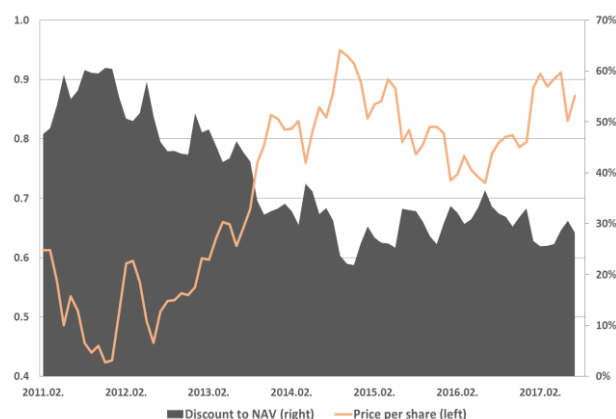
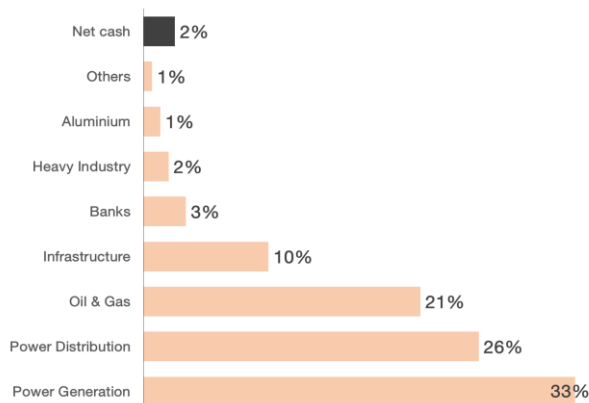


Fondul Proprietatea

Overweight (unch.)

Target price (e-o-2017): RON 1.00 (prev. RON 0.95)



Share price close as of 14/08/2017	RON 0.87	Bloomberg	FP RO
Market cap. [RON mn/EUR mn]	7,692/1,672	Reuters	FP.BX
Daily turnover 12M [EUR million]	1.6	52 week range	RON 0.68-0.92

Successful Electrica deal entails special dividend

Equity Analyst

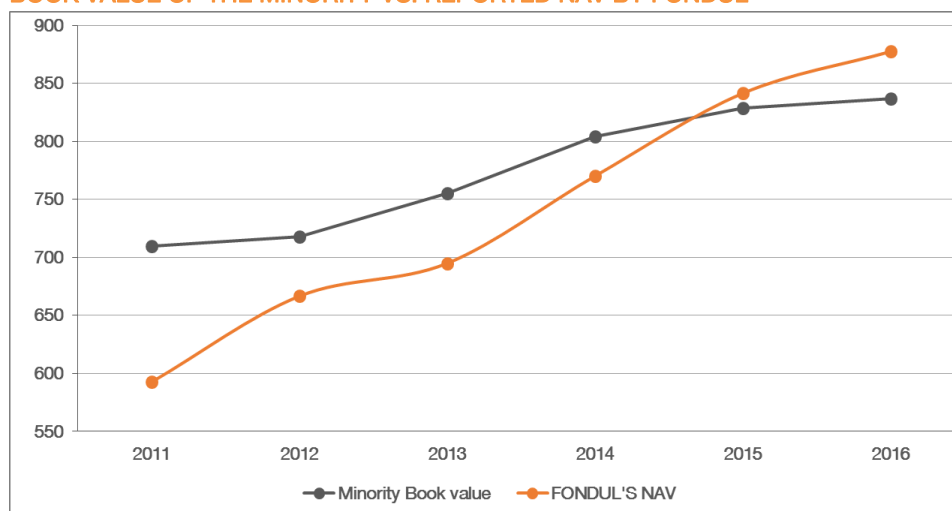
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- **Investment story:** Despite the strong ytd price increase we maintain our positive view on Fondul, since 1.) we wait for the regular and additional special dividends, 2.) furthermore the buy-back gives a protection against country and regulatory risks 3.) Hidroelectrica IPO might be in 2018 H2 and Electrica transaction at the end of this year 4.) Romanian GDP growth rate was 4.8% in 2016 and we believe that this year's growth will be around 4-5%, 5.) government passed a memorandum to request the SOEs to pay-out 90% of the 2016 profits 6.) last but not least MSCI watchlist inclusion will come soon after Fondul sells another Petrom stake after the lock-up ends in October.
- **Second quarter's results:** Fondul reached 0.09 RON EPS in the first half year of 2017 three times higher than the EPS was in H1 past year. Cash level went down to 2% after the dividend was paid, while the portion of listed companies was only 28% as of July. No major revaluations regarding the fair value of the unlisted portfolio.
- **Dividend income:** Gross dividend income reached RON 540 million or RON 0.06 per share 0.01 higher than the regular dividend. Major portion of the dividend income related to Hidroelectrica (RON 206 million vs. RON 134 million past year), but the increase was related to OMV Petrom (RON 106.8 million vs. zero), Bucharest Airport paid (RON 43.0 million vs. RON 27 million past year).
- **Net unrealised gain from equity investments** at fair value through profit or loss was RON 159 million mainly generated by OMV Petrom, as a result of the positive evolution of the share price (8.6% during H1 2017).
- **Management fee** was RON 54 million or 0.5% of NAV in H1 2017 vs. RON 36 million or 0.3% of NAV past year. The higher distribution fee compared to the same period of the previous year was due to the fees charged for the distributions made available to the Fund's shareholders, respectively through the tender offer within the 7th buy-back programme, finalised on 20 March 2017 and the return of capital in March 2017 of RON 0.05 per share for which the payment started on 27 March 2017.

