

EQUITY NOTE: PANNERGY NYRT.

Recommendation: BUY

Target price (12M): HUF 1,032

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Equity Analyst:
Dániel Módos

Phone:
+36 1 301 2810

Email:
modosd@otpbank.hu

News:

PannErgy's subsidiary (Kuala Ltd.) has entered into an agreement with the Japanese-owned GS Yuasa Hungary Ltd. The ten-year geothermal heat supply agreement is expected to begin this year. PannErgy Group has agreed to invest in the power-line necessary for the heat supply, up to the isolation heat exchanger that will be implemented in the plant's thermal centre. The geothermal (secondary) heat energy consumption is estimated at 3,000 GJ per year.

Comment:

As we wrote in our Initiation report, both the Miskolc and Győr projects are located in the vicinity of industrial centres, which could provide an excellent opportunity to expand revenues and boost profit margins through the sale of secondary heat. The management also pointed out this opportunity as a strategic goal in its 2017 Annual Report: 'The Company also wishes to make its still unutilized capacities and the associated saving benefits available to new partners.'

After starting secondary heat sales for Special Transport Kft (Győr) in November 2017, PannErgy continued to accomplish its strategic goal, as the above announcement shows.

The advantage of secondary heat sales is that it basically does not have additional costs (after the installation), although its price is less than that of primary heat, due to the lower temperature of the incoming water. (In the Initiation Report, we assumed that it could be around half of the price of primary heat.)

Based on the above, this agreement could boost revenues by at least HUF 3.5 million annually (0.1% of the HUF 4.7 billion revenue of 2017), and net income could increase comparably (aside from taxes and the cost of installation in the first year). No information was available about the amount of the installation cost.

Overall, because of the small size of the deal, we do not change our valuation, but this announcement confirms that the management is both committed and able to get closer to its long-term strategy (maximizing capacity utilization through secondary heat sales), which could further boost the company profitability in the long term.

Notes:

[The initiation report, which contains the assumptions of the models used, is available here.](#)

[The valuation methodology used in this present equity research note to determine our price targets and recommendations is available here. \(Also available in Hungarian\)](#)

This investment recommendation has not used proprietary models.

The risk warning, which includes the adequate explanations of the length of time of the investment to which the recommendation relates as well as a sensitivity analysis of the assumptions, is indicated in the part of this recommendation where the length of time and the risks of the investment are presented.

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OTP Bank Plc's recommendations and price targets history for Pannergy in the past twelve months:

| Date | Recommendations | Target Price | Publication |
|------------|-----------------|--------------|------------------------|
| 15/12/2017 | BUY | HUF 1,024 | Initiation of coverage |
| 16/01/2018 | BUY | HUF 1,024 | Equity note |
| 13/02/2018 | BUY | HUF 1,024 | Equity note |
| 21/03/2018 | BUY | HUF 1,032 | Equity note |
| 17/04/2018 | BUY | HUF 1,032 | Equity note |
| 17/07/2018 | BUY | HUF 1,032 | Equity note |

| Period | Recommendations | Percent of recommendation |
|--------|-----------------|---------------------------|
| 2017Q4 | BUY | 100% |
| | HOLD | 0% |
| | SELL | 0% |
| 2018Q1 | BUY | 100% |
| | HOLD | 0% |
| | SELL | 0% |
| 2018Q2 | BUY | 100% |
| | HOLD | 0% |
| | SELL | 0% |

[The list of all recommendations made in the past 12 months is available here.](#)

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This document was prepared by:

Dániel Módos

Senior Equity Analyst

OTP Research

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