Company report

Nat Resources & Energy
Multi-Utilities
Equity – Germany

HSBC Global Research

E.ON (EOAN GR)

Overweight

Target price (EUR)	34.00
Share price (EUR)	25.60
Potential total return (%)	32.8

Dec	2008a	2009e	2010e
HSBC EPS	3.01	2.85	2.86
HSBC PE	8.5	9.0	8.9

Performance	1M	3M	12M
Absolute (%)	-11.5	-2.4	-1.6
Relative^ (%)	-2.0	-1.5	-13.9

Note: (V) = volatile (please see disclosure appendix)

10 February 2010

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OW: Light at the end of the tunnel

- **Flat commodities and gas glut priced in; growth prospects from Russia and renewables ignored**
- **Following a year of downgrades of consensus estimates, the risk of further cuts seems modest and we expect the company to take a less bearish tone**
- **Stock still undervalued relative to its peer group: we reiterate our OW rating and EUR34 target price**

Event: With the impact of the gas over-supply in Europe, an unexciting outlook for commodity and carbon prices over the near term, the bulk of the targeted EUR10bn of cash disposals having been achieved, and encouraged by E.ON management's resolutely prudent tone, consensus estimates for 2010-11 have been steadily reduced over the last 12 months by an average of 12%, such that we believe the difficult environment in E.ON's core businesses – Central European, UK and Nordic power and Pan-European gas – are fully discounted in estimates and the share price.

Impact: We are increasingly confident that current market expectations for 2010 and 2011 can be met, assuming (as we do) that E.ON management presents a less pessimistic outlook at its 10 March presentation of the 2009 results. We are not expecting anything new to emerge regarding E.ON's traditional businesses, but believe that better confidence can lead to the market's focus switching to the reasons, ignored until now, for our OW rating: growth from Russia and renewables (1% of 2009e EBIT, 11% by 2013e), simplification and streamlining under the incoming CEO.

Valuation: We maintain our OW rating and our EUR34.0 target price. Our valuation is based on the rounded average of our sum-of-the-parts value of EUR32.0 (post 10% discount), DCF of EUR34.7 (WACC 6.5%, terminal growth rate 1%, post 10% discount), dividend discount model of EUR31.7 and peer group value of EUR36.5. Against the sector, the stock currently trades at 2010e discounts of 26% on PER and 20% on EV/EBITDA, as well as at a 6% yield premium. We think the shares should find support in the run-up to the cash payment, on 7 May, of the entire 2009 dividend; we estimate this will be flat at EUR1.5, implying a 5.9% yield.

Catalysts: E.ON could adopt a more positive tone at its 10 March 2009 presentation, given our belief that consensus fully discounts the current challenges; E.ON's new CEO Teyssens prioritises simplification and streamlining following his appointment (1 May).

Index^	DAX-100
Index level	1,698
RIC	EONGn.DE
Bloomberg	EOAN GR

Source: HSBC

Enterprise value (EURm)	80604
Free float (%)	100
Market cap (USDm)	70,026
Market cap (EURm)	51,226

Source: HSBC

Financials & valuation

Financial statements

Year to	12/2008a	12/2009e	12/2010e	12/2011e
Profit & loss summary (EURm)				
Revenue	86,753	87,847	90,538	92,707
EBITDA	13,385	13,797	14,145	14,851
Depreciation & amortisation	-3,456	-3,789	-3,999	-4,266
Operating profit/EBIT	9,929	10,008	10,146	10,585
Net interest	-539	-1,809	-1,516	-1,539
PBT	2,595	7,518	8,030	8,446
Taxation	-863	-1,804	-2,367	-2,514
Net profit	1,394	5,378	5,379	5,656
Cash flow summary (EURm)				
Cash flow from operations	6,738	10,117	10,235	10,777
Capex	-8,806	-10,000	-9,000	-8,000
Cash flow from investment	-17,078	-4,255	-7,900	-8,000
Dividends	-2,937	-2,857	-2,825	-3,009
Change in net debt	22,199	-2,402	491	232
FCF pre dividends	2,892	117	1,235	2,777
Balance sheet summary (EURm)				
Intangible fixed assets	23,915	23,915	23,915	23,915
Tangible fixed assets	56,526	57,381	61,682	65,416
Current assets	46,080	46,295	48,834	49,307
Cash & others	6,348	6,334	8,268	8,253
Total assets	157,045	158,115	164,955	169,162
Operating liabilities	41,426	41,588	42,167	42,633
Financial liabilities	41,058	38,642	41,066	41,283
Total liabilities	118,618	117,044	120,647	121,930
Net debt	29,693	27,291	27,781	28,013
Shareholders funds	34,467	36,932	40,041	42,854

