

Wednesday, 26 June 2024 | research report

# CEE Power Utilities

Poland, Czech Republic

## Like the legend of the phoenix

We resume coverage of Polish state-controlled power, with Enea (offering the biggest fundamental valuation gap) and PGE (the best play on coal unbundling) as our top picks. We also stand by our positive view on Polenergia, with its attractive RES portfolio and plans for more optimal capital management.

The medium-term earnings momentum expected in the power sector is not too appealing (declining forward prices, reduced load factors), but the valuation multiples of utilities remain very attractive, and their EBITDA potential is poised to shift to more stable and regulated business lines.

Moreover, the capex plans of state utilities are becoming more value creative than in the past, and they include optimization of legacy asset maintenance, re-investment premiums in distribution, no politically driven investments and M&As, and a more opportunistic approach to onshore renewables with Poland about to announce a more constructive energy policy.

The new market paradigm inevitably involves the discontinuation of coal energy generation, but we expect the government to offer transitional compensation for negative clean dark spreads as of 2028 to keep coal plants on standby as emergency backup. This expectation underlies our base case scenario for power utility valuations. A potential coal assets carve-out represents a bullish case with almost 100% upside on avg.

### Power Market Paradigm Shift

The European energy mix transition is affecting power prices faster than previously expected, with hourly spot prices falling deeper and deeper into the negative territory. The number of hours with negative prices in the German-Austrian electricity bidding zones increased from 148 in 2021 to 280 in 2023, and, this year, they have more than doubled in a continuation of the uptrend.

In Poland, excessive solar capacity development, combined with balancing market reform, have added to the power price paradigm shift, boosting intraday spreads and profile costs (a huge challenge for solar PV, but an opportunity for CCGTs and energy storage). At the same time, we are witnessing a dramatic fall in coal power plant load factors (only 20% expected in 2028 vs. 36% in 2023) which, together with capacity closures, may result in a 60% slump in Polish steam coal demand.

More stabilization may come only with structural changes in electricity demand (EV charging, heat pumps, green H2) and the expected deployment of utility scale battery storage facilities. Meanwhile, in order to stabilize the system, the operator may be forced to implement 'ancillary' services to keep sufficient conventional capacities on standby, offering compensation for negative CDS as of 2028 (our base case scenario).

### Coal Assets Carve-Out Back on Gov't Agenda

The concept of a coal power plant carve-out seems to be back on the table, although the whole endeavor is starting from scratch with no official schedule and framework as of yet. We expect that, contrary to the original NABE project, this time the prices offered by the state for the coal assets will be more aligned with their profitability profiles and decommissioning schedules.

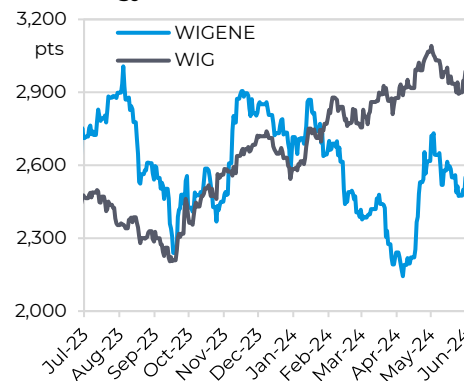
In our hypothetical calculations, we arrived at an implied EV of available capacity offered in 2026-30 of PLN 1.8m per MW – a more reasonable proposition from the government's vantage point than the alternative, i.e., building new gas balancing units with estimated capex of PLN 3.8m per MW. If we apply these estimates to the DCF valuations of Enea, PGE and Tauron, we arrive at upside potential of 135%, 156%, and 47%, respectively.

