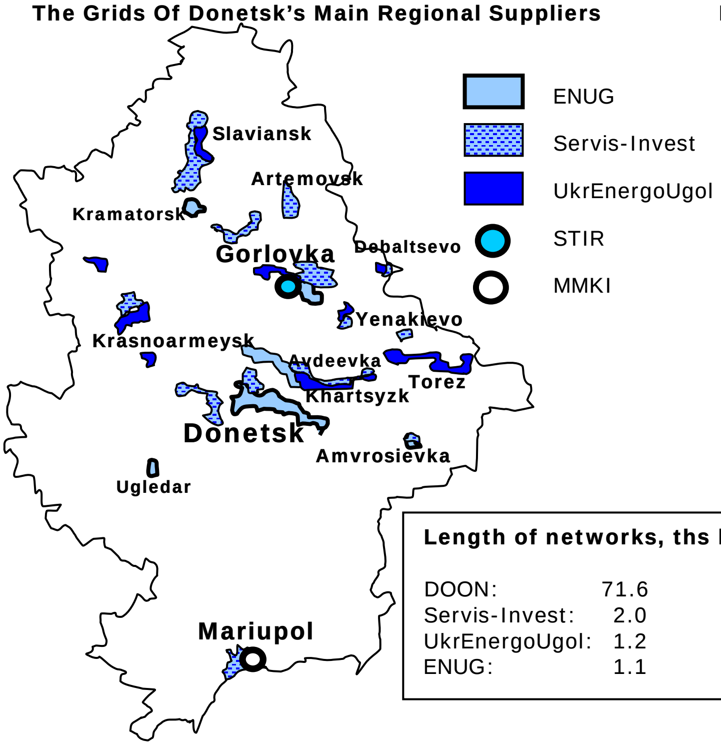
PGE Energougol – specializes in supplying energy to coal mines in Donetsk region and large consumers in the city of Donetsk.

UkrEnergoUgol – is a state-controlled company created in 2004 on the basis of the former regional state-owned company DonetskUgol, which also supplies electricity to coal mines. The company supplies coal mines in Donetsk, Luhansk, Volyn and Lviv regions.

Servis-Invest – is a private company controlled by SCM/DFEC and specializes in supplying electricity to metallurgy and coke plants in the Donetsk and Dnipropetrovsk regions. Its power grids were stripped from DOON. In 2002-2003 the company cannibalized a considerable share of DOON's market (see chart below).

The four companies that operate their own grids all supply electricity at tariffs fixed by Ukraine's market regulator, the National Energy Regulatory Commission (NERC). In addition, there are about ten companies with licenses to supply electricity in the Donetsk region at unregulated tariffs. The largest of these are the chemicals producer Stirol (STIR) and the steel mill Mariupol Illicha (MMKI), which supply electricity to themselves and related enterprises. These independent suppliers have no grids, so they pay transport tariffs to one or more of the four distributors listed above.

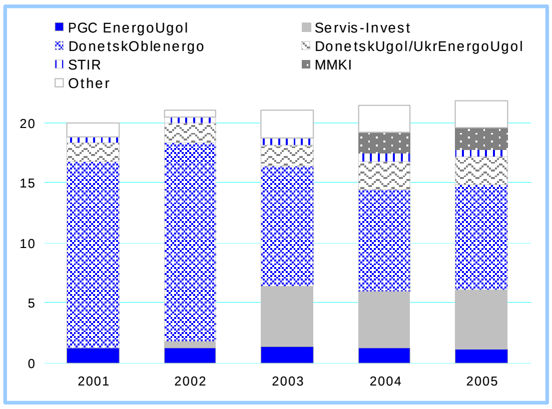
The Grids Of Donetsk's Main Regional Suppliers



Length of networks, ths km:

DOON:	71.6
Servis-Invest:	2.0
UkrEnergoUgol:	1.2
ENUG:	1.1

Donetsk Regional Supply Market, TWh



Source: EnergoBiznes, Concorde Capital estimates

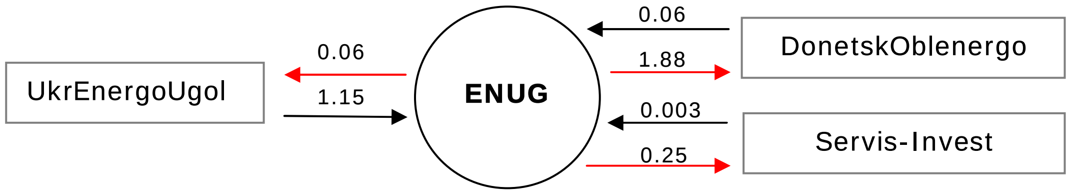
Crossed Networks

Because there are four companies with power grids in the Donetsk region, their networks are interconnected in a way that every transmission company has to use the networks of other companies to transmit electricity to some of its customers. For this reason, energy companies in the Donetsk region end up paying each other for transmission services.

DOON, as the company operating the largest network in the region (see the map above) receives the most income for its transmission services.

ENUG will pay USD 2.19 mln to other companies in 2006, and will obtain from them USD 1.21 mln for the provision of transmission services.

