

# Kazakhmys Plc (KAZ.L)

## Alert: Power Play? Implied Value of The Copper Rump

**Dilutive deal...** – As highlighted in our note yesterday ([Power Disposal Sensitivities](#)) we value KAZ's 50% stake in the Ekibastuz power business at \$2.2-2.7bn. As such media reports of a \$1.6bn valuation for the assets would appear dilutive on our numbers.

**Copper rump not cheap** – The key question for investors is what the implied market valuation of the remaining copper business is assuming a divestment is completed. Based on a valuation range of \$1.6-2.7bn (EV basis) we calculate the PE range of the copper assets at 6.4-9.2x. Copper equities have traditionally traded around 10x 1-year forward PE, so on this basis the copper assets appear fairly priced by the market in our view. We would expect a discount to peers based on the lower quality nature of KAZ's asset base and lack of growth. Indeed with Freeport (FCX.N; US\$35.69; 2) currently trading on 7.4x, the top end of our valuation range suggests the assets appear relatively expensive.

**How much debt?** – Our PE range is based on an assumption that any consideration payable would be on an EV basis, including debt. We attribute \$1bn of debt to the assets (c.60% of the group total) on the basis that the \$1bn capex programme at Ekibastuz (80% spent) has been 100% debt financed. We also assume residual carrying debt of \$200m. We adjust copper EBITDA for the business's elevated sustaining capex of c.\$500mpa to generate an underlying earnings number. This makes the underlying net income number more similar to cash flow and thus the range of 6.4-9.2x PE can also be interpreted as a 7-10 year cash payback period for an investor in KAZ post any power disposal.

Figure 1. Market Implied PE of KAZ Copper assets: power valuation scenarios

### Inputs

ENRC mcap	\$m	7,500
KAZ Share of ENRC (26%)	\$m	1,950
KAZ mcap	\$m	6,100
KAZ ex-ENRC	\$m	4,150

### Parameters

EV of power assets	\$m	1,600	2,200	2,700
Assumed Debt	\$m	1,000	1,000	1,000
Equity value of power	\$m	600	1,200	1,700

### PE of Copper

Implied equity value of copper assets	\$m	3,550	2,950	2,450
Headline copper EBITDA	\$m	1,000	1,000	1,000
Underlying EBITDA (ex sustaining capex)	\$m	500	500	500
Underlying Net Income	\$m	385	385	385
Implied PE of copper assets		9.2	7.7	6.4

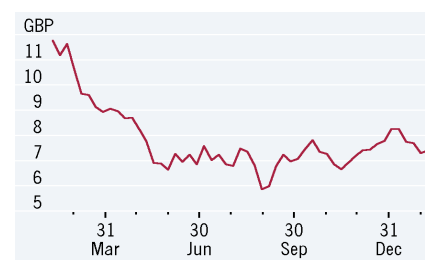
Source: Bloomberg, Citi Research

### Company Update

<b>Neutral</b>	<b>2</b>
Price (08 Feb 13)	£7.49
Target price	£8.20
Expected share price return	9.5%
Expected dividend yield	2.0%
<b>Expected total return</b>	<b>11.5%</b>
Market Cap	£3,923M
	US\$6,165M

### Price Performance

(RIC: KAZ.L, BB: KAZ LN)



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## Kazakhmys Plc

### Valuation

We have a target price of £8.2 on Kazakhmys. Our target price is based on a blend of NPV and earnings-based multiples (2013E EV/EBITDA and FCF yield). We derive a DCF value of £8.8 (based on a DR of 14%, terminal growth of 2% ). We calculate £8.7/share from a SOTP EV/EBITDA valuation and £7.2/share from free cash flow analysis, which are equally weighted with our DCF valuation to arrive at our target price.

### Risks

Adverse movements in the copper price away from our forecasts could see a significant delta in our forecasts from actual profits, both positively and negatively. The company conducts the bulk of its business in Kazakhstan and geopolitical risks could cause the share price to deviate significantly from our target price. If the impact on the company from any of these factors proves to be more or less negative than we anticipate, the stock could have difficulty achieving or exceed our financial and price targets.

## Appendix A-1

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Analyst: Michael E Flitton

Covered since January 21 2013



Date	Rating	Target Price	Closing Price
1 31-Mar-10	2M	*16.10	15.27
2 25-Jun-10	2M	*13.00	10.67
3 28-Oct-10	*1M	*15.30	13.26
4 7-Nov-10	1M	*16.00	14.97
5 29-Jun-11	*1H	*15.50	13.50
6 7-Oct-11	Stock rating system changed		

Date	Rating	Target Price	Closing Price
7 7-Oct-11	*1	15.50	8.58
8 9-Jan-12	1	*15.60	9.79
9 26-Jan-12	1	*15.20	11.94
10 26-Mar-12	1	*13.00	9.25
11 16-Apr-12	1	*14.00	8.74
12 30-Apr-12	1	*12.70	8.61

Date	Rating	Target Price	Closing Price
13 16-Jul-12	1	*11.00	7.28
14 28-Aug-12	1	*9.00	6.34
15 21-Jan-13	*2	*8.40	7.80
16 31-Jan-13	2	*8.20	7.30

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

## Kazakhmys Plc (KAZ.L)

### Ratings and Target Price History

#### Best Ideas Research

#### Relative Call (3 Month)

Analyst: Michael E Flitton

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12 Month Rating			Relative Rating		
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53%	49%	45%	60%	49%	55%

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