	EV/EBITDA adj.			DYield		
	2024E	2025E	2026E	2024E	2025E	2026E
CEZ	6.3	6.2	6.5	5.6%	5.5%	4.7%
Enea	1.4	1.2	1.2	0.0%	0.0%	0.0%
PGE	2.7	2.2	2.8	0.0%	0.0%	0.0%
Polenergia	8.1	11.7	18.6	0.0%	0.0%	0.0%
Tauron	3.8	3.3	3.3	0.0%	0.0%	0.0%
Integrated Utilities	6.1	6.2	6.5	6.3%	6.2%	6.2%
Network Utilities	9.3	8.8	8.7	5.0%	4.8%	5.0%
Renewables Mix	10.3	10.4	10.2	4.6%	4.7%	4.9%
Renewables Wind	10.4	9.9	8.9	3.5%	3.8%	3.8%
Renewables Solar	13.2	10.8	10.2	0.0%	0.0%	0.4%

WIG-Energia*	2,511.11
2024E EV/EBITDA	4.5x
2025E EV/EBITDA	4.9x

\*Price as of June 25, 2024, 5:00 PM

### WIG Energy vs. WIG



Name	Target Price		Rating	
	New	Old	New	Old
CEZ	948.40	893.60	hold	hold
Enea	18.16	-	buy	suspended
PGE	8.84	-	buy	suspended
Polenergia	104.09	103.62	buy	buy
Tauron	4.27	-	hold	suspended

Name	Current Price	Target Price	Upside
CEZ	933.50	948.40	1.6%
Enea	9.42	18.16	92.9%
PGE	6.91	8.84	28.0%
Polenergia	64.80	104.09	60.6%
Tauron	3.91	4.27	9.2%

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**List of abbreviations and ratios used by mBank:**

**EV** (Enterprise Value) – Equity Value + Net Debt; **EBIT** – Earnings Before Interest and Taxes; **EBITDA** – EBIT + Depreciation & Amortisation; **Net Debt** – Borrowings + Debt Securities + Interest-Bearing Loans - Cash and Cash Equivalents; **P/E** (Price/Earnings) – Price Per Share Divided by Earnings Per Share; **P/CE** (Price to Cash Earnings) – Price Per Share Divided by Earnings + Depreciation & Amortisation; **P/B** (Price to Book Value) – Price Per Share Divided by Book Value Per Share; **P/CF** (Price to Cash Flow) – Price Divided by Cash Flow from Operations; **ROE** (Return on Equity) – Earnings Divided by Shareholders' Equity; **ROCE** (Return on Capital Employed) – EBIT x (Average Assets - Current Liabilities); **ROIC** (Return on Invested Capital) – EBIT x (1-Tax Rate) / (Average Equity + Minority Interest + Net Debt); **FCFF** (Free Cash Flow to Firm) – Cash Flow from Operations - CAPEX - Lease Payments; **FCFE** (Free Cash Flow to Equity) – Free Cash Flow to Firm - Net Interest Expense (incl. Debt + Leases)

**EBITDA margin** – EBITDA/Sales

**OVERWEIGHT (OW)** – a rating which indicates that we expect a stock to outperform the broad market  
**NEUTRAL (N)** – a rating which indicates that we expect the stock to perform in line with the broad market  
**UNDERWEIGHT (UW)** – a rating which indicates that we expect the stock to underperform the broad market

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**CEZ (Kamil Kliszcz)**

Rating	hold	hold	sell	sell	sell
Rating date	2024-05-06	2024-02-01	2023-12-01	2023-10-02	2023-07-03
Target price (CZK)	893.60	959.93	959.93	884.00	853.62
Price on rating day	851.00	870.50	988.00	980.00	900.00

**Enea (Kamil Kliszcz)**

Rating	suspended	suspended	suspended	suspended
Rating date	2024-05-06	2023-12-01	2023-10-02	2023-07-03
Target price (PLN)	-	-	-	-
Price on rating day	8.63	8.59	7.30	6.40

**PGE (Kamil Kliszcz)**

Rating	suspended	suspended	suspended	suspended
Rating date	2024-05-06	2023-12-01	2023-10-02	2023-07-03
Target price (PLN)	-	-	-	-
Price on rating day	6.18	8.41	7.50	7.26

**Polenergia (Kamil Kliszcz)**

Rating	buy	buy	buy	buy
Rating date	2024-05-06	2023-12-01	2023-10-02	2023-07-03
Target price (PLN)	103.62	111.78	102.17	104.34
Price on rating day	66.80	72.90	73.00	82.90

**Tauron (Kamil Kliszcz)**

Rating	suspended	suspended	suspended	suspended
Rating date	2024-05-06	2023-12-01	2023-10-02	2023-07-03
Target price (PLN)	-	-	-	-
Price on rating day	2.93	4.12	3.59	2.75



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