

Enerjisa

BUY

(prev. Not Rated)

Superior operational visibility at an attractive valuation. Initiating with Buy.

Superior operational visibility; insulated from CPI and TRY volatility

We are initiating coverage of Enerjisa <ENJSA TI>, with a Buy rating and a 12M total return target of TRY8.43/sh (including a DPS of TRY0.40 (implying a yield of 6.6%)), corresponding to a 38% total return potential. Our conviction in the company is based on **1)** Supportive regulatory framework leading to a favorable real return component of 13.6% until 2021, **2)** Income structure protecting real returns from higher CPI at the operating level, **3)** Strong market position; leading to operational synergies, **4)** Robust RAB growth outlook to drive a CAGR of c. 20% in operational earnings and net income within 2017 and 2020, **5)** Strong shareholder structure allowing competitive financing, **6)** Absence of FX-denominated leverage insulating Enerjisa's earnings from TRY volatility, and **7)** Decent dividend outlook, 6.6% dividend yield in 2019; mid-term avg. yield of 8.3%.

The leading electricity distribution and retail company in Turkey

Enerjisa, the leading electricity distribution (26% market share) and retail (22% market share) company in Turkey, was founded in 1996; primarily as an electricity generation business. The Company had acquired the Baskent electricity distribution region in 2009; followed by the acquisition of Ayedas and Toroslar regions in 2013. Earlier in 2013; E.ON replaced Verbund as Sabanci Holding's partner in the Company. Enerjisa' generation and wholesale businesses were spun off from the distribution and retail businesses in 2017. Enerjisa, as the distribution and retail company; has been listed on the BIST since February 2018.

We expect the strong post IPO relative share perf. to be sustained

Enerjisa shares have outperformed the BIST-100 by 18% (mainly due to underperformance of the banking index) and delivered 4% higher return than the BIST-Industrial index since its IPO, while declining by 3% and 23% in nominal TRY and USD terms, respectively. The shares have underperformed the BIST-100 and BIST-Industrials by 4% over the last one month partially due to the uncertainty pertaining to the size of the fine to be levied by the Competition Authority, which is expected to be announced soon (originally expected to be disclosed on July19). Accordingly; we view the near term resolution of the investigation (and the potential accompanying fine) as a short-term negative yet long-term positive for the Company as it clears a significant uncertainty. The absence of significant further investigations on Enerjisa's operations should reorient the investors' focus back to Enerjisa's valuation and operating outlook both of which are promising, in our view

Highly visible 20%+ FY17-FY20E CAGR in EBITDA and net income

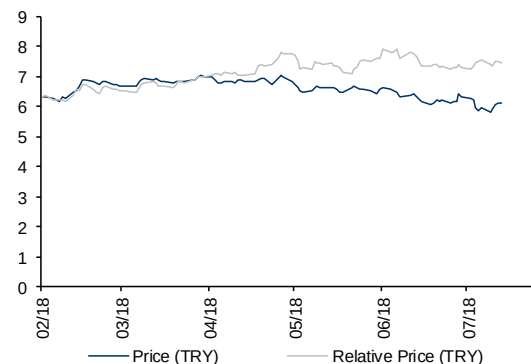
Coupled with the recent underperformance, we perceive the current price point as an attractive entry point to a highly foreseeable operational and earnings outlook (c.20% CAGR EBITDA and earnings growth FY17-FY20E); mostly insulated from the prospect of higher CPI (through real WACC mechanism) and weakness in TRY (practically nil FX exposure); with an average dividend yield of c.8% between FY17-FY20E which are significant differentiating factors vs. most of the other industrials in our coverage; considering the current global and domestic macro backdrop. Shares are trading at 8.4x 19E P/E (adjusted) of and 4.4x 19E EV/operational earnings (IFRS EBITDA + net other operating items (which we believe to be sustainable)+ CAPEX Reimbursement – one-off operational items).

Higher cost of financing and regulation developments are key risks

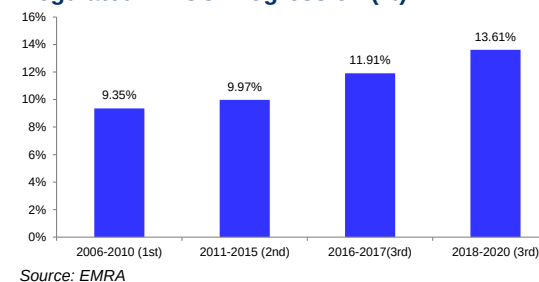
Continuation of Enerjisa's sequential operating performance is likely to be the key factor in building investor confidence in Enerjisa's post IPO outlook, which should be visible in its upcoming 2Q results (to be announced on August 13) as well. The key risks are **1)** Significant deterioration in borrowing liquidity and costs, and **2)** revisions in the regulatory framework.

Stock Data		20 July 2018
Current price		TRY6.12
Target price		TRY8.03
DPS		TRY0.4
Total return		38%
Current Mcap	TRY7,228mn/	US\$1506mn
Bloomberg Ticker		ENJSA TI
Capital (mn)		1,181
High / Low Price Range (12M)		7.02/5.81
3-m Average Daily Turnover (\$ mn)		6.1

Price Performance (%)	1M	3M	6M	Ytd
Return		-5	-10	
Relative to BIST100	-3	7		



Regulated WACC Progression (%)



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Financial Summary (TRYm)	2015	2016	2017	2018E	2019E	2020E
Income Statement						
Total revenues	9,154	9,103	12,345	14,168	16,205	17,806
COGS	7,108	6,501	8,412	9,940	11,368	12,468
Gross profit	2,045	2,602	3,932	4,228	4,837	5,338
Opex	-1,080	-1,228	-1,519	-1,743	-1,994	-2,190
EBITDA	1,185	1,593	2,649	2,720	3,079	3,383
Depreciation	219	218	235	235	235	235
Operating income	966	1,375	2,414	2,485	2,844	3,148
Financial income/expense	-575	-758	-957	-1,116	-1,382	-1,460
Net other income/expense	73	-102	-173	-299	-192	-211
Pre-tax income	463	514	1,284	1,070	1,270	1,477
Tax	0	-137	-296	-342	-407	-458
Minority interest/other	0	0	0	0	0	0
Net income	463	377	988	728	864	1,019

Balance Sheet						
Cash and liquid assets	608	75	173	43	88	138
Inventories	63	74	102	120	138	151
Accounts receivable	1,818	2,114	2,822	3,183	3,641	4,000
Other current assets	43	677	1,005	1,066	1,130	1,186
Total current assets	2,532	2,940	4,102	4,413	4,996	5,475
Fixed assets	31	58	138	206	275	345
Financial and equity investments	2,565	0	0	0	0	0
Other non-current assets	8,893	12,134	14,346	15,151	16,317	17,463
Total non-current assets	11,489	12,192	14,484	15,357	16,593	17,807
Total assets	14,021	15,131	18,586	19,770	21,589	23,282
Short-term debt	1,916	3,098	1,939	1,889	2,064	2,064
Accounts payable	827	1,118	1,512	1,089	1,246	1,366
Other current liabilities	1,838	735	1,404	1,499	1,623	1,736
Total current liabilities	4,581	4,951	4,855	4,477	4,933	5,166
Long-term debt	2,878	3,200	5,269	6,369	7,369	8,419
Other non-current liabilities	2,196	2,234	2,581	2,791	2,851	2,904
Total non-current liabilities	5,074	5,434	7,850	9,160	10,220	11,323
Minority interest	0	0	0	0	0	0
Total shareholders' equity	4,366	4,747	5,880	6,134	6,436	6,793
Total liabilities and equity	14,021	15,131	18,586	19,770	21,589	23,282

Cash Flow Statement						
Operating cash flow	1,021	1,859	1,858	1,582	2,430	2,385
Investing cash flow	-2,286	-2,709	-1,682	-1,796	-1,841	-1,880
Financing cash flow	1,305	772	-78	84	-544	-456
Total cash flow	40	-78	98	-130	45	50
Net debt	4,439	6,493	7,345	8,545	9,382	10,387

Key Ratios						
Gross margin	22.3%	28.6%	31.9%	29.8%	29.8%	30.0%
EBITDA margin	12.9%	17.5%	21.5%	19.2%	19.0%	19.0%
ROE	11.0%	8.3%	18.6%	12.1%	13.7%	15.4%
Sales growth	14%	-1%	36%	15%	14%	10%
EBITDA growth	115%	34%	66%	3%	13%	10%
Earnings growth	-276%	-18%	162%	-26%	19%	18%
Net debt-to-equity (x)	1.0	1.4	1.2	1.4	1.5	1.5
Net debt-to-EBITDA (x)	3.7	4.1	2.8	3.1	3.0	3.1

Key Ratios						
RAB	2,662	3,914	5,300	6,756	8,180	9,568
One-offs	-332	0	-582	-100	0	0
CAPEX Reimbursement	174	448	592	750	882	969
Operational Earnings *	1,100	1,938	2,565	3,072	3,769	4,141
Net income (Adjusted)	131	377	521	778	864	1,019
Net debt / Op. Earnings (x)	4.0	3.4	2.9	2.8	2.5	2.5
EV/RAB (x)	4.4	3.5	2.7	2.3	2.0	1.8

Source: The Company, YKY Research

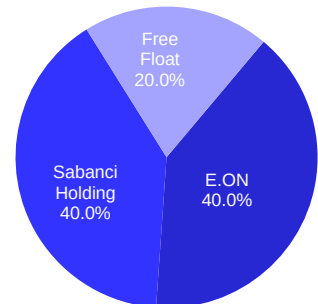
Investment Case

Enerjisa, the leading electricity distribution (26% market share) and retail (22% market share) company in Turkey has been founded in 1996; primarily as an electricity generation business. Enerjisa' generation and wholesale businesses were spun off from the distribution and retail businesses in 2017. Enerjisa, as the distribution and retail company; has been listed on the BIST since February 2018. Following its recent underperformance, we view the current price level as an attractive entry point to a company with highly foreseeable operational and earnings outlook (c.20% CAGR in EBITDA and earnings within FY17-FY20E); mostly protected from the prospect of higher CPI (through real WACC mechanism) and weakness in TRY (practically nil FX exposure); with an average dividend yield of c.8% between FY17-FY20E which are significant differentiating factors vs. most of the other industrials in our coverage; considering the current global and domestic macro backdrop. Shares are trading at 19E P/E (adjusted) of 8.4x and EV/operational earnings (EBITDA + net other operating items + CAPEX Reimbursement – One-off operational items) of 4.4x.