Mutual Payments for Transmission Services, 2006, USD mln



Source: NERC

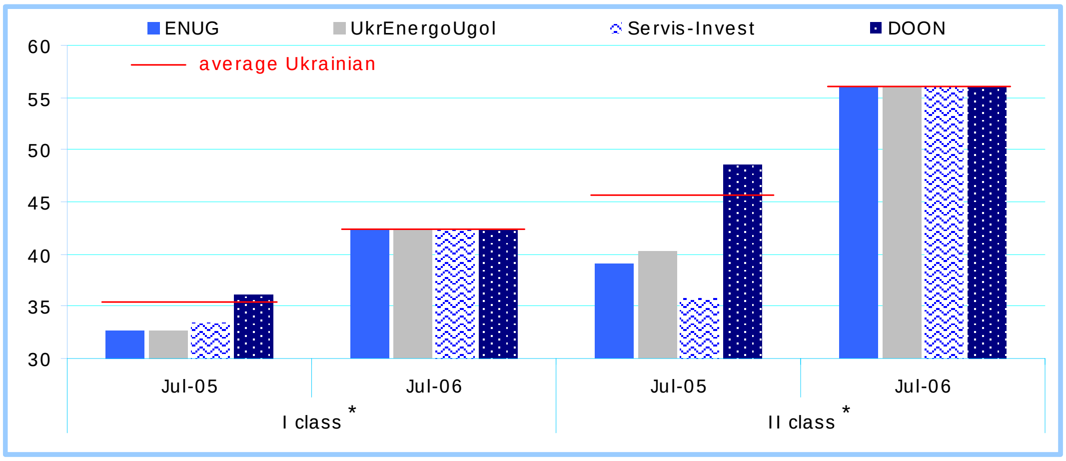
Note that ENUG has a positive payment balance with UkrEnergoUgol, the state-controlled company which has the same target customer base as ENUG. This means that many coal mines which are located near ENUG's grids are customers of UkrEnergoUgol. If ENUG manages to entice these consumers away from the state company, which is a probable outcome (see page 9), its market will increase by 15%.

Competition in the Local Market

No more price competition

The large number of electricity suppliers in Donetsk region means tough competition for consumers. In the past, Energougol's main competitive advantage was its low tariffs and high quality of additional services. However, in September 2005 tariffs were made equal for all suppliers nationwide, with the only differentiation being between several broad categories of consumers. Energougol thus lost its former ability to undercut its competitors with lower tariffs.

Retail Tariffs For Donetsk Region Suppliers, USD / MWh



Source: NERC, Concorde Capital calculations
** I class – high-voltage consumers; II class - low voltage consumers*

How to compete?

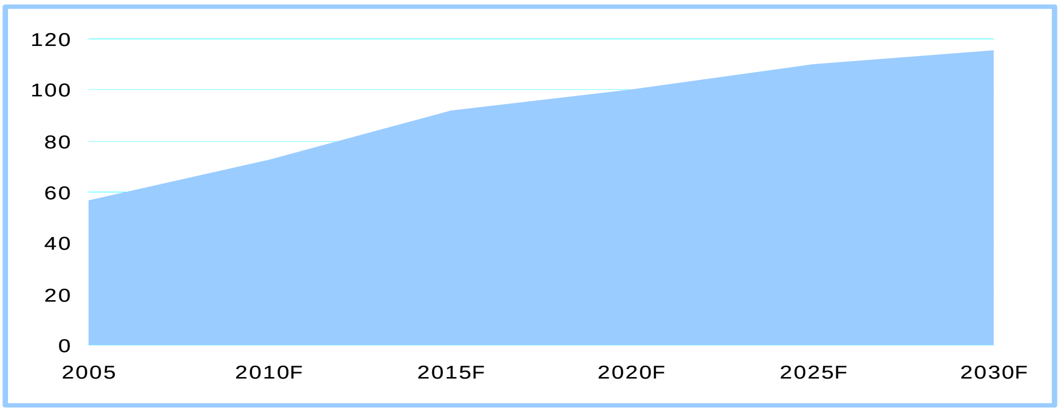
ENUG still has a significant advantage over other regulated-tariff suppliers in the Donestsk region, as ENUG also has a license to distribute electricity at <u>unregulated</u> tariffs. The company can only use this license in places where it has no grid. Thus, ENUG has the ability to enter territories occupied by its competitors and undercut them.

Another important advantage is the increased lobbying power of ENUG's parent company, SCM. Last month, after the new government was appointed, SCM managers were appointed to all the most important state positions controlling the power sector (the heads of the wholesale energy market Energorynok, the state energy sector holding company Energy Company of Ukraine, and NERC). This guarantees that there will be no decrease in ENUG's market share, and gives the company an opportunity to increase its market share in the mid-term by cannibalizing from energy companies not related to the DFEC group (see pages 8-9 for more details).

Coal Mines: a Growing Market

In addition to the prospect of increasing its supply market at the cost of other companies, ENUG's current customers are likely to increase their electricity use. The government's 25-year Energy Strategy foresees a doubling of coal output over the next 25 years. This growth is expected to come from increased efficiency of existing mines and new mines.

Ukrainian Coal Production Forecast, mln mt



Source: Ukrainian government, "Energy Strategy of Ukraine Through 2030"

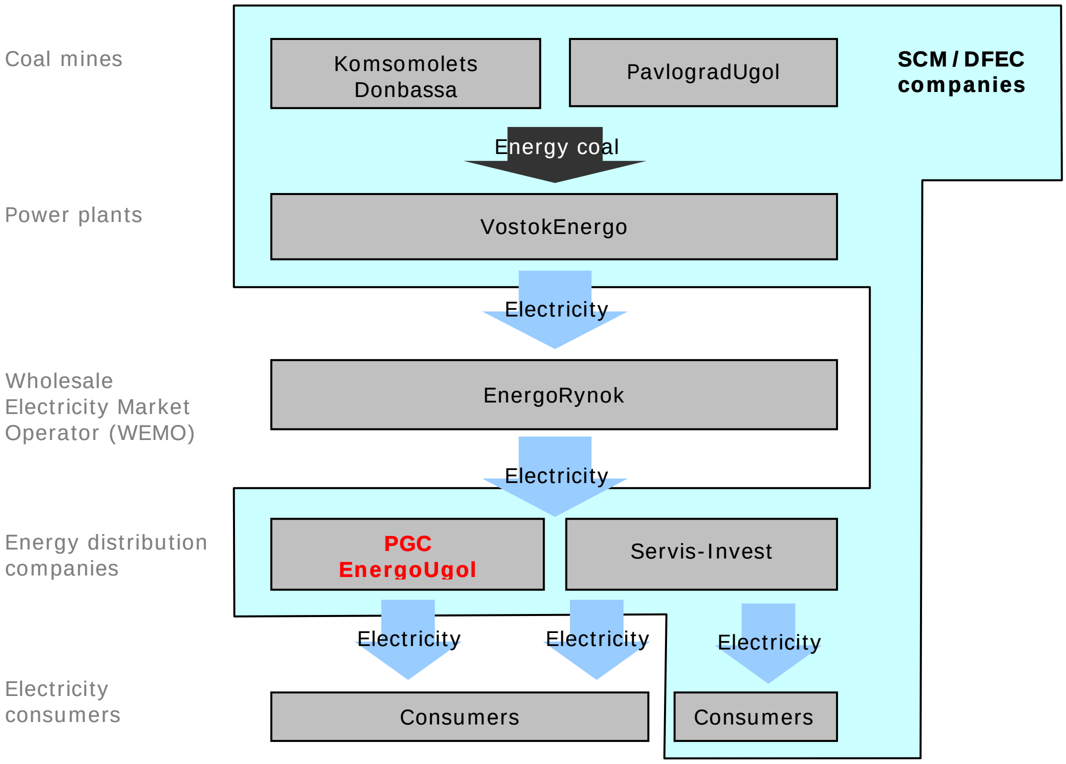
We expect the increase of production by ENUG's current customers alone will increase demand for the company's electricity supply by 60% in the long-term.

