CONCORDE CAPITAL

Ukraine / Iron Ore Mining

Poltava GOK

Initiating Coverage

BUY

16 Jun 2005	**USD 6.25**
12m Target	**USD 9.00**

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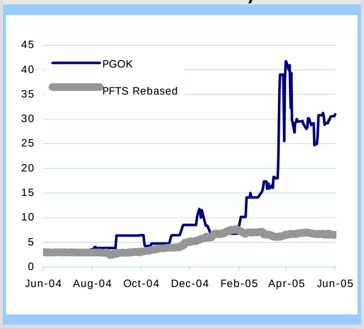
PGOK Mid-Market, UAH



Market Information	
Bloomberg	PGOK UZ
Reuters	PGOK.PFT

No of Shares, mln*	**81.6**
Reg S GDR to Ord.	**1:50**

Market price, USD	**6.25**
52Wk H/L, USD	2.00/41.75
MCap, USD mln	**510**
Free Float, %	**4%**

Stock Ownership	
Finance & Credit	77%
Dem DECOmetal	15%
Physical Persons	8%

Ratios 2004	
EBITDA Margin	17%
EBIT Margin	12%
Net Margin	3%

Net Debt/Equity	0.96

**An additional issue of 110.1 mln shares will be approved by PGOK's EGM.*

Poltava GOK (PGOK) is one of Ukraine's largest iron ore producers and will benefit from a 71% growth in global prices in 2005. The company dominates the Central and Eastern European market and its advantageous geographical location will guarantee its position in the medium-term. PGOK is in the process of increasing its capacity utilization and will boost output by 80% over the next five years. The company is an attractive acquisition target and IPO candidate next year. BUY.

The company has the same crude iron ore reserves as CVRD; greater than Rio Tinto, the world's largest iron ore producers, and is also working to make better use of its idle reserves. Last year, PGOK's growth in finished product output was limited to 5% in physical terms, due to insufficient crude ore processing capacities, which lead to an underutilization of its pellet making facilities. The problem will be solved by opening new mines and purchasing iron ore concentrate from Russian suppliers. All this will accelerate PGOK's output growth rate to 10% 2005, and will double output by 2010.

PGOK is the largest Ukrainian iron pellet producer, accounting for 45% of total domestic pellet output, and the company is the largest Ukrainian exporter of iron ore. While Ukraine exports 28% of its iron ore, PGOK delivers 90% of its output to foreign countries. The company benefits from more predictable market conditions in Central and Eastern Europe, through long-term contracts, and has ten-year agreements on iron ore prices.

PGOK's production costs are higher than its major global competitors, due to the low iron content in its ore. However, this cost is offset by its close location to its markets. As a result, transportation cost advantages effectively protect the company in CEE markets from competition by Russian, Brazilian and Australian iron ore producers and makes PGOK a major player in the region. In addition, the recent supply shortage at Magnitogorsk Iron and Steel has opened the Russian market for PGOK.

PGOK may consolidate with its affiliated trader through an IPO. Transfer pricing reduces PGOK's sales by about 30% and cuts net margins by 20%, but this effect could shrink two fold in 2006 with the anticipated IPO. The company has not been nominated as a re-privatization target, making it a very attractive asset for acquisition.

KEY FINANCIAL DATA, USD mln

	Net Revenue	EBITDA	Net Income	**DPS, USD
2004	272.7	47.1	7.2	0.014
2005E	533.6	160.1	84.5	0.016
2006E	557.4	142.1	69.4	0.026