Stock Triggers & Risks

Continuation of Enerjisa's sequential operating performance is likely to be the key factor in building investor confidence in Enerjisa's post IPO outlook, which should be visible at its upcoming 2Q results (due August 13) as well. The key risks are **1)** Significant deterioration in borrowing liquidity and cost, and **2)** potential regulatory developments.

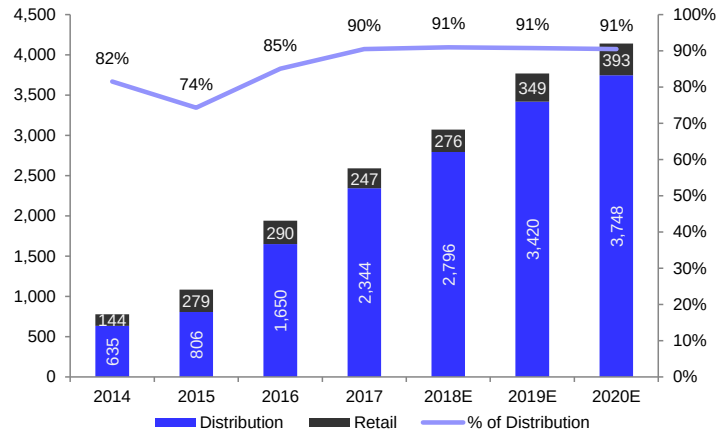
Chart 1: Shareholder Structure (%) *



Source: The company, * effective ownership structure

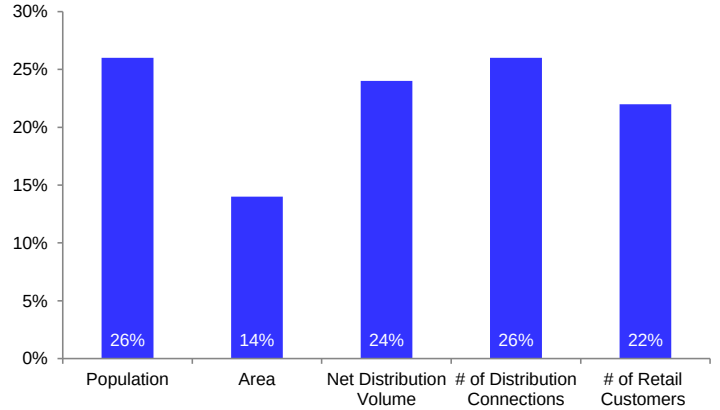
Key Charts

Figure 1: Progression of Enerjisa's Distribution & Retail Operating Income (Adjusted EBITDA) (TRYm)



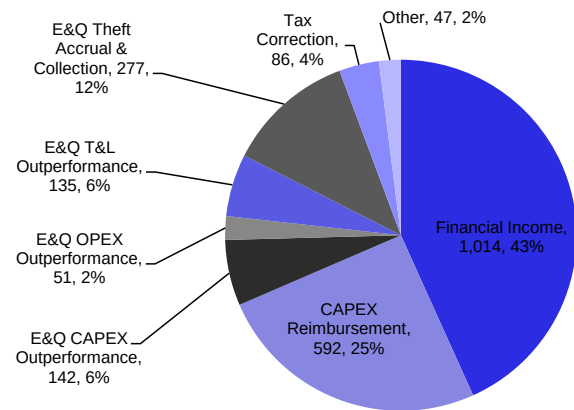
Source: The Company, YKY Research estimates

Figure 2: Enerjisa's market share in its operating territories (%)



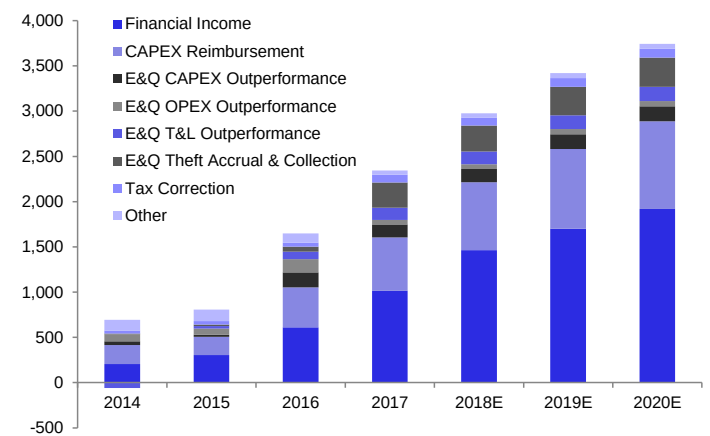
Source: The Company

Figure 3: Enerjisa's distribution operations' operating income breakdown (2017A) (%)



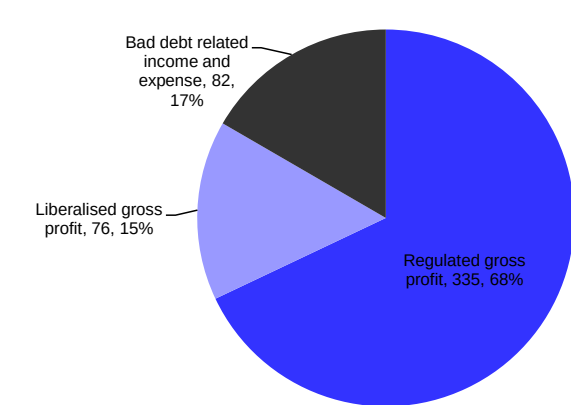
Source: The Company

Figure 4: Enerjisa's distribution operations' operating income progression (TRYm)



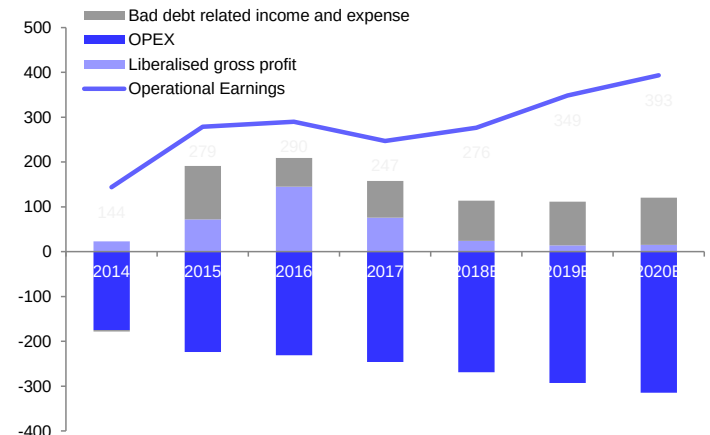
Source: The Company, YKY Research Estimates

Figure 5: Enerjisa's retail operations' operating income breakdown (2017A) (%) *



Source: The Company, *Excluding OPEX

Figure 6: Enerjisa's retail operations' operating income progression (TRYm)



Source: The Company, YKY Research Estimates

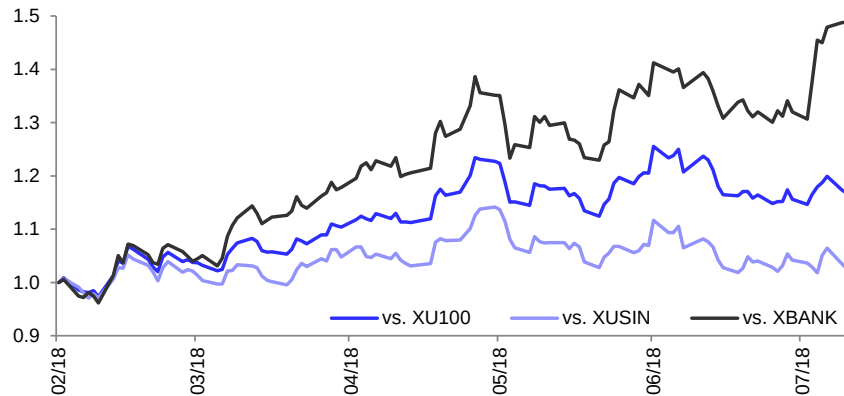
Superior operational visibility & growth

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Enerjisa, the leading electricity distribution (26% market share) and retail (22% market share) company in Turkey has been founded in 1996; primarily as an electricity generation business. The Company had acquired the Baskent electricity distribution region in 2009; followed by the acquisition of Ayedas and Toroslar regions in 2013. Earlier in 2013; E.ON had replaced Verbund as Sabanci Holding's partner in the Company. Enerjisa' generation and wholesale businesses were spun off from the distribution and retail businesses in 2017. Enerjisa, as the distribution and retail company; has been listed on the BIST since February 2018.