- **Recommendation:** We have increased our end of the year ex-div target price to RON 1.00 per share, due to the possible Electrica transaction, which might trigger an ENEL deal later. We wish to highlight that the buy-back program and special dividends gives also additional upsides. We remain Overweight in case of Fondul.
- **Electrica:** As Fondul reported in March 2017 that they have ongoing discussions with the management of Electrica about the minority stakes in the subsidiaries (8% of NAV). Electrica went public in 2014 with a visionary CAPEX plan and above average Regulated rate of return (8.52%), however wind has changed and the fix return rate was cut to 7.7% and the CAPEX pipeline was also drastically reduced. Despite these negative impacts the company's earnings improved thus it was rational to give an offer for the minority stake if the management believe in the future of the business. At the end of 2016 Electrica had more than RON 2.7 billion cash on its balance sheet, which is equal to ca. RON 8 per share or 60% of the market capitalization calculated with the current share price. As we highlighted several times, Electrica destroys shareholder value sitting on that great amount of cash, thus a quick and mutually beneficial deal is more than necessary for Electrica as well to show some positive development to the disappointed shareholders. The four assets have a non-core status in Fondul's portfolio, thus they are available for sale for a fair price. But the deal is more important currently for Electrica since the subsidiaries were paying stable and significant dividend in the past years, roughly RON 100 per year.
- 2016 was not a strong year for Electrica as earnings declined by 18% y-o-y on average basis except Furnizare, which increased to RON 185 million from RON 151 million during the year. Between 2011 and 2014 the book value of the minority in Electrica's balance sheet had a higher value than the NAV in Fund's portfolio, but in the past two years this has changed.

BOOK VALUE OF THE MINORITY VS. REPORTED NAV BY FONDUL

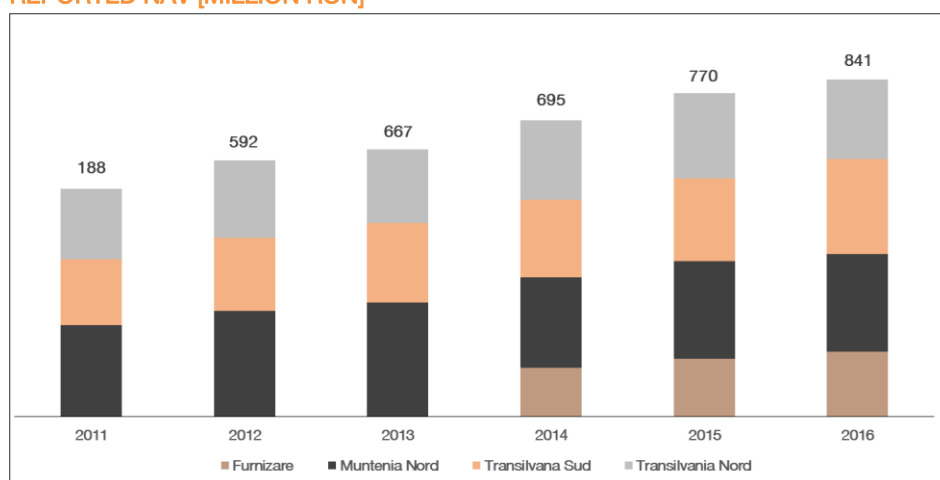


Sources: Fondul and Electrica

- Despondently, in the past year Fondul could not strike a deal with Electrica, mainly due to the different valuation assumptions. In March 2016 Fondul asked RON 805 million, and offered to pay back RON 36 million received as dividends from the subsidiaries, hence the net cash value of the ask side was RON 769 million (EV/EBITDA: 3.3x, P/RAB: 0.8x). The spread between the bid and ask was around RON 85 million, which was approximately 10% of the transaction value, and roughly equals to the dividend, which was paid that year.
- Early May 2016 Fondul informed its shareholders that it has initiated a competitive process leading to potential disposals of the Fund's holdings in Electrica subsidiaries. The marketing and sale process will be managed by Ithuba Capital AG, acting as sole financial advisor in connection with the envisaged transaction.