Ownership: The Key Issue

ENUG is managed by the Donbass Fuel And Energy Company (DFEC), which is controlled by Rinat Akhmetov's SCM group. As Akhmetov is now arguably the most powerful person in Ukraine, we expect ENUG to enjoy significant benefits.

The DFEC Group

DFEC manages a vertically integrated group of coal mines, fossil fuel power plants and electricity suppliers. DFEC units are owned by SCM and its various affiliates.



ENUG and Servis-Invest represent the energy distribution wing of DFEC. Both companies are focused on supplying industrial consumers in the Donetsk region, but their target consumers do not overlap, as Servis-Invest is concentrated on metals and coke plants while ENUG is responsible for coal mines.

DFEC People Rule The Roost

Since the new government was appointed, several DFEC managers have moved to key state positions controlling the energy sector, including the heads of Energorynok, the state-run wholesale electricity monopoly; the National Electricity Regulatory Commission, which regulates the electric power and gas sectors; and the National Energy Company, the holding company for state stakes in the power sector. As a result, DFEC people *de facto* control the entire electric power regulatory chain.

Market Share to Increase

SCM's increased clout is likely to help DFEC companies boost their market shares in the Donetsk region.

- Servis-Invest, which controls 2,000 km of power grid that was stripped from Donetskoblenergo (DOON) in 2003-2004, can further increase its market share by crowding out DOON.

- ENUG is likely to grab a large chunk of the coal market from UkrEnergoUgol, ENUG's main competitor.

  Note that UkrEnergoUgol was created to supply electricity to state-run coal mines, at cheaper tariffs, which was possible because UkrEnergoUgol's specialization meant its customers did not have to cross-subsidize residential customers. UkrEnergoUgol's retail tariffs were lower than average before September 2005 (see chart on page 6). But after tariffs were standardized for industrial consumers, there is no longer any purpose for a specialized company supplying state mines. Therefore**,** ENUG is likely to take at least part of UkrEnergoUgol's customer base**.** We expect ENUG will increase its market share by at least 15% in the mid-term.

Expected Tariff Policy Benefits

The new chairman of NERC, with his close ties to SCM, suggests that we could see some tariff privileges for Sevis-Invest and ENUG. Note that a new tariff policy for Oblenergos is currently being drafted, in which tariffs will be based to their regulatory asset basis (RAB). DEFC's two distribution companies are likely to be given favorable tariffs or at least enjoy a more flexible tariff policy.

Less to Fear from Showing Higher Profits

The current regulatory environment in the energy distribution sector discourages companies from disclosing profits higher than those prescribed in their tariff negotiations, as to do so could lead to their tariffs being reduced (see our Oblenergo report of Dec. 15, 2005). As people close to DFEC now control the regulator, we expect ENUG to be willing to report extra profits.

Dilution Risks

The SCM group has been involved this year in two scandals connected to share dilutions, at Azovstal (AZST) and more recently at ZaporizhCoke (ZACO). This implies growing risks associated with investment in SCM-controlled companies.

The expected restructuring and consolidation of DFEC-controlled assets, with possible share swaps, adds even more uncertainty to ENUG's future. In Azovstal's case, a buyback offer was made at slightly less than the market price (see our notebook on AZST of July 10). In ZACO's case, we were told by an SCM official that there would be a buyback offer to minorities but it would be less than market price (see our notebooks on ZACO of August 29 and 31).

However, this week, the Justice Ministry registered new regulations approved by the State Securities and Exchange Commission which require companies that carry out dilutive share issues to make buyback offers at market prices. Although we haven't seen the final text – the crucial question is, how will market price be determined? – any such mechanism should substantially reduce dilution risks for Ukrainian stocks.

Also, the main purpose of DFEC is to consolidate assets in order to gain more access to international capital markets. DFEC and SCM are unlikely to want to be involved in additional scandals with minority shareholders. Therefore, we think the risk of a dilutive share issue at Energougol without a fair buyback offer is too small to be significant.