Enerjisa shares have outperformed the BIST-100 by 18% (mainly due to underperformance of the banking index) and delivered 4% higher return than the BIST-Industrial index since its IPO, while declining by 3% and 23% in nominal TRY and USD terms, respectively. The shares have underperformed the BIST-100 and BIST-Industrials by 4% over the last one month partially due to the uncertainty pertaining to the size of the fine to be levied by the Competition Authority, which is expected to be announced soon (originally expected to be disclosed on July19). Accordingly; we view the near term resolution of the investigation (and the potential accompanying fine) as a short-term negative yet long-term positive for Enerjisa as it clears a significant uncertainty.

Figure 7: Enerjisa's Post IPO Share performance



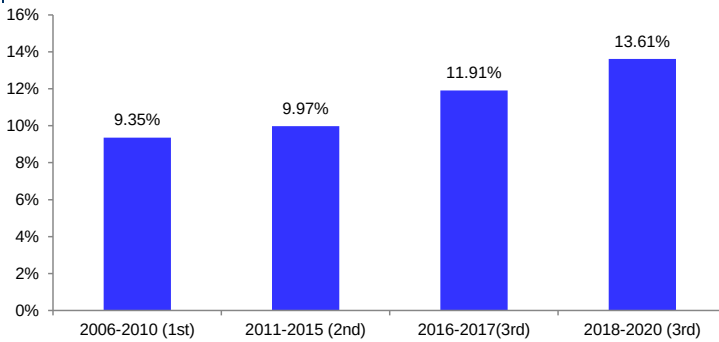
Source: Rasyonet

Following the recent underperformance, we perceive the current price level as an attractive entry point to a company with a highly foreseeable operational and earnings outlook (c.20% CAGR in EBITDA and earnings within FY17-FY20E); mostly insulated from the prospect of higher CPI (through real WACC mechanism) and weakness in TRY (practically nil FX exposure); with an average dividend yield of 8% between FY17-FY20E, which are significant differentiating factors vs. most of the other industrials in our coverage; considering the current global and domestic macro backdrop. Shares are trading at 19E P/E (adjusted) of 8.4x and EV/operational earnings (IFRS EBITDA + net other operating items) + CAPEX Reimbursement – one-off operational items) of 4.4x.

The key investment positives are as follows:

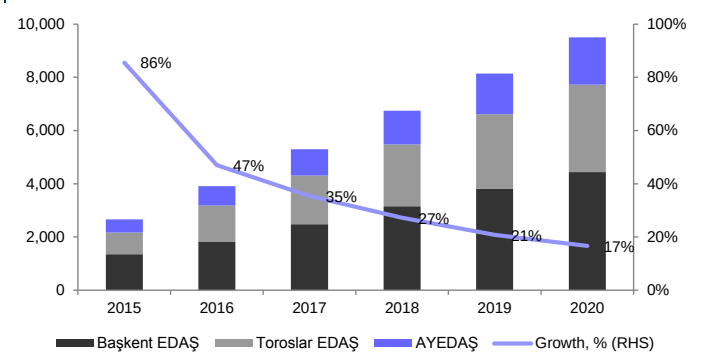
Favorable regulatory structure had led to higher real return component: EMRA, Energy Market Regulatory Authority, has progressively increased the real return component (the key component of the profitability of distribution companies). Accordingly, on December 20, 2017, EMRA has revised up the rate of return component for electricity distribution companies for the 3rd term (2018 – 2020) electricity distribution tariff period, effective until December 2020. Accordingly, the adjusted reasonable rate of return (real terms & before tax, also referred as “WACC”) has been increased by 1.7pps to 13.61% from 11.91% (3.6 pps higher than the WACC of 9.97% set for 2010-2015).

Figure 8: Regulated WACC (Real terms) progression (%)



Source: EMRA

Figure 9: RAB breakdown (TRYm) & growth (%)

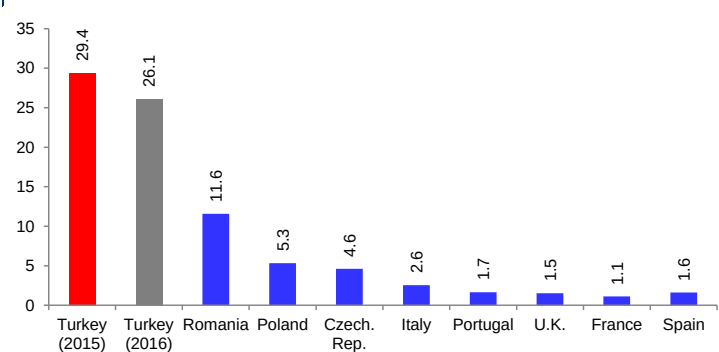


Source: EMRA, YKY Estimates

The more generous return component offered by EMRA has been partially motivated to alleviate the FX debt-burdened balance sheets of various companies in the sector considering the significant depreciation of the TRY against the USD given the mostly TRY denominated revenue stream of the distribution companies. While we are not anticipating further tangible increase in the return component of the sector for the current tariff period (up until the end of 2020); we perceive the current real return component (13.61%) as attractive for Enerjisa's operational outlook.

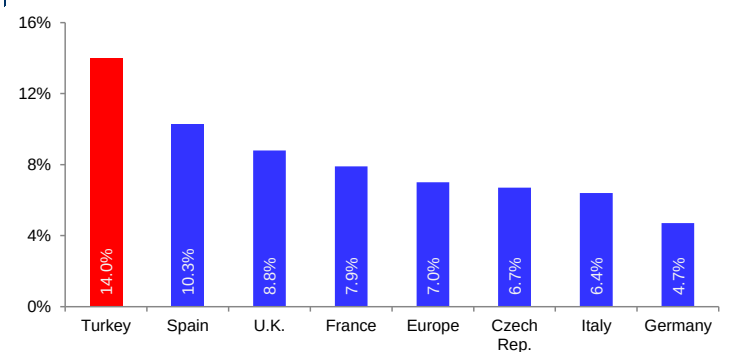
It is difficult to ascertain a credible approximation of the magnitude of the WACC revisions for the upcoming regulatory periods (2021-2025, 2026 -2030, etc.) as it is **1)** determined by a regulator (“EMRA”), and **2)** not tied to a specific formula. In our reasoning it could be close to the upper range of the 9.35% to 13.61% WACC range observed over the past decade; if not higher. This is due to **1)** our expectation of the overall financial health of the sector (mainly due to their mostly FX denominated financial obligations) unlikely to exhibit a significant improvement; thus necessitating a relatively favorable return component and, **2)** continued investment needs in historically underinvested grids coupled with the above EU average population and electricity consumption growth outlook in Turkey .

Figure 10: Duration of outages and theft loss (hours/year) *



Source: The Company, Eurostat, * 2014 for European countries

Figure 11: T&D Losses in Turkey vs. E.U. countries

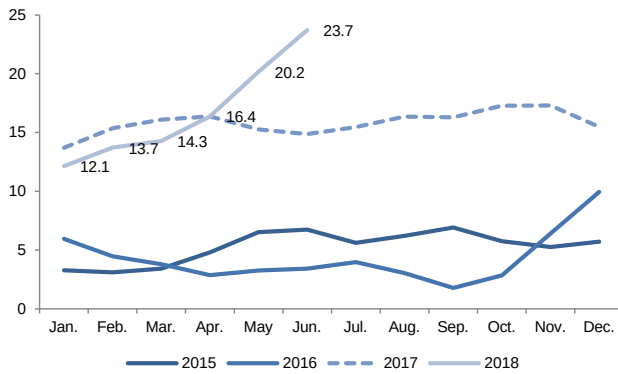


Source: The Company, Eurostat

Income structure insulates real returns from higher CPI at the operating level:

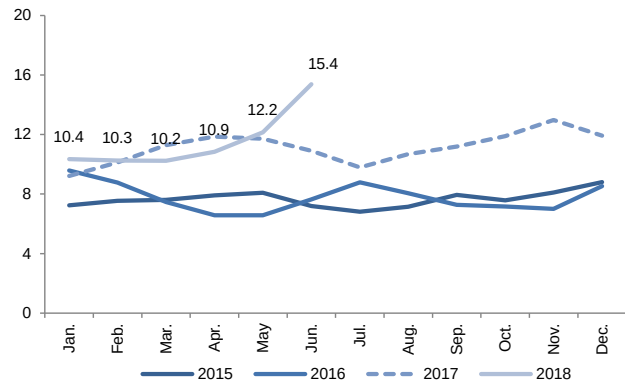
Financial Income (CPI inflated by WACC (set at 13.61% between 2018-2020) is the main component of Enerjisa's operational earnings. The end of June inflation data point is used as the CPI component of the income formula. While CPI could continue to rise going forward given the continued heightened pace of PPI and FX pass-through impact; we believe that Enerjisa's income model allows the Company to benefit from higher inflation at the operating level through maintaining its real return (WACC). We believe that this attribute is a key differentiating factor for Enerjisa in addition to the benefit of the mostly inelastic nature of electricity demand, vs. other industrials which may find it difficult to pass-through higher costs to end-users.

