



**METROPOL**®  
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# Utility company bonds – competitive positions

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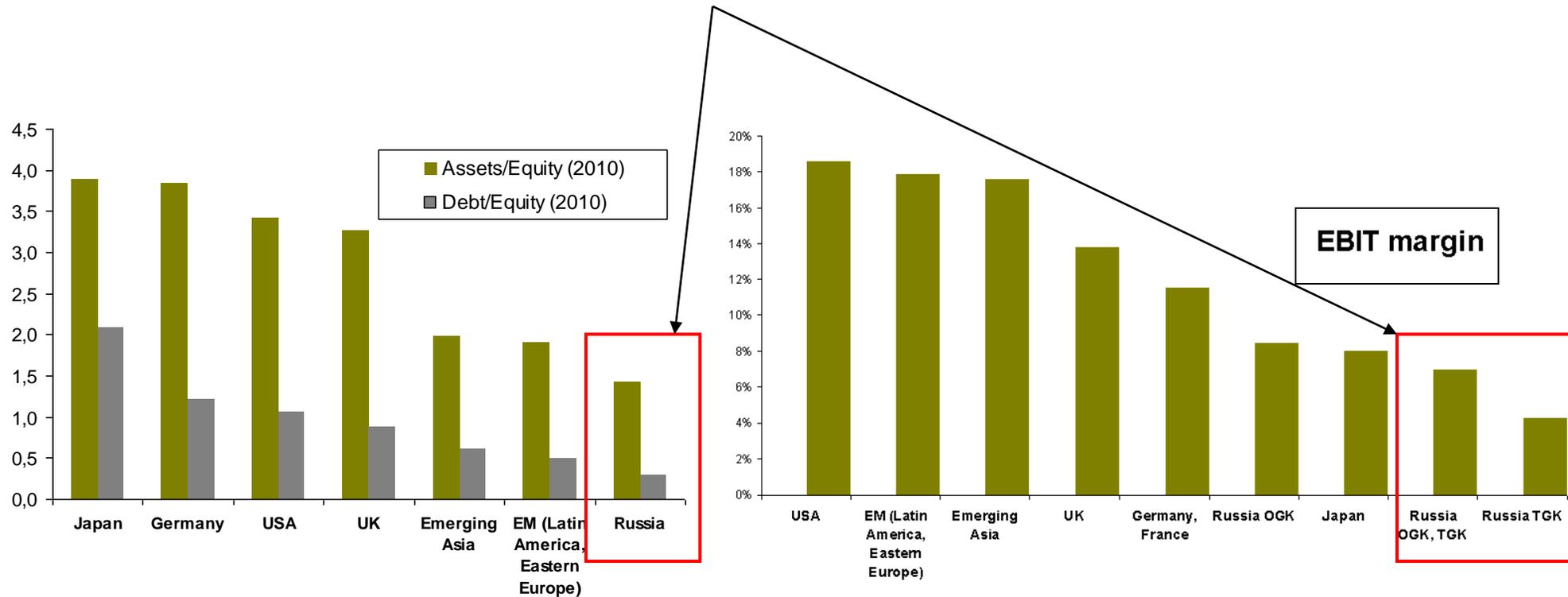
September 2011

# Summary

- Utility companies have initiated investment programs to replace/upgrade depreciated assets
- Russian electric companies are about to experience revenue growth significantly above the historical trend
- We expect declining credit risk in the Russian utility industry
- Spreads for some bonds in the sector may narrow by more than 75 b.p. in the medium term