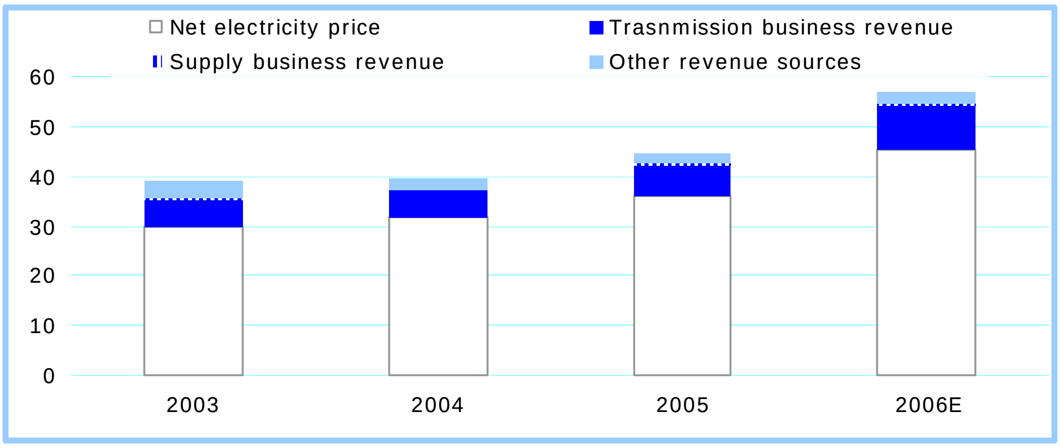
Financials

Revenue Breakdown

Like many Oblenergos, Energougol is obliged to deposit all the money it collects from its customers into a special distribution account. The net value of the electricity is paid from this account directly to the wholesale market operator. Although recorded as revenues (and simultaneously as costs), ENUG has no access to these funds. Only the value of transmission and supply services provided by ENUG goes to he company's business account.

ENUG is subject to this restriction because it has debts to the wholesale market. If the debts were cleared, ENUG would be allowed to deposit the money it collects from customers into its own business account.

Reported Revenue Breakdown, USD mln



Source: Company data, Concorde Capital estimates

Transmission and Supply Revenues to Grow 39% in 2006

As ENUG has a relatively constant customer base, revenues from the distribution and supply of electricity depend mainly on the tariffs set by the NERC. In 2001-2004, ENUG's tariffs changed only once, and therefore the company's revenue was relatively stable. In 2005, ENUG saw two changes, with an average growth in tariffs by 22% yoy, which was reflected by a noticeable increase of the company's top and bottom lines.

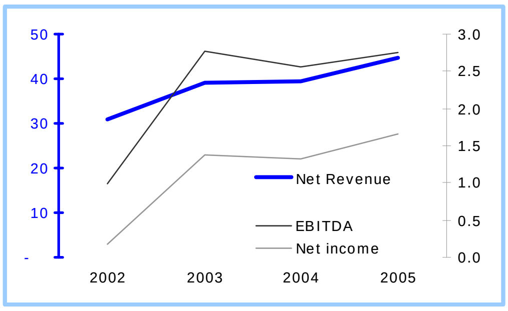
Another increase in tariffs occurred in February 2006, which will yield an average distribution tariff growth of 40% yoy in 2006 and supply tariff growth of 27% yoy.

To sum up, we expect ENUG's revenue from the transmission and supply business to increase 39% yoy in 2006, assuming stable energy supply demand. The expected 27% yoy jump in net electricity prices will add significantly to ENUG's reported revenue in 2006.

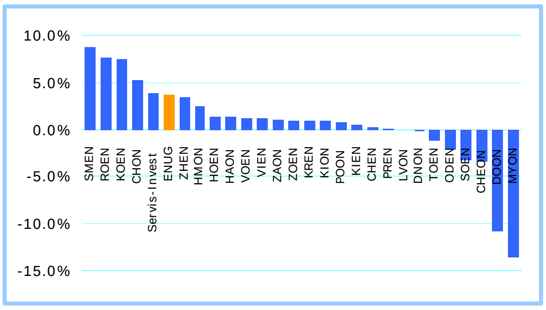
Relatively High Margins

Energougol reports the most stable EBITDA and net income of Ukraine's energy distribution companies. The company ranks as the 6th most profitable distributor (as of 2005), with margins comparable to privatized Oblenergos.

ENUG Financials, USD mln



Oblenergo Net Margins, 2005



Source: Company data

After the latest tariff increase, we expect ENUG's EBITDA to grow by USD 1.34 mln, and net income to grow by USD 0.95 mln in 2006.

According to 1H results, ENUG has increased sales by 56% yoy and more than doubled EBITDA and net income.

ENUG Financials, USD mln

	1H04	1H05	1H06	1H06: yoy growth
Sales	20.4	20.2	31.5	56%
EBITDA	1.4	0.9	2.6	192%
Net income	0.7	0.4	2.9	609%

Source: Company data

Change in Tariff Policy to Positively Affect Margins?

Current tariff policy for energy distribution companies is based on their investment needs.

Allowed Net Income, Current Approach, USD mln

	Investment program	D&A	Needed Profit to fulfill inv. program	Actual profit
2005	2.04	0.38	**1.66**	1.65

Source: NERC, company data, Concorde Capital estimates

The NERC is working on a new tariff policy for Oblenergos to be introduced since 2007, based on the regulated asset base (RAB) methodology. The base for the company's profits (RAB) is most likely to be tied to the fixed assets of energy distribution companies.

We consider two parameters to be the most reliable in estimating RAB: the book value of fixed assets, and the replacement value of fixed assets. We provided separate estimates based on each of those parameters. We understand that NERC is planning the after-tax rate of return to be about 11%.

Expected Mid-Term Return Calculation: Fixed Assets Approach, USD mln

	Assets Value	Rate of return	Allowed Net Income
Fixed Assest, gross value	7.85	11%	**0.86**
Fixed Assets, replacement value (Est.)	28.9	11%	**3.18**

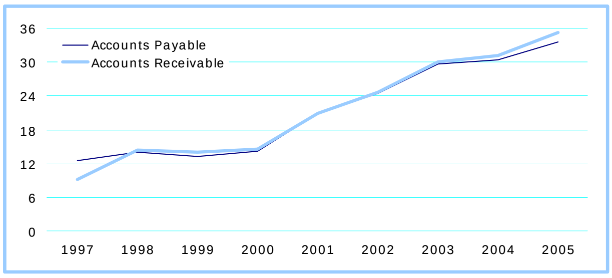
Source: NERC, company data, Concorde Capital estimates

The estimates of ENUG's allowed profit after the new RAB-based tariffs are implemented ranges from USD 0.86 mln to USD 3.18 mln. Given the lobbying power of ENUG's owners, we expect the allowed profit to be close to the upper limit of this range in the midterm.