Figure 12: PPI annual rate of change, %



Source: Turkstat

Figure 13: CPI annual rate of change, %



Source: Turkstat

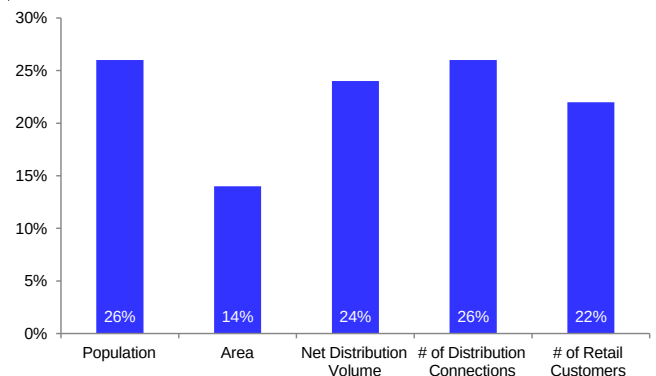
Strong market position; leading to operational synergies: The combined distribution network positions Enerjisa Enerji A.S. ("Enerjisa") as the largest grid operator with 10.9m distribution connections (26% of Turkey as of 2017) and 9.2m retail customers (22% of Turkey as of 2017). Enerjisa is also involved in the retail sale of electricity; which has accounted for c.10% of Enerjisa's 2017 EBITDA (adjusted). Enerjisa benefits from 1) operational synergies across its distribution (consolidated management and fixed costs, personnel allocation optimization, implementation of best practices across regions, etc.) 2) lower CAPEX (per unit) given the substantial purchasing power of Enerjisa which is captured through a CAPEX outperformance item in its operational earnings

Figure 14: Enerjisa's distribution network layout



Source: The Company

Figure 15: Enerjisa's market share (%)

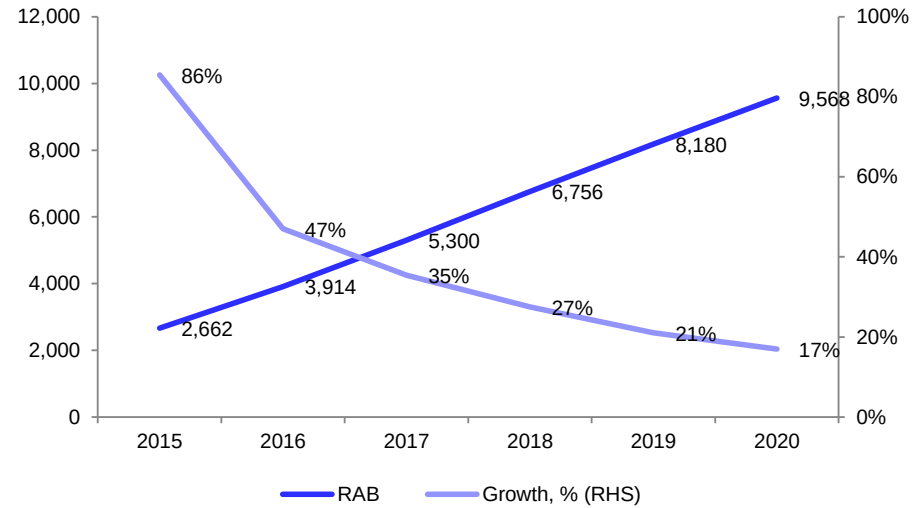


Source: The Company

Robust RAB growth outlook to drive a CAGR of c. 20% in operational earnings and net income from 2017 to 2020: Enerjisa' RAB (regulated asset base) has grown at a CAGR of 55% between 2014 and 2017, reaching TRY5.3bn mainly driven by the substantial CAPEX on its grid. This is important as the regulated return on the distribution grid is based on the size of Enerjisa's RAB. We expect Enerjisa's RAB to register a

CAGR of 22% from 2017 to 2020 reaching to TRY9.6bn. Accordingly, we expect the RAB growth to drive a 18% CAGR EBITDA (adjusted, including CAPEX reimbursement) and 22% CAGR net income growth between 2017 and 2020.

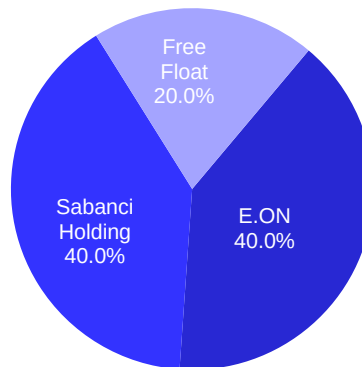
Figure 16: Enerjisa's RAB progression and growth (%)



Source: The Company, YKY Research estimates

Strong shareholder structure allows competitive financing: With equal partnership (40% each) between Sabanci Holding and E.ON (Germany) since 2013 and 20% free float since the IPO, Enerjisa has arguably the strongest shareholder structure amongst the other electricity distribution regions, in our view. We believe that the accompanying more competitive financing terms (vs. peers) are one of the key drivers of the profitability of its distribution business given its substantial contribution to the delta between the nominal return component regulated by EMRA minus the cost of financing of its grid CAPEX.

Figure 17: Enerjisa's shareholder structure

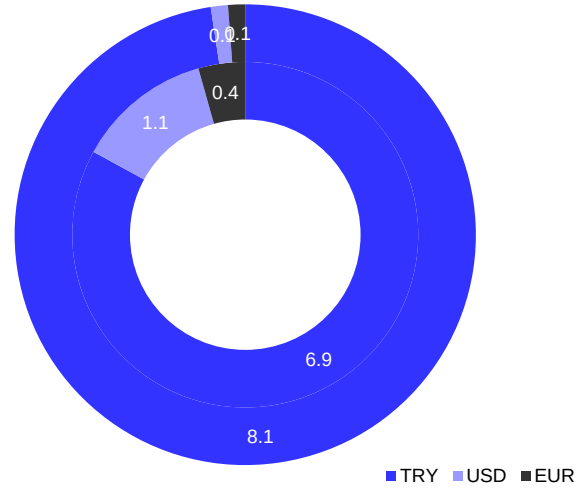


Source: The Company

Absence of FX-denominated leverage; insulates the Company's earnings from TRY volatility: Enerjisa has a gross debt position of TRY8.3bn (86% in TRY; 13% in USD and 4% in EUR) as of 1Q18; with the FX portion of its debt being swapped into TRY based liabilities; thus providing protection from the volatility of the TRY. Accordingly; we view this attribute as a differentiating factor for Enerjisa vs. most of the BIST industrials in terms of dividend visibility; particularly considering the significant YTD weakening of the TRY against hard currencies. We expect Enerjisa's management to maintain its hedging

policies. That said; the potentially higher cost of the implementation of hedging instruments could lead to slightly higher net financial expenses going forward.

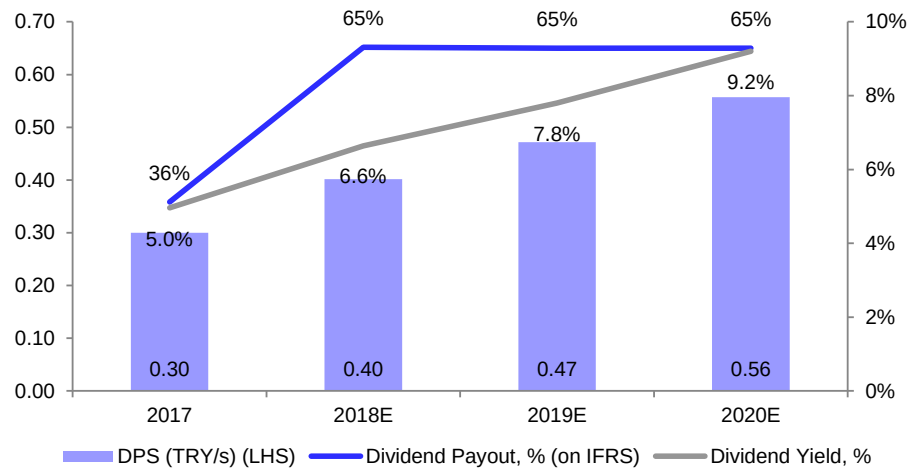
Figure 18: Enerjisa's Gross Debt Breakdown (pre and post-swap agreements) (TRYbn)



Source: The Company

Descent dividend outlook, c.6.6% dividend yield in 2019E; mid-term average yield of 8.3%: Enerjisa has dividend policy of 60%-70% dividend payout of its underlying net income (net income excluding one-off and/or extraordinary items). Accordingly, Enerjisa has distributed a DPS of TRY0.30/sh., corresponding to a 68% of underlying net income; and 36% of IFRS net income) in April, 2018. We expect Enerjisa to maintain a c.65% dividend payout (on underlying net income) going forward (barring any extraordinary developments pertaining to the cost of financing and the sector); implying a DPS of TRY0.40 (corresponding to a yield of 6.6%) to be distributed in 2019 and averaging at a yield of 8.3% going forward.

Figure 19: Enerjisa's Dividend payout, DPS and yield progression



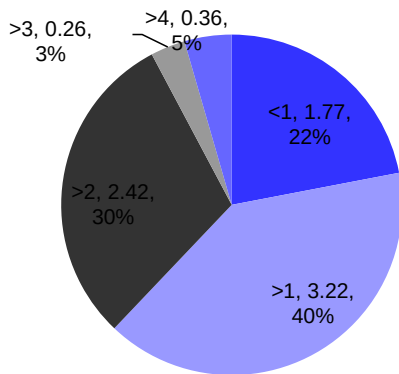
Source: The Company, YKY Research estimates

We perceive that the management views the continuity of dividends as one of the key objectives of the Company. That said; the relatively high dividend payout rate; does not leave any room for Enerjisa to de-lever its balance sheet from the viewpoint of its gross debt in TRY terms considering our avg. consolidated free cash flow yield estimate of nil within 2017-2020.

