Ellomay Capital

9M16 results

Short-term factors cloud results, story intact

Utilities

Despite its reported 8.9% revenue decrease in 9M16 vs 9M15, we remain convinced of Ellomay's ability to generate cash flow dependably from its solar assets in Italy and Spain to reinvest in its diverse pipeline of international power generation assets. Temporary factors – both lower solar radiation (worse weather) and lower spot prices – hit Ellomay's 9M16 results and we therefore reduce our FY16 revenue forecast by 9.7% to take account of this. However, we leave our FY17 forecasts little changed and increase our FY18 numbers on power price forecasts and currency moves. 9M16 results contained nothing to permanently unsettle investors on Ellomay and its equity story. On the contrary, there has been good progress towards the development of several Dutch waste-to-energy assets, which could meaningfully enhance Ellomay's returns.

Year end	Revenue ($m)	PBT* ($m)	EPS* ($)	DPS ($)	P/E (x)	Yield (%)
12/14	15.78	2.46	0.21	0.00	39.5	N/A
12/15	13.82	1.86	0.35	0.00	23.7	N/A
12/16e	12.81	0.64	0.08	0.23	103.7	2.8
12/17e	14.29	4.85	0.33	0.23	25.2	2.8

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

FY16 earnings reduced, but little change thereafter

We take account of temporary factors – low radiance and lower spot power prices – in reducing our FY16 forecasts. We also factor in higher expenses associated with the Manara project in arriving at our new FY16 revenue and reported EBITDA estimates, which are down 9.7% and 22.0% respectively versus our previous numbers. Our FY17 forecasts are little changed as we anticipate a return to normal levels of radiation and a recovery in spot power prices.

Optionality: Pipeline a key part of the story

While difficult to quantify and not explicitly forecast in our earnings estimates, we maintain our view that there will be significant upside in the medium term for Ellomay equity holders as management realises value from its project pipeline. Both the Manara Cliff pumped storage and the Dutch waste-to-energy (WTE) projects have been making steady progress and in December management announced that the Dutch assets have achieved financial close on its first €10m WTE project, with revenues expected as soon as 2018.

Valuation: Cost of capital rising globally

Our new sum-of-the-parts derived fair value of $10.44 offers 25.8% upside to the stock's current price. For FY17 and FY18, our earnings forecasts are either unchanged or rise slightly, but Ellomay, like most regulated utilities, suffers in a macroeconomic environment of rising inflation and steepening yield curves. Our fair value per share decline of 10% from $11.50 to $10.44 is driven by an increase in our cost of capital for the Dorad investment.

17 January 2017

Price*	**US$8.30/ NIS32.14**
Market cap	**US$90m/ NIS343m**

*Priced at 12 January 2017

NIS3.82/US$

Net debt (US$m) at 30 September 2016	31.3
Shares in issue	10.7m
Free float	31%
Code	ELLO
Primary exchange	NYSE
Secondary exchange	TASE

Share price performance

%	1m	3m	12m
Abs	19.6	(6.8)	(1.6)
Rel (local)	16.1	(10.8)	(10.9)
52-week high/low		US$9.6	US$7.0

Business description

Ellomay Capital owns an international portfolio of power generation assets comprised of solar plants in Italy and Spain and a gas-fired power plant in Israel. It operates principally in regulated markets.

Next events

FY16 results	March 2017

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Edison profile page

Short-term headwinds mask enduring returns

Ellomay's 9M/Q3 results, announced on 28 December, were hit by lower radiance levels, as well as lower spot power prices. These factors combine to reduce our FY16 EBITDA forecasts by 22% and turn our net profit forecast negative. However, our forecasts for FY17 are largely unchanged as a result of power prices improving and radiance reverting to mean. Furthermore, we have been heartened to see spot power prices in Italy and Spain recover in recent months, so we beef up our long-term power forecasts, which, together with our forecast of a strengthening euro, has the effect of increasing our FY18e EBITDA by 7.1% and EPS by 15.7%.

