

EDP

Utilities

Reduce

Medium Risk

January 2015

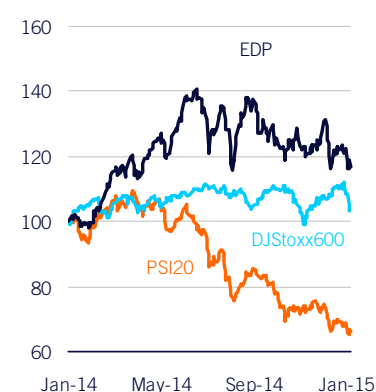
Portugal

Far from its best shape

(YE15 Price Target cut from €3.75 to €3.20; Reduce Recommendation maintained)

- Hurdles along 2014-17^F path:** EDP expects modest growth beyond 2014, a transition year in which regulatory cuts and Brazilian drought should be only partly offset by positive one-offs. We are behind the company's 5% CAGR 14-17^F guidance at both EBITDA (+3%) and EPS (+2%) due to regulatory cuts in Portugal (Distrib.), worse than expected evolution in Brazil and continued tough momentum in Iberian generation. We remain more conservative on leverage targets too (3.4x adj. ND/EBITDA17^F vs. 3.0x guidance) following the acquisition of a 50% stake in Pecém. The 5.9% DY seems supported by management commitment going forward though.
- Several one-offs added to estimates:** Besides a general fine-tuning we have incorporated the new Portuguese distribution regulation and several one-offs to be booked in 4Q14 and 2015 (Jari and Murcia assets capital gains, accounting change in Brazil, re-consolidation of Pecém, asset sales). One-offs fuelled EPS 14^F 17% up, while forecasts for 15-16^F remain broadly unchanged. A new upgrade in EDPR valuation to reflect the USD appreciation was offset by lower value in Brazil (MtM) and liberalised. We set a **YE15 PT of €3.20/sh. (-10%)**.
- Continued tough earnings momentum:** EDP remains a value proposition, boasting a friendly dividend policy (5.9% DY15^F, 1.3x covered by FCFE), lower than sector operational risk (c. 85% EBITDA regulated and LT contracted) and a competitive generation portfolio, 72% CO₂-free by 15^F. We see upside from asset rotation with last deals spurring a positive read-across to wind farms and Brazilian hydro valuations. Sovereign, overhang and regulatory risks have dropped considerably, but high leverage, stretched profitability in Iberia and ongoing drought in Brazil justify some caution. The 13% stock price drop since we downgraded the stock to Reduce (vs. -5% Stoxx utils.) is not enough comfort to weather the risks and earnings trend ahead. **REDUCE.**

EDP vs. PSI20 vs. DJ Stoxx600



Source: Bloomberg.

EDP valuation sensitivity to EDPR valuation and CRP in Iberia

		EDPR Price Target (Δ)		
		-10%	0%	10%
CRP (Δ)	Iberia	-1%	3%	8%
		0%	-5%	0%
		+1%	-13%	-7%

Source: BPI Equity Research.

Stock Data

Price (9 th Jan.):	3.11	Price Target (YE15):	3.20
# shares (mn):	3 657	M. Cap (€ mn) / F. Float:	11 379 / 43%
Reuters/Bloomberg:	EDP.LS/EDP PL	Avg. Daily Vol. [€'000]:	17 315
Major Shareholders:	CTG (21.35%); Capital Group (10.13%); Oppidum (7.19%); IPIP (4.06%); BCP PF (2.4%); Sonatrach (2.38%); Qatar H. (2.27%); Mello (2.0%); Blackrock (2.0%)		

Estimates	2011	2012	2013 ^F	2014 ^F	2015 ^F	2016 ^F	2017 ^F
PE Adj.	7.8	8.3	9.7	10.7	12.3	11.3	10.2
Dividend yield	7.7%	8.1%	6.9%	5.9%	5.9%	5.9%	5.9%
FCFE Yield	0.2%	-5.4%	12.8%	7.2%	7.0%	9.5%	12.2%
FCFF Yield	2.0%	2.3%	3.4%	2.8%	5.5%	5.4%	6.4%
PBV	1.4	1.4	1.4	1.3	1.3	1.2	1.2
EV/EBITDA ⁽¹⁾	8.5	8.8	8.8	8.7	8.8	8.3	8.0
EV/Sales ⁽¹⁾	2.1	2.0	2.0	2.2	2.1	2.1	2.1

(1) EV is fixed with current market cap and MV of remaining items.