The key investment risks/negatives are as follows:

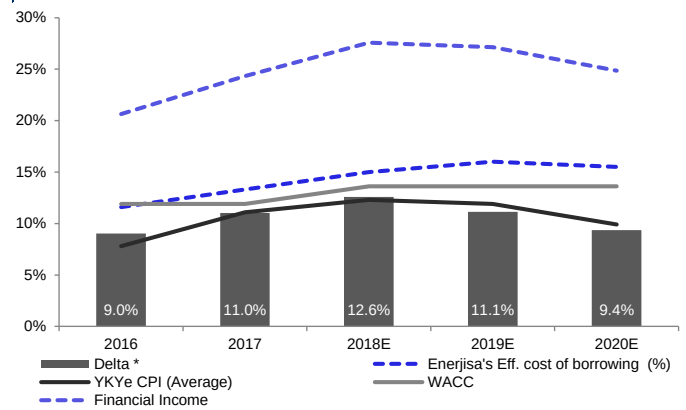
Potential increase in the effective cost of borrowing is likely to be detrimental to the financial income component of Enerjisa's distribution business: Enerjisa has TRY8.0bn of gross financial debt as of 1Q18; of which TRY1.8bn (22%) to be refinanced in less than a year and TRY3.2bn (40%) portion to be financed in 1-2 years. This is inclusive of Enerjisa's CPI linkers (CPI + 4%-5%) bond portfolio of TRY1.3bn, which constitutes 17% of Enerjisa's gross debt. Given the background of potentially higher inflation; and higher borrowing costs (in tandem with higher U.S. bond yields); we anticipate Enerjisa's cost of borrowing to increase gradually in 2018 and 2019; while moderating in 2020. Accordingly; while the financial income (WACC + CPI) reflects the higher CPI; we expect the back loaded increase in Enerjisa's cost of borrowing to lead to a decline in the real return of its distribution business in 2019 and 2020; which is incorporated in our estimates.

Figure 20: Tenure of Enerjisa's financial debt(1Q18) (TRYbn)



Source: Company Financials

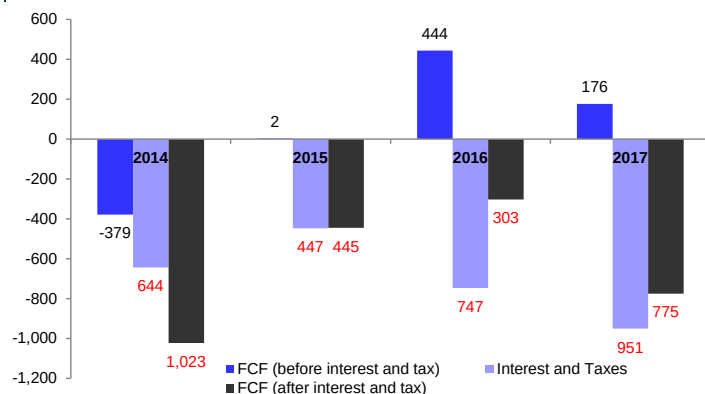
Figure 21: Enerjisa's cost of financing progression (%)



Source: Company financials, YKY Research estimates, * Differential between the nominal financial income and Enerjisa's estimated cost of borrowing

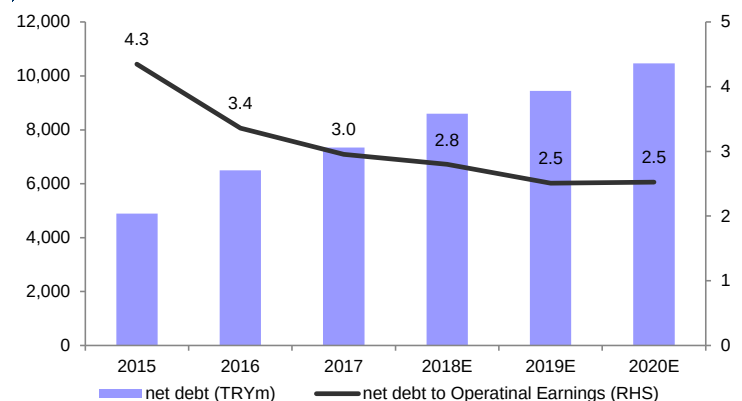
Relatively high nominal debt, c. 2.6x net debt to EBITDA as of FY18E: Enerjisa has a net debt of TRY8.3bn as of 1Q18 which we expect to increase to TRY8.6bn as of the end of FY18 and TRY9.5bn as of FY19. This is mainly due to **1)** CAPEX intensity of the business; with Enerjisa aiming to sustain an even higher level of CAPEX over the regulatory allowance in order to grow its RAB base, **2)** generous dividend distribution policy of 60%- 70% payout ratio and **3)** substantial interest expense.

Figure 22: Enerjisa's FCF progression (TRYm)



Source: Company Financials

Figure 23: Net debt & net debt to EBITDA (x) progression



Source: The Company, YKY Estimates

That said, Enerjisa's net debt to operational earnings (EBITDA including CAPEX reimbursement, exc. one-off items) of 3.0x as of 2017; has declined significantly from 7.0x in 2014, which we expect to decline further and to be sustained at c.2.5x after 2018.

Competition Authority's decision is likely to be announced soon: Competition Authority's investigation on whether Enerjisa has violated Article 6 of the Competition Law is likely to be announced soon, which was expected to be disclosed on July 19.

The Competition Authority can impose a fine up to 10% of Enerjisa's distribution and retail businesses' revenues for the fiscal year preceding the decision (implying a ceiling of TRY1.2bn; corresponding to 17% of Enerjisa's market cap and 162% of its adjusted FY18E net income). While the wide range of the potential fine; and lack of reliable precedents; lower the quality of a potential estimate; we have incorporated an arbitrary TRY150m fine (corresponding to 2.1% of Enerjisa's mcap) in our estimates; in order to partially incorporate the potential impact to our financial estimates.

Enerjisa had not set aside any provision for the potential fine. We expect Enerjisa to book the potential fine in its upcoming 2Q18 results with the potential cash payment taking place in 2019. While it will ultimately be the Company's BoD's decision to recognize the expense as a one-off or not; we perceive that the fine is unlikely to impact Enerjisa's underlying net income (IFRS net income excluding one-offs); which constitutes the base for Enerjisa's dividend payout policy (60% - 70%).

Recall that on November 26, 2016, the Competition Authority has initiated a preliminary examination, against Enerjisa and its distribution and retail companies. Following the preliminary examination, in December 2016, the C/A has proceeded with a full investigation on, "1) whether Enerjisa's distribution companies and retail companies are acting in compliance with legal unbundling rules, 2) whether the sales agreements executed between Enerjisa's customers and retail companies are in compliance with competition rules, 3) whether the necessary measures resolved in the previous preliminary examination initiated against AYEDAS and AYEPSAS in 2014 were taken and 4) whether Enerjisa's distribution companies and retail companies are in abuse of dominant position". Following the investigation, Competition Authority has alleged that Enerjisa has abused its dominant position and should be liable for administrative fines.

Accordingly; we view the near term resolution of the investigation as a short-term negative yet long-term positive for the Company as it clears a significant uncertainty on Enerjisa's earnings outlook, in our view.

We are not expecting a medium term share overhang following the expiry of the post IPO lockup period on August 7: The 180-day lockup period for Sabanci Holding and E.ON to sell Enerjisa shares expires on August 7. Neither party has signaled an intention to sell additional shares on BIST and we are not anticipating a meaningful divestiture of additional Enerjisa shares for the foreseeable future with the current share price trading 1% lower than the IPO share price of TRY6.25/s (adjusted for dividends: TRY5.95/s). That said; we believe that an increase in the free float of 20% in the longer term; would be beneficial to increase the trading volume (3M ADV: TRY28m (equivalent of USD6m)) and be supportive of the foreign ownership in Enerjisa shares which stand at 62.0%, close to the foreign ownership level in the overall market.

Valuation

We value Enerjisa through its blended FY19E P/E, EV/EBITDA and EV/RAB multiples: We value Enerjisa through a blended multiple valuation (50% P/E (adjusted) at 10.0x, 25% EV/EBITDA (adjusted) at 6.0x, 25% EV (adjusted)/RAB at 2.5x) based on our FY19E forecasts.

Figure 24: Enerjisa's distribution & retail operations valuation summary (TRYm)

	Multiple (x)	Implied Equity Value	Weight (%)
FY19E P/E* @ 10x	10.0	8,639	50%
FY19E EV/EBITDA* @ 6x	6.0	14,069	25%
FY19E EV/RAB* @ 2.5x	2.5	11,905	25%
12M Target Mcap (TRYm)		9,954	
Current Market Cap (TRYm)		7,228	
Total Return Potential, %		38%	
12M Target Share Price (inc. divs) (TRY/s)		8.43	
DPS (TRY/s)		0.40	
Dividend Yield (%)		6.6%	
12M Target Share Price (TRY/s)		8.03	
12M Upside Potential, (%)		31%	

Source: The Company, YKY Estimates, * adjusted for one-offs

We assigned a higher weight to Enerjisa' P/E (adjusted for one-offs recurring net income) in order to **1)** provide a more standard valuation parameter given the abundance of moving parts and adjustments at the operating level, **2)** to capture the impact of the higher risk free rate and borrowing costs through higher financial expenses; thus lower net income. In our calculations; we have added the CAPEX reimbursement component to the IFRS EBITDA, as we believe it is a recurring item related to its operations.

