

**UKRAINE**  
Steel Pipe & Tube



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# Ukraine's Steel Pipe Industry

## Cost Competitive Global Player

### Companies Covered:

NPR	(NITR)
Khartsyzk Tube	(HRTR)
Novomoskovsk Pipe	(NVTR)
Dnipropetrovsk Pipe	(DPTR)

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# Global Market Overview

## The demand-supply side:

Global demand for pipes is generally pegged to the pace of global economic development.

Pipes are not a commodity. They are used in a variety of unrelated industries and have different applications even within the same industry, which makes it difficult to aggregate demand and price factors for the pipe industry as a whole.

Booming oil & gas industry comprises the largest and most promising pipe market segment at present.

Region-wise, China's economic powerhouse is both the largest pipe consumer and producer.

## The cost side:

The key cost component in pipe production is steel comprising 60-75% of total cost. Steel price surge in 2003 – 2004 hurt pipe producers' profits, but for many was offset by favorable markets.

Labor is usually the second largest cost item in pipe making.

For pipe exporters, transportation costs and logistics-related costs/ benefits are an important competitive factor.

Intensified cost and logistics competition forces pipe makers' consolidation.

Vertically integrated producers are cost-competitive usually due to being subsidiaries of steel companies, and horizontally integrated pipe makers mainly benefit from financial strength and distribution networks of their holding companies.

# Ukrainian Pipe Industry Overview

## Ukraine's competitive advantages:

Labor cost is amongst the lowest in the world.

Proximity to large markets (Russia, Central Asia, Middle East).

Proximity to suppliers of relatively cheap steel (domestic and Russian).

Vertical/ horizontal integration benefits.

## Industry specifics:

Exports account for lion's share of revenues. Russia is by far the largest market.

'Controlling stake' of the industry belongs to a powerful business group Interpipe, who currently is facing huge political risks and may dispose of its assets.

Another strong player in the Ukrainian pipe industry is System Capital Management (SCM). Its target segment is high value-added large diameter pipes catered mostly to Russia (Gazprom).

Corporate governance is poor.

Significant transfer pricing undercuts reported sales and erodes profitability of pipe makers.

Determined stance of the new government in regard to untoward practices by current pipe asset owners should put an end to this in the medium term.

# Investment Summary

	Liquidity	Current Price, USD	12-Month Target Price, USD	Upside/ (Downside)	Recommendation
NITR	Blue chip	6.25	<b>8.34</b>	33.5%	<b>BUY</b>
HRTR	Medium	0.15	<b>0.09</b>	-38.0%	<b>SELL</b>
NVTR	Low	5.75	<b>8.82</b>	53.4%	<b>BUY</b>
DPTR	Not traded	N/A	<b>86.65</b>	N/M	<b>N/R</b>

## Trading

Out of more than 35 Ukrainian pipe makers only five are traded.

Four companies are large enough to pose an interest to portfolio investors.

Liquidity differs significantly stock by stock.

## Valuation

Reported financials bear low relevancy to the true economics of pipe business, which complicates valuation.

All pipe stocks are massively overpriced based on reported financials.

Nonetheless, three out of the four stocks in consideration offer a considerable upside if true financials are considered.

Our target prices are based on DCF analysis under the assumption that true financials will be reported starting from 2007.

We recommend NITR and NVTR. Recommendation on DPTR, which is not traded, would depend on the offering price.

# Introduction To Pipe Making

# Pipe Types By Production Process

There are two principal types of pipes/tubes by production process:

**Welded pipes** are made from **skelp** (strip) of hot-rolled plate steel which are passed through forming rolls and welded. Either **electric resistance welding (ERW)** or **butt (continuous) welding** is employed.

*Skelp* is coiled strips of plate steel used to produce welded seam pipe

- *Longitudinally welded pipes:* the weld seam runs along the axis of the pipe.
- *Spiral-welded pipes:* the weld seam spirals around the circumference of the pipe.

**Seamless pipes** are made from a solid billet, which is heated, then rotated under extreme pressure. This rotational pressure creates an opening in the center of the billet, which is then shaped by a mandrel to form a hollow body. The latter is usually drawn to its final dimensions by **cold drawing**.

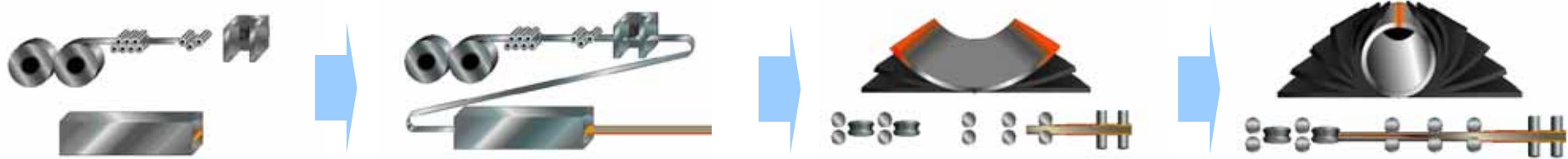
*Cold drawing* is the process of reducing the cross sectional area of tube by drawing the material through a die without any pre-heating. It changes the mechanical properties of the steel and the finished product is accurate to size, free from scale with a bright surface finish.

**Seamless pipe** is traditionally **stronger and more expensive** than comparable welded pipe.

Yet, ERW technology is improving and it now accounts for approximately 48% of OCTG (see next slide for definition) shipments by tonnage.

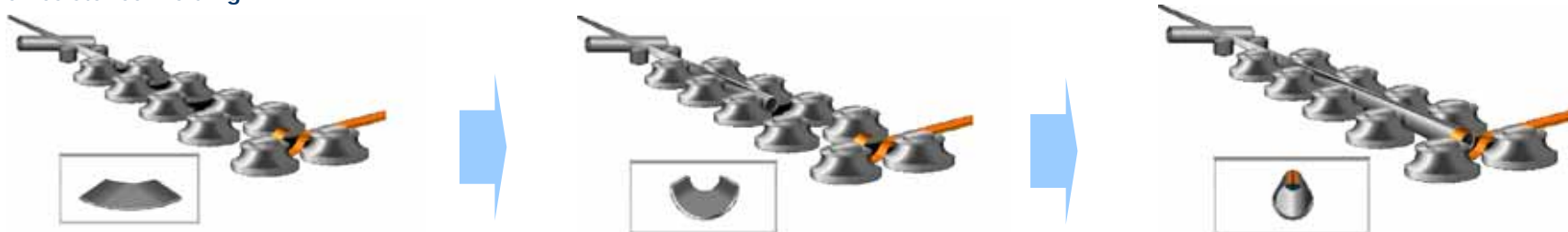
# Basics Of Pipe Making Technology

## Butt (Continuous) Welding



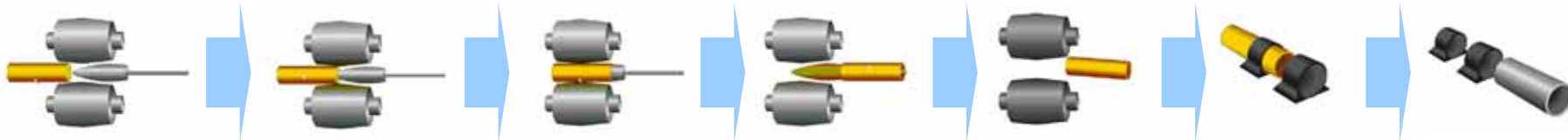
The continuous process produces a full range of pipe sizes from only a few different widths of skelp. The coils of skelp, or strip, are fed into the mill and their ends welded together to provide a continuous flow. The strip passes through a pre-heater and into a furnace. The heated strip is shaped into an arc of about 270° in a forming stand before passing into the welding stand.