Debts to be Reconciled & Restructured

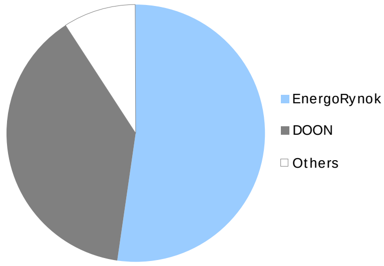
The low payment discipline of energy consumers in the early part of the decade caused a significant increase in ENUG's payables and receivables. The company's main debtors are coal mines, and its largest creditors are EnergoRynok and Donetskoblenergo.

ENUG Debt Accounts, USD mln



Source: Company data

Creditor Breakdown, 2005

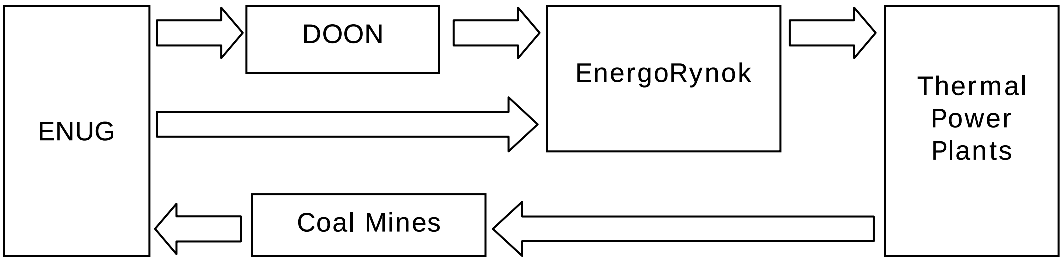


Note that a process of debt reconciliation and debt restructuring is underway in Ukraine (see our Oblenergo report of September 2005). The process is intended to clear all energy companies' debts.

Special Case Of ENUG

ENUG is in a good position to reconcile its debts during the government program, as its main debtors are coal mines, who in turn are the main creditors of generation companies, who in turn are creditors of Energorynok and DOON, who are the main creditors of ENUG. This means the mutual reconciliation process could decrease ENUG's payables and receivables by up to 90%.

Who Owes What to Whom in the Ukrainian Energy Sector:
ENUG: In a Closed Circle



Now that EnergoRynok, all thermal power plants and coal mines are regulated and/or controlled by people close to SCM, ENUG should have an easier time completing the process of mutual debt reconciliation. We will see by the end of 2006 if the company takes advantage of this opportunity.

In any case, ENUG, along with other companies in the energy sector, will restructure all its debt accounts in the midterm.

Valuation

For valuation purposes we use peer multiples with three groups of peers:

- Ukrainian Oblenergos, which are closest in business profile and regulation environment
- Peers from Hungary and the Czech Republic, which are also close in business profile to ENUG
- Russian power companies, whose main activity is the transmission of electricity, which is also ENUG's main activity

We do not use the DCF method of valuation, as uncertainty over how the tariff model will change yields too wide of a range of implied values.

Local Peers: Oblenergos

Because Oblenergos are mostly illiquid stocks, we were selective in choosing an appropriate peer group for ENUG: only Oblenergos with relatively low bid-ask spreads have been included in the pool to estimate the benchmark for Energougol.

The Oblenergos we use are comparable to ENUG. Relatively more efficient private companies and relatively less efficient and less profitable state companies are included in equal proportion.

Oblenergos Key Data

		Bid/Aks Spread	Stock Price*, USD	MCap, USD mln	EV, USD mln	Sales, USD mln 2005	Sales, USD mln 2006E	EBITDA, USD mln 2005	EBITDA, USD mln 2006E	Electricity Transm., TWh 2006E
DniproOblenergo	DNON	9.6%	49.5	296.6	286.6	839.3	1074.3	15.2	21.0	26.37
KharkivOblenergo	HAON	22.5%	0.35	88.9	83.9	194.2	225.3	14.1	16.5	4.98
Krymenergo	KREN	18.9%	0.32	56.1	55.1	135.6	162.7	9.2	15.6	4.09
Sevastopolenergo	SMEN	13.0%	0.99	26.6	29.4	33.7	42.8	5.1	5.6	0.86
ZaporizhyaOblenergo	ZAON	30.8%	1.09	195.3	194.1	348.4	456.4	12.7	15.2	10.22
ZhytomirOblenergo	ZHEN	36.1%	0.71	87.3	90.1	71.1	90.3	8.6	9.5	1.86
PGC EnergoUgol	**ENUG**					**44.6**	**55.8**	**2.8**	**4.1**	**1.20**

Source: Company data, PFTS, Concorde Capital estimates
** Price of the last deal*

Oblenergo Market Multiples

		EV/S 2005	EV/S 2006E	EV/EBITDA 2005	EV/EBITDA 2006E	EV/El. transm, USD/MWh 2006E
DniproOblenergo	DNON	0.34	0.27	18.9	13.7	10.9
KharkivOblenergo	HAON	0.43	0.37	6.0	5.1	16.8
Krymenergo	KREN	0.41	0.34	6.0	3.5	13.5
Sevastopolenergo	SMEN	0.87	0.69	5.8	5.2	34.1
ZaporizhiaOblenergo	ZAON	0.56	0.43	15.3	12.7	19.0
ZhytomirOblenergo	ZHEN	1.27	1.00	10.5	9.4	48.3
Mean		**0.51**	**0.42**	**9.1**	**6.9**	**18.8**
Median		**0.49**	**0.40**	**8.2**	**7.3**	**17.9**

Source: Company data, PFTS, Concorde Capital estimates

Implied ENUG MCap, USD mln

	EV/S 2005	EV/S 2006E	EV/EBITDA 2005	EV/EBITDA 2006E	EV/El. 2006E
@ peer average	22.9	23.2	25.1	28.1	22.6
@ peer median	22.1	22.2	22.6	30.0	21.5

Source: Company data, PFTS, Concorde Capital estimates

The average local peer valuation yields a relatively narrow range of implied values for ENUG, from USD 22.2 mln to USD 30.0 mln.