Figure 25: Consolidated sectoral and peer multiples & KPI *

	Current multiples	Historic multiples	Forward EBITDA CAGR	Historic EBITDA CAGR
	Mcap weighted average EV/NTM EBITDA trading multiple	Mcap weighted average EV/LTM EBITDA trading multiples for Q1 2013–Q4 2017	Two o-year forward from Q1 2018 CAGR of select utilities' mcap. weighted adjusted EBITDA	Five-year (Q1 2013–Q1 2018) CAGR of select utilities' mcap. weighted adjusted EBITDA
Transmission and distribution (T&D)	10.6	10.4	1.7%	6.3%
Renew able energy (RE)	15.0	15.9	3.3%	4.7%
Integrated utilities	11.9	9.9	2.2%	4.3%
Independent power producers (IPPs)	10.8	20.0	n.m.	n.m.
Water and wastewater (W/WW)	14.5	12.2	3.0%	4.0%
Americas	12.6	13.7	3.2%	5.2%
TD	11.1	10.5	0.8%	0.2%
RE	11.4	12.8	2.3%	4.3%
Integrated	7.2	8.4	0.8%	-3.9%
IPP	n.a.	n.a.	n.a.	n.a.
W/WW	n.a.	n.a.	n.a.	n.a.
Europe	8.7	10.6	1.2%	-2.8%
TD	9.4	10.7	3.0%	1.0%
RE	11.3	10.7	6.0%	5.0%
Integrated	8.1	11.8	3.0%	13.0%
IPP	9.1	12.8	6.0%	2.0%
W/WW	n.a.	n.a.	n.a.	n.a.
Asia Pacific	9.5	12.2	3.0%	12.0%

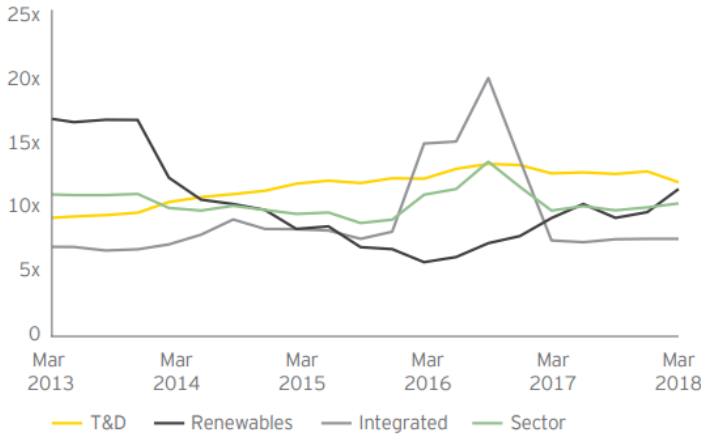
Source: Ernst Young, * Trading multiples dashboard, 1Q18

Our EV/RAB assumption is higher than developed markets' EV/RAB range of 1.0x to 1.5x given **1)** continued growth of Enerjisa's RAB; due to the heightened pace of CAPEX for the mostly underinvested and old grids, and **2)** The RAB having been reset to TRY0.0bn as of 2006; thus implying a low base compared to distribution companies in mature markets, which we expect to reach TRY9.5bn in 2020, implying a CAGR of 25% (13% in

real terms) and reach TRY15.7bn in 2025 implying a CAGR of 10% (2% in real terms) between 2021 – 2025.

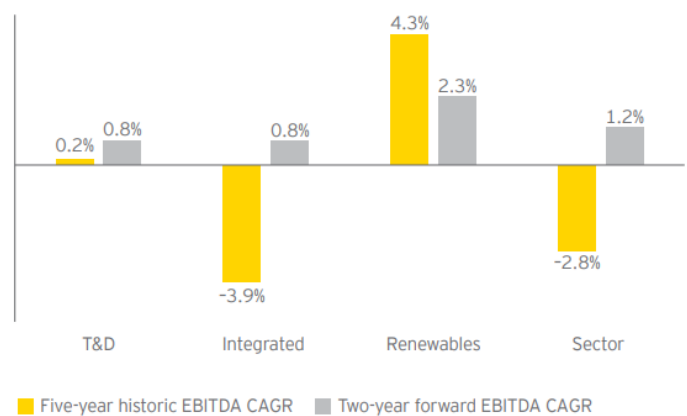
While international transmission and distribution companies trade at relatively rich EV/EBITDA multiples (Americas:10.6x, Europe: 9.4x, and Asia Pacific: 9.5x) with lower EBITDA growth profiles; we have opted to be conservative for our target EV/EBITDA multiple (6.0x) for Enerjisa; which can attain higher multiples as its operational track record becomes more established in our view.

Figure 26: Mcap weighted average EV/NTM EBITDA trading multiples for selected European utilities (Q1 2013–Q1 2018) *



Source: Bloomberg, EY analysis. * The valuations analysis only contains pure-play publicly listed companies in each relevant market segment

Figure 27: Adjusted market capitalization weighted EBITDA CAGR for selected European utilities *



Source: Bloomberg Finance L.P. via EY analysis. * Historic EBITDA CAGR: five-year (Q1 2013–Q1 2018) compound annual growth rate (CAGR) of select utilities' market capitalization weighted adjusted EBITDA

The most relevant domestic transaction in the sector remains Zorlu Enerji's acquisition of the Osmangazi DisCo in January 2017 for USD360mn, which implies an EV/RAB (2018E) of 2.0x based on our calculations.

It is worth noting that the implied EV based on our valuation for Enerjisa (in USD terms) is visibly lower than the cumulative acquisition price of USD4.2bn for the assets (AYEDAS: USD1.2bn (July 2013), Baskent EDAS: USD1.2bn (July 2008) and Toroslar: USD1.7bn (September 2013). This is mainly due to the significant depreciation of the TRY vs. the USD since then and relatively heightened appetite for the distribution assets at the time; that had led to more demanding valuations at their prospective privatizations, in our view.

Our estimates are close to that of the consensus (Bloomberg). Our inclusion of a potential Competition Authority fine in our 2018 estimates and higher tax rate assumption (32% in 2018E and 2019E) appears to be the main reason for the deviation of our net income estimates from consensus.

Figure 28: YKY Research estimates vs. consensus (Bloomberg) for Enerjisa

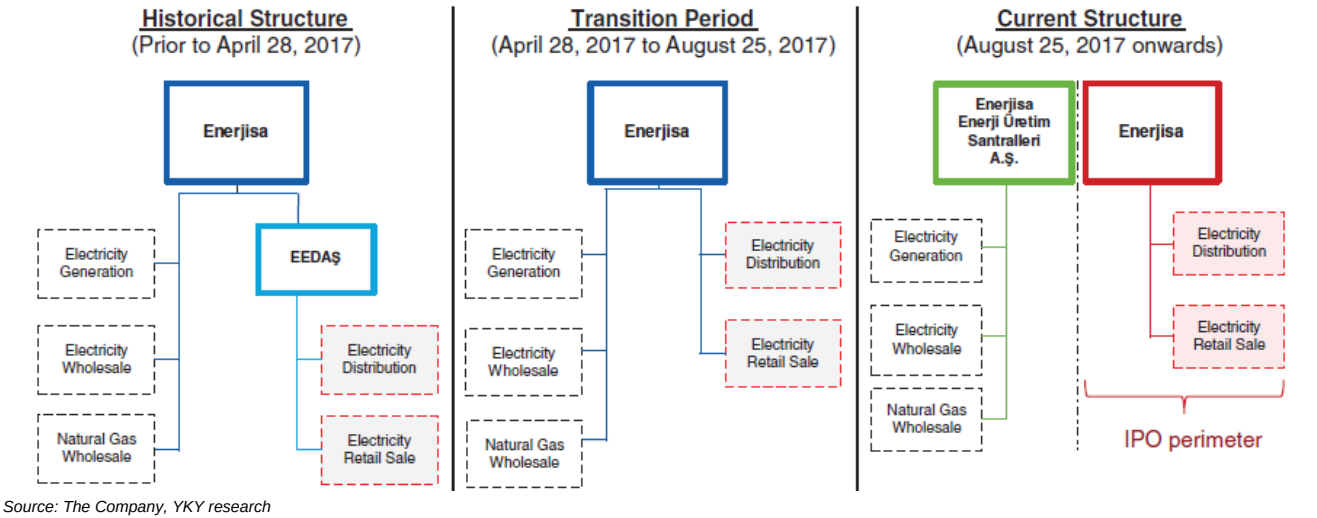
	2018E			2019E		
	YKY	Cons.	Diff., %	YKY	Cons.	Diff., %
Revenues	14,168	13,935	2%	16,205	15,842	2%
EBITDA	2,720	2,690	1%	3,079	3,068	0%
EBITDA M., %	19.2%	19.3%	-0.1 pps	19.0%	19.4%	-0.4 pps
Net Income	728	790	-8%	857	986	-13%

Source: YKY Research Estimates, Bloomberg Finance L.P.

Company Background

Enerjisa, the leading electricity distribution (26% market share) and retail (22% market share) company in Turkey has been founded in 1996; primarily as an electricity generation business. The Company has acquired the Baskent electricity distribution region in 2009; followed by the acquisition of Ayedaş and Toroslar regions in 2013. Earlier in 2013; E.ON had replaced Verbund as Sabanci Holding's partner in the Company.

Figure 29: Evolution of Enerjisa's corporate structure progression



Enerjisa's generation and wholesale businesses were spun off from the distribution and retail businesses in 2017. Enerjisa, as the distribution and retail company; had been IPO'ed in February, 2018 on BIST.

Figure 30: Enerjisa's distribution network layout



While distribution business revenues are primarily TRY-denominated; the underlying inflation pass-through mechanism offers a natural hedge against the prospect of sticky inflation in our view and protective of the business' real returns. This should be supportive of the returns on Enerjisa's RAB (TRY5.3bn as of 2017), which we expect to increase to c.TRY9.6bn in 2020E.