## Electric Resistance Welding



Strip is unwound from coils and side-trimmed to control width and condition the edges for welding. The strip then passes through a series of contoured rolls which progressively cold-form it into a circular shape. The edges are forced together under pressure and welded by heating the steel to temperatures between 2200° F and 2600° F.

## Seamless



Steel billet is heated to about 2250° F. The red-hot billet is then rotated and drawn by rolls over a piercing rod, or mandrel. The action of the rolls causes the metal to flow over and about the mandrel to create a hollow pipe shell. After reheating, the shell is moved forward over a support bar and is hot-rolled in several reducing/sizing stands to the desired wall thickness and diameter.



# Pipe Types By Application

Pipes are classified by the consuming industry. The following industries are principal pipe consumers:

- Oil & gas (pipes referred to as OCTG)
- Machine building
- Power generation
- Chemical & petrochemical
- Construction
- Water & gas utilities

**Drill pipe** is used in the drilling of an oil or gas well. Drill pipe is the conduit between the wellhead motor and the drill bit. Drilling mud is pumped down the center of the pipe during drilling, to lubricate the drill bit and transmit the drilled core to the surface. Because of the high stress, torque and temperature associated with well drilling, drill pipe is a seamless product.

**Tubing** (when referring to OCTG) is a separate pipe used within the casing to conduct the oil or gas to the surface. It is always made by seamless process. Depending on conditions and well life, tubing may have to be replaced during the operational life of a well.

## OCTG (Oil Country Tubular Goods)

Pipe products used by oil exploration and transportation customers.

Includes oil & gas line, casing, drill pipe and oil well tubing, which, depending on their use, may be formed through welded or seamless processes.

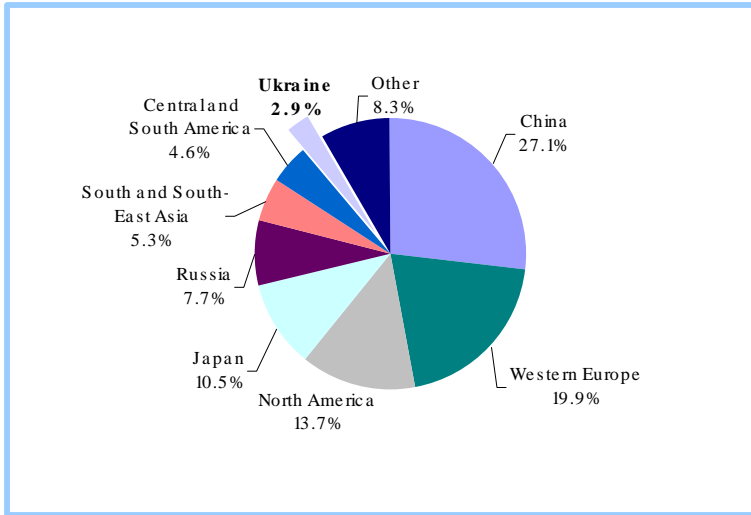
**Oil & gas line pipe** is used in the surface transmission of oil, natural gas and other fluids and can be either welded or seamless.

**Casing pipe** is the structural retainer for the walls of oil and gas wells, and accounts for 75% (by weight) of OCTG shipments. Casing is used to prevent contamination of both the surrounding water table and the well itself. Casing lasts the life of a well and is not usually removed when a well is closed. Can be made either by seamless or welded process.

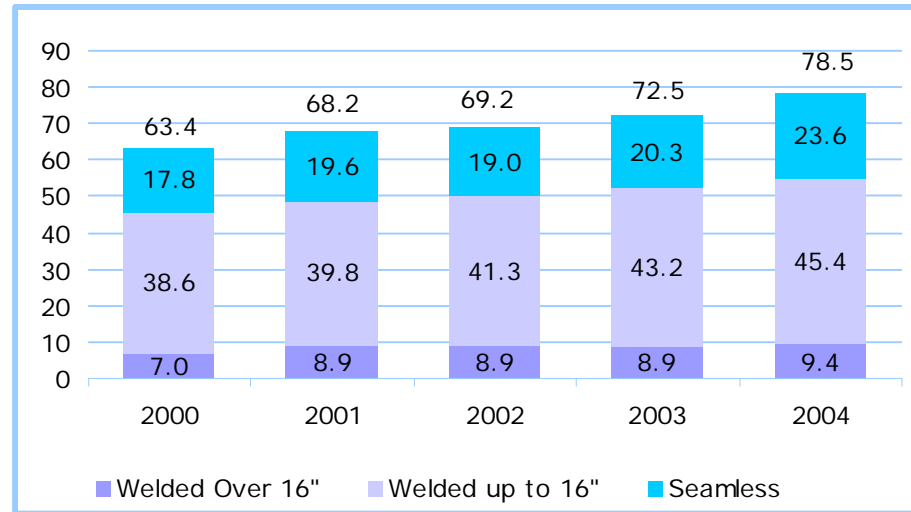
# Global Environment

# Demand Is Up, Competition Is Strong

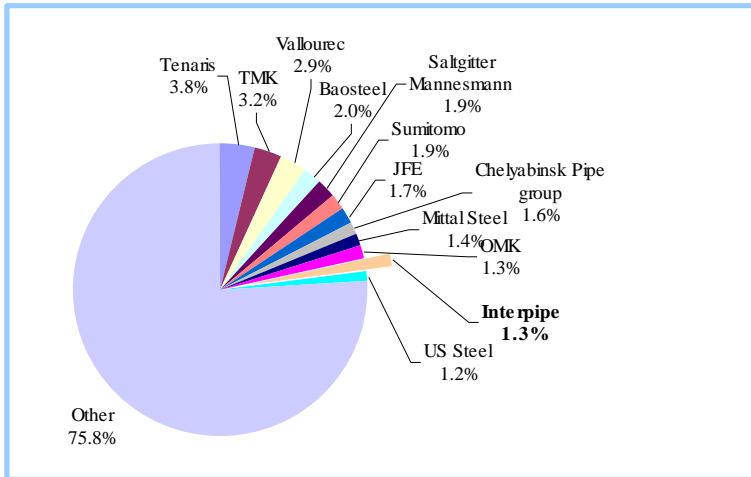
Pipe Output 2004 By Region, '000 mt



Global Steel Pipe Production, '000 mt



Global Steel Pipe Makers, 2004\*



Due to cyclicity, global pipe industry is geared to the pace of global economy. **China's** economic upsurge (27.1% of global pipe output in 2004) and demand from **oil & gas industry** were the key drivers of recent increase in pipe production.

Intense competition and growing input prices necessitate **consolidation of pipe industry worldwide**. Tenaris, TMK and Vallourec are the three world's largest **horizontally integrated** pipe holdings.

