

Energy

Sector Review - January

January 2013



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Energy Universe:

- EDP
- Endesa
- Vestas
- GALP
- Royal Dutch Shell

This month's detailed company review:

- Endesa



Joana Martins
joanamartins@nova
investmentclub.com



Tobias Rabenstein
Tobiasrabenstein@nova
investmentclub.com

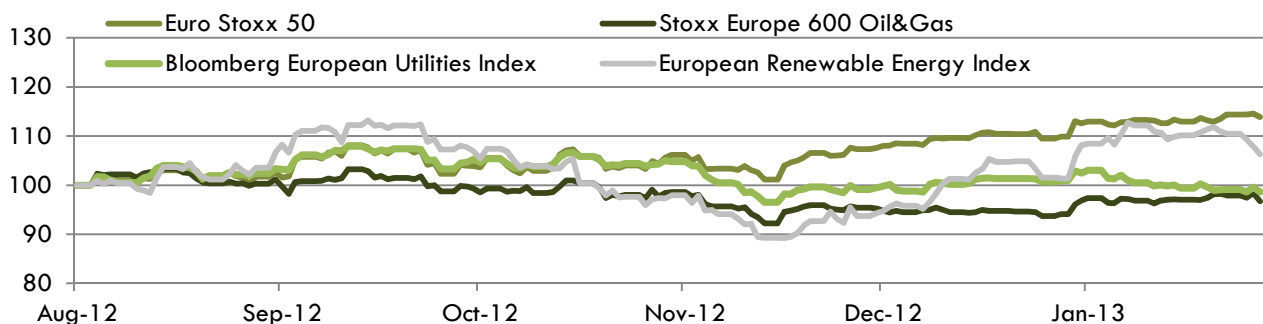
1. Sector Overview

- During January, three of the four indexes analysed performed well (Euro Stoxx 50, Stoxx Europe 600 Oil&Gas and European Renewable Energy Index), with gains of 3.6%, 2.8% and 4.9%, respectively. The only sector presenting negative results is Utilities, with the Bloomberg European Utilities Index declining 2.3%.
- Ukraine is planning to replace 4bn cubic meters of Gazprom's gas with local coal, which could lead them to save up to \$1.5bn per year. In exchange, Gazprom would have the possibility of redirecting this gas to European countries.
- Many energy firms, such as Royal Dutch Shell, Chevron, Kinder Morgan or BG Group are strengthening their presence in Canada, aiming to expand the production and distribution of liquefied natural gas on the West Coast of the country.
- Uranium is recovering from its downward trend, as Japan is considering to restart its atomic plants in the near future and China keeps reinforcing its position in the nuclear energy sector, with the world's biggest nuclear building program.
- Demand for natural gas is increasing, as it is beginning to be used for non-peak power generation, becoming an important substitute for coal.

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Energy Sector vs. Overall market

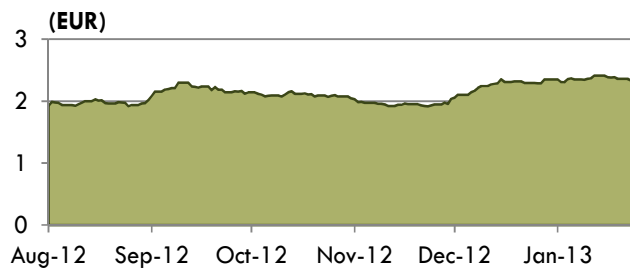


- In spite of its upward trend during the last month, the Oil&Gas Index is the one performing the poorest among the four analysed, followed by the Utilities Index. Both indexes are far below the reference index (Euro Stoxx 50), that has been outperforming all the energy indexes in the last months.

3. Followed Companies

- EDP is planning to add 500MW of new solar and water capacity worldwide during this year, much below the average figures from previous years. This reduction is justified by the environmental policies in Spain and US, both core markets for the Portuguese company.

EDP
(Ticker: EDP)



Price (EUR):	↑	2,36
Target Price (EUR):		2,59
Up/downside:		9,9%
Performance 3M:		13,2%
P/E Ratio:		8,0x
ROC/WACC:		0,9x

- Vestas is negotiating with an important competitor in order to be able to sell 375 turbine towers per year, for which it will use 25% of the capacity in its factory located in Colorado. This aims to make up for the company's disappointing profits due to overcapacity among turbine producers.