Analysts

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Historical Recommendation

Date	Recommendation
02-Jan-14	Buy
21-Feb-14	Neutral
09-Sep-14	Reduce

Source: BPI Equity Research.

Available on our website:
www.bpiequity.bpi.pt, BPI Online,
 and Bloomberg at **NH BPD.**

P&L (€ mn)								CAGR 13-17
	2011	2012	2013	2014 ^f	2015 ^f	2016 ^f	2017 ^f	
Revenues	15121	16340	16103	14635	14867	15050	15286	-1%
EBITDA	3756	3628	3617	3678	3647	3832	4016	3%
EBITDA adj.	3756	3628	3617	3678	3647	3832	4016	3%
EBITDA adj. mg.	24.8%	22.2%	22.5%	25.1%	24.5%	25.5%	26.3%	n.s.
Depreciation & others	1488	1485	1532	1390	1440	1488	1497	-1%
EBIT	2267	2143	2085	2288	2207	2344	2519	5%
EBIT adj.	2267	2143	2085	2288	2207	2344	2519	5%
Net financial results	-675	-678	-703	-541	-696	-677	-656	-2%
Income tax	260	283	188	456	347	383	447	24%
Others	0	0	0	0	0	0	0	n.s.
Minority Interests	207	170	188	225	242	279	299	12%
Net Profit reported	1125	1012	1005	1067	922	1005	1117	3%
Net Profit adj.	1125	1012	1005	1067	922	1005	1117	3%

Balance Sheet (€ mn)								CAGR 13-17
	2011	2012	2013	2014 ^f	2015 ^f	2016 ^f	2017 ^f	
Net Intangibles	10128	9860	9324	9324	9324	9324	9324	0%
Net Fixed Assets	20708	20905	20316	20294	20640	20515	20222	0%
Net Financials	332	587	1115	1046	1046	1046	1046	-2%
Inventories	346	378	280	243	239	236	237	-4%
ST Receivables	7321	3154	3135	3341	3738	4055	4283	8%
Other Assets	713	5620	5850	5850	5850	5850	5850	0%
Cash & Equivalents	1732	2124	2629	2629	2629	2629	2629	0%
Total Assets	41280	42628	42649	42727	43466	43655	43591	1%
Equity & Minorities	11387	11432	11528	12088	12515	13054	13717	4%
MLT Liabilities	17224	17099	16357	16425	16225	15644	14754	-3%
o.w. Debt	15786	16716	15969	15831	15711	15306	14592	-2%
ST Liabilities	12669	14098	14764	14215	14726	14957	15120	1%
o.w. Debt	2999	3808	4192	4192	4192	4192	4192	0%
o.w. Payables	9670	10290	10572	10023	10534	10765	10928	1%
Equity+Min. + Liabilities	41280	42628	42649	42727	43466	43655	43591	1%

Cashflow (€ mn)							
	2011	2012	2013	2014 ^f	2015 ^f	2016 ^f	2017 ^f
+ EBITDA	3756	3628	3617	3678	3647	3832	4016
- Chg in Net W.C.	926	353	-168	718	-119	83	66
- Income Taxes	260	283	188	456	347	383	447
= Operating Cash Flow	2570	2992	3596	2504	3418	3366	3503
- Growth Capex	1423	1319	1322	1004	984	949	762
- Replacement Capex	752	692	656	669	683	696	710
- Net Fin. Inv.	-259	255	528	-69	0	0	0
= Cash Flow after Inv.	653	726	1091	900	1751	1720	2031
- Net Fin. Exp.	675	678	703	541	696	677	656
- Dividends Paid	622	676	676	676	676	676	676
+/- Equity	0	0	0	0	0	0	0
Other	40	-657	1071	455	-259	39	15
=Change in Net Debt	604	1285	-782	-138	-120	-406	-714
Net Debt (+)/Net Cash (-)	16948	18233	17451	17313	17193	16788	16074

