

## Renewables: going green will get profitable

- **Current global energy mix (80% fossil fuels) unsustainable; renewables could remove major shortcomings of current system**
- **Key drivers for renewables: increasing returns, energy independence, job creation**
- **EU member states to invest EUR 1,100bn in new renewables capacity; bond investors could tap a new market that offers stable, safe yields**
- **Top picks: Andritz as leading supplier of hydro power technology, Verbund as strong hydro energy play, CEZ due to expected recovery of electricity prices**

Human economic development is closely tied to humanity's ability to replace human power with other sorts of power and global per capita GDP growth took off as soon as humans extensively utilized fossil fuels. Recent developments, however, with prices for major primary energy sources going from boom to bust and significant supply disruptions due to political issues, have revealed the weakness of the current energy system the world economy relies on. Erste Group analysts think renewable sources of energy could remove the shortcomings of the current system: renewables generate no additional CO2 emissions; hydro, wind and solar power are unlimited in their supply; technological progress reduces costs for renewable energy and nearly every region on earth is well suited for at least one renewable energy source, biomass, hydro, wind, geothermal or solar power.

But can renewable energy sources like solar, wind and hydro power cover the global demand for energy? Gerald Walek, Equity research analyst at Erste Group, thinks the answer is a resounding yes. *"So far, we lack the technologies to economically harvest this potential, but we believe several economic and political considerations will support the development of renewables in future: 1) replacement of imported fossil fuels with energy from renewables creates jobs; 2) the recent gas row between Russia, Ukraine and the EU has reminded politicians of the importance of energy independence; 3) rising R&D spending will lead to declining costs for renewables",* says Walek.

### **EU member states to invest EUR 1,100bn in new renewables capacity**

Erste Group analysts say that due to the potential to create new sustainable jobs, especially in Europe and North America, **renewables could play a major role in government support to fight the economic crisis and in turn drive energy independence.** They estimate that, in order to reach the 20% renewables target, EU member states will have to invest the amount of EUR 1,100bn in new renewables capacity. They believe that, if EU governments were to create the right framework (including feed-in tariff - guaranteeing investors a stable return, forcing utilities and clients to purchase renewables electricity gradually lowering feed-in tariffs - forcing industry to cut costs and improve efficiency), then it should be possible to mobilize the capital required.

Under these circumstances, **bond investors can tap a new market that offers stable, safe yields** - an attribute that is highly favored in the current turbulent markets.

**Recommendation and target price overview:**

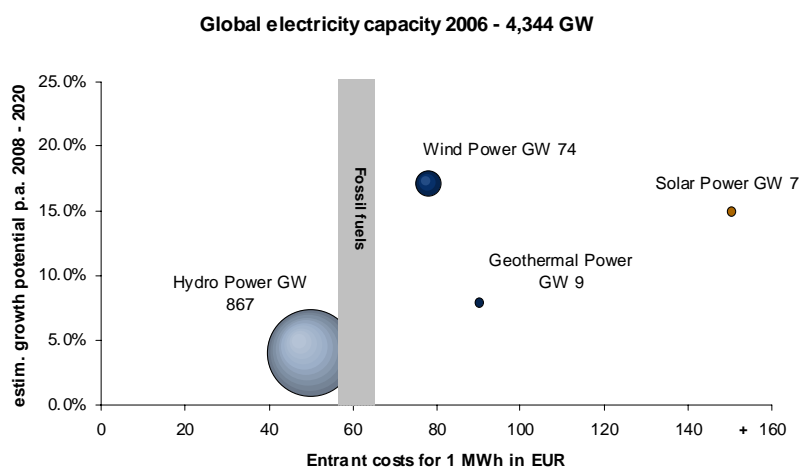
30.01.2009 Company	Rep. Curr.	Mcap (EURmn)	Price		Recommendation	Performance in %			
			Current (LC)	Target		1M	3M	6M	12M
Agrana	EUR	642	45,2	44,0	Hold	8,6%	-7,1%	-21,1%	-42,6%
Andritz	EUR	1.198	23,3	37,0	Buy	0,6%	-13,9%	-46,9%	-42,0%
A-TEC	EUR	162	6,15	6,2	Hold	-23,4%	-50,3%	-50,3%	-67,6%
CEZ	CK	14.573	753,5	1230,0	Buy	5,7%	-14,1%	-40,5%	-35,2%
EVN	EUR	1.982	12,12	18,9	Buy	8,4%	-18,9%	-37,4%	-50,0%
PannErgy	HUF	49	700	793,0	Hold	-4,7%	-13,1%	-42,8%	-55,1%
Polish Energy Partners	PLN	404	21,47	n.r.	n.r.	13,8%	-19,6%	-18,9%	-27,1%
Verbund	EUR	9.237	29,97	43,0	Buy	-1,0%	-23,5%	-42,7%	-38,0%