Exhibit 1: Earnings forecast changes

	EPS ($)			PBT ($m)			Reported EBITDA* ($m)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2016e	0.23	0.08	-65.6	3.29	0.64	-80.6	10.24	7.99	-22.0
2017e	0.32	0.33	3.1	4.72	4.85	2.8	11.25	11.32	0.7
2018e	0.38	0.44	15.7	5.60	6.46	15.3	11.43	12.24	7.1

Source: Edison Investment Research, Ellomay Capital. Note: *Reported EBITDA includes income from the Dorad gas-fired power plant in Israel, which is an associate.

FY16 revenues to be hit by a lower radiance and spot prices

Despite the fact that 9M16 results are heavily obscured by a series of non-cash items, the fact that (relatively) clean items such as revenues (-8.9% y-o-y) and EBITDA (-19.5% y-o-y) were down versus the previous year shows that conditions in 2016 have been difficult for Ellomay. Solar radiance and spot power prices, both of which are entirely beyond management's control, combined to penalise Ellomay. However, as we explain below, we view these factors as temporary and have actually increased our forecasts in FY18.

Exhibit 2: 9M16 results

9M16 vs 9M15 (as reported)	US$000s	9M15	9M16	% y-o-y
Revenues		11,613	10,574	-8.9%
Operating expenses		(1,930)	(1,858)	-3.7%
General and administrative costs		(2,735)	(3,359)	22.8%
Share of profits (losses) of equity accounted investees		1,112	1,097	-1.3%
Reported EBITDA		8,120	6,539	-19.5%
Depreciation		3,694	3,654	-1.1%
Other		60	85	41.7%
Operating profit		4,426	2,885	-34.8%
Financing income (expenses), net		940	(4,522)	
Profit before taxes		5,366	(1,637)	-130.5%
Tax		2,122	(568)	
Profit for the year		7,488	(2,205)	-129.4%
Attributable to owners of the company		7,672	(1,910)	-124.9%
Basic profit per share from continuing operations ($)		0.72	(0.18)	-125.0%
Dividend per share ($)		0.00	0.00	

Source: Edison Investment Research, Ellomay Capital

Exhibit 3 shows our power output forecast changes for Ellomay's Italian and Spanish solar assets.

Exhibit 3: Solar output forecast changes

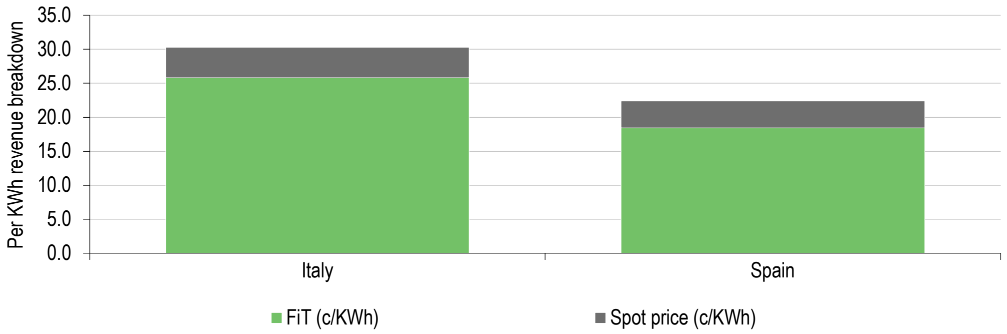
Assumptions changes	[unit]	2016e	2017e	2018e
New Italy power output	[KWh]	29,401,347	31,381,506	31,381,506
Old Italy power output	[KWh]	31,383,593	31,383,593	31,383,593
± new vs old		-6.3%	-0.0%	-0.0%
New Spain power output	[KWh]	12,045,730	12,715,876	12,715,876
Old Spain power output	[KWh]	12,736,806	12,736,806	12,736,806
± new vs old		-5.4%	-0.2%	-0.2%

Source: Edison Investment Research, Ellomay Capital

The 6.3% decrease in our FY16 forecast for Italy and 5.4% output reduction for Ellomay's four Spanish solar assets is a reflection of the weaker levels of solar radiance in southern Europe over the year. It is noteworthy that our estimates for FY17 are virtually unchanged as we forecast radiance levels to revert to mean. In other words, we view reduced output as temporary and driven by weather.