Growth, per share data and ratios							
	2011	2012	2013	2014 ^f	2015 ^f	2016 ^f	2017 ^f
Sales growth	7%	8%	-1%	-9%	2%	1%	2%
EBITDA Adj. growth	4%	-3%	0%	2%	-1%	5%	5%
EPS Adj. growth	4%	-10%	-1%	6%	-14%	9%	11%
Avg. # sh (mn)	3657	3657	3657	3657	3657	3657	3657
Basic EPS	0.31	0.28	0.27	0.29	0.25	0.27	0.31
EPS Adj. Fully diluted	0.31	0.28	0.27	0.29	0.25	0.27	0.31
DPS	0.19	0.19	0.19	0.19	0.19	0.19	0.19
Payout	60%	67%	67%	63%	73%	67%	61%
ROCE (after tax)	6.6%	6.2%	7.2%	7.0%	6.8%	7.2%	7.7%
ROE	14.1%	12.4%	12.1%	12.3%	10.3%	10.9%	11.6%
Gearing (ND/EV)	56%	58%	58%	58%	58%	57%	62%
Net Debt/EBITDA	4.5	5.0	4.8	4.7	4.7	4.4	4.0

Source: Company data and BPI Equity Research (F).

Sum of Parts Valuation			
	€ mn	% EV	% Chg.
Iberian Generation	9510	31%	-17%
CMEC (DCF)	1258	4%	-8%
Liberalized (DCF)	8252	27%	-18%
Dist. Portugal (DCF)	4269	14%	-3%
Dist. Spain (DCF)	912	3%	-1%
Gas Portugal (DCF)	386	1%	0%
Gas Spain (DCF)	1321	4%	17%
EDPR (100% EV, DCF)	11028	36%	14%
Brazil (100% EV, MV)	1909	6%	-13%
Total Core business	29334	96%	-3%
REN (MV)	44	0%	-8%
BCP (MV)	8	0%	-25%
Others	1094	4%	0%
Total EV	30481	100%	-3%
Net debt (YE15 ^f)	16542		2%
Regulatory items	-2563		-7%
Pensions, prov. & other	1714		0%
Net Institutional Partnerships	962		12%
Minorities	2216		-9%
Equity	11610		-10%
# shares (mn)	3657		0%
YE15 P. Target (€/sh)	3.20		-10%

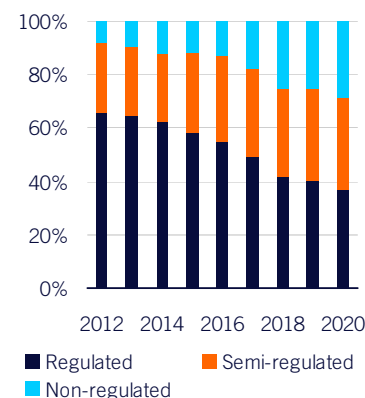
Source: BPI Equity Research.

DCF Assumptions

	Liberalised		Distrib.	
	Liberalised	CMECs	PT	
Re	12.1%	8.6%	10.8%	
Rf	3.25%	3.25%	3.25%	
CRP	0.7%	1.2%	1.2%	
Be	1.4	0.7	1.1	
Mkt premium	6.0%	6.0%	6.0%	
Tax rate	29.0%	29.0%	29.0%	
D/EV	50%	50%	52%	
Rd	5.3%	5.3%	5.3%	
WACC	7.9%	6.2%	7.1%	

Source: BPI Equity Research.

Regulated profile (% of EBITDA)



Source: BPI Equity Research.

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INVESTMENT RATINGS AND RISK CLASSIFICATION (TOTAL RETURN IN 12-18 MONTHS):

	Low Risk	Medium Risk	High Risk
Buy/CoRe Buy	>15%	>20%	>30%
Neutral	>5% and < 15%	>10% and <20%	>15% and < 30%
Reduce	>-10% and < 5%	>-10% and < 10%	>-10% and < 15%
Sell	< -10%	< -10%	< -10%

These investment ratings are not strict and should be taken as a general rule.

INVESTMENT RATINGS STATISTICS

As of 31st December BPI Equity Research's investment ratings were distributed as follows:

CoRe Buy	9%
Buy	26%
Neutral	43%
Reduce	11%
Sell/Accept Bid	5%
Under Revision/Restricted	5%
Total	100%

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