**Vertically integrated** pipe makers are steel mills with pipe making capacities whose access to cheap steel makes them **cost-competitive**. The largest players in this group are Baosteel, Salzgitter Mannesmann, Sumitomo, JFE and US Steel.

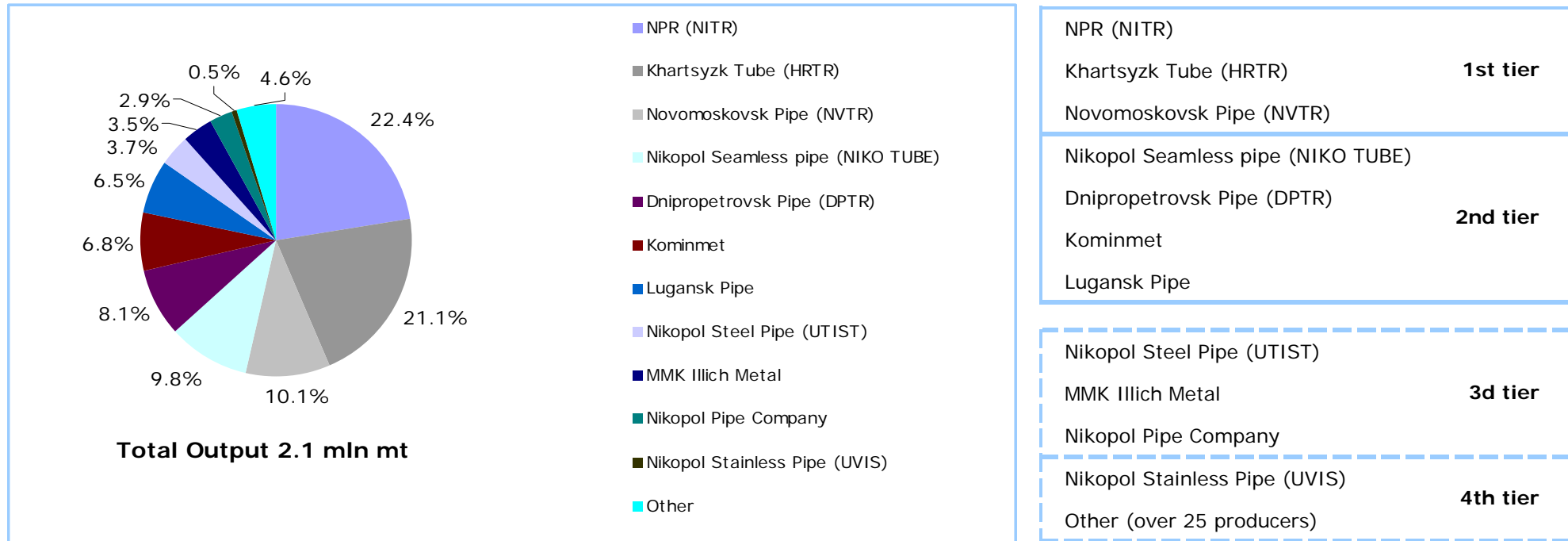
**Interpipe**, Ukraine's largest pipe corporation, **ranked #11** in the world by output in 2004.

\* Other large players (second and third tier) whose share is difficult to accurately estimate are Condesa, Corus, Marcegaglia, Maverick Tube, Rautaruuki, Riva Group, SIT Group, Arvedi

Source: Wirtschaftsvereinigung Stahlrohre; OMK; Xinhua News Agency; Borusan Mannesmann

# Ukrainian Pipe Industry At A Glance

Ukraine's Pipe Output By Producer, 2004



Highly concentrated: seven producers account for 84.7% of the industry's output and three producers comprise 53.6% of the market.

Estimated design capacity of the seven largest pipe makers is over 5 mln mt of pipes annually.

Overall industry's design capacity is over 7 mln mt of pipes annually.

Large pipe producers are associated with powerful business groups with easier access to raw materials and established distribution chains.

Most smaller plants are closely held.

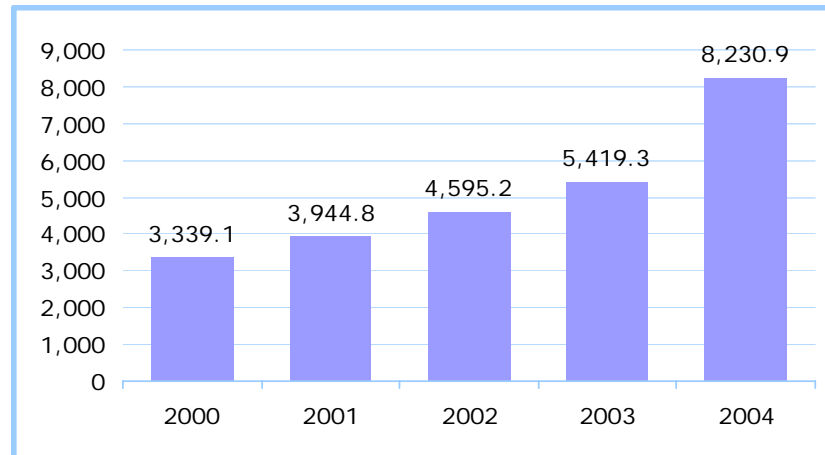
Smaller pipe producers (mini mills) are mostly focused on low value water & gas line pipes for utilities and construction industry.

Share of mini mills in total pipe output has diminished from 9% in 2002 to 5% in 2004.

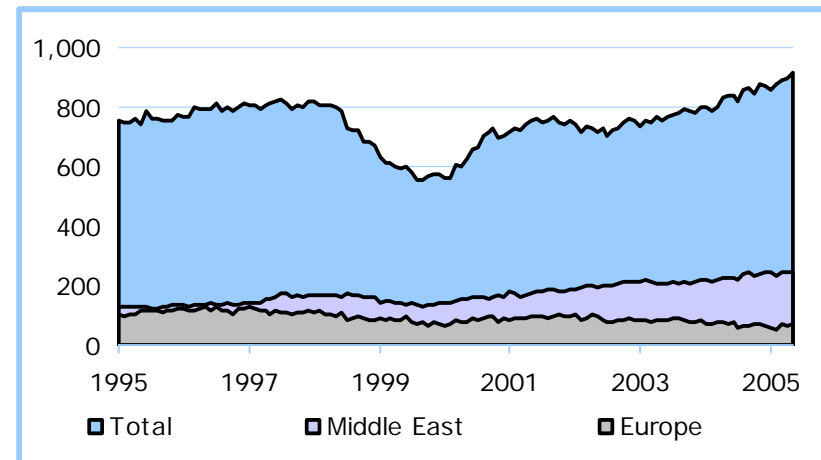
Source: State Statistics Committee; Company data