The combined distribution network positions Enerjisa as the largest grid operator in Turkey, serving a population of 20.6m with 44.2TWh of electricity distribution in 2017.

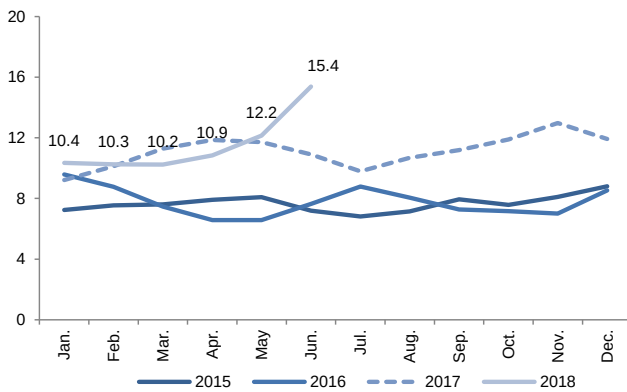
Figure 31: Summary of Enerjisa' distribution network

	2014	2015	2016
Regulated Asset Base (TRYm)	1,435	2,662	3,914
Baskent EDAS	844	1,353	1,830
AYEDAS	192	491	732
Toroslar EDAS	399	818	1,352
Length of distribution network (km)	207,106	211,378	213,918
Baskent EDAS	106,330	107,837	107,111
AYEDAS	20,790	21,535	22,740
Toroslar EDAS	79,986	82,006	84,067
Population (m)	19.9	20.3	20.6
Baskent EDAS	7.0	7.1	7.2
AYEDAS	5.0	5.2	5.2
Toroslar EDAS	7.9	8.0	8.2
Distribution connection points (m)	9.9	10.2	10.5
Baskent EDAS	3.8	4.0	4.1
AYEDAS	2.6	2.7	2.8
Toroslar EDAS	3.4	3.6	3.7
Electricity Distributed (TWh) (Gross)	40.2	42.3	43.5
Baskent EDAS	14.3	15.0	15.3
AYEDAS	11.1	11.6	11.9
Toroslar EDAS	14.9	15.7	16.3
Electricity Distributed (TWh) (Net)	36.4	38.5	39.7
Baskent EDAS	10.3	10.8	11.1
AYEDAS	12.9	13.8	14.3
Toroslar EDAS	13.2	13.9	14.3
Transformer Centers	55,698	76,232	77,502
Baskent EDAS	11,014	29,267	28,670
AYEDAS	6,508	6,707	7,084
Toroslar EDAS	38,176	40,258	41,748
Total transformer capacity (' 000 MVAR)	30,450	32,501	32,639
Baskent EDAS	12,232	13,156	11,877
AYEDAS	7,016	7,323	7,806
Toroslar EDAS	11,202	12,022	12,956

Source: The Company, YKY Research

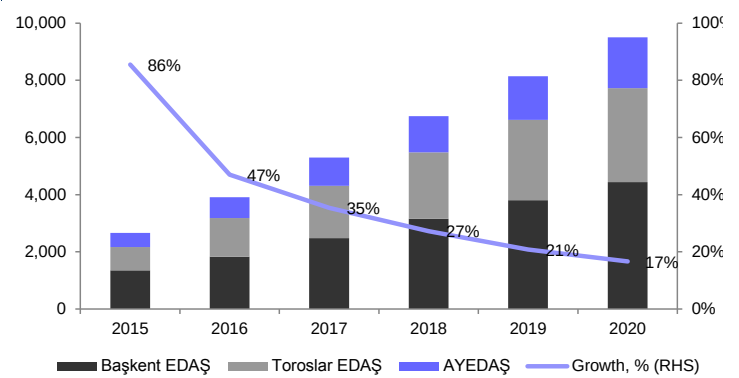
While the distribution business revenues are primarily TRY-based; the underlying CPI pass-through mechanism offers a natural hedge against the prospect of upside risks to inflation in our view and protective of the business' real returns.

Figure 32: Change in CPI (%)



Source: Turkstat

Figure 33: ENJSA's RAB progression (TRYm) and growth (%)



Source: Company financials, YKY Research

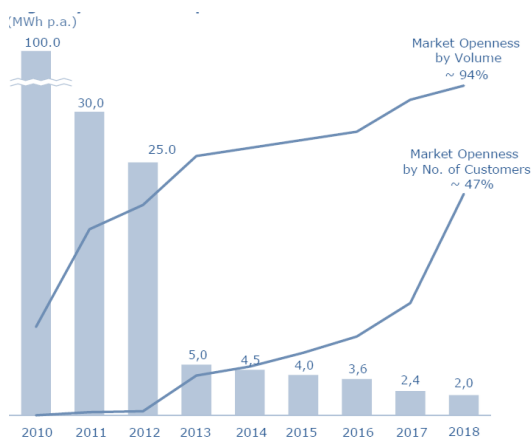
Key charts on regulatory background

Figure 34: Comparison of Western Europe and Turkey's electricity distribution regulation

		Western Europe	vs.	Turkey
Key Features of Distribution Infrastructure	RAB Growth	Low		High
	Connections Growth	Low		High
	Demand Growth	Low		High
	Level of Interruptions	Low		High
	Dispersion in Performance by Concessionaires	Low		High
Regulation Approach	Regulatory Period Length	4-8 years		5 years
	RAB-Based	✓		✓
	Capex Reimbursement Accounting	In EBITDA		Regulatory: in EBITDA IFRS: in Cash Flow Statement
	Capex Reimbursement Period	30-45 years		10 years
	Outperformance Incentives	✓		✓

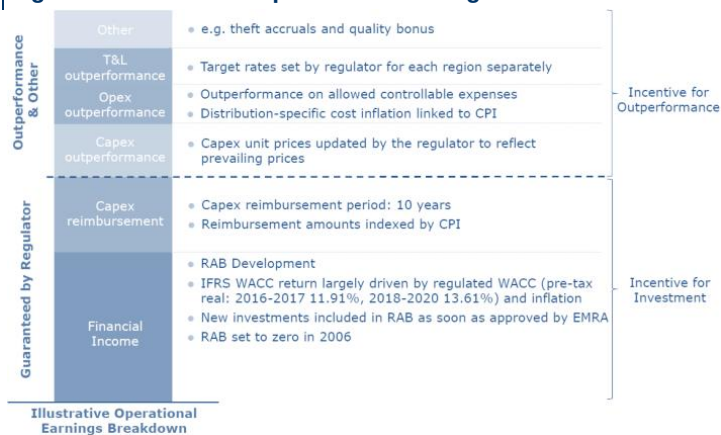
Source: The Company Regulatory Bodies, Moody's™, Regulated Electric and Gas Networks – EMEA™ reports dated November 2016 and June 2017.

Figure 36: Eligibility Limit Development (by consumption limit)



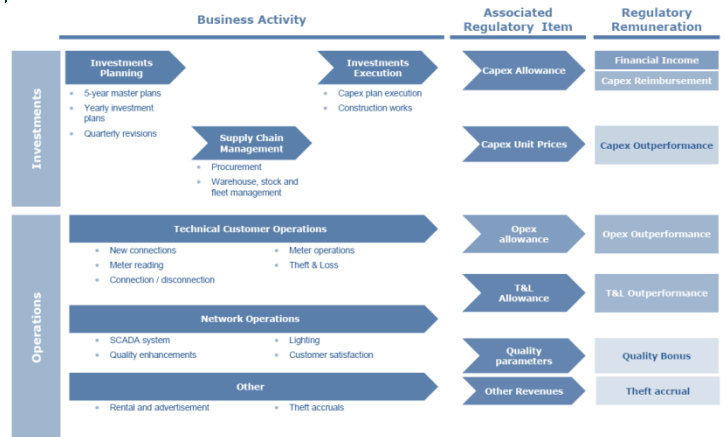
Source: The Company

Figure 38: Illustrative operational earnings breakdown



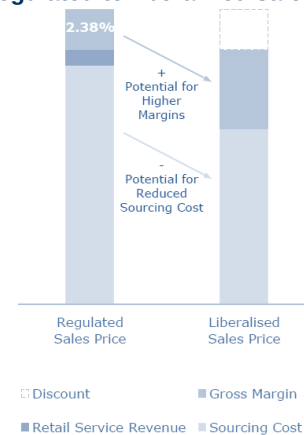
Source: The Company,

Figure 35: Scope of Distribution Business



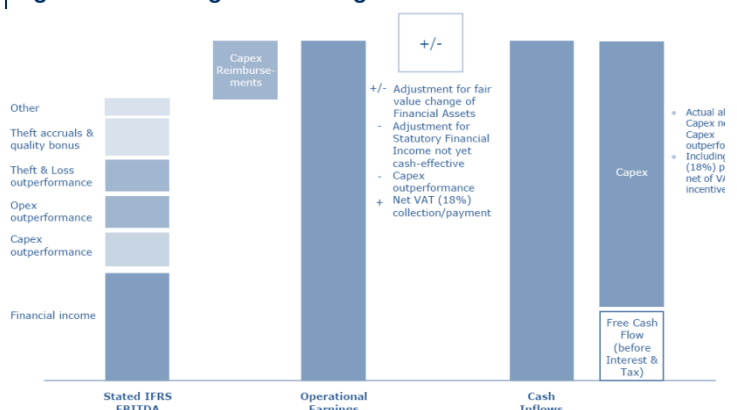
Source: The Company

Figure 37: Illustrative profitability structure in retail segment transition from regulated to liberalized sales