Ellomay also suffered during the first nine months due to lower spot power prices, especially in Italy where the bulk of its assets are located. According to Bloomberg, Italian spot prices averaged €0.52/KWh in the first nine months of FY15 and the equivalent figure for 9M16 was €0.38/KWh, a decrease of 36%. In Spain the figures were €0.50/KWh in 9M15 and €0.34/KWh in 9M16. However, spot prices in Italy have recovered to €0.60/KWh and Spanish prices have rallied to €0.66/KWh. Indeed, we have upgraded our spot price forecasts in the coming years to reflect the improved fundamentals in both power markets as the oil price recovers. More important, however, as Exhibit 4 shows, is that Ellomay's revenues per KWh of output are predominantly fixed due to feed-in-tariffs (fixed price subsidies). Therefore, unlike traditional merchant generators, Ellomay has minimal commodity exposure. We calculate that a €0.05/KWh increase in spot prices, in both Italy and Spain, increases Ellomay's reported EBITDA by c €250k, or 2%.

Exhibit 4: Ellomay FY16e per KWh revenue breakdown (feed-in-tariff vs spot price)



Source: Edison Investment Research, Ellomay Capital

…but the story remains intact (and cash generation is strong)

Despite weather and commodity headwinds in FY16, we believe Ellomay's model is robust. Our forecasts for FY17 are virtually unchanged and for FY18 are actually higher than our previous estimates. For its core solar operating assets, the equity story remains the same: long-term, highly dependable and visible cash flows that will be reinvested in further power generation assets internationally. Dorad also continues to perform in line with expectations. We maintain our forecasts for Dorad as before and view the fact that its regulated tariff was reduced by less than 0.5% as a positive factor. Finally, cash generation in the first nine months of 2016 was strong, with the repayment of a loan from Dorad benefiting Ellomay to the tune of $7.8m. Its conservative balance sheet and liquid cash put Ellomay in a strong position for future investments.

Manara Cliff, and now Dutch waste-to-energy, offer upside

As discussed in our initiation, a key tenet of Ellomay's equity proposition is optionality. Manara Cliff, a 340MW pumped storage project 75% owned by Ellomay, is a good example of the company's project pipeline. Given management's extensive experience in power investing and finance more generally, we believe in Ellomay's ability to source, assess and deliver future projects. We await further news on the progress of the Manara Cliff project.

A further example of Ellomay's project pipeline is in the Netherlands. First announced in August, the Dutch waste-to-energy joint venture, in partnership with Ludan, moved closer in December with the announcement that financial close had been achieved on the first of its planned plants in the Netherlands. This first plant is small in a group context (perhaps contributing €400,000 in free cash flow by 2018), but the opportunity is significant, with Ellomay stating that the JV could construct several additional plants in the years ahead. The first plant will require approximately €10m of upfront capex split 60/40 debt to equity with financing from Rabobank secured. The total potential capex across all proposed WTE plants is c €200m. At this scale, the Dutch WTE plants would meaningfully enhance Ellomay's equity proposition. We do not have enough detail, nor do we know about the accounting treatment for the plants, so we do not include explicit forecasts for these assets. However, we will revisit our estimates once we understand more about the projects.

Financials and forecasts

The new operating, commodity and currency assumptions outlined above have the effect of reducing our forecasts for Ellomay's profitability in FY16 and increasing it by FY18. We have reduced our EBITDA (Ellomay definition) estimate for FY16 by 22.0%, increased it by 0.7% for FY17 and our FY18 estimate is 7.1% above our previous forecast for the same year. Cash flow was strong over the half, with a large loan repayment from Dorad contributing $7.8m and thus our FY16 net debt forecast is reduced by 24.2% versus our previous forecast.