# Demand Drivers

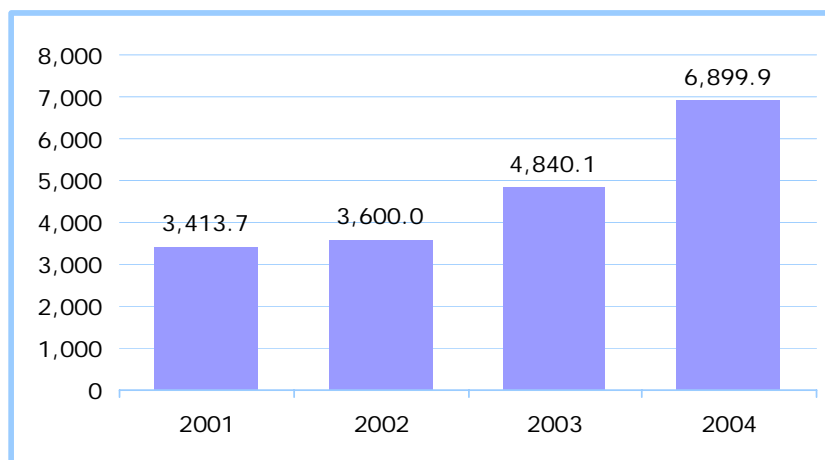
Ukrainian Machine Building Output, USD mln



International Oil & Gas Rig Count



Ukrainian Construction Volume, USD mln



Pipe industry prospects are determined by needs of a number of unrelated industries and specific projects.

Ukrainian pipe makers traditionally catered for domestic machine building as well as oil & gas industry of the entire FSU, construction and water & gas utilities.

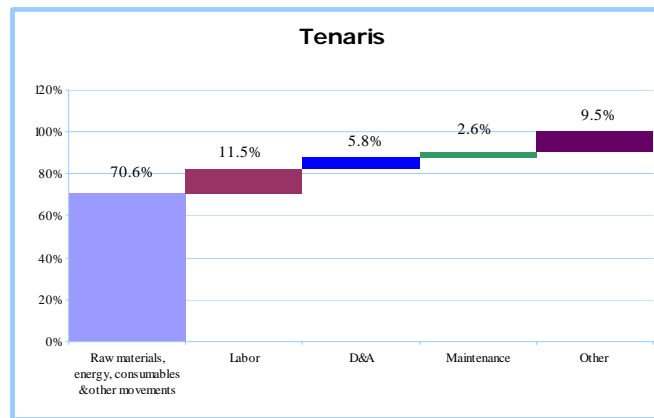
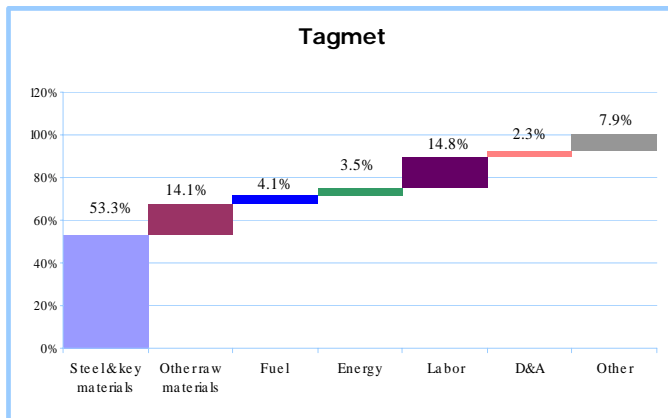
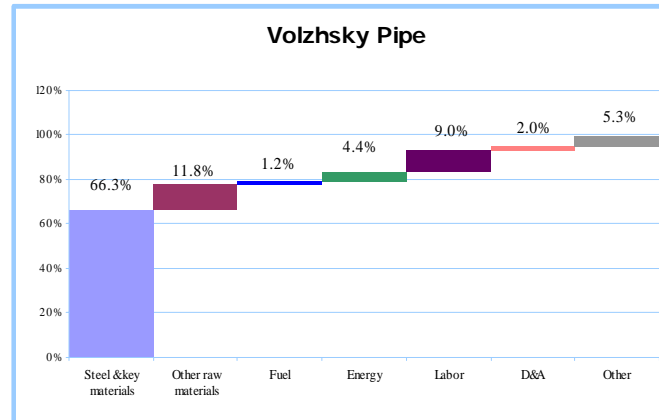
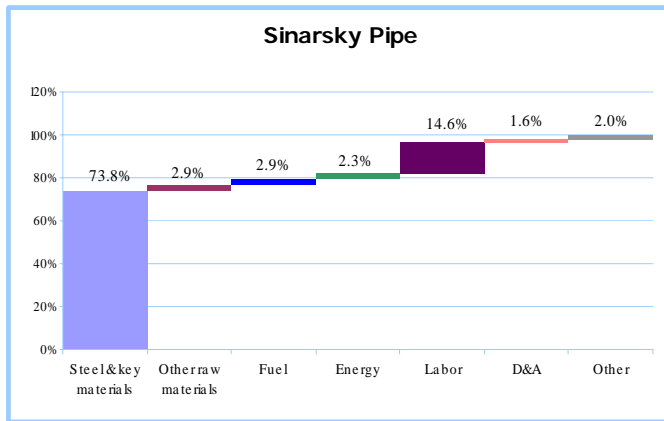
Ukraine's economic collapse in the 1990s changed the **focus** of Ukrainian pipe industry to **exports of OCTG**.

Rising demand and prices for hydrocarbon fuel have driven demand for OCTG in the past three years.

Apart from OCTG segment, reviving Ukraine's **machine building and construction buttress domestic demand** for pipes.

Source: Baker Hughes; State Statistics Committee

# Pipe Makers' Cost Structure 2004\*



Due to **poor disclosure** and low reliability of official financials for Ukrainian pipe makers, we **use peer data for cost structure**.

The **cost structure of Russian companies** is a **good proxy** due to similar economic environment and technology of Russian and Ukrainian pipe companies.

**Russian pipe makers** are **main competitors** of Ukrainian pipe producers because their key market is also Russia.

The **cost structure of Tenaris**, the world's largest pipe producer, is **similar** to that of Russian pipe manufacturers.

**Similarity** of different companies' cost profiles **assures reliability** of the cost analysis.

The **largest cost items** in pipe making:

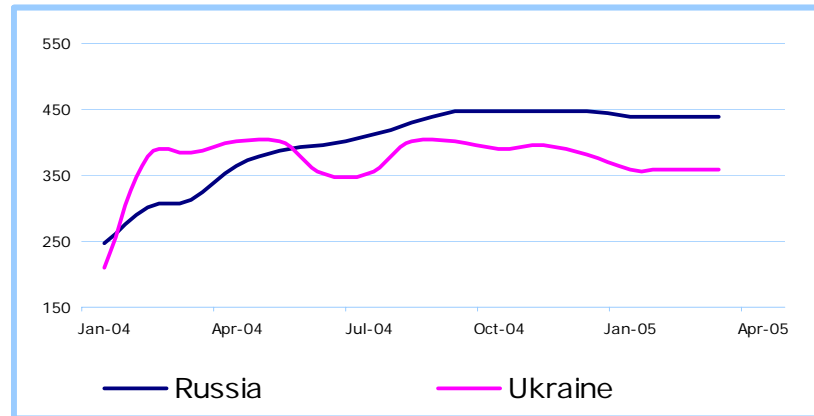
- Cost of steel
- Cost of labor

\*Sinarsky Pipe, Volzhsky Pipe and Tagmet are Russian pipe producers controlled by TMK. Tenaris is a multinational pipe holding incorporated in Luxembourg.