Spot Exch Rate 5.05

***No of shares before additional shares issue is used for DPS and Div Yield calculations*

KEY RATIOS

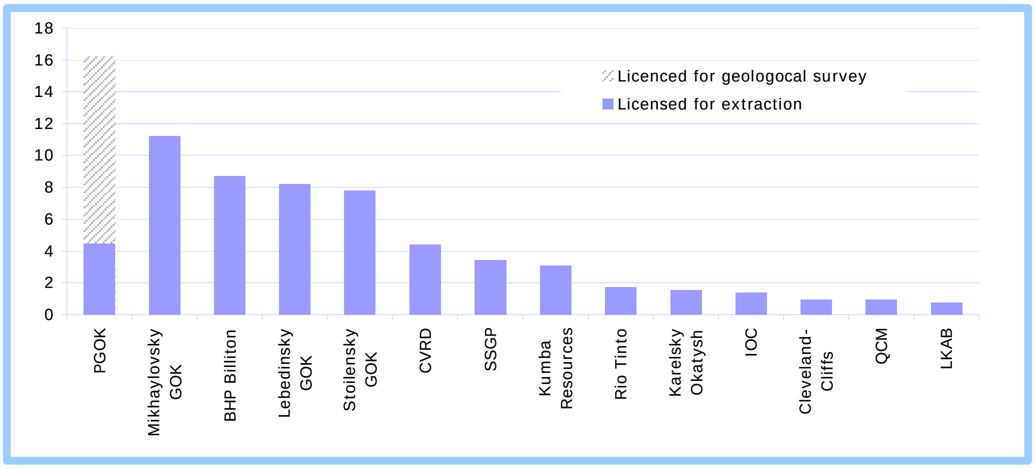
	P/S	P/E	EV/EBITDA	**Div Yield
2004	1.87	70.77	13.50	0.228%
2005E	0.96	5.99	3.78	0.248%
2006E	0.92	7.32	4.30	0.410%

Production: Capacity Utilization On The Rise

Poltava GOK (PGOK) is an iron ore enterprise with complete mining and processing facilities. The company is located in the city of Komsomolsk in the Poltava region, which borders with Dnipropetrovsk and is close to the Zaporizhya, Donetsk and Lugansk regions – the heart of Ukraine's steel production industry.

PGOK is the largest Ukrainian producer of pellets, a value-added product of high quality, manufactured from concentrate or fine ore. The material is refined from detrimental impurities in iron ore and contains additives that make it more valuable in pig iron production. One additional application of pellets is in Direct Reduced Iron and Hot Briquetted Iron production. The reduction of pellets increases the iron content from 63-65% to more than 90% to obtain direct reduced iron, a material used for steel production and bypasses the blast furnace (BF) stage.

Iron Ore Reserves by Company, bln



Source: Company Data

PGOK's current reserves amount to more than 4 bln mt of crude ore, comparable to the reserves at the world largest iron ore producers CVRD and Rio Tinto. In addition, the company has obtained geological survey licenses for four other deposits.

PGOK's Licenses for Iron Ore Extraction

Deposit	Reserves, bln mt	Start
Gorishni Plavni	1.2	Operating
Lavrivkovskoye	0.5	Operating
Yeristovo	0.9	Start in 2005
Belanovskoye	1.7	2007
Galeschina	0.3	2007
Total	**4.5**	

PGOK's Licences to conduct geological surveys

Vasilievskoye	2.8	n/a
Kharchenkovskoye	3.1	n/a
Manuilovskoye	2.8	n/a
Brovarskoye	3.0	n/a
Total	**11.8**	

Source: Company Data

The company's expected expansion into crude ore extraction is necessary, due to the fact its existing capacity is underutilized for concentrating and "pelletizing". In 2004, the problem was partially solved through the purchase of iron ore concentrate (to be further processed into pellets) from Russia's Lebedinsky GOK for ~8% of total concentrate produced at PGOK. This year PGOK will increase its share of Lebedinsky-supplied concentrate to 15%, until it can significantly expand its own capacities in 2007. Despite the expensive feedstock, a favorable market for pellets means the purchase is economically justifiable. Below we show our gross margin estimates based on transfer prices to their trading company.