Exhibit 5: Detailed forecast changes

US$000s	2015	2016e	2017e	2018e
New revenues	13,817	12,811	14,293	15,134
Old revenues	13,817	14,185	14,318	14,318
± new vs old		-9.7%	-0.2%	5.7%
New EBITDA (company definition)	9,685	7,990	11,323	12,244
Old EBITDA (company definition)	9,685	10,242	11,248	11,433
± new vs old		-22.0%	0.7%	7.1%
New equity investments	2,446	2,488	2,871	3,174
Old equity investments	2,446	2,488	2,855	3,188
± new vs old		0.0%	0.6%	-0.4%
New EBITDA (Edison definition)	7,218	5,502	8,451	9,070
Old EBITDA (Edison definition)	7,218	7,754	8,393	8,245
± new vs old		-29.0%	0.7%	10.0%
New operating profit	4,773	3,204	7,187	8,325
Old operating profit	4,773	5,855	7,090	7,492
± new vs old		-45.3%	1.4%	11.1%
New profit for the year	7,298	(605)	3,561	4,750
Old profit for the year	7,298	2,416	3,466	4,114
± new vs old		-125.0%	2.7%	15.5%
New reported basic EPS (c)	0.70	(0.06)	0.33	0.44
Old reported basic EPS (c)	0.70	0.23	0.32	0.38
± new vs old		-125.0%	2.7%	15.5%
New EPS (Edison definition) (c)	0.35	0.08	0.33	0.44
Old EPS (Edison definition) (c)	0.35	0.22	0.32	0.38
± new vs old		-64.7%	2.7%	15.5%
New net debt	33,636	23,846	20,562	15,066
Old net debt	33,636	31,454	27,203	21,885
± new vs old		-24.2%	-24.4%	-31.2%

Source: Edison Investment Research, Ellomay Capital

Valuation: Rising cost of capital nudges fair value downwards

Our sum-of-the-parts derived valuation implies a fair value per share of $10.44 (from $11.50/share), which offers equity holders a total return (including a 2.7% dividend yield) of 28.5%. We derive our fair value for Ellomay's solar assets in Italy and Spain via an average value based on 10x FY17e EBITDA, a DCF (WACC 5.7%) and a per KW multiple of $3,500. This implies an EV below our last published fair value and the change is mainly due to a higher WACC for Dorad – 8.0% versus 7.5%. – which reflects rising benchmark yields globally.

Exhibit 6: Ellomay sum-of-the-parts valuation

Segment	Note	EV (US$000s)
Solar Operations	Blended: 10x FY17e EBITDA, DCF (WACC 5.7%), $3,500/KWh installed capacity	94,050
Dorad Investment	DCF (WACC 8.0%, terminal growth 1%)	51,463
Group enterprise value		145,513
Less: FY15 net debt		33,636
Less: pensions and other		0
SOP valuation		111,877
Current number of shares (m)		10.7
Current price (US$/share)		8.30
Fair value per share (US$)		10.44
Upside/(downside) to FV (%)		25.8%
Dividend yield (%)		2.7%
Total return (%)		28.5%

Source: Edison Investment Research, Ellomay Capital. Note: Priced as at 12 January 2017.