International Peers

We use a group of traded Hungarian and Czech regional distribution companies as ENUG's closest international peers.

Key peer data, USD mln

	MCap	EV	Sales		EBITDA		Net income		El. Suppl, TWh
			2005	2006E	2005	2006E	2005	2006E	2006E
DEMASZ	296.4	360.1	442.8	451.0	75.9	74.3	26.8	25.4	3.9
EMASZ	230.1	275.4	359.0	378.2	51.8	57.7	20.3	26.2	2.9
ELMU	730.3	800.0	964.0	981.0	177.4	165.4	90.1	88.2	7.4
Prazska Energetika	744.2	710.2	506.1	533.1	102.9	114.1	51.3	52.5	5.8
PGC EnergoUgol			**44.6**	**55.8**	**2.8**	**4.1**	**1.7**	**2.6**	**1.2**

Source: Bloomberg, IBES, company data, Concorde Capital estimates

Peer Multiples

	EV/S		EV/EBITDA		P/E		EV/El. Suppl.,
	2005	2006E	2005	2006E	2005	2006E	USD/MWh
DEMASZ	0.81	0.80	4.7	4.8	11.1	11.7	92
EMASZ	0.77	0.73	5.3	4.8	11.3	8.8	94
ELMU	0.83	0.82	4.5	4.8	8.1	8.3	108
Prazska Energetika	1.40	1.33	6.9	6.2	14.5	14.2	122
Average	0.80	0.78	4.9	4.8	10.2	9.6	98
Median	0.82	0.81	5.0	4.8	11.2	10.2	101

Source: Bloomberg, IBES, company data, Concorde Capital estimates

We apply the same valuation approach by sales that we developed for Oblenergos (refer to our Oblenergo reports of Sept. 15, 2005 and Dec. 15, 2005). ENUG's performance scores 4.3, implying a 25% discount to its peers' EV/S benchmark.

ENUG performance rating:

Parameter	Value	Score
Change in supply, 1H06 yoy	0%	4
EBITDA margin, 1H06	8.1%	4
Payment level, 1h06	116%	5
NERC algorithm	Less than 100%	4
Excessive losses (est.)	1.10%	4
Market position sustainability	High	5
Average Score		**4.3**

Source: Company data, Concorde Capital

Implied ENUG MCap, USD mln

	EV/S		EV/EBITDA		P/E		EV/El. suppl.
	2005	2006E	2005	2006E	2005	2006E	2006E
@ peer average	35.8	43.5	13.4	19.7	16.8	25.0	117.5
@ peer median	36.6	45.0	13.8	19.8	18.5	26.7	120.8

Source: Bloomberg, IBES, company data, Concorde Capital estimates

Valuation by international peer multiples yields a wider range for ENUG's implied MCap. This is due to the difference in tariffs between Ukraine and peer countries. The valuation by P/E yields results within the range implied by Ukrainian peers.

Russian Power Companies

Another group of peers are Russian regional electricity distribution companies, which were created in 2005-2006 as a result of the restructuring of vertically integrated regional energy companies. Russian are not involved in the electricity supply business and only transmit electricity, they do not match up well with ENUG as do the Czech or Hungarian peers. However, transmission is ENUG's main business, so the Russian peers are suitable enough for valuation.

We cannot directly apply a sales multiple from Russian peers to value ENUG, because of the significant difference in revenue structure. Valuation by the P/Electricity (output) multiple also needs significant adjustment due to electricity price differences between Ukraine and Russia.

Thus, we refer only to EBITDA and net income multiples for valuation purposes, and provide P/S and P/El. valuation results for illustration purposes only.

Russian Network Companies: Key Parameters, 2006E, USD mln

		Price*, USD	**MCap**	**Sales**	**EBITDA**	**Net Income**	**Electricity Output**, TWh
Servdlovenergo	SVER	0.61**	319.0	448.7	31.3	3.6	35.8
Rostovenergo	RTSE	0.05	140.8	162.2	32.3	6.0	12.0
NizhNovenergo	NNGE	20.00	78.4	202.4	26.0	-3.9	14.5
Lenenergo	LSNG	0.65	497.9	343.8	13.8	-53.6	25.5
Chelyabenergo	CHNG	0.04	185.9	188.1	18.4	0.0	21.6
Orelenergo	OREN	0.22	42.4	41.8	5.9	0.6	2.3
Voronezhenergo	VZEN	1.45	81.4	100.4	15.3	-0.1	7.0
Volgogradenergo	VGEN	0.46	146.7	176.5	28.5	4.3	14.6
Kurskenergo	KUEN	0.06**	65.6	83.0	8.2	4.9	4.8
Smolenskenergo	SMOE	0.33	64.4	81.2	15.1	1.1	3.3
Stavropolenergo	STRG	0.09	73.0	94.2	17.2	2.4	4.9
Novgorodenergo	NGNR	0.25	41.4	51.2	10.8	0.5	2.6
PGC EnergoUgol	**ENUG**			**55.75**	**4.09**	**2.61**	**1.2**

Source: RTS, IES, RAO UES forecasts
** price of the last deal*
*** mid-market prices were chosen for companies lacking information about the last deal*

