CONCORDE CAPITAL

Ukraine / Electricity

Prykarpatoblenergo

Clients come & go, profits stay the same

November 27, 2007

Current Price: USD 2.48
12M Target: USD 2.40

HOLD

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Bloomberg	PREN UZ

Market information

No of Shares, mln	103.6
Market Price, USD	2.48
52Wk H/L, USD	2.66/0.38
MCap, USD mln	256.5
Free float	7.0%
Free float, USD	18.0

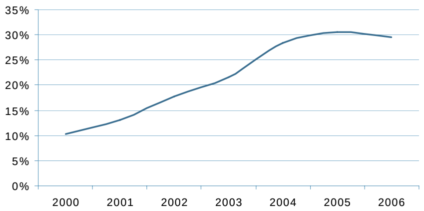
Corporate Governance Rating* BA

** The rating is based on Concorde Capital's corporate governance survey. Q denotes quality corporate governance standards, AA - above average standards, A - average, BA - below average and P – poor.*

Ownership

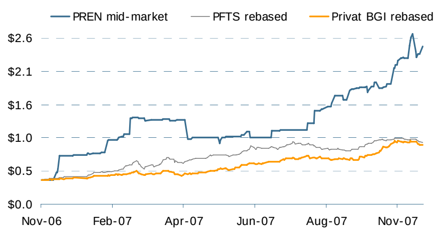
State (NC ECU)	25.0%
Privat group	27.6%
Privat/Energy Standard	33.8%
Other	13.6%

LukOR in PREN's customer base



Source: Prykarpatoblenergo, Concorde Capital estimates

Stock performance



Source: PFTS, Bloomberg

Last week, the National Electricity Regulatory Commission (NERC) granted a license for electricity supply to Prykarpatoblenergo's main electricity consumer, LukOR. Despite the risk of its market for supply services shrinking by 30%, the earning power of the company will not be impaired. We stick to our USD 2.40 target price and HOLD investment rating.

New licensee

Last week, the NERC approved a license for electricity supply (600 GWh per year) at a non-regulated tariff for petrochemical enterprise LukOR. This amount roughly corresponds to LukOR's annual electricity consumption and 30% of electricity supplied by Prykarpatoblenergo. The license raises the risk of Prykarpatoblenergo no longer supplying electricity to LukOR, thus loosing a significant share of its market.

Will LukOR do it?

The annual economy for LukOR from internal electricity supply at current tariffs is estimated at USD 0.7 mln (1% of sales). In the past, LukOR has not been successful in realizing its license: from Feb. 2003 to Oct. 2005, LukOR remained a customer of Prykarpatoblenergo, even though it held an electricity supply license. We see the probability of realization this time at somewhere above 50%.

"Worst case" scenario: No changes in the bottom line

The possible departure of its main customer threatens Prykarpatoblenergo's top line. Nevertheless, earning power will not be impaired as:

- The current tariff policy prevents the company from reducing its bottom line. Distribution/supply tariffs are designed to generate a pre-determined profit, which is linked to an Oblenergo's investment program. A decrease in Prykarpatoblenergo's customer base by more than 5% allows the company to apply for a tariff revision and thereby preserve its predetermined profit in absolute terms, effectively increasing margins, as unexpected as it may seem.
- In the longer term, the regulator's transition to a RAB-based tariff policy will render the point moot altogether by correlating an Oblenergo's value with its asset base. A customer exodus has no effect on the company's asset value, and only a minor effect on the company's regulatory asset base (RAB) via working capital.

Forecasts for 2008

	with LukOR in customer base	w/o LukOR
Electricity supply, TWh	1.88	1.33
Sales, USD mln	131.3	102.4
EBITDA margin	9.7%	12.2%
Net margin	3.3%	4.1%

Source: Company data, Concorde Capital estimates

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