Ratio, growth and per share analysis

Year to	12/2008a	12/2009e	12/2010e	12/2011e
Y-o-y % change				
Revenue	26.2	1.3	3.1	2.4
EBITDA	7.5	3.1	2.5	5.0
Operating profit	6.5	0.8	1.4	4.3
PBT	-73.2	189.7	6.8	5.2
HSBC EPS	14.8	-5.2	0.3	5.2
Ratios (%)				
ROE	13.4	15.1	14.0	13.6
ROCE	3.7	8.9	8.2	8.1
EBITDA margin	15.4	15.7	15.6	16.0
Operating profit margin	11.4	11.4	11.2	11.4
Net debt/equity	77.3	66.4	62.7	59.3
CF from operations/net debt	22.7	37.1	36.8	38.5
Per share data (EUR)				
EPS reported (fully diluted)	0.75	2.85	2.86	3.01
HSBC EPS (fully diluted)	3.01	2.85	2.86	3.01
DPS	1.50	1.50	1.60	1.75
Gross CFPS	3.77	5.40	5.46	5.74

Key forecast drivers

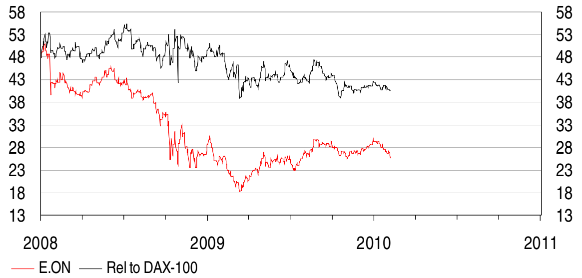
Year to	12/2008a	12/2009e	12/2010e	12/2011e
Oil (USD/b)	59	75	76	77
Coal (USD/t)	108	84	79	88
CO2 (EUR/t)	18	13	14	15
German baseload power (EUR/MWh)	71	42	45	53
LTC gas (USD / mmbtu)	8.1	9.3	8.6	10.4

Valuation data

Year to	12/2008a	12/2009e	12/2010e	12/2011e
EV/sales	1.0	0.9	0.9	0.9
EV/EBITDA	6.2	5.8	5.7	5.5
P/CF	6.8	4.7	4.7	4.5
PE*	8.5	9.0	8.9	8.5
FCF yield (pre div) (%)	5.4	0.2	2.3	5.2
Dividend yield (%)	5.9	5.9	6.3	6.8

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 05 Feb 2010

Increasing confidence

- Extent of gas squeeze understood and 2010-11 consensus estimates now sufficiently reduced
- Focus could switch to growth segments and approach of incoming CEO, although we see little near-term news-flow on disposals
- Overweight rating and EUR34 target price maintained

Introduction

Since mid-November 2009, the stock has virtually eliminated its price differential against GDF Suez (GSZ.PA, EUR26.49, Neutral), which has a similar level of earnings exposure to gas, from EUR3.0 to EUR0.5 and outperformed its energy conglomerate peers, and the sector performance (flat against MSCI Europe) has featured outperformance from the purer regulated and commodity plays. We look at factors liable to affect E.ON over the upcoming months and conclude that the stock retains an attractive valuation.

Gas contracts: some progress

At least 90% of E.ON's gas comes through long-term gas contracts, the prices of which we would estimate are determined 95% by gas oil and fuel oil and 5% by other items, in particular coal and spot gas. We expect E.ON to reduce its exposure to oil products by around 10% through:

1. not replacing long-term contracts as they expire in upcoming years
2. using renegotiating clauses contained in existing contracts to raise slightly the influence of spot gas.

