Enagas SA

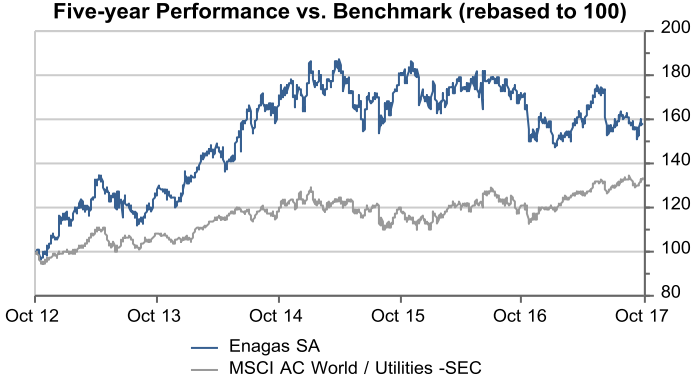
European Conviction List Member

Isin / FactSet Code	**ES0130960018 / ENG-ES**	Market cap (in EUR mn)	**5 726**	52-week high	**26.81**	Rating	**BUY**
Sector	**Utilities**	Market cap (in local curr. mn)	**5 726**	52-week low	**22.38**	12-month target price	**29.00**
Industry	**Utilities**	Local currency	**EUR**	YTD return%	**-0.37**	Last price (23/10/17)	**24.02**
Benchmark	**MSCI AC World / Utilities -SEC**	Free-float	**91%**	12-month return%	**-7.68**	Potential upside	**21%**

Investment Case:

- Enagas enjoys a six-year period (2015–20) where regulated returns will be calculated based on backward-looking nominal bond yields. Declining sovereign bond yields will have a positive impact on cost of capital. Regulated returns for Spanish utilities were set at a period when the country's 10-year sovereign bond yields were at 3.7%. These have now eased to 2.8%, offering ~6.6% real returns (including variable remuneration).
- While the Spanish capex outlook is set for a further decline (system overcapacity), Enagas pursued opportunities abroad. The group recently acquired 50% of Swedegas and increased its stake in TgP (Peru's largest gas-transmission pipeline) to 28.94%, along with a few acquisitions in Spain.
- At a FY18E P/E of 10.5x, Enagas is trading at a discount to its peers. Post its 3Q17 results, we lower our target price to EUR 29.00 (from EUR 30.00) to account for higher opex and higher non remunerated capex in Spain and potential earnings impact due to USD depreciation.

Five-year Performance vs. Benchmark (rebased to 100)



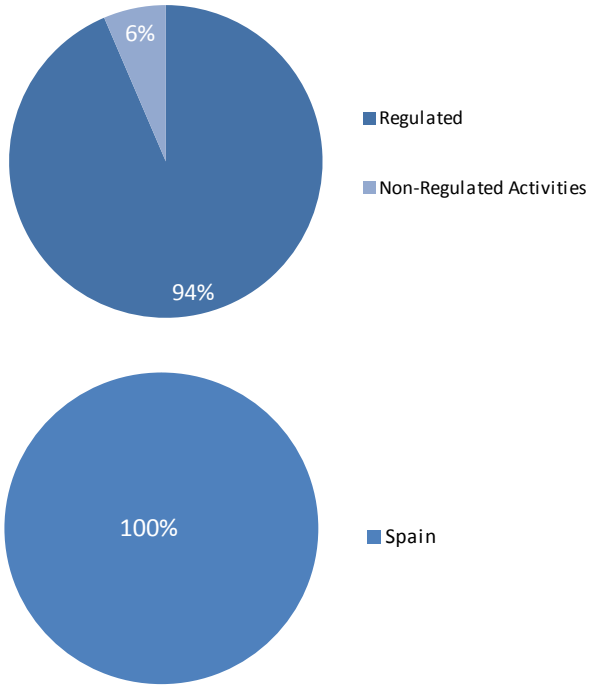
Sources: SGPB, FactSet

Company Description:

Enagas is a Spanish system technical manager engaged in the transportation and underground storage of natural gas, as well as the re-gasification of natural gas to the National Pipeline Network. The company has a resilient earnings outlook and shareholder-friendly policies in the form of growing dividends.

