

EOS Russia – MRSK Newsletter 11/11/20

MRSK 9m results burdened by the weather, lockdowns and other virus economic impacts

MRSKs have been burdened this year first by abnormal weather patterns, then the lockdowns and other negative impacts of the coronavirus pandemic on economic activity. Their revenues are generally down Y/Y and this has also hit their profit lines, although the extent of this hit varies by company.

IFRS	EBIT margin		Net margin		Revenue
	9m20	9m19	9m20	9m19	9m20
MRSK Center-Volga	12,5%	15,0%	8,6%	7,5%	-1,2%
MRSK Volga	-2,6%	5,8%	-2,5%	3,2%	-5,2%
MRSK Urals	2,7%	7,9%	0,8%	2,9%	-24,6%
MRSK North-West	4,1%	6,2%	0,7%	0,4%	-2,6%
Lenenergo	27,5%	28,7%	20,1%	17,0%	0,6%

Source: Companies, EOS Russia

	EBIT	Net profit
	growth Y/Y	growth Y/Y
MRSK Center-Volga	-18%	14%
MRSK Volga	n/a	n/a
MRSK Urals	-75%	-81%
MRSK North-West	-36%	70%
Lenenergo	-4%	19%

Source: Companies, EOS Russia

MRSK Center-Volga has weathered the crisis quite well. Its numbers put it on track for a 13-20% dividend yield for 2020. MRSK Volga has had major problems this year, and even though its IFRS numbers are clearly better than its RAS numbers, it is likely to post a loss for the year at least on a RAS basis. MRSK North-West could be expected to pay a 3-10% yield depending on the seasonally strong last quarter, while for MRSK Urals a yield in the 1-4% range is a reasonable expectation. Lenenergo pref shares are likely to yield more than 10% for 2020.

These dividend yield projections could be higher if the Ministry of Finance were to succeed in enforcing a requirement on all state-owned companies to pay out 50% of their IFRS net profit for this year. This is what the deputy minister of finance, Alexey Moiseev, demanded on November 2 despite the coronavirus. According to him, the companies should borrow money if needed to fulfil this requirement.

MRSKs Center-Volga, Volga, Urals and North-West paid out 27-33% from their IFRS net profits for 2019. The payouts were somewhat negatively impacted by the coronavirus concerns that appeared in March.

MRSK Center-Volga bad debtors risk: TNS-Energo

In the past two weeks, some top managers of TNS-Energo have been arrested. TNS-Energo is an electricity supply company that operates in several of Russia's regions. In the electricity business as now structured the volumes of electricity distributed by the low-voltage grid companies (mainly the MRSKs) are channelled through such supply companies which manage the billing to end users.

MRSK Center-Volga has big overdue receivables from TNS-Energo that, according to sources quoted in an article on the subject in the *Kommersant* business newspaper, exceeded Rb17 billion in Nizhny Novgorod and at Rb4 billion in Tula. However, a big part of these receivables are likely 'normal course of business', as there are constant court and other disputes between distribution and supply companies.

TNS-Energo seems to have stable operations and the company made an IFRS net profit of more than R1bn in 1H20.

It is unclear at this stage if the arrests could result in new bad debts for MRSK Center-Volga.

In the summer of this year, the Energy Ministry drew up two alternative plans for dealing with TNS-Energo. In the first plan, Rosseti's Yantarenergosbyit would take over TNS-Energo. In this case, the debts of TNS-Energo would be paid over 10 years. Under the second plan, the state-owned VTB Bank would increase its stake in TNS-Energo to 50% minus one share, while Rosseti would take a 19.9% stake.

The arrests were a result of MRSK Center-Volga raising the issue with law enforcement agencies, and they may not necessarily be negative news for the company. If TNS-Energo comes under new stable and reliable ownership, there might be a prospect for recovering some already written-down bad debts.

Minorities could discuss structural changes

On 23 October, *Kommersant* reported on a letter sent by MRSK minority shareholders had sent to the prime minister Mikhail Mishushtin. According to the letter, the minority shareholders are ready to discuss possible structural changes to Rosseti's corporate structure. This could mean a pilot privatisation or privatisations of some MRSKs or it could mean a conversion of MRSK shares into a single Rosseti share. In the letter, the minorities stated that they preferred the privatisation approach as the more effective option.

Valuations and share prices

MRSK share prices have generally been quite flat in the past months in ruble terms, although they have declined quite significantly in USD and SEK terms. The ruble has been very weak lately probably partially due to oil price weakness on fears about renewed declines in demand, especially in the transport sector, resulting from the second wave of pandemic-related lockdowns restrictions.

The MRSKs continue to be attractively valued. They are currently trading at substantial discounts of 51-74% to emerging market peers on P/E multiples based on 2020-22e earnings.

	P/E				
	2018	2019	2020e	2021e	2022e
MRSK Average	2,9	3,9	9,2	4,3	3,2
GEM Average	18,5	9,5	18,8	14,2	12,6
MRSK Discount	-85%	-59%	-51%	-70%	-74%

Note: MRSK average: Center-Volga, Volga, North-West, Urals; GEM average: Light (BRA), Equatorial Energia (BRA), Manila Electric (PHI).

Note: Ratios exceeding 25 have been excluded. Source: Companies, Marketscreener, EOS estimates, Date: 6 November, 2020