Russian Peer Multiples

		P/S	**P/EBITDA**	**P/E**	**P/El., USD/MWh**
Servdlovenergo	SVER	0.71	10.2	87.8	8.9
Rostovenergo	RTSE	0.87	4.4	23.3	11.8
NizhNovenergo	NNGE	0.39	3.0	neg.	5.4
Lenenergo	LSNG	1.45	36.1	neg.	19.5
Chelyabenergo	CHNG	0.99	10.1	n/m	8.6
Orelenergo	OREN	1.01	7.2	70.7	18.5
Voronezhenergo	VZEN	0.81	5.3	neg.	11.6
Volgogradenergo	VGEN	0.83	5.2	34.0	10.0
Kurskenergo	KUEN	0.79	8.0	13.5	13.7
Smolenskenergo	SMOE	0.79	4.3	59.3	19.6
Stavropolenergo	STRG	0.77	4.3	30.5	15.0
Novgorodenergo	NGNR	0.81	3.8	85.1	16.2
Mean		0.85	8.5	50.5	13.2
Median		0.81	5.2	46.7	12.7

Source: RTS, IES, RAO UES forecasts

Implied ENUG MCap, USD mln

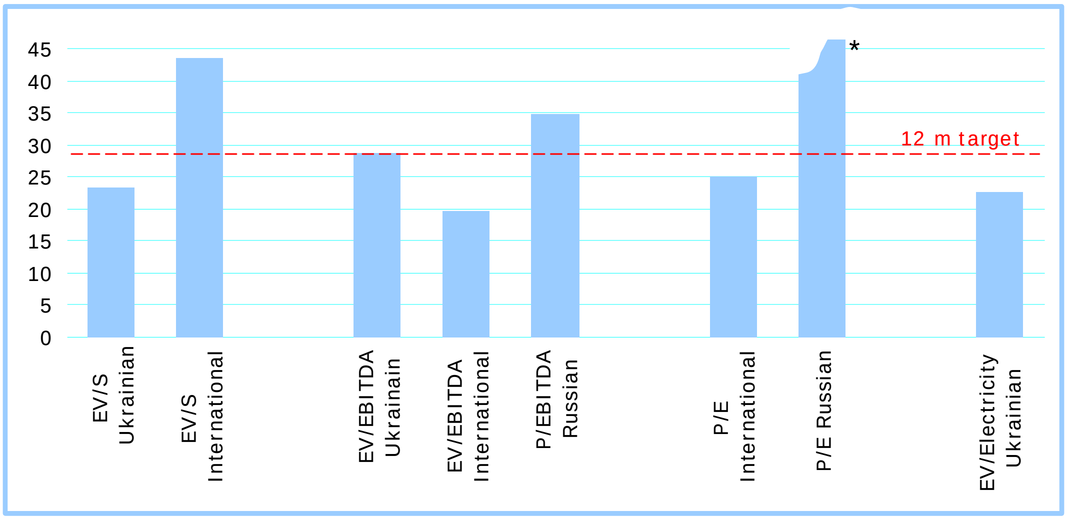
	P/S	**P/EBITDA**	**P/E**	**P/El.**
@ peer average	47.5	34.7	131.9	15.9
@ peer median	45.1	21.4	121.8	15.3

Source: RTS, IES, RAO UES forecasts

Valuation Summary

The most reliable multiples (presented below) put ENUG's equity value in the range between USD 20 mln and USD 43 mln. To avoid subjectivity in our valuation, we estimate its target value as the average between all the implied MCaps we have presented, except P/E for Russian companies, which is a clear outlier.

ENUG Implied MCaps, USD mln



Source: Concorde Capital
** outlier*

Our valuation yields a USD 28.1 mln target MCap, which implies a price of USD 5.1 per share. With an indicative price of USD 3.6 per share, we see a 42% upside and initiate a BUY recommendation for ENUG.

Financials According To Ukrainian Accounting Standards (UAS)