Revenue by Key Segments & Geographies: FY16

(FY ending December)



Sources: SGPB, FactSet

Recent Developments Analysis:

- Enagas' 3Q17 net profit of EUR 106.6 mn was largely in-line with consensus of EUR 104.4 mn. Domestic demand for natural gas rose 9.3% YoY for 9M17. Conventional demand grew 4.5%, driven by industrial demand due to a broad-based increase in demand across all industries and the addition of new customers. Further, the demand for gas in the electricity sector increased by 12.5 TWh due to lower hydroelectric and wind generation.
- Enagas' Chairman (post its discussion with secretary of state for Energy) was positive about the mid-period regulatory review in Spain as he does not expect any meaningful adjustment in the regulations to mark-to-market operating expenses (opex) and capex standards as the rise in gas demand is likely to eliminate gas deficit ahead of the planned 15-year period. We believe this is a key positive as it reduces the uncertainty about potential government intervention to lower opex and capex standards.
- Enagas currently faces a declining domestic asset base. Also, we do not expect any significant international expansion options until it recovers some of its cash (~EUR 1.0 bn) which is locked in various past setbacks (like termination of GSP concession or tariff deficit).

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DESCRIPTION			VALUATION					GROWTH				PROFITABILITY			BALANCE SHEET		
FactSet Code	Company	Cap (mn€)	EV/EBITDA (e)		P/E (e)		Div. Yield	Sales Growth		EPS Growth		EBITDA Margin	Net Margin	ROE	Net Debt/ EBITDA		Net Debt/ Equity
			FY1x	FY2x	FY1x	FY2x	FY1%	FY1%	FY2%	FY1%	FY2%	FY1%	FY1%	FY1%	FY0x	FY1x	FY0x
NG-GB	**National Grid plc**	35 694	11.1	11.0	15.9	14.9	4.9	0.5	2.7	-19.6	6.3	32.3	12.9	11.4	4.4	4.9	0.98
SRG-IT	**Snam S.p.A.**	14 548	13.1	12.9	16.0	15.3	5.2	0.1	2.2	12.4	3.5	79.1	36.6	14.0	5.4	5.7	1.70
TRN-IT	**Terna S.p.A.**	10 211	11.7	11.6	14.9	14.7	4.3	6.4	2.4	7.9	0.3	71.4	30.7	18.2	5.4	5.2	2.31
REE-ES	**Red Electrica Corp. SA**	9 807	9.7	9.5	14.6	13.9	5.1	3.3	1.7	5.3	5.6	75.8	33.2	21.3	3.4	3.3	1.75
ELI-BE	**Elia System Operator SA**	3 076	15.3	14.6	14.5	13.7	3.2	14.1	4.1	25.4	6.5	40.6	22.2	8.0	7.2	7.4	1.00
		Average:	**12.2**	**11.9**	**15.2**	**14.5**	**4.5**	**4.9**	**2.6**	**6.3**	**4.4**	**59.8**	**27.1**	**14.6**	**5.1**	**5.3**	**1.55**
ENG-ES	**Enagas SA**	5 726	10.6	10.5	12.2	13.4	6.1	11.7	-1.7	13.1	-9.9	77.7	35.4	17.3	5.8	5.1	2.11

na=Not available, nm=Not meaningful
Financial terms detailed in glossary
Sources: SGPB, FactSet

Risks To Our Investment Case:

- The uncertainty about Catalonia and potential political upheaval is a key risk. However, it is difficult to draw conclusion about the financial impact of the potential outcome in Catalonia
- Lack of development on Enagas' domestic capex or international expansion plans could have a significant negative impact on earnings growth.
- There are some concerns on Enagas' increasing investments in international operations (such as high competition for infrastructure projects and risks around operating in new markets, among others). The recent termination of GSP contract in Peru, highlights the risk in emerging market projects.

Business Quality Review:

- Enagas provided targets for 2016–20E, expecting the Spanish gas demand to increase at 2015–20E average annual growth of >3.5% and increased guidance for 2016–20E net profit average annual growth to 3–4% (from 2%).
- The company recorded EUR 5.27 bn total net financial debt (including debt of GNL Quintero) in 9M17. About 80% of Enagas' net debt was fixed rate debt. The net average financial cost of debt was at 2.8% (2.3% excluding Quintero's cost of debt) at 9M17. It has no major debt maturity till 2022.

Dividend Policy:

- The company paid a DPS of EUR 1.46 in FY16, which translates to a dividend payout of ~80%.
- Enagas also targets +5% annual dividend growth until 2020.
- In addition, there is a high visibility of expected dividends from its subsidiaries, which are either regulated assets or protected by long-term ship-or-pay contracts.
- Enagas offers FY17E dividend yield of 6.1%.