In addition, we believe that E.ON may have reached agreement with some or all of its gas suppliers to allow more flexibility in making up for the breach we assume it made in 2009 of its minimum gas uptake. E.ON states in its current company presentation that renegotiation of 80% of its long-term contracts is ongoing, that 'limited extra flexibility' is being targeted, and that 'clear progress' is being made on 'constructive, long-term relationships'. In 2008, E.ON bought 28% of its gas via long-term contracts with Gazprom. Gazprom stated at its 9 February 2010 investor day that negotiations with E.ON have been completed, with a complex agreement encompassing supplies to both Germany and Hungary and no departure from either the take-or-pay principle or from the oil link in the gas pricing formula.

This is not to say that E.ON is well-placed, since it has agreed with the European Commission to concede market share in Germany by cutting the amount of capacity it has booked on Germany's import pipelines from a current share that we estimate at roughly two-thirds to a share of 54% by October 2015 (by selling capacities to interested parties on a non-discriminatory basis): the EC is now talking to E.ON's competitors with a view to making E.ON's commitments legally binding. We expect similar commitments by GDF Suez in its domestic market to the European Commission will allow both E.ON and GDF Suez to offset volume pressure at home with increased volumes in France (E.ON) and Germany (GDF Suez). Unlike E.ON, however, GDF Suez is committed to taking more gas through long-term procurement contracts over 2010-12, although GDF Suez starts from a position of slightly less dependence than E.ON on long-term contracts (and thus on prices of oil products). E.ON states in its current company presentation that its minimum take-up obligation is 'tight but manageable'. It still needs the European market, now over-supplied with LNG no longer wanted by the shale gas-rich US, to recover, which we cannot see before 2012 at the earliest and conceivably not before 2014-15. However:

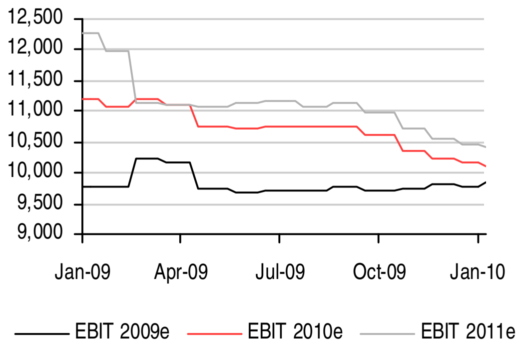
- we do not see the US exporting shale gas as LNG, at least in the foreseeable future
- we do not see shale gas making major inroads in Europe, where initial studies have put the extraction cost of shale gas well into double-digit USD/MMBtu, versus USD5/MMBtu in the US
- E.ON has gained some margin for manoeuvre through utilisation of renegotiation clauses in its long-term gas contracts
- we believe the market's understanding of E.ON's challenges in downstream non-regulated gas is now adequate, and that E.ON's communication efforts have been clear.

Market estimates for 2010-2011: for once, little downside risk

E.ON the main bear in 2009

In 2009, E.ON was rightly perceived as the most pessimistic in the utilities sector with its consistent painting of a bearish scenario. We believe E.ON's bearishness was triggered to a large extent by its view that consensus estimates were too optimistic. Although 2010 may not prove an exciting year, we believe consensus forecasts are realistic given that we expect a slight demand recovery, flattish commodity prices, the fact that virtually all this year's power output has been sold, and the fact that E.ON has no nuclear reactors risking short-term shut-down under the 32-year nuclear phase-out. At its results presentation on 10 March, therefore, our expectation is that E.ON management will set out a slightly more positive tone than that to which we have become accustomed.

Consensus EBIT for E.ON (EURm)



Source: Thomson Reuters Datastream

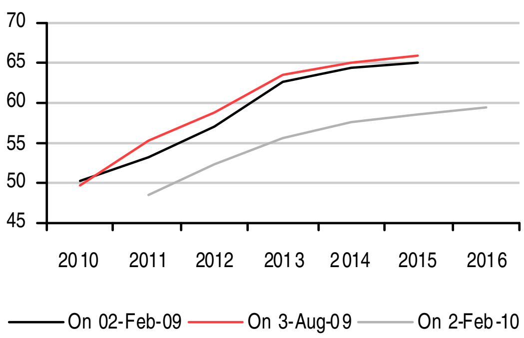
We see potential upside on Russia in particular, where demand and (especially) non-regulated prices have rebounded. In our 30 October 2009 report on E.ON, we stated that improved market grasp over gas supply and power prices could allow the focus finally to switch to areas of potential EBIT growth on which E.ON has been investing substantially – Russia and renewables.