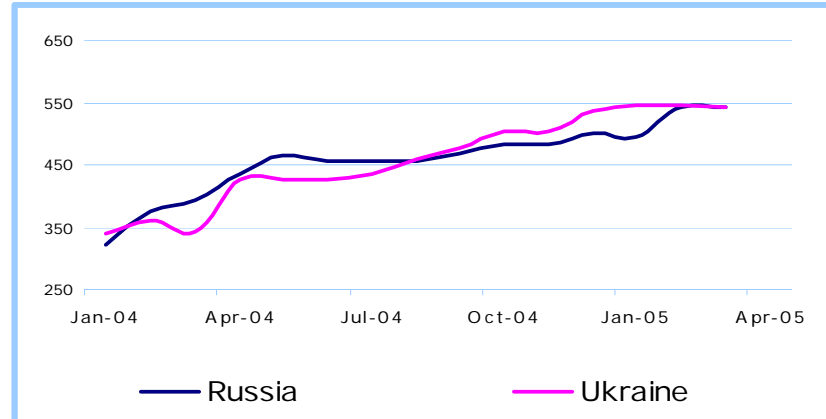
Source: Company data

# Key Input Price Dynamics

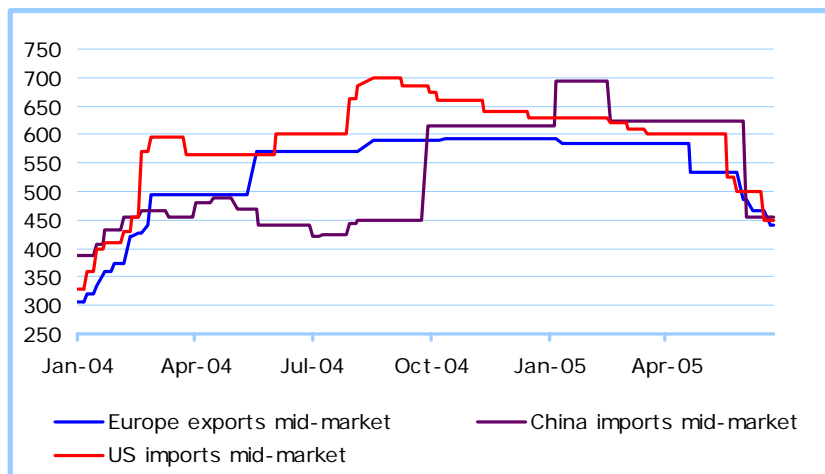
Tubular Billet Mid-Market Prices In Ukraine/ Russia, USD/mt



Hot Rolled Coil Mid-Market Prices In Ukraine/ Russia, USD/mt



Hot Rolled Coil Global Mid-Market Prices, USD/mt



**Steel** is the major input in the steel pipe production comprising **60% - 75% of pipe cost**. Tubular billet is used for production of seamless pipes and hot rolled coil (HRC) is the feedstock for welded pipe.

**Managing 'delta'** (pipe price less steel price) is the **key to success** in pipe making business.

Surge of steel prices in 2004 due to a strong demand from China adversely affected pipe makers worldwide, since **demand for pipes is more elastic than demand for steel**.

**Current downward trend in steel prices** coupled with a strong demand for pipes **bodes well for pipe industry** in 2005.

**Ukrainian pipe makers enjoy lower steel prices than pipe manufacturers in the EU and US**, but do not have this advantage over their Russian rivals.

Source: Business World - Ukrainian Metal Magazine; Bloomberg

# Labor Cost

	Country	Headcount, '000	Output, '000 mt	Labor cost, USD mln	Labor cost, USD/mt	Labor cost per capita, USD '000	Output per capita, mt
<b>International Peers</b>							
Tenaris	Luxembourg	16.4	2,997.0	369.7	123.4	22.5	182.2
Vallourec	France	17.5	2,275.1	763.9	335.8	43.8	130.3
Maverick Tube	USA	2.8	1,253.9	N/A	N/A	N/A	443.1
<b>Russian Peers</b>							
Vyksa Steel Works	Russia	14.9	867.6	51.5	59.3	3.5	58.4
Volzhsky Pipe	Russia	11.0	786.6	40.8	51.9	3.7	71.7
Cheliabinsk Pipe	Russia	8.9	749.6	43.8	58.4	4.9	84.5
Seversky Pipe	Russia	10.3	525.1	37.0	70.4	3.6	50.9
Tagmet	Russia	12.3	607.7	41.6	68.5	3.4	49.3
Sinarsky Pipe	Russia	12.3	580.6	50.7	87.4	4.1	47.3
<b>Ukrainian Pipe Makers</b>							
NITR	Ukraine	9.6	476.3	26.7	56.0	2.8	49.6
HRTR	Ukraine	6.6	448.2	16.7	37.3	2.5	67.8
NVTR	Ukraine	3.6	213.8	8.3	38.9	2.3	58.9
DPTR	Ukraine	4.4	172.8	9.6	55.5	2.2	39.5

- Labor is the second largest constituent of pipe cost.
- Ukrainian pipe makers possess an advantage of low per capita labor cost.
- In terms of labor cost per tonne of pipe, Ukrainian pipe producers are comparable to their Russian peers

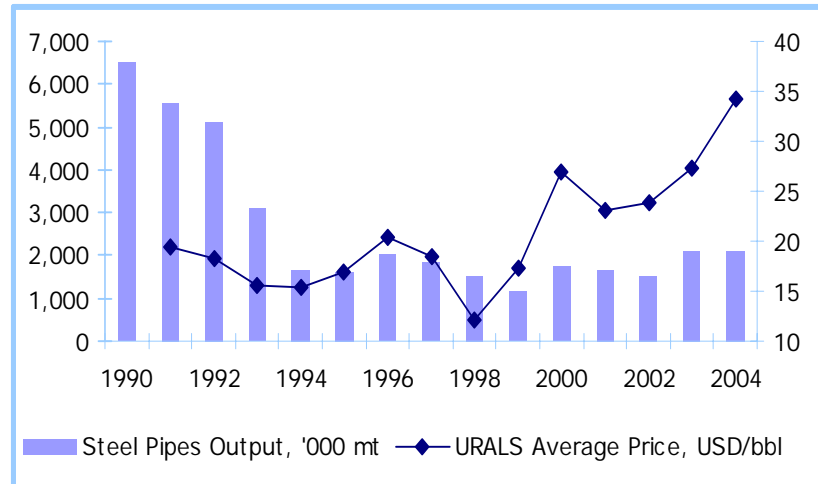
Source: Company data-2004



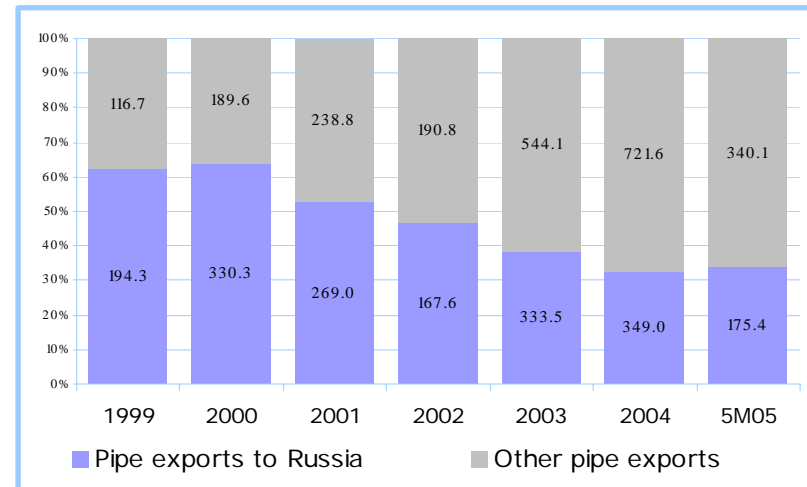
## Major Markets: Need For Diversification