Exhibit 7: Financial summary

US$000s	2013	2014	2015	2016e	2017e	2018e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue	12,982	15,782	13,817	12,811	14,293	15,134
EBITDA (company definition)	16,807	15,694	9,685	7,990	11,323	12,244
EBITDA (Edison definition, excluding associates)	7,152	8,442	7,218	5,502	8,451	9,070
Operating Profit (before amort. and except.)	3,131	2,990	2,306	715	4,316	5,150
Intangible Amortisation	0	0	0	0	0	0
Exceptionals	10,195	5,433	21	0	0	0
Other	1,543	(1,048)	3,485	(1,458)	0	0
Operating Profit	14,869	7,375	5,812	(743)	4,316	5,150
Net Interest	(3,997)	(2,347)	(2,893)	(2,568)	(2,342)	(1,863)
Share of assocs/JVs gains/(losses)	(540)	1,819	2,446	2,488	2,871	3,174
Forex gains/(losses	0	0	0	0	0	0
Other	0	0	0	0	0	0
Profit Before Tax (norm)	(1,406)	2,462	1,859	635	4,845	6,462
Profit Before Tax (FRS 3)	10,332	6,847	5,365	(823)	4,845	6,462
Tax	(245)	(201)	1,933	218	(1,284)	(1,712)
Profit After Tax (norm)	(1,651)	2,261	3,792	853	3,561	4,750
Profit After Tax (FRS 3)	10,068	6,658	7,553	(605)	3,561	4,750
Average Number of Shares Outstanding (m)	10.7	10.7	10.7	10.7	10.7	10.7
EPS - normalised ($)	(0.15)	0.21	0.35	0.08	0.33	0.44
EPS - normalised and fully diluted ($)	(0.15)	0.21	0.35	0.08	0.33	0.44
EPS - (IFRS) ($)	0.94	0.62	0.70	(0.06)	0.33	0.44
Dividend per share ($)	0.00	0.00	0.00	0.23	0.23	0.23
EBITDA Margin (%)	55.1	53.5	52.2	42.9	59.1	59.9
Operating Margin (before GW and except.) (%)	24.1	18.9	16.7	5.6	30.2	34.0
BALANCE SHEET						
Fixed Assets	124,395	129,273	126,814	115,536	114,522	114,026
Intangible Assets	0	0	0	0	0	0
Tangible Assets	93,671	93,513	78,975	74,439	70,553	66,884
Investments	24,601	27,237	33,970	28,686	31,557	34,732
Other	6,123	8,523	13,869	12,411	12,411	12,411
Current Assets	22,535	29,814	33,513	41,702	40,866	41,863
Stocks	0	0	0	0	0	0
Debtors	4,491	6,143	8,218	7,617	8,497	8,997
Cash	7,238	15,758	18,717	27,507	25,791	26,287
Other	10,806	7,913	6,578	6,578	6,578	6,578
Current Liabilities	(26,919)	(10,924)	(10,103)	(10,041)	(9,721)	(9,708)
Creditors	(7,465)	(5,363)	(4,092)	(4,030)	(3,710)	(3,697)
Short term borrowings	(19,454)	(5,561)	(6,011)	(6,011)	(6,011)	(6,011)
Other	0	0	0	0	0	0
Long Term Liabilities	(20,250)	(54,037)	(56,159)	(55,159)	(50,159)	(45,159)
Long term borrowings	(11,050)	(44,081)	(48,117)	(47,117)	(42,117)	(37,117)
Other long term liabilities	(9,200)	(9,956)	(8,042)	(8,042)	(8,042)	(8,042)
Net Assets	99,761	94,126	94,065	92,037	95,508	101,021
CASH FLOW						
Operating Cash Flow	8,390	7,317	9,989	6,041	7,250	8,558
Net Interest	(1,788)	(3,721)	(2,904)	(2,568)	(2,342)	(1,863)
Tax	(213)	(260)	(2,174)	218	(1,284)	(1,712)
Capex	(9,152)	(709)	0	(250)	(250)	(250)
Acquisitions/disposals	(30,742)	(13,126)	0	0	0	0
Equity financing	0	0	0	7,772	0	0
Financing	0	0	0	0	0	0
Dividends	0	0	0	(2,411)	(2,411)	(2,411)
Other	(2,885)	(2,230)	(4,485)	2,488	2,871	3,174
Net Cash Flow	(36,390)	(12,729)	426	11,290	3,834	5,496
Opening net debt/(cash)	(12,960)	23,892	32,932	33,636	23,846	20,562
HP finance leases initiated	0	0	0	0	0	0
Other	462	(3,689)	(461)	1,500	550	0
Closing net debt/(cash)	23,892	32,932	33,636	23,846	20,562	15,066

Source: Edison Investment Research, Ellomay Capital