Forward prices in 2013 and beyond: lower than market

The risk for E.ON, as well as for the commoditised utility plays, comes from changes in medium-term power prices.

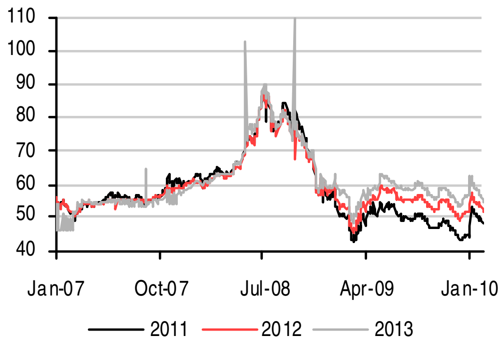
Our medium-term (ie from 2013) German base-load power price forecast is EUR60/MWh, and we believe consensus is at EUR61-62. The contango in the German baseload prices, as shown in the charts below, has narrowed by about EUR5/MWh compared to six months and a year ago, triggered by carbon weakness post-Copenhagen (December) and recent declines in oil and coal forwards. The profitability of stable-cost and carbon-free nuclear would suffer the most from a low commodity/carbon price environment. At present, 2013 forward prices are equivalent to the average achieved price of E.ON's Central European market unit in 2008, we estimate, and below that in 2009-11, we anticipate. E.ON has the benchmark balance in terms of power generation split (24% nuclear in 2008, 27% in gas, 39% in coal and lignite) and buys in roughly half of its end-demand.

Flattening German baseload forward curve (EUR/MWh)



Source: Platts

Range-bound German baseload power (EUR/MWh)



Source: Thomson Reuters Datastream

Our EUR60/MWh power price forecast retained

Our EUR60/MWh power price forecasts, which we maintain, are based on Brent around USD75/b, long-term gas at around USD10.6/MMBtu, carbon at EUR17-18/t, and spreads showing signs of upward pressure as signal for the approaching need to commit to build new capacity. Our view is not that the commodity pricing outlook is spectacularly positive, but that short-term fluctuations such as we are currently seeing should not bring fundamental valuation adjustments for E.ON and its peers.

Disposals: little of significance in the near term

E.ON's target is to achieve at least EUR10bn of cash disposals in 2009-10. Divestments completed in 2009 (Thuega and German generation, for the most part) and committed for in 2010 (municipal stakes separated from Thuega, Italian gas distribution, remaining German generation) amount to at least EUR6.5bn, we estimate.

Limited strategic value of LG&E, awaiting rate case result

Given E.ON's Europe-wide priority in all of its businesses except for renewables (which has a global remit), we believe the strategic attraction of retaining LG&E, the Kentucky-based regulated power and gas supplier inherited when E.ON bought Powergen in 2003, is limited and the mid-2009 unwinding of out-of-the-money contracts 'cleans up' LG&E's position. We believe the market would welcome a divestment of LG&E. E.ON has at no point stated that it is looking to divest LG&E.

There still remains the outcome of the 29 January 2010 filing by LG&E and its subsidiary Kentucky Utilities for USD252.5m of rate increases based on sales for the financial year ended October 2009 and effective from March 2010 (implying an average rate increase of over 11% and an 11.5%

return on equity, up from an average of below 6% in 2008-09). Given the typical process of public hearings, we would not expect a decision until around August, with new rates applicable from that time. To a large extent, the Kentucky regulator's final decisions will determine the valuation that any potential buyer might be willing to offer. It seems unrealistic to expect any offer taking place before the rate decision, if indeed LG&E is for sale.

Taking the peer group average of 6.8x 2010e EV/EBITDA (source: Bloomberg), we value LG&E at EUR4.6bn. If E.ON does sell LG&E, we do not think the market should be surprised to see earnings dilution since LG&E is a division in its own right whose EBIT is disclosed, unlike the 5GW of divested German generation, the removal of whose earnings triggered a negative share price reaction when these earnings were disclosed following the divestment.