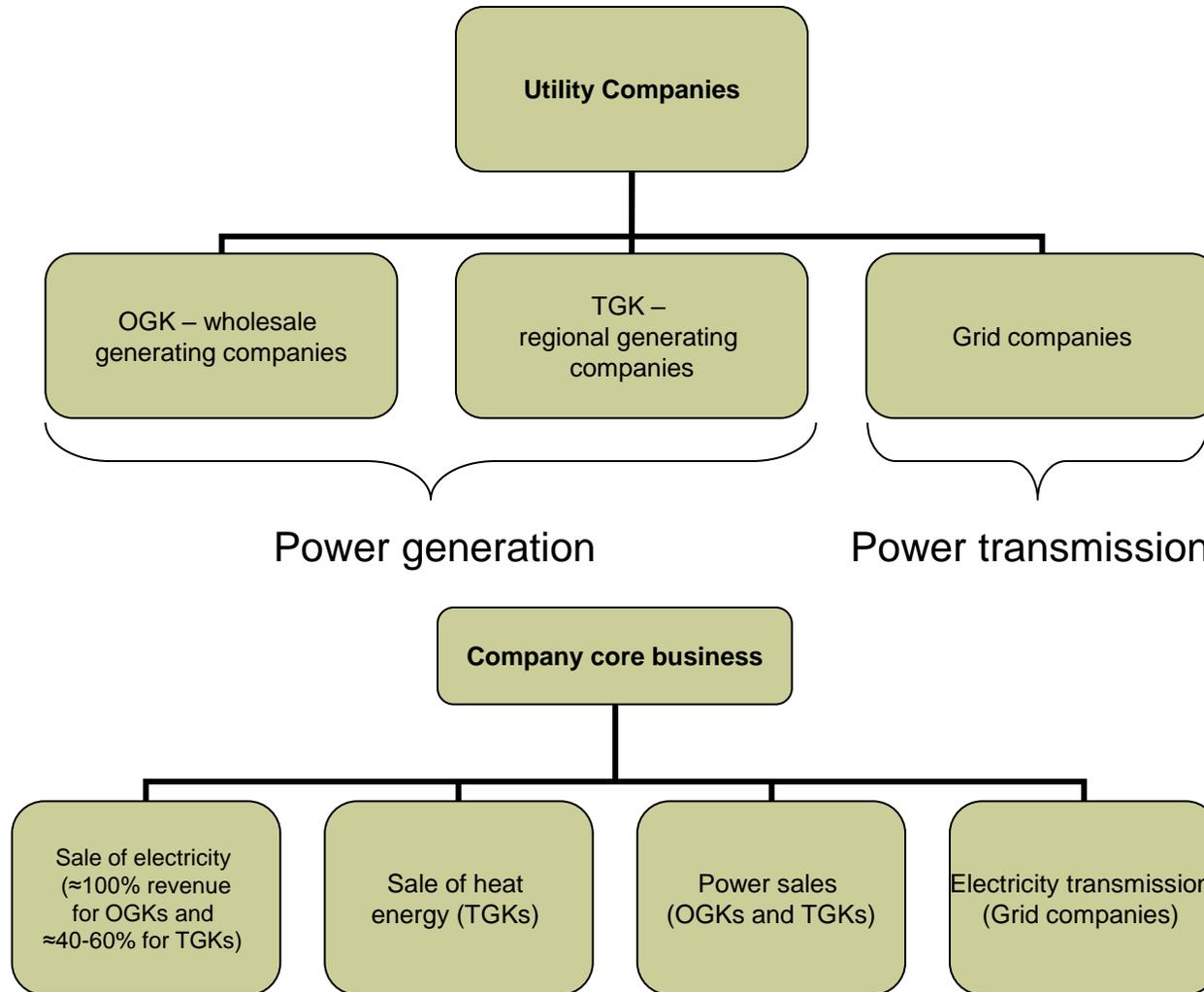
# Russian Utility Industry – Relative Comparison

Aggregate debt and profit margins are low compared to international peers



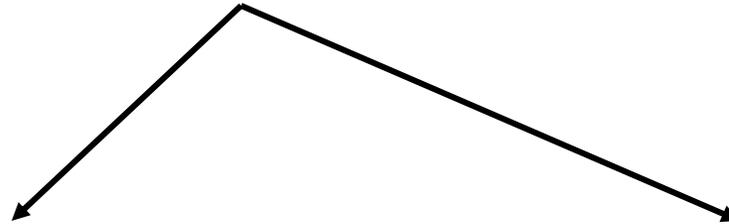
Source: Bloomberg, Company data

# Utility Industry Structure



# Potential factors affecting company operations

## Major factors affecting financial results



### Negative factors

### Positive factors

#### Generating companies

Regulatory factors – caps on retail customer tariffs for heat and electricity. This limits revenue

Government guaranteed return on investment for new capacity (DPM) – significant increase in financial results