Income Statement Summary, USD mln

	1Q03	2Q03	3Q03	4Q03	1Q04	2Q04	3Q04	4Q04	1Q05	2Q05	3Q05	4Q05	1Q06	2Q06
Net Revenues	**9.6**	**18.5**	**28.5**	**39.0**	**11.1**	**20.4**	**29.3**	**39.4**	**10.6**	**20.2**	**30.6**	**44.6**	**16.4**	**31.5**
Change y-o-y														
Cost Of Sales	(8.8)	(16.7)	(25.7)	(35.1)	(9.9)	(18.2)	(26.2)	(35.6)	(9.8)	(18.7)	(28.1)	(40.6)	(15.2)	(28.4)
Change y-o-y														
% of Net Revenues	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*	*0.9*
Gross Profit	0.8	1.8	2.9	3.9	1.2	2.2	3.1	3.8	0.7	1.5	2.5	4.0	1.2	3.1
Change y-o-y														
% of Net Revenues	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*	*0.1*
Other Operating Income/Costs, net	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.3)	(0.4)	(0.4)	(0.0)	(0.2)	(0.3)	(0.4)	(0.0)	(0.0)
Change y-o-y														
% of Net Revenues	*-1%*	*0%*	*0%*	*0%*	*-1%*	*-2%*	*-1%*	*-1%*	*0%*	*-1%*	*-1%*	*-1%*	*0%*	*0%*
SG&A	(0)	(1)	(1)	(1)	(0)	(1)	(1)	(1)	(0)	(0)	(1)	(1)	(0)	(1)
Change y-o-y														
% of Net Revenues	*3%*	*4%*	*3%*	*3%*	*3%*	*3%*	*2%*	*2%*	*2%*	*2%*	*2%*	*2%*	*2%*	*2%*
EBITDA	**0.4**	**1.0**	**1.9**	**2.8**	**0.8**	**1.4**	**2.0**	**2.6**	**0.5**	**0.9**	**1.5**	**2.8**	**1.0**	**2.6**
Change y-o-y														
EBITDA margin, %	4.5%	5.7%	6.7%	7.1%	6.9%	6.9%	6.9%	6.5%	4.7%	4.3%	5.0%	6.2%	5.8%	8.1%
Depreciation	(0.1)	(0.1)	(0.2)	(0.3)	(0.1)	(0.2)	(0.3)	(0.4)	(0.1)	(0.2)	(0.3)	(0.5)	(0.1)	(0.3)
Change y-o-y														
% of Net Revenues	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*	*1%*
EBIT	**0.4**	**0.9**	**1.7**	**2.5**	**0.7**	**1.2**	**1.8**	**2.2**	**0.4**	**0.7**	**1.2**	**2.3**	**0.8**	**2.3**
Change y-o-y														
EBIT margin, %	3.7%	4.9%	5.9%	6.3%	6.1%	6.0%	6.0%	5.6%	3.7%	3.2%	3.9%	5.1%	5.0%	7.3%
Interest Expense	-	-	-	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	-	-	-	-	-	-
Financial income/(expense)	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Other income/(expense)	(0.1)	(0.3)	(0.3)	(0.6)	(0.1)	(0.1)	(0.1)	(0.2)	(0.0)	(0.0)	0.0	0.0	(0.0)	(0.0)
PBT	**0.3**	**0.6**	**1.4**	**1.9**	**0.6**	**1.1**	**1.6**	**2.0**	**0.4**	**0.6**	**1.2**	**2.3**	**0.8**	**2.3**
Tax	(0.1)	(0.2)	(0.4)	(0.5)	(0.2)	(0.4)	(0.6)	(0.7)	(0.1)	(0.2)	(0.4)	(0.6)	(0.1)	(0.4)
Effective tax rate	*28%*	*36%*	*26%*	*28%*	*40%*	*40%*	*36%*	*34%*	*31%*	*36%*	*32%*	*28%*	*19%*	*18%*
Minority Interest	-	-	-	-	-	-	-	-	-	-	-	-	-	1.0
Extraordinary Income/(loss)	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	**0.2**	**0.4**	**1.0**	**1.4**	**0.3**	**0.7**	**1.0**	**1.3**	**0.3**	**0.4**	**0.8**	**1.7**	**0.6**	**2.9**
Change y-o-y														
Net Margin, %	*2%*	*2%*	*4%*	*4%*	*3%*	*3%*	*3%*	*3%*	*3%*	*2%*	*3%*	*4%*	*4%*	*9%*
Dividend Declared	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Balance Sheet Summary, USD mln

	1Q03	2Q03	3Q03	2003	1Q04	2Q04	3Q04	2004	1Q05	2Q05	3Q05	2005	1Q06	2Q06
Current Assets	**29.6**	**30.3**	**32.3**	**32.4**	**34.1**	**33.8**	**32.5**	**34.1**	**36.8**	**36.5**	**37.0**	**38.2**	**40.0**	**39.7**
Cash & Equivalents	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.3	0.1	0.0	0.0	0.0	0.1	0.2
Trade Receivables	28.0	28.6	30.5	30.1	31.3	30.8	29.6	31.1	33.7	33.5	34.0	35.2	37.1	36.5
Inventories	0.6	0.7	0.8	1.5	1.9	2.3	2.3	2.3	2.4	2.4	2.4	2.6	2.6	2.7
Other current assets	0.9	0.9	0.9	0.8	0.8	0.6	0.5	0.5	0.6	0.6	0.5	0.4	0.2	0.3
Fixed Assets	**2.7**	**2.9**	**2.8**	**3.0**	**3.2**	**3.2**	**3.3**	**3.3**	**3.4**	**3.7**	**3.8**	**4.2**	**4.3**	**4.6**
PP&E, net	2.3	2.4	2.4	2.5	2.7	2.7	2.7	2.8	2.8	2.9	3.0	3.5	3.4	3.8
Other Fixed Assets	0.4	0.5	0.4	0.4	0.5	0.5	0.5	0.5	0.6	0.8	0.8	0.7	0.9	0.8
Total Assets	**32.3**	**33.1**	**35.1**	**35.4**	**37.3**	**36.9**	**35.7**	**37.5**	**40.2**	**40.2**	**40.8**	**42.3**	**44.4**	**44.4**
Shareholders' Equity	**2.9**	**3.2**	**3.7**	**4.2**	**4.6**	**4.9**	**5.3**	**5.6**	**6.1**	**6.2**	**6.6**	**6.2**	**6.9**	**8.1**
Share Capital	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9	2.0	2.0	2.0	2.0	2.0	2.0
Reserves and Other	0.5	0.5	0.5	0.6	0.7	0.6	0.6	0.7	0.7	0.7	0.7	0.8	1.1	1.1
Retained Earnings	0.6	0.8	1.4	1.7	2.0	2.3	2.7	2.9	3.3	3.5	3.9	3.3	3.8	5.0
Current Liabilities	**29.4**	**30.0**	**31.4**	**31.2**	**32.7**	**32.0**	**30.5**	**31.9**	**34.2**	**34.0**	**34.2**	**36.2**	**37.5**	**36.3**
ST Interest Bearing Debt	-	-	-	-	0.1	-	-	-	-	-	-	-	-	-
Trade Payables	27.8	28.4	29.7	29.7	30.9	30.3	29.0	30.4	32.6	32.3	32.5	33.6	34.6	33.2
Accrued Wages	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Accrued Taxes	0.1	0.2	0.2	0.1	0.3	0.3	0.2	0.1	0.2	0.2	0.3	0.3	0.3	0.4
Other Current Liabilities	1.4	1.3	1.4	1.3	1.3	1.3	1.2	1.2	1.2	1.3	1.3	2.1	2.4	2.4
LT Liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-	-
LT Interest Bearing Debt	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Other LT	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total Liabilities & Equity	**32.3**	**33.1**	**35.1**	**35.4**	**37.3**	**36.9**	**35.7**	**37.5**	**40.2**	**40.2**	**40.8**	**42.3**	**44.4**	**44.4**

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