Source: The Company

Figure 39: Earnings and cash generation in IFRS



Source: The Company

1Q18 Review & 2Q18 Preview

1Q18 Review: In its 1Q18 results; Enerjisa reported revenues of TRY4,070mn (up 49% YoY, up 8% QoQ); EBITDA of TRY671mn (up 42% YoY, down 37% QoQ), operational earnings (EBITDA + CAPEX reimbursements excluding exceptional items) of TRY867mn (up 68% YoY) and net income of TRY243mn (vs. TRY78mn in 1Q17, down 55% QoQ). There is no consensus or in-house estimate for the 1Q18 results. Enerjisa's 1Q operating performance has been primarily driven by the improvement in financial income (booked under operational earnings) at its distribution segment led by **1)** 38% YoY increase at its RAB to TRY5.8bn **2)** higher real regulated distribution WACC revision to 13.61% (from 11.91%) coupled with a 33% YoY increase in CAPEX reimbursement alongside efficiency gains and regulatory outperformance items. Normalization in its sourcing costs at the retail segment; which had been hurt by higher costs in 1Q17; has also been supportive of the results. Revenue growth has been led by the retail segment which registered a 51% YoY growth at its gross revenues (pre-elimination) to TRY3.76bn; with the distribution segment gross revenues (pre-elimination) growing by 23% YoY to TRY1.28bn. Retail segment's pre-elimination EBIT was realized at TRY95m in 1Q18 (vs. TRY1m in 1Q17), led by improvement in sourcing costs, with the distribution segment's pre-elimination EBIT, registered at TRY576m (up 40% YoY; 86% of total pre-elimination EBIT), primarily led higher RAB, WACC, and other allowances.

Figure 40: Segmental Breakdown of Enerjisa's 1Q18 results

1Q18 Segmental Breakdown (TRYm)

	Distribution	Retail	Unclassified	Elimination	Total
Revenues	1,283	3,763	6	-981	4,070
COGS	-423	-3,598	0	976	-3,046
Gross Profit	860	164	6	-5	1,025
Opex	-284	-70	-68	6	-415
Other Expenses	-2	-12	0	-1	-14
EBIT (IFRS)	574	83	-62	0	595
EBIT (YKI)	576	95	-62	1	610
Financial income	1	65	51	-85	32
Financial expense	-220	-1	-160	85	-296
PBT	356	147	-171	0	332
Tax Expense	-7	-2			-9
Deferred Tax Expense	-62	-28	10		-80
PAT	286	118	-161	0	243

YoY, Change	Distribution	Retail	Unclassified	Elimination	Total
Revenues	23%	51%	n.m.	20%	49%
COGS	13%	49%	-100%	19%	55%
Gross Profit	28%	99%	n.m.	n.m.	36%
Opex	22%	20%	29%	82%	22%
Other Expenses	-93%	-52%	n.m.	-78%	-75%
EBIT (IFRS)	40%	n.m.	18%	n.m.	67%
EBIT (YKI)	31%	285%	18%	-78%	47%
Financial income	448%	81%	373%	114%	349%
Financial expense	54%	-68%	14%	114%	20%
PBT	33%	345%	-6%	n.m.	182%
Tax Expense	-60%	n.m.	n.m.	n.m.	-50%
Deferred Tax Expense	158%	290%	0%	n.m.	280%
PAT	27%	354%	-7%	n.m.	210%

Source: The Company, YKY research

Recall that Enerjisa' 4Q17 results have been inflated by a non-recurring change in fair value of financial assets (amongst other items); which accounts for the QoQ decline in Enerjisa's EBITDA and net income in its 1Q18 IFRS results. Enerjisa's net debt increased to TRY8.3bn as of 1Q18 (vs. TRY7.3bn in 4Q17) due to continued accelerated pace of

CAPEX and rise in its net working capital requirement in 1Q (up TRY1.2bn QoQ due to higher receivables and lower payables corresponding to a net debt to 12M trailing EBITDA stands of 2.9x as of 1Q18 (vs. 2.8x as of 4Q17). Enerjisa registered net financial expense of TRY271m in 1Q18 (vs. TRY318m in 1Q17); most of which are interest payments related to debt obligations at the distribution segment.

Figure 41: Summary KPI of Enerjisa's 1Q18 results

IFRS, TRYmn					
Income Statement	1Q18	1Q17	Chg YoY(%)	4Q17	Chg QoQ (%)
Revenues	4,070	2,726	49%	3,753	8%
COGS	-3,046	-1,971	55%	-2,275	34%
Gross Profit	1,025	755	36%	1,478	-31%
OPEX	-415	-340	22%	-483	-14%
Operating Profit	610	415	47%	995	-39%
EBITDA	671	472	42%	1,058	-37%
Other income, net	-14	-58	-75%	-40	-64%
Financial income, net	-264	-240	10%	-275	-4%
Profit Before Tax	332	117	182%	680	-51%
Minority interest	0	0	n.m.	0	n.m.
Taxes	-89	-39	127%	-146	-39%
Net Profit	243	78	210%	534	-55%
Margins(%)	1Q18	1Q17	Chg YoY(%)	4Q17	Chg QoQ (%)
Gross	25.2%	27.7%	-2.5 pp	39.4%	-14.2 pp
EBITDA	16.5%	17.3%	-0.8 pp	28.2%	-11.7 pp
Net	6.0%	2.9%	3.1 pp	14.2%	-8.3 pp
Balance Sheet	1Q18	1Q17	Chg YoY(%)	2017-12	Chg QoQ (%)
Cash and cash equivalents	79	n.a.	n.m.	173	-54%
Trade receivables	2,852	n.a.	n.m.	2,382	20%
Inventories	153	n.a.	n.m.	102	50%
LT assets	14,347	n.a.	n.m.	14,484	-1%
Total assets	18,968	n.a.	n.m.	18,586	2%
Financial debt	1,766	n.a.	n.m.	1,939	-9%
Trade payables	951	n.a.	n.m.	1,512	-37%
LT liabilities	9,028	n.a.	n.m.	7,850	15%
Equity	5,773	n.a.	n.m.	5,880	-2%
Total liabilities	18,968	n.a.	n.m.	18,586	2%

Source: The Company, YKY Research

2Q18 Preview: We expect Enerjisa to disclose its 2Q18 IFRS results on August 13; to be followed by a conference call on August 14. A YoY comparison is not applicable as the Company has started to disclose its quarterly financials in 4Q17. That said, while we believe that the results could be similar to Enerjisa's 1Q18 performance; with two one-off factors likely to distort the results. Accordingly, we expect Enerjisa to book **1)** c. TRY100m in revaluation gains (booked under headline EBITDA), and **2)** a potential Competition Authority fine under net other income. Accordingly, we expect Enerjisa to post revenues of TRY3.9bn (down 5% QoQ), EBITDA of TRY754m (up 12% QoQ), operating income of TRY849m (down 2% QoQ), and, net income of TRY141m (down 42% QoQ) and underlying net income of TRY191m (down 21% QoQ).

We expect the management to reiterate the Company's 2018 guidance of consolidated group operating earnings of TRY3.0bn to TRY3.3bn (up c. 23% YoY at mid-range, vs. YKYe: TRY3.1bn). We also expect Enerjisa to maintain its mid-term outlook which is as follows: **1)** Operational earnings: +20% CAGR between 2016-2020E, **2)** Underlying net income (excluding extraordinary items): significantly higher than 20% CAGR between 2016-2020E, **3)** dividend payout policy of 60% -70% of underlying net income, and **4)** net debt to operational earnings to be maintained below 3.5x.

APPENDIX

Figure 42: Enerjisa Enerji's distribution ops. I/S summary

	2016	2017	YoY, %
Sales Revenue	3,477	4,934	42%
Financial Income	610	1,014	66%
Distribution Revenue	2,166	3,146	45%
Pass-through transmission revenue	558	597	7%
Lighting sales revenue	143	177	24%
Cost of Sales	-1,337	-1,402	5%
Energy purchases (Lighting, T&L)	-779	-795	2%
Pass-through transmission cost	-558	-597	7%
Other	0	-10	n.m.
Gross Profit	2,140	3,532	65%
OPEX	-837	-1,072	28%
Other Income / (Expense)	-87	-143	64%
Operating profit before financial income	1,216	2,317	91%
D&A adjustment	9	16	70%
Interest income related to revenue cap regulation	-19	1	-105%
EBITDA	1,207	2,334	93%
CAPEX Reimbursements	443	592	34%
EBITDA + CAPEX Reimbursements	1,650	2,926	77%
Fair value changes of financial assets	0	-467	n.m.
Non-recurring income related to fiscal year	0	-115	n.m.
Operational Earnings	1,650	2,344	42%

Source: Company financials

Figure 43: Enerjisa Enerji's retail ops. I/S summary

	2016	2017	YoY, %
Sales Revenue	8,495	10,520	24%
Regulated	4,052	5,075	25%
Liberalised	1,587	2,256	42%
Pass-through grid revenue	2,856	3,189	12%
Cost of Sales	-8,029	-10,109	26%
Regulated	-3,739	-4,740	27%
Liberalised	-1,434	-2,180	52%
Pass-through grid cost	-2,856	-3,189	12%
Gross Profit	466	411	-12%
OPEX	-223	-253	14%
Other income / Expense	24	4	-85%
Operating profit before financial income	267	161	-40%
D&A adjustment	0	8	n.m.
TradeCo related pro-forma EBITDA adjustments	-16	0	n.m.
Adjustment related to fair value difference arising f	40	79	99%
Operational Earnings (EBITDA)	290	247	-15%

Source: Company financials

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