- In July 2016 the Fund reported that Fund has signed a Memorandum of Understanding (MOU) with Electrica for the disposal of the Fund's holdings in Electrica subsidiaries. The aggregated value of the transaction would amount to RON 752 million. Shares would be acquired by Electrica together with all the rights attached to them under the applicable law, including the right to receive dividends, except for those for the financial year ending on 31 December 2016, which remain to be collected by the Fund. The parties plan to execute the transactional documents pertaining to the envisaged transaction after obtaining the necessary corporate and shareholding approvals at Electrica and Subsidiaries level, by 31 October 2017.
- The transaction still needs the greenlight from Electrica's shareholders meeting but both the management team of Fondul and Electrica have disclosed having agreed to the MOU. The transaction is a clean win-win for both parties. Electrica would start to create shareholder value on that part of the cash, buying the minority stake vs. short term government bond yielding below 0.7%. Electrica will increase its profit after minorities by roughly 30% and pay more dividend from the core operation to the shareholders, while the huge CAPEX plans is more rational after the purchase of the minority.
- It is also an important and positive news for Fondul since 1.) the company receive RON 752 million cash, which is equal to RON 0.07 per share thus we assume the Fund will pay special dividend this year like in past year (RON 0.05 per share) 2.) the holding discount will narrow since the Fund is to sell 8.2% of its NAV and 12% of its unlisted holdings 3.) the unlisted portion of the portfolio increased and reached 70% in the past quarter, which is a significant threshold for the portfolio manager, but with this transaction the unlisted portion will decline to 64%, thus it is most likely that the Fund will be able to sell another Petrom stake after this transaction and lock-up of past ABB.
- **Transaction pricing:** Pricing of the 22% in Electrica's three distribution companies and the remaining subsidiary seems to be tough for the first blink since the NAV in July 2017 was at RON 877 million, while the transaction value was set significantly below at RON 752 million. However the transaction value is net of dividend, which was RON 98 million thus the exit price including the dividends was RON 850 million resulting 4% discount compared to the NAV. The value of the transaction was priced at 3.6x EV/EBITDA and 0.85x P/RAB. All in all, we assume the transaction is a win-win for the two listed companies and spice up the investment cases. After a successful E.ON and Electrica deal we might be closer to see an ENEL one.

REPORTED NAV [MILLION RON]



Sources: Fondul Proprietatea

TOP EQUITY HOLDINGS [RON MILLION]

	FY 2015	Q1 2016	H2 2016	9M 2016	FY 2016	Q1 2017	H2 2017
OMV Petrom	3,120	2,582	2,582	2,625	1,858	2,153	2,018
Romgaz	613	608	0	0	0	0	0
BRD	307	266	249	279	301	313	342
Banca Transilvania	234	234	12	12	21	18	0
Nuclearelectrica	176	146	138	135	132	184	175
Alro	96	86	75	89	85	106	123
Conpet	40	46	39	40	41	59	50
Hidroelectrica	2,654	2,654	2,654	3,269	3,384	3,384	3,384
Bucharest Airport	498	498	633	633	761	761	761
Engie Romania	446	446	446	446	453	453	453
ENEL	1,621	1,481	1,621	1,621	1,575	1,575	1,575
ELECTRICA	841	841	841	841	877	877	877
Salrom	177	177	177	177	181	181	181
Top 20	11,434	10,832	10,364	10,448	9,908	10,305	10,201
% of total equity	97%	96%	99%	98%	99%	99%	99%
Total equity Holdings	11,841	11,247	10,521	10,621	10,034	10,428	10,308
Net cash	247	194	1,284	736	1,394	262	262
NAV	12,088	11,440	11,805	11,357	11,427	10,690	10,570
NAV per share	1.16	1.10	1.14	1.17	1.19	1.19	1.22
Price per share	0.81	0.77	0.73	0.80	0.80	0.90	0.87
Discount to NAV	-30%	-30%	-37%	-31%	-33%	-25%	-28%

PROFIT AND LOSS [RON MILLION]

	FY 2015	Q1 2016	H2 2016	9M 2016	FY 2016	Q1 2017	H2 2017
Gross dividend	569	0	347	351	353	0	540
Net losses	-1241	-536	-541	-499	-378	296	159
Impairment losses	-91	-30	-41	-43	-122	19	21
Interest income	4	1	3	4	8	6	7
Gain on disposal	345	0	913	926	926	6	0
Other items	19	2	20	22	-110	-4	39
NOI	-394	-563	701	761	677	323	766
OPEX	-125	-19	-56	-90	-132	-40	-66
Finance costs	-3	0	0	0	0	0	0
Tax expense	-44	-4	-104	-101	-97	10	9
Net profit	-565	-586	541	571	447	293	709
Other income	212	-31	-189	-154	101	75	107
Adj. profit	-353	-617	352	417	548	368	816
EPS	-0.03	-0.06	0.03	0.04	0.06	0.04	0.09

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