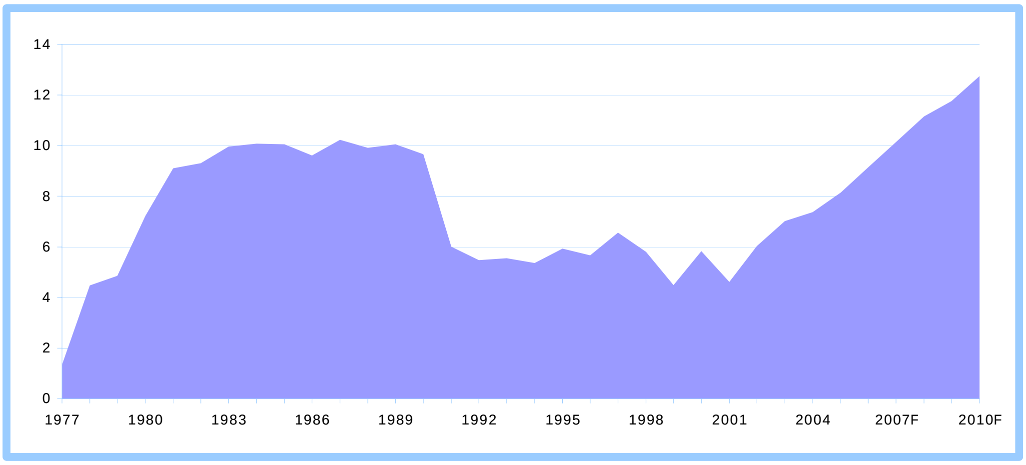
Gross Margin Analysis

	2005	2006	2007	2008	2009	2010
Purchased ore	4%	14%	19%	12%	12%	12%
Own ore	43%	41%	31%	19%	15%	13%
Total	**41%**	**38%**	**29%**	**18%**	**14%**	**13%**

Source: Company Data, Concorde Capital Estimates

Another source of cheap ore will come from the Nova mine, 30% of which was acquired by Ferrotrans, a company related to PGOK. The mine is expected to begin operation in 2005. We estimate PGOK will invest about 5% CapEx/Sales on a consolidated basis into the Nova mine this year. Its contribution to the mine is expected to be low this year, providing only 1% of iron ore produced. After 2006, the mine's projected output is estimated at about 11%-13% of PGOK's total concentrate production, thus lowering costs.

PGOK's Pellet Production, mln mt



Source: Company Data

Due to the company's efforts to increase its supply of concentrate for final production, we expect production growth to accelerate to ~10% in 2005 (compared to only 5% in 2004) and remain at this level in the medium term. The output level will reach Soviet-era highs by 2006-07 and rise substantially higher during the next several years. Opening new mines will enable the company to almost double its output by 2010.

In the long term, plans by PGOK's shareholders to construct their own steel mini-mill may lead to lower margins for PGOK. If PGOK is not divested by Finance and Credit by the time the mini-mill is constructed, those steel facilities will consume about 5 mln mt of pellets annually – meaning up to 40% of PGOK's output will be delivered at below-market prices to this affiliated company.

One profitability driver should be the optimization of its production mix. PGOK produces two types of pellets: pellets with 62% of iron content, which accounted for 90% of total output in 2004, and 68% pellets. As prices for iron ore materials are set for 1% of iron content in ore (DMTU), the price for materials with 68% iron content is about 10% higher than that of 62%. This year, PGOK made a step toward 68%-pellets, raising its share to 14% for the first five months of the year.

Distribution: Export Exposure

The Ukrainian pellet market is dominated by two large producers, PGOK and SGOK, which combined control 87% of total domestic output. However, PGOK exports a large percentage of its output, while SGOK supplies iron ore to Ukrainian steel mills. As a result, PGOK mainly competes with European and Russian iron ore producers.