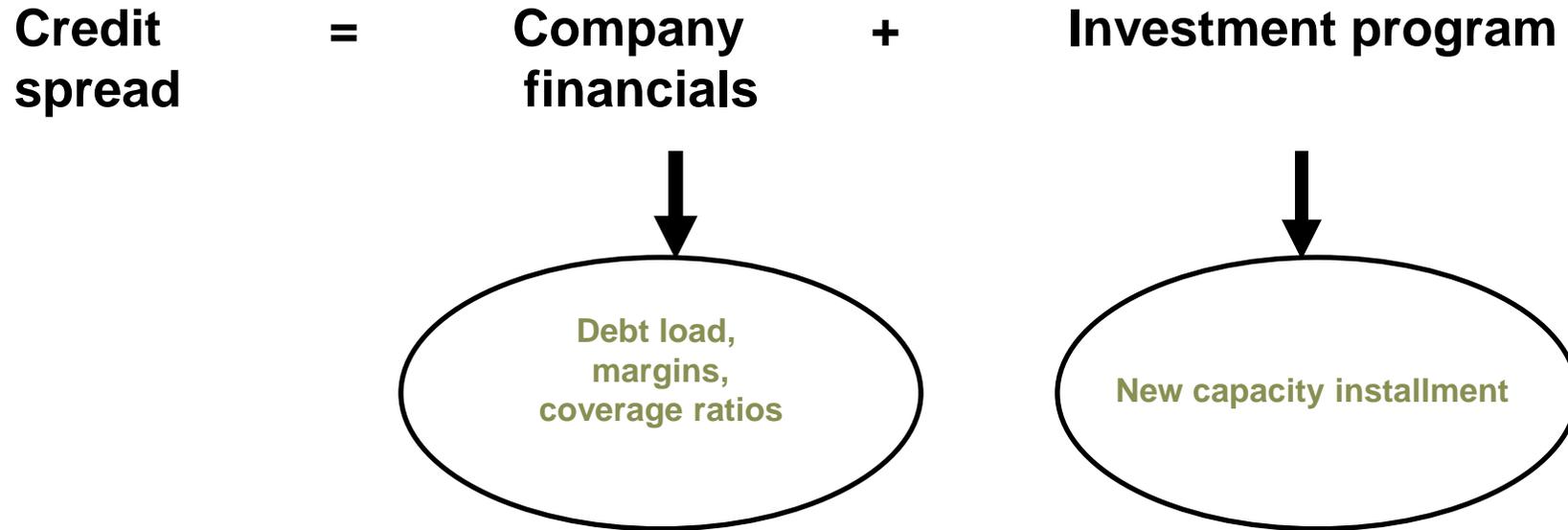
#### Grid companies

Regulatory factor – possible limit on tariff growth from the regulator

Government guaranteed return on investment

# Regression indicates factors influencing spread

## The model:



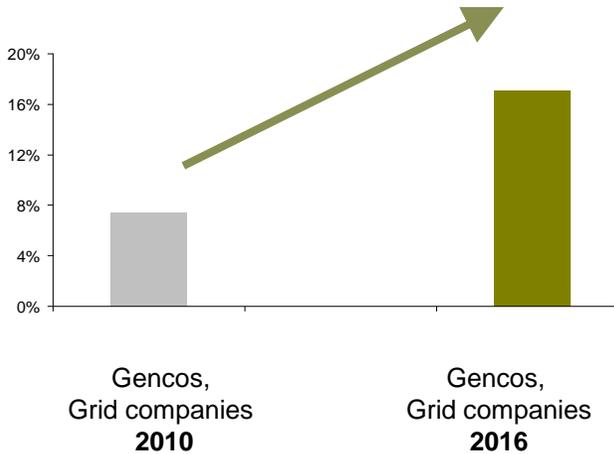
## Results:

- Approved Investment program **does not** affect the bond's credit spreads
- Major financial indicators **affect** company credit spreads

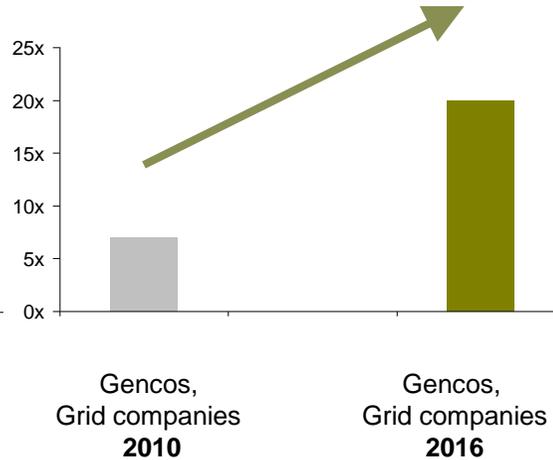
# Impact of investment on major financial indicators

Completion of approved investment programs will significantly improve financial results