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Financial Terms And Acronyms

BV (Book Value): is the total value of net assets of a company.

BV/S (Book Value Per Share): is the total value of the net assets of a company divided by the total number of outstanding shares.

C/I (Cost Income Ratio): is used for valuing banks. It shows a company's costs in relation to its income.

CAGR (Compound Annual Growth Rate): is a term used for the geometric progression ratio that provides a constant rate of return over a specific time period.

CAPEX (Capital Expenditure): is the fund used by the company to acquire or upgrade the physical assets such as property, industrial buildings or equipment. The most capital intensive industries include oil, telecom and utilities.

CAR (Capital Adequacy Ratio): is a measure of a bank's capital. It is expressed as a percentage of a bank's risk-weighted credit exposures.

CET I (Common Equity Tier I Ratio) : is a measure of the bank's common equity capital as a percentage of risk-weighted assets. It is generally compared to a defined benchmark stipulated by the regulatory authority to determine whether a bank is sufficiently capitalised.

COMBINED RATIO: It represents the total of acquisition and administrative expenses, and claims and insurance benefits incurred, divided by net premiums earned.

DIVIDEND PER SHARE (DPS): Dividend per share or DPS (total dividend paid out divided by the total number of shares) expressed as a percentage of current stock price.

EBIT (Earnings Before Interest and Taxes): profit before taking into account interest payments and income taxes.

EBIT Margin: Ratio that expresses EBIT as a percentage of total sales (EBIT/Sales*100)

EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortisation): profit before taking into account interest payments, income taxes and non-cash operating expenses (depreciation and amortisation).

EPS (Earnings Per Share): is the division of total net profit by the number of shares.

EQUITY is the difference between the value of the assets and the cost of the liabilities.

EV (Enterprise Value) is a measure of a company's value, often used as an alternative to straightforward market capitalisation. It is calculated as (market cap + debt + minority interest + preferred shares) − total cash − cash equivalents.

FCF (Free Cash Flow): represents the difference between operating cash flow and capital expenditures.

FFO (Funds from Operations): measures a REIT's operating performance. It is net income plus gains (minus losses) from property sale and purchase. FFO per share is often used in place of earnings per share when analysing REITs.

FY0: Realised year, **FY1**: Current unrealised year, **FY2**: next year, **FY17E:** Fiscal year 2017 estimation

GOODWILL: is an intangible asset that arises as a result of the acquisition of one company by another company for a premium value.

GROSS INCOME: gross profit calculated as a company's total sales minus its cost of goods sold (COGS) that corresponds to labour and production costs.

GROSS MARGIN: expresses gross income as a percentage of total sales.

LIKE FOR LIKE (LFL) GROWTH: is a measure of growth in sales, adjusted for new or divested businesses.

Loan-to-deposit (L/D) ratio: Loans/Deposits. This helps in assessing a bank's liquidity, lending capacity and balance sheet quality.

LTV (Loan-To-Value Ratio): is a financial term used to express the ratio of a loan to the value of an asset purchased.

NAV (Net Asset Value): is similar to book value and is also called per investment unit. NAV is the marked-to-market value of the company's property investments less liabilities.

ND (Net Debt): is calculated as a company's total debt minus cash and other similar liquid assets.

NET MARGIN: is a financial ratio which measures the profitability of the net income of a company.

NI (Net Income or Bottom Line): represents a company's total earnings (or profit) which is calculated by adjusting revenues for the costs, depreciation, interest, taxes and other expenses.

NIM: Net Interest Margin

NON-PERFORMING LOANS (NPL) RATIO: NPLs/Loans. This indicates the percentage of the loans that are non-performing or are in stressed segments.

OPERATING MARGIN: See definition of EBIT Margin.

ORGANIC GROWTH: is the growth rate that a company can achieve by increasing its output and enhancing sales, excluding any profits or growth from takeovers or M&A activities.

P/E or PER (Price Earnings Ratio): reflects the trading price of a share in relation to the expected earnings.

P/BV (Price To Book Value): expresses the share price with regard to the accounting value of the company.

PAYOUT RATIO: is the proportion of earnings paid out as dividends to shareholders and typically expressed as a percentage.

PROFIT WARNING: is the announcement made by the company before its earnings release indicating the investors that its earnings would not meet the analysts' expectations.

RWA (Risk Weighted Assets): is a measure of the bank's assets, weighted according to their risk. It involves the risk weighting of both on and off-balance-sheet exposures.