Source: Erste Group estimates, Prices as of Jan. 30, 2009

- **Agrana** built the first industrial-scale bioethanol production facility in Austria with a capacity of up to 240,000m<sup>3</sup> a year at a total investment volume of EUR 125mn. Revenues should reach at least EUR 100mn from the bioethanol sales this fiscal year. **Hold**.
- **Buy** recommendation for **Andritz**. Andritz is a leading supplier (world no. 2) of hydro power technology. Due to its high order backlog (EUR 4.5bn) and rising sales exposure to the renewables industry (around 50% for 2009e), we believe that Andritz is in a good position to weather the storm.
- **Hold** recommendation for **A-TEC**. Via its plant construction division, A-TEC has interesting exposure to the waste to energy market. Additionally, the machine tools division supplies the wind turbine industry with specialized machinery.
- **Buy** for **CEZ**. Despite the decreasing CO2 permit price, CEZ is also now considering a move into the renewable generation segment; wind power could gain some 3% in its product portfolio. Given the fact that CEZ already sold 75% of its installed capacity for 2009, the negative impact of the current situation will be visible only in 2010, as contracts will mainly be traded and sold during this year.
- **EVN** currently operates 68 hydropower plants, 63 windmills and 44 biomass heating plants. In addition, the company will complete the refurbishing of 11 small-scale hydropower plants in Macedonia and is further screening the potential for wind and photovoltaic projects in SEE. By 2009, EVN envisages 30% share of renewable energy in overall production by 2010. **Buy**.
- **Hold** confirmed on **PannErgy**, which has successfully engaged in two heating plant development projects. The company has now contracted with 30 towns for geothermal energy cooperation.
- **Polish Energy Partners (PEP)** is a company specializing in the development, implementation and management of electricity and heat generation projects. In the segment of green energy, the company develops wind farm projects for sale during their first stage of development. It also builds ready-to-use wind farms in order to provide electricity for sale.
- A new target price of EUR 43.0 and **Buy** recommendation for **Verbund**. Terminal value growth rate reduced to 2.0% (from 2.5%). However, this growth rate should still reflect the enormous investment program of Verbund (EUR 6.7bn until 2015), which will fully pay off beyond 2015.

## Excurs: Competitive position and relevance of renewables

- Electricity generated by **hydro power** is already cheaper compared to power generated with fossil fuels. On top of that, it has two major qualitative advantages: (1) it is highly predictable; (2) run-of-river plants generate electricity 24h a day. It will play an increasingly important role in the global energy mix in the near future.
- **Wind power** is already on the verge of being competitive. However, wind power has two major quality drawbacks: (1) it is unpredictable; (2) depending on the site, windmills generate electricity a maximum of 6-7h per day. While that restricts the share of wind power in an energy mix, there are cases (Denmark) where extensive use of wind power (+20%) could be proven to work.
- As of now, **solar power** is the most expensive renewable energy source. To a certain extent, solar power shares the quality issues of wind power: (1) it is unpredictable; (2) it cannot generate energy during the night, so some kind of storage medium is required.
- For the time being, **geothermal power** is also not cost competitive, but could have a bright future considering that: (1) with the use of enhanced technology, geothermal power can be used almost anywhere; (2) it can supply heat & electricity; (3) it can be used very predictably, 24h a day.



Source: Erste Group Research assuming EUR 12.1 per ton of CO<sub>2</sub>

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