Gazprom stake: may be linked to other agreements

If E.ON does not sell LG&E, we think it may struggle to reach its EUR10bn objective. E.ON still owns 3.5% of Gazprom (USD23.2, GAZPq.L, OW(V)) directly, currently worth EUR3.6bn (and providing E.ON with a negligible dividend income of, we estimate, EUR6m on 2009 earnings [our Gazprom ADR dividend estimate is USD0.03 for 2009]). E.ON sold down treasury stock (to Statkraft, July 2008) and an earlier near-3% indirect stake in Gazprom (final agreement announced June 2009) in return for operating assets, and the remaining Gazprom stake represents its final such financial holding of real substance. Unlike other disposals, this would not be dilutive. In our view, there is no legal obstacle to E.ON selling this stake but the company has not stated that it intends to do so. Nonetheless, given the complexity of the industrial relationship between the two companies, we believe it is possible that other agreements could be jeopardised by exiting Gazprom, such as E.ON's 25% interest in the Yuzhno-Russkoye super-giant gas field, a position agreed, after lengthy and stop-start negotiation, on 5 June 2009.

Logical to retain a balance between regulated and non-regulated in the UK?

We do not see E.ON looking to sell its UK regulated distribution activities, for which we estimate a RAV of EUR2.7bn. RWE is absent from distribution in the UK and EDF has started the process to divest its networks, although we see an increasing possibility that this process will be shelved. Although Ofgem's price controls of December 2009 were harsh, in our view, they offered incentives for efficiency gains that could well encourage E.ON to retain the business, which it has in the past stated offers a balance against more volatile generation and supply.

Valuation: OW maintained; target price of EUR34

We maintain our OW rating and target price of EUR34. Our valuation is based on the rounded average of our sum-of-the-parts value of EUR32.0 (post 10% discount), DCF of EUR34.7 (post 10% discount), dividend discount model of EUR31.7 and peer group value of EUR36.5.

Summary of E.ON valuations: EUR34.0 target price

Valuation technique	EUR
DCF, 10% discount	34.7
Sum-of-the-parts, 10% discount	32.0
Dividend discount model	31.7
Peer group comparison, at sector average	36.5
E.ON target price (rounded)	**34**

Source: HSBC estimates

DCF: remains EUR38.5, EUR34.7 after discount

Our DCF is based on a WACC of 6.5%, as calculated below.

E.ON sum-of-parts summary: EUR35.5, or EUR32.0 after 10% discount

Activity	Valuation methodology	EV EURm	EUR per share	% gross SOP
Central Europe	DCF/MW, EUR/customer	39,477	20.9	34.4%
Pan-European Gas	Upstream 7.5x EBIT, Infra at 8.0x EBIT 2010e	17,962	9.5	15.6%
UK	DCF/MW, EUR/customer	8,861	4.7	7.7%
Nordic	DCF/MW, EUR/customer	10,730	5.7	9.3%
US Mid-West	At 7.3x peer average EV/EBITDA 2010e	4,642	2.5	4.0%
Energy trading	At 0.15x External sales 2010	2,175	1.2	1.9%
New markets	DCF/MW, EUR/customer, peer multiples	14,144	7.5	12.3%
Core assets		**97,991**	**51.9**	**85.3%**
Add: Associates, long-term investments	Incl 3.5% stake in Gazprom at market	17,412	9.0	14.7%
Total assets		**114,863**	**60.9**	**100.0%**
Total debt, provisions, minorities	**End-2010 estimates**	**(47,801)**	**-25.3**	
SOP value per share - EUR		**67,062**	**35.5**	

Source: HSBC estimates

E.ON WACC calculation

Risk-free rate	4.0%
Country risk premium	4.5%
Beta	1.04
Cost of equity	**8.7%**
Gross cost of debt	5.0%
Corporate tax rate	28.0%
Cost of debt, post tax	**3.6%**
Weight of debt	44%
Weight of equity	56%
WACC, post tax	**6.5%**

Source: HSBC estimates

We continue to assume a terminal growth rate of 1%.