REVENUE GROWTH: Illustrates the growth of sales over a given period.

ROA (Return on assets): a financial ratio that is calculated as net income divided by total assets and shows how profitable a company is relative to its total assets.

ROC (Return on invested capital): a profitability ratio which is calculated as net income minus dividends divided by total invested capital.

ROE (Return On Equity): The amount of net income returned as a percentage of shareholders' equity. Return on equity measures a corporation's profitability by disclosing how much profit a company generates with the money shareholders have invested.

TBV (Tangible Book Value): is the book value excluding intangible assets.

TBV/S (Tangible Book Value Per Share): allows to estimate the accounting value of a company by measuring its stockholders' equity per share. Formula: Re-valued Net Assets/Total Shares of Company.

WACC (Weighted Average Cost of Capital): also referred to as the firm's cost of capital, it is the rate that a company is expected to pay on an average to all its security holders to finance its assets.

WORKING CAPITAL: is the difference between a company's current assets and current liabilities and shows whether the company has sufficient short-term assets to cover its short-term debts.

Appendix

Investment Rating Definitions:

Buy Stock that is expected to outperform its MSCI sector index over a 12-month investment horizon.

Neutral Stock that is expected to perform in line with its MSCI sector index over a 12-month investment horizon.

Sell Stock that is expected to underperform its MSCI sector index over a 12-month investment horizon.

Restricted Covered stock that is not rated or assigned a target price as the Societe Generale group has a capital market transaction with that company.

Termination Stock is subject to be deleted from the SGPB recommended universe and will no longer be followed. In this case, a coverage termination alert is issued.

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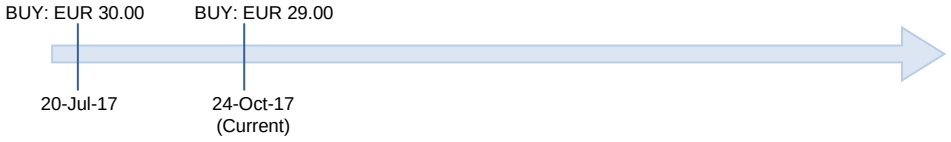
Product Risk Rating:

The product category of single equity, stock, share is rated at '4'.

In order to draw the attention of potential investors to the risk linked to each investment solution, Societe Generale Private Banking has ranked each product according to its own specific risk scale from the lowest risk (class 0) to the highest risk (class 4). The risk classification in 5 levels, is a Societe Generale Private Banking internal risk indicator. These internal indicators are based on the Value at Risk 95% 1 year (VaR). The VaR corresponds to the maximum amount that the portfolio being considered could lose in normal market conditions over a given period with a given probability (past performances and simulations of performance shall not be considered as a reliable indicator of future performance). If the VaR 95% 1 year is y%, this means that there is a 95% probability that the portfolio will not lose more than y% of its value in one year.

Risk Levels	Losses
0 - Lowest Risk	There is a 95% probability that the product will not depreciate in value in one year.
1 - Low Risk	There is a 95% probability that the product will not lose more than 5% of its value in one year.
2 - Medium Risk	There is a 95% probability that the product will not lose more than 15% of its value in one year.
3 - High Risk	There is a 95% probability that the product will not lose more than 30% of its value in one year.
4 - Highest Risk	There is a minimum of 5% probability that the product will lose more than 30% of its value in one year.

1Y Target Price:



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SG acted as joint bookrunner in SNAM's bond issue (EUR, 4yr).

SG has been mandated by SNAM as dealer manager in their tender offer on the following notes: XS1061410962, XS1126183760, XS1318709497, XS0806449814, XS0853682069, XS0914294979, XS0829190585, XS1019326641 and as joint bookrunner in their new bond issue (10y EUR, RegS).

SG acted as joint bookrunner in Terna's bond issue (EUR, Senior, RegS, 12yr)

SG acted as Passive Bookrunner on Enagas Bond isuue (EUR 10y)

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Risk Classification:

R0: Lowest Risk
R1: Low Risk
R2: Medium Risk
R3: High Risk
R4: Highest Risk

These internal indicators are based on the Value at Risk 95% 1 year (VaR). The VaR corresponds to the maximum amount that the portfolio being considered could lose in normal market conditions over a given period with a given probability (past performances and simulations of performance shall not be considered as a reliable indicator of future performance). If the VaR 95% 1 year is y%, this means that there is a 95% probability that the portfolio will not lose more than y% of its value in one year.

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