Ukrainian Iron Ore Producers, mln mt

Company	Crude Ore			Concentrate Output			Sinter Output			Pellet Output		
	Fe Content	*Open Pit*	*Under ground*	*2004*	*% YoY*	*Market Share*	*2004*	*% YoY*	*Market Share*	*2004*	*% YoY*	*Market Share*
IGOK	27%	34.7	-	13.8	*0.3%*	21%	-	-	-	-	-	-
SGOK	33%	17.9	-	8.8	*16.6%*	13%	-	-	-	6.9	*15.8%*	42%
KRST	30%	15.7	1.3	8.5	*2.0%*	13%	10.1	*3.4%*	22%	-	-	-
YGOK	30%	16.9	-	8.3	*6.2%*	13%	3.9	*16.4%*	8%	-	-	-
PGOK	**26%**	**19.7**	**-**	**7.9**	***4.7%***	**12%**	**-**	**-**	**-**	***7.4***	***4.9%***	**45%**
KRIO	52%	-	7.4	6.5	*2.3%*	10%	-	-	-	-	-	-
CGOK	30-33%	6.1	-	4.8	*14.7%*	7%	-	-	-	*2.2*	*6.4%*	13%
ZIO	62%	-	3.9	3.9	*0.7%*	6%	-	-	-	-	-	-
SUBA	56-59%	-	3.6	3.1	*-2.7%*	5%	-	-	-	-	-	-
Other	-	-	-	-	-	-	32.7	*6.4%*	70%	-	-	-
Total		**111**	**16.2**	**65.5**	***4.8%***	**100%**	**46.7**	***6.5%***	**100%**	**16.4**	***9.4%***	**100%**

Source: State Statistics Committee

The global pellet market has two main leaders – Brazil's CVRD, which mostly exports its output to Western Europe and Asia, and the US' Cleveland Cliffs, which focuses on domestic markets. The third-largest pellet producer, US Steel, is an integrated steel producer that supplies pellets to its own steel capacities.

Top Global Pellets Producers, mln mt

	Company	Country	2003	2004	2005E	CAGR (04-05)	Share 05 %
1	CVRD	Brazil	40.5	51.6	45.1	5.5%	14%
2	Cleveland-Cliffs	USA	30.8	34.4	37.3	10.0%	12%
3	US Steel	USA	18.6	24.3	20.6	5.2%	6%
4	LKAB	Sweden	15.3	15.9	15.9	1.9%	5%
5	IOC (Rio Tinto)	Canada	11.6	9.9	12.3	3.0%	4%
6	Lebedinsky GOK	Russia	9.2	9.6	9.5	1.6%	3%
7	SSGPO	Kazakhstan	8.8	9.5	9.9	6.1%	3%
8	QCM	Canada	8.7	9.2	9	1.7%	3%
9	Mikhaylovsky GOK	Russia	8.4	8.8	9.5	6.3%	3%
10	NISCO	Iran	7.5	n/a	8.8	8.3%	3%
11	**PGOK**	**Ukraine**	**7.0**	**7.4**	**8.2**	**8.2%**	**3%**
12	Karelsky Okatysh	Russia	7.0	7.5	7.2	1.4%	2%
13	BHP Billiton	Brazil	6.6	7.7	7.1	3.7%	2%
	China		35	n/a	39.8	6.6%	12%
	Other		71	n/a	79.8	6.0%	25%
	Total		**286**	**n/a**	**320**	**5.8%**	**100%**

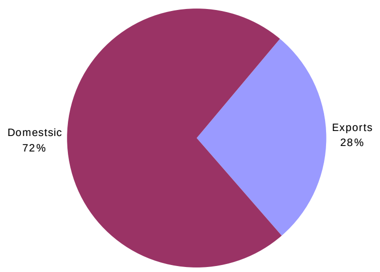
Source: Company Data, AME

PGOK's global pellet market share of 3% is not enough to influence world pricing, however the company has a strong position in the Central European market. Also, the prices and amount of ore to be supplied are fixed annually through long term contracts, ensuring a guaranteed price for its ore. Other major market players work similarly.

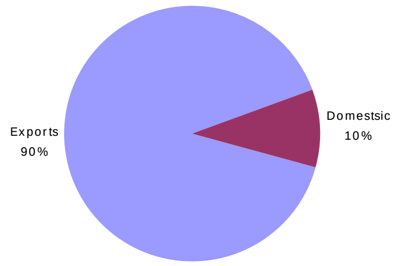
As it is the largest domestic producer of pellets, PGOK is also the largest Ukrainian exporter of iron ore. The company delivers about 90% of its output to foreign countries, while the Ukrainian industry exports only 28% of its total output. Thus, PGOK benefits from more stable market conditions than its Ukrainian peers.