E.ON - DCF equity valuation: EUR38.5 (EUR34.7 post discount)

	EURm
DCF value (core operations)	**103,632**
Associates, ST marketable assets, others	16,857
EV (asset side)	**120,489**
Less: Financial net debt	(27,781)
Less: Provisions, minorities & others	(20,020)
Total non-equity claims/liabilities	**(47,801)**
Value of equity	**72,688**
Shares (m)	1,886
DCF value per share - EUR	**38.5**
DCF value per share - EUR with 10% discount	**34.7**

Source: HSBC estimates

Sum-of-parts: remains EUR35.5, EUR32.0 after discount

In our sum-of-the-parts (summarised in the table at the top of this page), we continue to assume that E.ON's nuclear reactors each obtain a 10-year extension (from the present 32-year operating life), that half of the economic benefit is taken by the government/customers, and that taxation on the additional earnings is paid in advance of the extra output such that the overall economic benefit to E.ON is negligible.

Peer group comparison: remains EUR36.5

Our peer group comparison is based on our universe of European energy utilities' combined prospective 2010e earnings multiples of 13.2x PER and 7.5x EV/EBITDA.

E.ON - peer group valuation: EUR36.5

	EUR
PER 2010e at: 13.2x	37.8
EV/EBITDA 2010e at: 7.5x	35.3
Average	**36.5**

Source: HSBC estimates

Dividend discount model: remains EUR31.7

Our DDM is based on explicit forecasts for four years (19% of valuation) with a terminal growth rate of 3% (81% of valuation).

E.ON - DDM value: EUR31.7

	EUR	Split
Explicit forecast (4 years)	5.9	19%
Terminal value (3% growth)	25.8	81%
DDM value	**31.7**	**100%**

Source: HSBC estimates

HSBC

E.ON forecasts: unchanged

(EURm)	2008a	2009e	2010e	2011e	2012e	2013e
Revenues	86,753	87,847	90,538	92,707	94,594	97,997
EBITDA	13,385	13,797	14,145	14,851	16,380	16,298
EBIT	9,878	10,008	10,146	10,585	11,914	11,632
Change y-o-y	*+7.3%*	*+0.8%*	*+1.4%*	*+4.3%*	*+12.6%*	*-2.4%*
EBIT split						
- Central Europe	4,720	4,870	5,251	5,160	5,575	5,183
- Pan-European gas	2,631	1,987	1,623	1,955	2,441	2,550
- UK	922	489	612	584	624	382
- Nordic	770	549	478	526	565	567
- US Mid-West	395	457	476	492	491	495
- Energy Trading	645	936	943	953	956	956
- New markets	90	846	949	1,106	1,458	1,698
- Corporate centre	-295	-126	-186	-191	-195	-199
Financial result	-7,293	-2,490	-2,116	-2,139	-2,078	-1,950
Pre-tax profit	2,595	7,518	8,030	8,446	9,836	9,682
Consolidated net profit	1,604	6,104	6,062	5,932	6,918	6,805
Reported group share of net profit	1,266	5,768	5,779	5,656	6,588	6,481
Adjusted net profit	5,598	5,378	5,379	5,656	6,588	6,481
Adjusted EPS (EUR)	3.01	2.85	2.86	3.01	3.50	3.45
Dividend per share (EUR)	1.50	1.50	1.60	1.75	1.90	2.00
Cash flow and balance sheet						
Operating cash flow	6,738	10,117	10,235	10,777	11,962	12,041
Net investments	-17,078	-4,255	-7,900	-8,000	-6,000	-6,000
Free cash flow (ex acquisitions/disposals)	-2,068	117	1,335	2,777	5,962	6,041
Dividends paid	-2,937	-2,837	-2,825	-3,009	-3,291	-3,573
Net debt	-29,693	-27,291	-27,781	-28,013	-25,343	-22,875
Net debt + provisions/EBITDA ('Debt factor') (x)	3.36x	3.08x	3.04x	2.91x	2.48x	2.34x
Gearing: Net debt/Equity	77.3%	66.4%	62.1%	59.3%	53.4%	46.2%
Average capital employed (EURm)	79,485	79,713	85,374	88,515	89,490	90,253
ROCE (%)	12.5%	15.1%	114.0%	13.6%	14.0%	13.6%

Source: HSBC estimates

Downside risks to our valuation and rating

- Management surprises us by maintaining its ultra-cautious outlook in its results presentation of 10 March;
- Commodity prices weaken and demand fails to recover;
- The government demands several nuclear closures in return for a nuclear extension as well as a high share of the economic benefit;
- E.ON fails to make disposals, or uses disposals proceeds to make a large acquisition at what is viewed as a high price;
- The gas market glut looks set to last longer.