Vestas
(Ticker: VWS)



Price (DKK):	↓	36,26
Target Price (DKK):		33,25
Up/downside:		-8,3%
Performance 3M:		13,3%
P/E Ratio:		NA
ROC/WACC:		-2,0x

- GALP's projects in the Brazilian market are raising the company's results in the fourth quarter. The company plans to invest €1.2bn per year, during the next three years. While growing in the Brazilian market, the company is trying to reduce its dependence from the Iberian market.

GALP
(Ticker: GALP)



Price (EUR):	↑	12,06
Target Price (EUR):		15,50
Up/downside:		28,5%
Performance 3M:		-5,4%
P/E Ratio:		25,4x
ROC/WACC:		0,3x

- Royal Dutch Shell is planning to create a company with Kinder Morgan Inc., aiming to export liquefied natural gas from the United States. The project is expected to cost around \$1bn and the construction is planned to start soon after 2015.

Royal Dutch Shell
(Ticker: RDSA)



Price (EUR):	↑	26,85
Target Price (EUR):		29,17
Up/downside:		8,7%
Performance 3M:		1,1%
P/E Ratio:		7,9x
ROC/WACC:		1,1x

3. Stock Analysis: Endesa

Corporate News

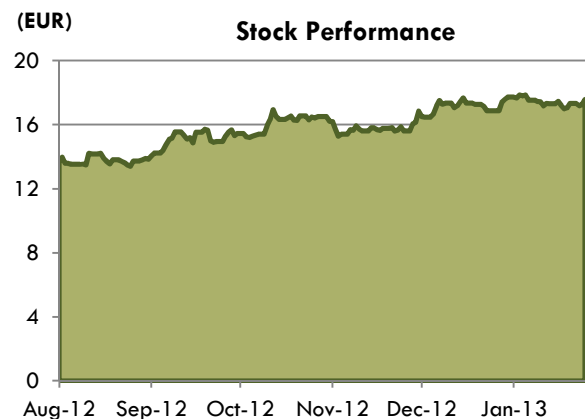
- Endesa, which is 92% owned by the Italian utility Enel, announced it increased its number of clients in Latin America by about 14 million during 2012, 2.6% higher than 2011; the company distributed 81.8 TWh in the region in 2012.
- During January, Spanish homes and businesses, which is the main customer group for Endesa, received 44% of electricity from renewable sources; total electricity demand fell 4.3% from a year earlier.

Market Performance

- In January, Endesa's stock gained 0.7% and thus outperformed the Spanish lead index IBEX 35, which lost 1.0% during the same period.
- This performance looks even better when compared to Endesa's main competitors GDF Suez and Iberdrola, which lost 4.5% and 5.9%, respectively, during January.

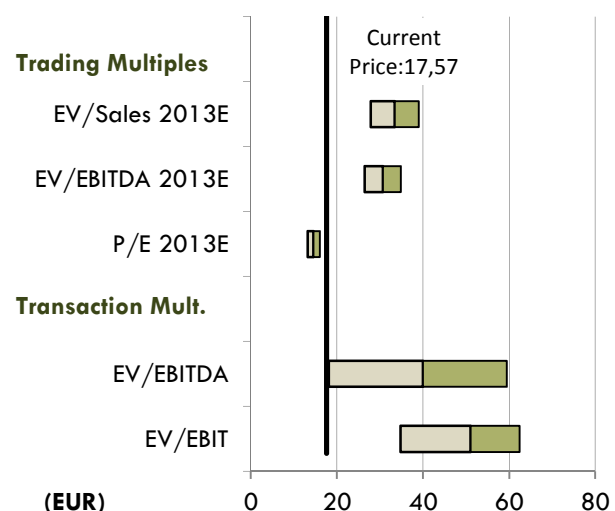
Valuation Summary

- Endesa's stock, currently valued at EUR 17.57, appears cheap when looking at our applied range of multiple valuations; only the 2013E P/E ratio suggests a slight overvaluation.
- The current target price for Endesa of 19.85 implies an upside of approx. 13.0%; this is supported by both EV/Sales and EV/EBITDA trading multiples, that even propose a higher upside to a value of around EUR 30 per share.
- Transaction multiples give a slightly higher valuation of around EUR 45 a share; discounting the implied control premium we again arrive at a valuation close to the one given by trading comparables.



Endesa (EUR)	
Current Price (30/01/2013)	17,57
52-week high % change	-1,7%
Median Target Price	19,85
Market Capitalisation (mn)	17.978
Return on Common Equity	9,7%
Dividend Yield	3,6%
Beta (vs. S&P500)	0,8x
Total Debt/Equity	55,0%

Valuation Summary (Price per Share)



BUY

- Given Endesa's current clear undervaluation, its strong market presence within the Iberian energy sector and the backing of Enel, we recommend buying the stock.