Export Share

…Ukraine



…PGOK

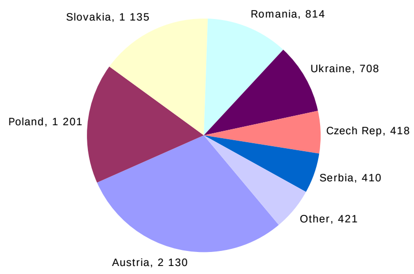


Source: Company Data

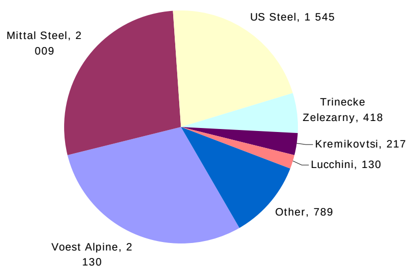
PGOK enjoys a strong market position. About 80% of PGOK output is delivered to the steel mills that belong to three steel producing heavy-weights: Mittal Steel, US Steel and Voest Alpine. In 2004, PGOK was the exclusive pellets supplier for Voest Alpine (Austria), US Steel Balkan (Serbia), Huta Katowice (Mittal Steel, Poland) and Trinecke Zelezarny (Czech Republic). Also, the company delivered pellets to Mittal's Huta Sendzimira in Poland and Sidex in Romania, supplying 80% and 54% of their respective needs.

Sales Structure 2004, mln mt

…by Country



…by Company



Source: Company Data

Since late 2004, PGOK has delivered pellets to China. Despite the trial nature of the deliveries, the company has already received proposals from Japanese iron ore traders to establish long-term relations for pellet supplies to China. At the same time, PGOK is considering cooperating with Japanese and Chinese partners to process its deposits.

A conflict between Russia's Magnitogorsk Iron and Steel (MMK) and its major iron ore suppliers, Mikhaylovsky GOK and Kazakhstan's Sokolovsko-Sarbayskoye GPO, opened the Russian market for PGOK. As a result, MMK began using Ukrainian materials and PGOK now plans to supply as much as 200K mt per month to Russia. MMK even lobbied for a decrease in railway tariffs for the transportation of imported Ukrainian iron ore in Russia at domestic shipping rates. New tariffs are expected to come into force starting in July and will significantly improve PGOK's competitiveness in Russia.

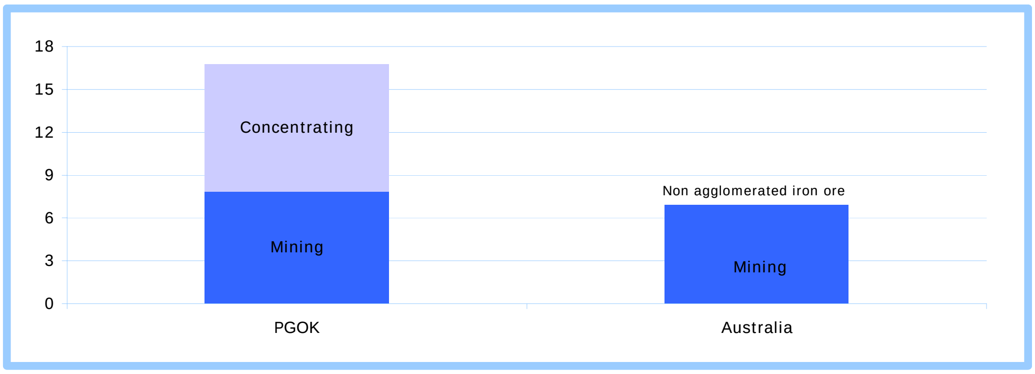
After losing its Kazakh ore supplier, MMK is in dire straights. The company has begun buying PGOK's ore and is also interested in acquiring the business, as it has enough capacity to satisfy MMK's pellet needs. PGOK also faces no risk of re-privatization and thus is a non-political acquisition.