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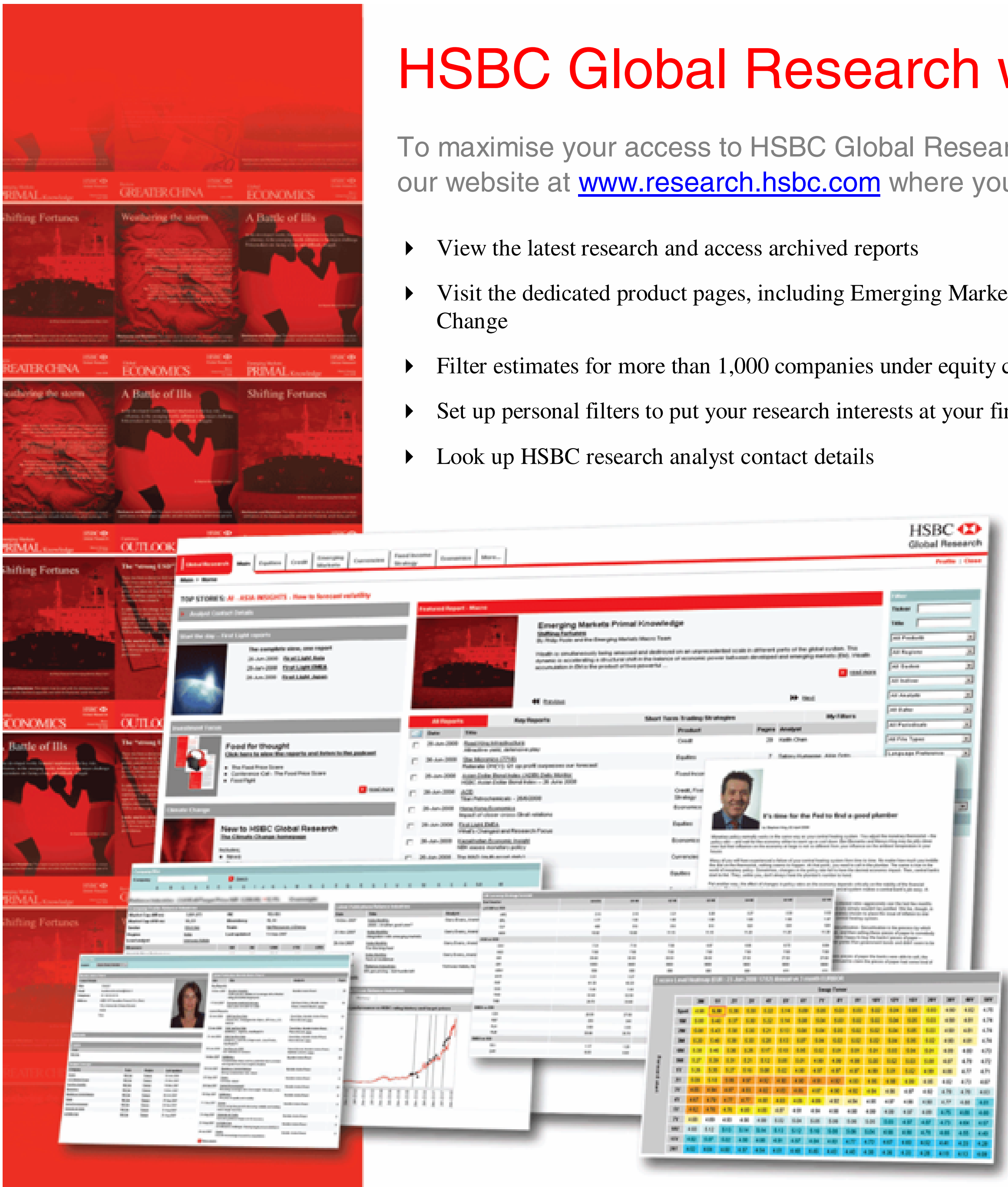

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This report addresses only the long-term investment opportunities of the companies referred to in the report. As and when HSBC publishes a short-term trading idea the stocks to which these relate are identified on the website at www.hsbcnet.com/research. Details of these short-term investment opportunities can be found under the Reports section of this website.