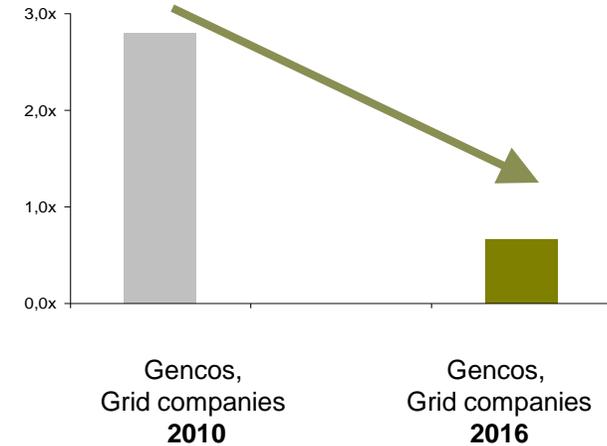
## Net profit margin



## Interest coverage



## Debt/EBIT

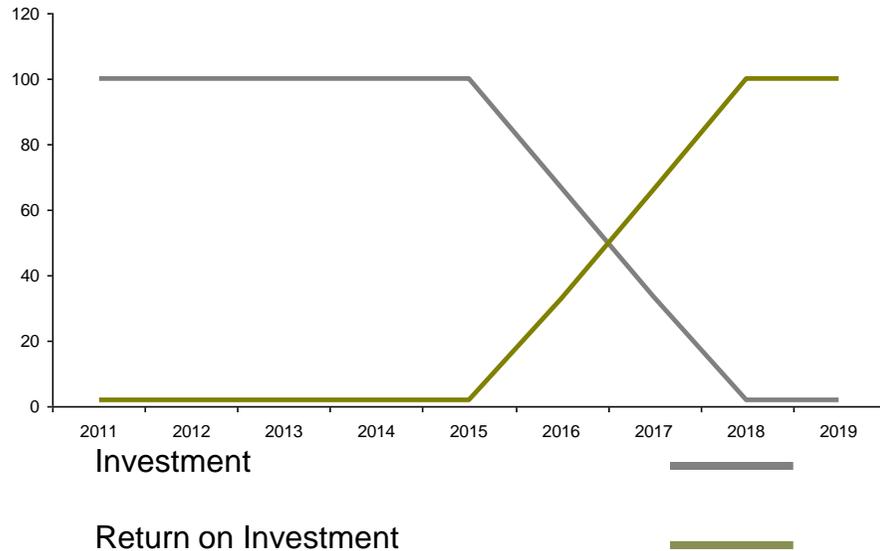


Consequently, we expect credit spreads to narrow by 50-150 bps

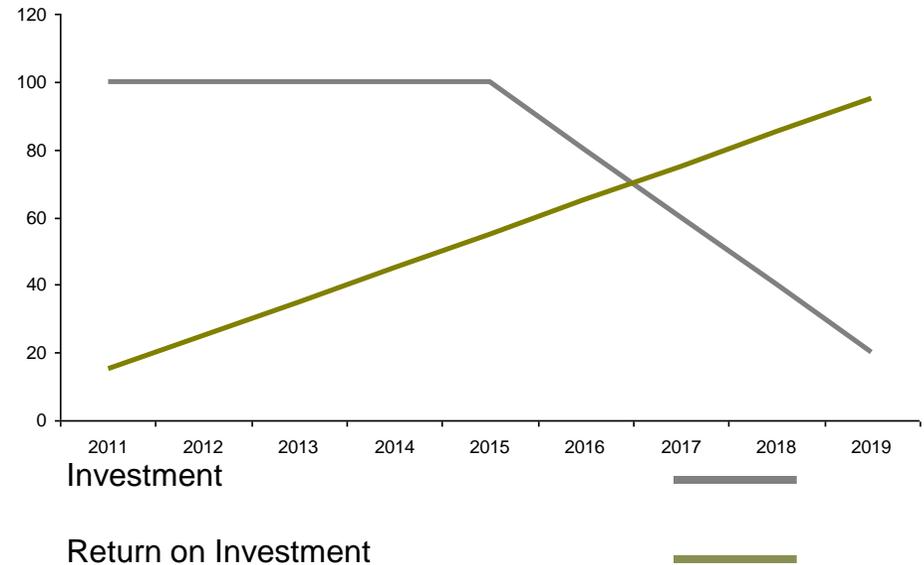
# Significant difference in payback period of invested capital

Payback period for grids companies is much lower than for GenCos

## Generating companies



## Grid companies



Source: IFC Metropol estimates

# Conclusions

- Currently the return from investment programs is not included into company spreads.
- As investment programs are implemented, financial results will significantly improve. As a result, we expect credit spreads to decrease.

	Short term	Medium to long term
TGKs	+/-	+ Spread narrows by 50-150 bps
OGKs	0	+
Grids	0	+ Spread narrows by 50-150 bps

# Yield map