COSTS: Transportation Leverage

PGOK has an advantageous geographic location relative to other iron ore exporters, due to its proximity to consumers in Eastern and Central Europe. Russian GOKs, Swedish LKAB and Brazilian and Australian companies are much further from their potential markets, offsetting their lower production costs with higher transportation costs.

The main negative factor of Ukraine's production costs compared to major global producers is the low iron content of its ore. For example, Brazilian and Australian ores do not require beneficiation (concentration), so the only major cost is the mining process. While Ukrainian mining costs are on the same level as Australian/Brazilian producers, the process of ore beneficiation doubles total costs.

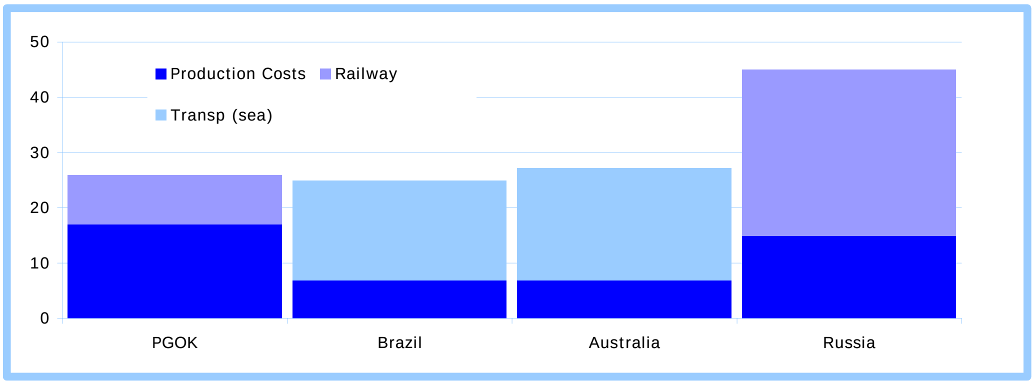
Cost Structure, USD



Source: Company Data, AME

However, exposure to Eastern and Central European markets provides significant transportation cost advantages for PGOK. Thus, PGOK's transportation costs for deliveries to Europe are two times lower than Brazil and Australia's and more than three times lower than Russian transportation costs.

***Costs, CIF USD**



Source: Company Data, Concorde Capital Estimates. * Delivery to EU border

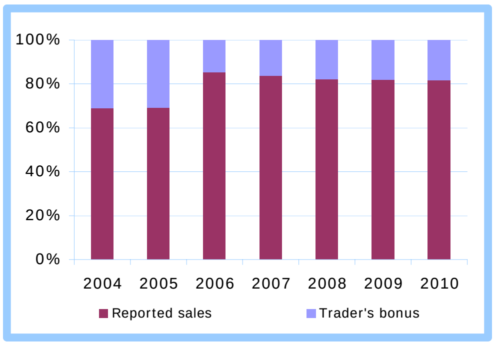
Though railway transportation is more expensive than sea-borne shipping, PGOK preserves its competitiveness in Central and Eastern Europe through the considerably shorter distances it needs to ship its products than its main competitors.

As iron ore and coke (feedstock for pig iron production) account for more than 55% of world dry bulk cargo shipping, we do not expect tariffs to fall for sea-borne transportation in the mid-term. The demand for these products will continue to grow, thereby keeping tariffs at high levels and keeping long distance export deliveries expensive.

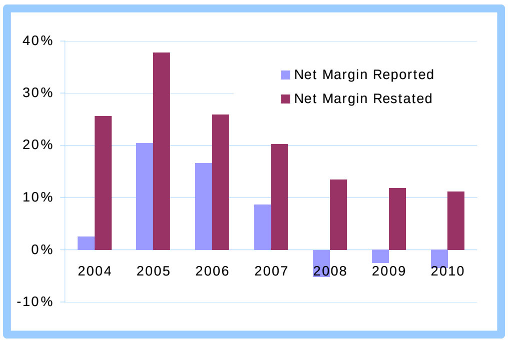
Transparency Issues

PGOK operates through an affiliated trading company, Ferrexpo, and PGOK's reported financials are substantially understated due to transfer pricing. According to our estimates, PGOK's off-shore trader collected about 30% of revenues in 2004. We expect that the situation will not change substantially in 2005, however the company will change its policy starting in 2006, cutting transfer pricing in half.