# Importance Of The Russian Market

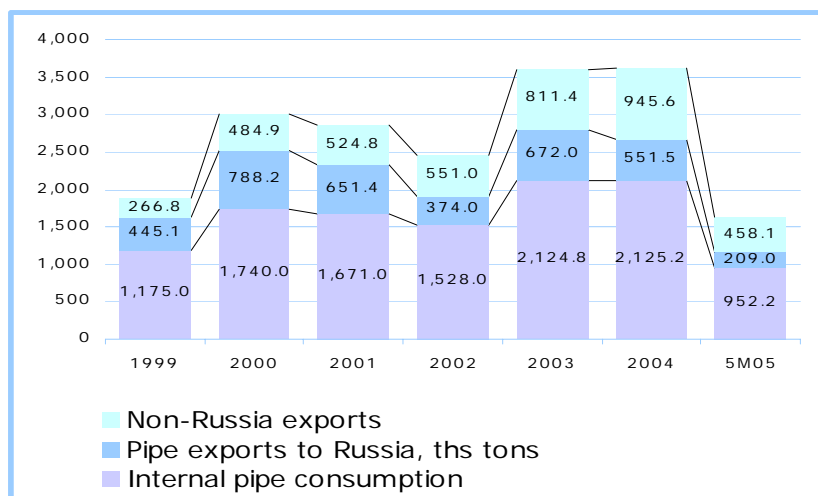
Steel Pipe Output Responsiveness To URALS Price



Exports Structure: Russia Vs. Other Markets, USD mln



Industry Sales Structure, '000 mt



**Ukrainian pipe makers are highly export-dependent** due to Ukraine's excess capacities.

**Russia is by far the largest single export market** for Ukrainian pipe mills and its **oil & gas industry is the key pipe consumer**.

Volume of Russian pipe market comprised 5.7 mln mt in 2004 and is projected to grow to 6.4 mln in 2006, 7.0 mln mt in 2007 and 7.5-8 mln mt in 2008.

Since 2002, non-Russia pipe exports have been exceeding exports to Russia.

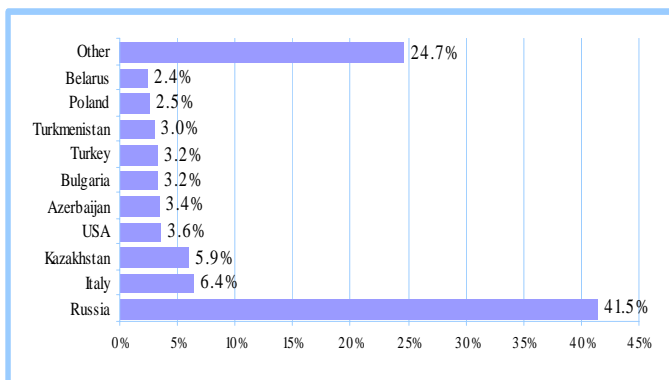
**Russia's share has been diminishing since 2000** in terms of export sales proceeds, which suggests **increasing diversification** of Ukrainian pipe exports.

**Domestic demand for pipes grew significantly** after 2002.

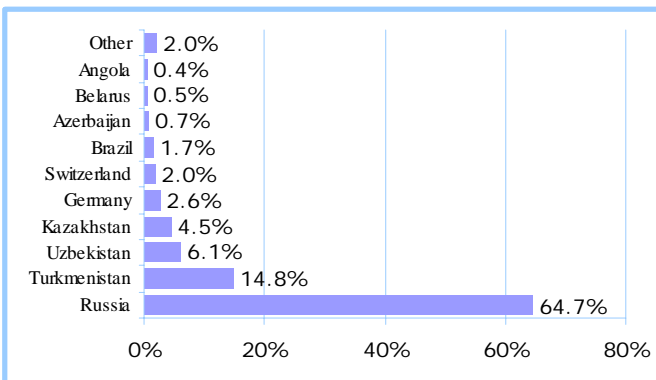
Source: State Statistics Committee; Ukrainian News; Bloomberg

# Growing Pipe Export Diversification

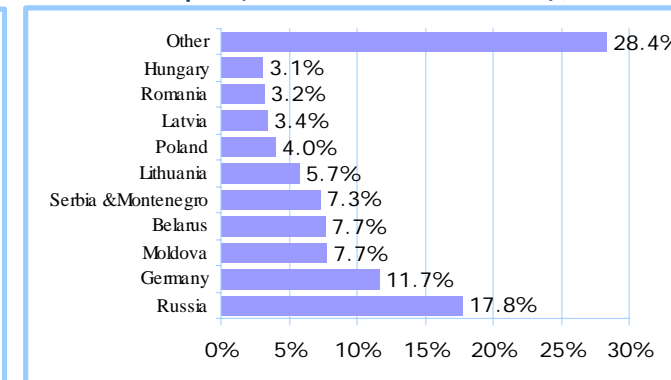
Seamless Pipes (A Total Of 735.8 ths mt), 2003



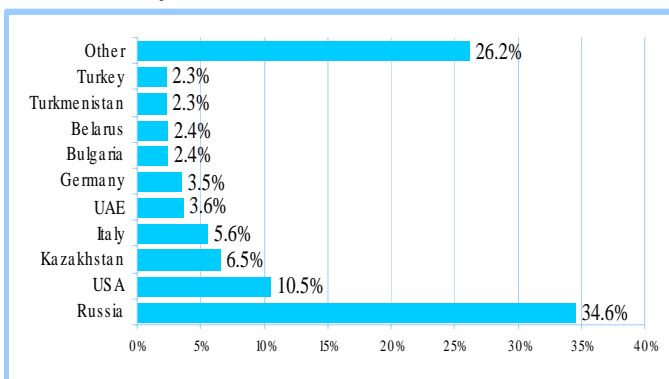
LD ERW Pipes (A Total Of 508.2 ths mt), 2003\*



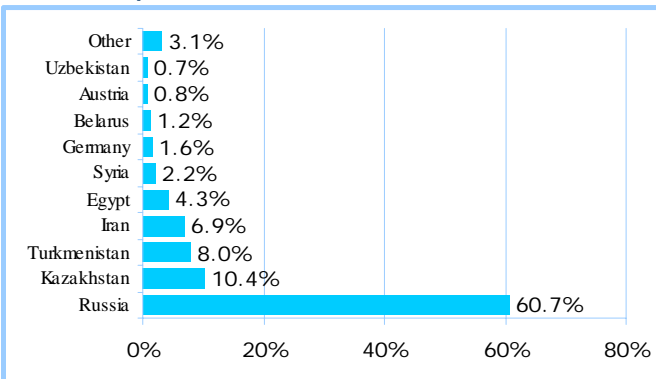
Other ERW Pipes (A Total Of 257.9.2 ths mt), 2003