HSBC believes an investor's decision to buy or sell a stock should depend on individual circumstances such as the investor's existing holdings and other considerations. Different securities firms use a variety of ratings terms as well as different rating systems to describe their recommendations. Investors should carefully read the definitions of the ratings used in each research report. In addition, because research reports contain more complete information concerning the analysts' views, investors should carefully read the entire research report and should not infer its contents from the rating. In any case, ratings should not be used or relied on in isolation as investment advice.

Rating definitions for long-term investment opportunities

Stock ratings

HSBC assigns ratings to its stocks in this sector on the following basis:

For each stock we set a required rate of return calculated from the risk free rate for that stock's domestic, or as appropriate, regional market and the relevant equity risk premium established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the implied return must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

*A stock will be classified as volatile if its historical volatility has exceeded 40%, if the stock has been listed for less than 12 months (unless it is in an industry or sector where volatility is low) or if the analyst expects significant volatility. However,

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stocks which we do not consider volatile may in fact also behave in such a way. Historical volatility is defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility has to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Prior to this, from 7 June 2005 HSBC applied a ratings structure which ranked the stocks according to their notional target price vs current market price and then categorised (approximately) the top 40% as Overweight, the next 40% as Neutral and the last 20% as Underweight. The performance horizon is 2 years. The notional target price was defined as the mid-point of the analysts' valuation for a stock.

From 15 November 2004 to 7 June 2005, HSBC carried no ratings and concentrated on long-term thematic reports which identified themes and trends in industries, but did not make a conclusion as to the investment action that potential investors should take.

Prior to 15 November 2004, HSBC's ratings system was based upon a two-stage recommendation structure: a combination of the analysts' view on the stock relative to its sector and the sector call relative to the market, together giving a view on the stock relative to the market. The sector call was the responsibility of the strategy team, set in co-operation with the analysts. For other companies, HSBC showed a recommendation relative to the market. The performance horizon was 6-12 months. The target price was the level the stock should have traded at if the market accepted the analysts' view of the stock.

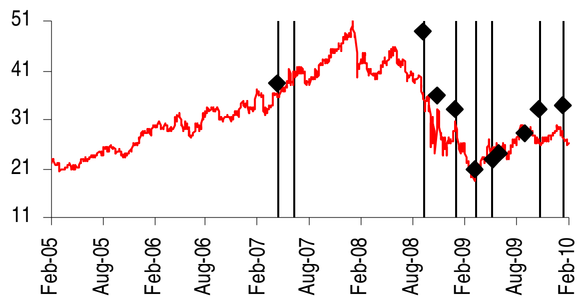
Rating distribution for long-term investment opportunities

As of 09 February 2010, the distribution of all ratings published is as follows:

Overweight (Buy)	46%	(12% of these provided with Investment Banking Services)
Neutral (Hold)	38%	(12% of these provided with Investment Banking Services)
Underweight (Sell)	16%	(11% of these provided with Investment Banking Services)

Share price and rating changes for long-term investment opportunities

E.ON (EONGn.DE) Share Price performance EUR Vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
Overweight	Neutral	17 April 2007
Neutral	N/A	11 June 2007
N/A	Overweight	16 September 2008
Overweight	Overweight (V)	05 January 2009
Overweight (V)	Neutral (V)	12 March 2009
Neutral (V)	Underweight (V)	14 May 2009
Underweight (V)	Overweight (V)	30 October 2009
Overweight (V)	Overweight	21 January 2010
Target Price	**Value**	**Date**
Price 1	38.31	17 April 2007
Price 2	N/A	11 June 2007
Price 3	49.00	16 September 2008
Price 4	36.00	31 October 2008
Price 5	33.00	05 January 2009
Price 6	21.00	12 March 2009
Price 7	23.00	14 May 2009
Price 8	24.00	05 June 2009
Price 9	28.00	10 September 2009
Price 10	33.00	30 October 2009
Price 11	34.00	21 January 2010

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
E.ON	EONGn.DE	25.95	09-Feb-2010	4, 6, 7

Source: HSBC

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