Transfer Pricing Rate



Profitability



Source: Concorde Capital Estimates

The company's IPO plan is a major positive factor for PGOK's transparency. We expect a substantial shift in profits from the trading division to the parent company – to the benefit of shareholders.

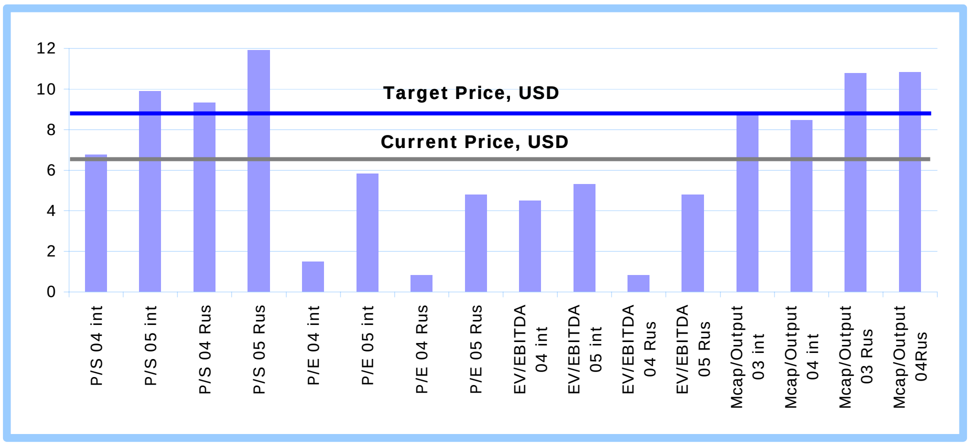
As the iron ore market is in its peak phase and no significant slowdown is expected in the next few years, iron ore companies have become targets for strategic mergers and acquisitions. Not only MMK, but also Russian businessman Alisher Usmanov who wants to create a CIS ore mining holding that would include some Ukrainian GOKs. So far, PGOK has remained neutral to proposals to join any group.

Valuation: Peer Comparison

Company	MCap USD mln	P/S 2004	P/S 2005E	P/E 2004	P/E 2005E	EV/EBITDA 2004	EV/EBITDA 2005E	MCap/ Output 2003	MCap/ Output 2004
PGOK	**510**	**1.9**	**1.0**	**70.8**	**6.0**	**13.5**	**3.8**	**67.1**	**64.6**
International Peers*									
BHP Billiton	43 752	1.8	1.5	12.9	6.9	7.4	3.9	n/m	n/m
CVRD	31 313	4.5	2.9	12.5	7.2	n/a	5.3	159.8	143.6
Rio Tinto	14 133	1.0	0.8	5.0	3.3	n/a	1.8	n/m	n/m
Kumba Resources	2 679	1.8	1.4	18.3	7.3	n/a	3.9	89.3	86.4
Cleveland-Cliffs	1 275	0.9	0.7	3.9	3.8	5.6	2.4	41.1	34.4
Portman	465	2.2	1.7	19.3	5.2	10.6	3.4	84.6	84.6
Assmang	1 449	n/a	n/a	45.3	n/a	18.5	n/a	n/m	n/m
AVG		2.0	1.5	16.7	5.6	10.5	3.5	93.7	87.3
Median		1.8	1.4	12.9	6.1	9.0	3.6	86.9	85.5
AVG w/o BHPB, CVRD, RT		1.6	1.3	21.7	5.4	11.5	3.2	71.7	68.5
Median w/o BHPB, CVRD, RT		1.8	1.4	18.8	5.2	10.6	3.4	84.6	84.6
Premium/ (Discount)		-8%	-37%	323%	8%	29%	14%	-28%	-26%
Implied Price, USD		**6.8**	**9.9**	**1.5**	**5.8**	**4.5**	**5.3**	**8.7**	**8.4**
Upside (Downside)		8%	58%	-76%	-7%	-28%	-15%	40%	35%
Russian Peers									
Mikhaylovsky GOK	2 266.0	3.0	1.7	10.3	4.0	7.5	3.1	126.6	118.0
Lebedinsky GOK	2 618.0	3.6	2.1	9.9	4.2	7.0	4.4	137.1	130.2
Stoilensky GOK	1 191.0	3.1	2.3	7.7	5.0	5.5	3.7	92.3	94.5
Kachkanarsky GOK	1 088.0	2.8	2.0	11.9	6.3	7.7	6.2	126.5	120.9
Vysokogorsky GOK	124.0	1.4	1.0	6.9	3.8	n/a	n/a	95.4	95.4
AVG		2.8	1.8	9.3	4.6	6.9	4.3	115.6	111.8
Median		3.0	2.0	9.9	4.2	7.3	4.0	126.5	118.0
Premium/ (Discount)		-33%	-47%	659%	30%	95%	-9%	-42%	-42%
Implied Price, USD		**9.3**	**11.9**	**0.8**	**4.8**	**2.4**	**7.0**	**10.8**	**10.8**
Upside (Downside)		49%	90%	-87%	-23%	-61%	13%	72%	73%