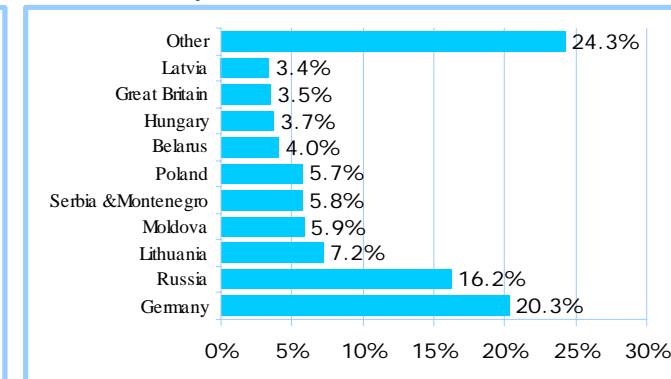
Seamless Pipes (A Total Of 733.6 ths mt), 2004



LD ERW Pipes (A Total Of 448.8 ths mt), 2004



Other ERW Pipes (A Total Of 314.8 ths mt), 2004



\*LD stands for 'large diameter' pipes defined as pipes with an outer diameter in excess of 508 mm and used in construction of oil- and gas-main pipelines

ERW pipes are electric resistance welded ones

- Seamless pipes comprised 49%, and LD ERW pipes accounted for 30% of total Ukrainian pipe exports in 2004.
- Primary markets for Ukrainian pipes alternative to Russia are those of the EU, Middle East/Persian Gulf and Central Asia.

- LD pipes continue to be the segment most dependent on the Russian market and thus most vulnerable to the risk of being ousted from it.

# Free Trade Restrictions

	May - Dec 2001	2002	2003	2004
<b>All pipe categories</b>				
Annual quota	413.3	620	740	715
Completion	80.9%	60.3%	91.9%	97.8%
<b>Ø1,450 mm pipes</b>				
Annual quota	90	135	255	230
Completion	49.5%	92.4%	119.5%	99.3%
<b>Stainless pipes</b>				
Annual quota	-	-	-	4.2
Completion	-	-	-	99.8%
<b>Other pipes</b>				
Annual quota	323.3	485	485	480.8
Completion	89.6%	51.4%	77.4%	97.0%

Quota is in '000 mt

	2000	2001	2002	2003	2004
Pipe consumption in Russia, ths mt	5,321	5,564	4,927	6,086	5,698
Ukrainian exports, ths mt	788	651	374	672	552
Share, %	14.8%	11.7%	7.6%	11.0%	9.7%

## Regulations On Other Markets

**2002:** In March, the U.S. introduced duties on Ukrainian pipes (reduced from 15% in 2002 to 9% in 2005). Expired in March 2005.

**2002:** In September, the EU imposed exports duty on Ukrainian pipe exports of 30.9% for NITR and 44.1% for others.

**2002:** Hungary and Poland imposed duties and set quotas on Ukrainian pipe exports. In May 2004, EU's export duties on Ukrainian pipes were adopted by all EU's new members.

**2004:** In August, Belarus started an antidumping investigation into Ukrainian pipe exports.

## Russian Quota: Finally Over

**2001:** In May, Russia introduced export quota on Ukrainian pipes at 620 ths mt annually (413.3 ths mt for eight months). In July, a 20% VAT charge on goods imported to Russia introduced which was more detrimental than the quota.

**2003:** The quota was raised by 19.35%, to 740 ths mt, due to the increased allotment for Ø 1,420 mm pipe exports from 135 ths mt to 255 ths mt to meet Gazprom's growing needs. Only HRTR benefited from this.

**2004:** Russia cut the quota for LD Ø 1,420 mm pipes to 230 ths mt per year and introduced a separate quota on stainless pipes of 4.2 ths mt to protect Volzhsky and Sinarsky Pipe plants.

**2005:** Quota system was abolished due to a free trade agreement between Russia and Ukraine

## Not So Easy: Russia's Antidumping Investigations

**2004:** In July, Russia initiated a new antidumping investigation into Ukrainian pipe exports.

**2005, January:** Five pipe plants associated with Interpipe (NITR, NVTR, NIKO Tube, Nikopol Pipe Company and Nikopol Stainless Pipe Plant) signed a voluntary export restriction agreement with Russia fixing their combined exports to Russia at 395 ths mt in 2005, on par with the 2004 quota. The agreement allowed them to avoid antidumping investigations.

**2005, July:** Four other Ukrainian pipe makers filed for voluntary self-restriction of small and medium diameter pipe exports to Russia. These are Dnipropetrovsk Pipe, MMK Illich Metal, Nikopol Steel Pipe and HRTR. Their offer is yet to be accepted by Russian regulators.

**Meanwhile,** HRTR continues unrestricted exports of LD pipes to Russia. Russian competition will likely result in HRTR's share in the Russian market diminishing significantly in the medium term.

## Surviving Competition

# Pipe Makers Within Business Groups

## Business Groups

Interpipe

SCM

IUD

Privat

Zaporizhstal Group

MMKI

## Steel Producers Controlled/ Owned By Business Group

NPR (has in-house steel making capacities)

- Azovstal
- Yenakiyevo Iron & Steel
- Metalen
- Kerch Steel

- Alchevsk Steel
- DMK Dzerzhynskogo
- DAM Steel
- Huta Chestochowa
- Dunaferr
- Kramatorsk Iron & Steel

DMK Petrovskogo

Zaporizhstal

MMKI

## Pipe Makers Controlled/ Owned By Business Group

- NPR
- Novomoskovsk Pipe
- NIKO TUBE
- Nikopol Pipe Company
- Mogilev Metal Works (Belarus)

Khartsyzk Tube

Dnipropetrovsk Pipe

Kominmet

Lugansk Pipe (closely held)

MMKI (has in-house pipe making capacities)

Pipe plants of major business groups benefit from **strong distribution chains and availability of funds** when needed.

**Interpipe** is Ukraine's largest **horizontally integrated** pipe holding who accounts for 45% of Ukraine's pipe output.

Interpipe's pipe plants except for NPR have to buy steel from Ukrainian and Russian plants not belonging to group.

NPR's steel needs are partially met by in-house steel production.

**Quasi-vertical integration** with steel mills is typical of pipe plants belonging to other Ukrainian business groups.

Khartsyzk Tube's primary supplier of wide strip as well as one of the traders in its pipes is Azovstal.

**MMKI** is a steel maker with significant pipe making capacities, and is a **vertically integrated** player in the pipe market.

