KEGOC: Results of 2018 and plans for 2019.

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The results for 2018 indicate an increase in revenues by 15% y/y to T176bn. The main share of revenue comes from the power transmission (61%), revenues from which increased by. The power transmission generates most of the revenues (61%) of the company that increased 15% y/y. Overall KEGOC demonstrates positive dynamics in all types of services that resulted from both of average growth of tariffs relative to 2017, to a great extent, and form the growth of physical volumes of electricity consumed, to some extent.

We also observe an increased cost in the purchase of electricity (+40%y/y) and an increase in technical expenditure of electricity consumption (+12% y/y), which led to an increase in the prime cost by 18% y/y to T89bn.

Operating profit amounted to T8.9bn, having increased by 18% compared to 2017. In addition to the 11% y/y growth in gross profit, the growth in operating profit resulted from the receipt of revaluation revenue of T3.3bn.

Profit for the period amounted to T40bn, which is 22% higher than in 2017. The tenge weakened, as a result of which the foreign exchange loss increased by 35% to T5.9bn and the assets depreciation amounted to T2.9bn (+31% y/y), that had a restraining effect on net income.

At a meeting of investors, the Company announced the plans to implement new investment projects. In particular, the project on reconstruction of 220-500 kV overhead lines of KEGOC branches with a cost of T126bn planned for 2018-2028. that KEGOC is going to implement at 70% by borrowed funds. The second project on Strengthening of the electrical network of the Western zone of UPS of Kazakhstan (2018-2023) is estimated by the company at T45bn and is also being considered for implementation mainly through borrowed funds (80%). The company also does not exclude the possibility of launching other equally large projects if the need arises. The company plans to borrow funds in tenge through issuing bonds. Note that at the end of 2018 the company's debt amounted to T162bn and Debt/Equity at 0.34x.

The company focuses on the reduction of tariffs for services by the regulator for 2019, while in 2020, judging by KEGOC's statements, the tariffs for regulated services will increase: for electricity transmission by 12% y/y, for dispatching - by 29% and for balancing - by 11%. With a profit rate corresponding to the market (about 14.8%), the Company is optimistic about tariffs after 2019.

On May 3, at the AGM, the proposal of the Board of Directors of KEGOC to pay out 87.7% of the net profit for dividends will be considered, minus the amount already paid for 1Q2018. the dividend of T80.53/share is 14.2 billion tenge or T54.53/share.

Our view

We estimate KEGOC’s results for 2018, as neutral, the deviation in operating profit is a reasonable 2.3% of our forecast. Adjusted net income (excluding impairment) is also in line with our expectations (T42bn vs. T44bn).

In connection with the completion of major projects, we expected the launch of the next capital-intensive projects only by 2021. However, in our assessment, we laid Capex at a rate of no more than 35bn until 2025, which, in our opinion, would correspond to the company's new investment outflows, taking into account the long-term expected projects (125bn tenge for 10 years).

In terms of tariffs for the subsequent period, high uncertainty remains: the company’s optimism regarding tariffs is partially adequate. We maintain our forecast for tariff stagnation in 2019-2020 at levels accepted by the regulator and on the basis of a constant value of the profit margin of ~ 15% with full involvement of assets, we maintain our expectations for the growth of transmission and balancing tariffs in 2021-2025 by 5% (CAGR) and by dispatching - by 8%.

At the end of 2018, our dividend forecast was T135/share. Taking into account the expected approval of payment of 87.7% of net income for dividends for 2018, the total dividend size is exactly in line with our expectations and amounts to T135.6 tenge/share.

Attracting a new loan make changes to our model and our target price could be adjusted. We put our recommendation on a revision.

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