****P/EBITDA 05 stated for international peers***
Source: Bloomberg, IBES Estimates, Concorde Capital estimates

Valuation Summary: Implied Prices, USD



Financial Statements

All financial statements according to Ukrainian Accounting Standards.
Trading company not consolidated

Income Statement Summary, USD mn

	2003	2004	2005E	2006E
Net Revenues	**206**	**273**	**534**	**557**
Change y-o-y	*23%*	*33%*	*96%*	*4%*
Cost Of Sales	(135)	(173)	(315)	(346)
Change y-o-y	*21%*	*28%*	*82%*	*10%*
% of Net Revenues	*66%*	*63%*	*59%*	*62%*
Gross Profit	71	100	219	212
Other Operating Income/Costs, net	(2)	(3)	-	-
SG&A	(34)	(50)	(59)	(70)
EBITDA	**35**	**47**	**160**	**142**
EBITDA margin, %	17%	17%	30%	26%
Depreciation	(14)	(15)	(21)	(27)
EBIT	**21**	**32**	**139**	**115**
EBIT margin, %	10.1%	11.8%	26%	21%
Interest Expense	(11)	(14)	(9)	(8)
Financial income/(expense)	0	1	-	-
Other income/(expense)	(2)	(3)	-	-
PBT	**7**	**16**	**130**	**107**
Tax	(4)	(9)	(45)	(38)
Effective tax rate	*51%*	*55%*	*35%*	*35%*
Extraordinary Income/(loss)	-	-	-	-
Net Income	**3.4**	**7**	**84**	**70**
Net Margin, %	*2%*	*3%*	*16%*	*13%*
Dividend Declared	**0.7**	**1.2**	**1.3**	**2.1**

Balance Sheet Summary, USD mn

	2003	2004	2005E	2006E
Current Assets	**81**	**119**	**169**	**178**
Cash & Equivalents	5	19	27	28
Trade Receivables	12	10	22	28
Inventories	19	34	49	50
Other current assets	44	57	71	72
Fixed Assets	**167**	**182**	**282**	**348**
PP&E, net	149	164	254	325
Other Fixed Assets	18	18	28	22
Total Assets	**248**	**301**	**451**	**526**
Shareholders' Equity	**110**	**130**	**297**	**365**
Share Capital	123	137	219	219
Reserves and Other	6	6	7	7
Retained Earnings	(19)	(13)	71	138
Current Liabilities	**110**	**108**	**101**	**107**
ST Interest Bearing Debt	93	83	70	75
Trade Payables	11	16	19	21
Accrued Wages	1	1	2	2
Accrued Taxes	1	1	3	3
Other Current Liabilities	5	9	7	7
LT Liabilities	**28**	**62**	**53**	**55**
LT Interest Bearing Debt	27	62	53	54
Other LT	1	0	0	0
Total Liabilities & Equity	**248**	**301**	**451**	**526**

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