Comparable Analysis

Company Name	Currency	MCap (mn)	Enterprise Value (mn)	EV/Sales			EV/EBITDA			P/E		
				LTM	2013E	2014E	LTM	2013E	2014E	LTM	2013E	2014E
Endesa	EUR	17.978	28.827	0,8x	0,9x	0,9x	4,0x	4,1x	4,3x	9,3x	8,6x	9,6x
Iberdrola	EUR	23.699	51.306	1,4x	1,6x	1,6x	7,1x	6,6x	6,7x	7,5x	8,2x	9,5x
EDF	EUR	26.180	72.368	1,2x	1,0x	1,0x	6,2x	4,5x	4,5x	5,4x	6,8x	7,6x
E.ON	EUR	25.713	49.572	0,5x	0,4x	0,4x	10,9x	4,6x	5,2x	10,6x	5,8x	9,8x
RWE	EUR	16.806	33.953	0,8x	0,7x	0,7x	4,4x	3,9x	3,9x	7,3x	6,7x	6,9x
ENI	EUR	27.721	102.723	1,2x	1,3x	1,3x	5,3x	6,2x	6,3x	#N/A N/.	8,0x	8,3x
75th Percentile				1,2x	1,2x	1,2x	6,9x	5,8x	6,0x	9,3x	8,2x	9,6x
Median				1,0x	1,0x	0,9x	5,7x	4,6x	4,9x	7,5x	7,4x	8,9x
25th Percentile				0,8x	0,7x	0,7x	4,7x	4,2x	4,3x	7,3x	6,7x	7,8x

- Looking at comparable trading companies, Endesa appears to be undervalued when trading at 2013E EV Sales of 0.9x and EV/EBITDA of 4.1x compared to the sector median of 1.0x and 4.6x, respectively.
- Especially when looking at its main competitor Iberdrola, which as Endesa serves primarily the Iberian peninsula, this undervaluation becomes clear; IBE trades at 1.6x EV Sales and 6.6x EV/EBITDA for 2013E.
- It is important to mention here that most of the European utility universe suffered from recently dropping energy prices within the continent due to a persisting oversupply and the rise of new energy sources, namely the shale gas boom in the US.

Precedent Transactions

Announced Date	Target		Buyer		EV		
	Company	Country	Company	Country	(EUR mn)	EV/EBITDA	EV/EBIT
24-Jul-12	MGN Gas Network UK Ltd	UK	Cheung Kong Ltd	CN	2.517	10,1x	16,2x
03-May-12	Cia de Gas de Sao Paulo	BZ	Cosan SA Industria e Comercio	BZ	1.343	7,9x	11,9x
29-Mar-12	International Power PLC	UK	GDF Suez	FR	7.662	9,5x	15,0x
14-Feb-12	HEAG Suedhessische Energie AG	DE	HEAG Holding AG	GE	280	5,6x	10,1x
02-Feb-12	Redes Energeticas Nacionais SA	PT	China State Grid Corp	CN	387	3,4x	5,6x
27-Dec-11	Edipower SpA	IT	A2A SpA	IT	684	3,3x	13,5x
22-Dec-11	EDP - Energias de Portugal SA	PT	China Three Gorges Corp	CN	2.690	3,5x	5,7x
23-Jun-11	Central Vermont PS Corp	US	IPL / Laurentides / TRENAP	CA	463	13,6x	22,1x
75th Percentile						9,7x	15,3x
Median						6,8x	12,7x
25th Percentile						3,5x	9,0x

- From the listed transactions, the acquisition of a 21.35% stake in EDP of China Three Gorges, is the most popular recent transaction in the European utilities sector; however, the relatively low EV/EBITDA and EV/EBIT multiples of 3.5x and 5.7x, respectively, have to be considered carefully first because of the minority stake acquisition and second because the Portuguese government had to sell this stake given the imposed rules of the Troika.
- The most recent transaction comparable by size and sector actually dates back to July 2012, when the Chinese Cheung Kong Ltd acquired the British MGN Gas Network UK Ltd; the valuation of 10.1x EV/EBITDA and 16.2x EV/EBIT; this on the one hand shows clearly higher multiples as for the EDP deal and on the other also proves a relatively quiet M&A market in the sector in recent month.