**Transfer pricing is commonly found along the chain: Steel Maker=>Trader=>Pipe Producer=>Trader.**

# Ukrainian Pipe Makers Vs. Russian Peers

Factor	Location	Price	Quality	Delivery Speed	After-Sales Servicing	Total Score
Relative Importance	10%	30%	30%	25%	5%	100%
Vyksa Steel Works	5	4	5	4	3	4.35
Volzhsky Pipe	5	4	5	3	3	4.10
Cheliabinsk Pipe	5	4	4	4	3	4.05
Sinarsky Pipe	4	4	5	3	3	4.00
Tagmet	5	4	4	3	3	3.80
Seversky Pipe	4	4	4	3	3	3.70
Pervouralsky Pipe	4	4	3	3	3	3.40
HRTR	5	5	5	4	3	4.65
NITR	5	4	5	4	3	4.35
NVTR	5	4	4	4	3	4.05
DPTR	5	4	4	3	3	3.80

Each factor is quantified within a range [1;5]; higher score indicates higher competitiveness.

As a result of a **massive tax bail-out in 1999 – 2001**, Ukrainian pipe makers entrenched themselves in the Russian market.

Despite current competitive advantages, Ukrainian pipe makers **will face an intensified competition from their Russian rivals**.

Russian pipe makers have embarked upon massive investment programs to be completed in 2007 - 2008. These projects aim at construction of steel making capacities, broadening product assortment and quality improvements.

In 2003 - 2004, Ukrainian pipe companies invested a total of ~USD 55 mln in CapEx (~**USD 13.2 per mt of output**), while CapEx of their Russian peers comprised ~USD 300 mln (~**USD 24.7 per mt of output**).

Due to availability of excess capacities, owners of Ukrainian pipe plants until recently deemed large CapEx inappropriate and invested primarily in ancillary equipment and energy saving technologies. **Investment sluggishness may cost Ukrainian producers a large share of the Russian market.**

Protectionist measures taken by Russia pose another risk.

# International Financial Comparison

Company		NTR* Ukraine	HRTR Ukraine	NVTR Ukraine	DPTR Ukraine	Tenaris Luxembourg	Vallourec France	US Steel USA	Maverick Tube USA	Sumitomo Pipe & Tube Japan	Vyksa Steel Works* Russia	Voizhsky Pipe Russia	Cheliabinsk Pipe Russia	Seversk Pipe Russia	Tagmet Russia
Pipe Output, '000 mt	2003	546.5	455.5	224.6	177.7	2 633.0	2 391.2	900.0	1 281.6	1 449.2	884.7	756.3	822.5	565.0	560.6
	2004	476.3	448.2	213.8	172.8	2 997.0	2 275.1	1 100.0	1 253.9	1 490.6	867.6	786.6	749.6	525.1	607.7
Sales, USD mln	2003	315.7	75.0	84.5	47.6	3 179.7	2 683.5	8 354.0	884.3	315.1	612.4	434.1	451.0	276.7	267.5
	2004	493.7	109.1	121.3	85.2	4 136.1	3 773.4	12 930.0	1 456.3	386.5	924.0	631.5	563.1	367.2	370.5
Sales, USD per mt	2003	577.7	164.6	376.1	267.8	1 207.6	1 122.3	9 282.2	690.0	217.4	692.2	573.9	548.4	489.8	477.1
	2004	1 036.7	243.3	567.5	492.9	1 380.1	1 658.6	11 754.5	1 161.4	259.3	1 065.0	802.8	751.2	699.4	609.6
EBITDA, USD mln	2003	13.9	15.1	2.2	0.6	602.0	253.6	-367.0	67.8	9.4	119.5	22.5	32.9	N/A	N/A
	2004	42.5	8.8	5.4	2.6	899.0	542.4	1 962.0	351.8	33.5	145.4	43.5	35.2	N/A	N/A
EBITDA per mt	2003	25.5	33.2	9.9	3.5	228.6	106.1	-407.8	52.9	6.5	135.1	29.7	40.0	N/A	N/A
	2004	89.2	19.6	25.3	14.8	300.0	238.4	1 783.6	280.5	22.5	167.6	55.3	47.0	N/A	N/A
EBITDA Margin, %	2003	4.4%	20.2%	2.6%	1.3%	18.9%	9.5%	-4.4%	7.7%	3.0%	19.5%	5.2%	7.3%	N/A	N/A
	2004	8.6%	8.0%	4.5%	3.0%	21.7%	14.4%	15.2%	24.2%	8.7%	15.7%	6.9%	6.3%	N/A	N/A
EBIT, USD mln	2003	6.6	10.2	0.5	-1.0	288.2	133.9	-730.0	45.3	-2.0	95.0	13.7	20.4	10.0	14.9
	2004	35.2	3.8	3.5	0.9	813.5	409.8	1 580.0	324.1	21.2	119.8	31.5	22.0	38.6	-1.3
EBIT per mt	2003	12.0	22.4	2.3	-5.9	109.5	56.0	-811.1	35.4	-1.4	107.4	18.1	24.8	17.8	26.6
	2004	73.9	8.6	16.2	5.2	271.4	180.1	1 436.4	258.4	14.2	138.1	40.0	29.4	73.6	-2.2
EBIT Margin, %	2003	2.1%	13.6%	0.6%	-2.2%	9.1%	5.0%	-8.7%	5.1%	-0.6%	15.5%	3.2%	4.5%	3.6%	5.6%
	2004	7.1%	3.5%	2.9%	1.1%	19.7%	10.9%	12.2%	22.3%	5.5%	13.0%	5.0%	3.9%	10.5%	-0.4%
Net Income, USD mln	2003	3.3	2.1	0.1	-1.1	210.0	86.9	-463.0	23.0	20.7	59.6	2.4	7.7	1.8	4.0
	2004	19.3	0.4	2.2	0.4	785.0	312.8	1 091.0	193.8	10.8	70.3	10.2	1.8	18.5	16.0
Net Income per mt	2003	6.1	4.6	0.6	-6.1	79.8	36.4	-514.4	17.9	14.3	67.4	3.1	9.4	3.2	7.2
	2004	40.4	0.9	10.3	2.1	261.9	137.5	991.8	154.6	7.3	81.1	13.0	2.4	35.3	26.4
Net Income Margin, %	2003	1.1%	2.8%	0.2%	-2.3%	6.6%	3.2%	-5.5%	2.6%	6.6%	9.7%	0.5%	1.7%	0.7%	1.5%
	2004	3.9%	0.4%	1.8%	0.4%	19.0%	8.3%	8.4%	13.3%	2.8%	7.6%	1.6%	0.3%	5.0%	4.3%
Gross PP&E, USD mln	2003	228.4	135.8	58.5	53.5	5 546.8	1 613.6	10 371.0	340.8	217.8	690.7	58.9	372.3	N/A	N/A
	2004	234.5	137.7	58.7	54.3	5 973.8	1 816.0	10 864.0	391.3	225.6	867.3	87.8	459.6	N/A	N/A
D&A, USD mln	2003	7.4	4.9	1.7	1.7	208.1	119.7	363.0	22.4	11.5	24.4	8.8	12.5	N/A	N/A
	2004	7.3	4.9	1.9	1.7	199.8	132.7	382.0	27.7	12.3	25.6	12.0	13.2	N/A	N/A
Net CAPEX, USD mln	2003	6.3	2.7	0.6	0.5	156.7	81.6	222.0	20.8	N/A	23.1	15.4	39.6	N/A	N/A
	2004	2.8	5.5	1.4	1.4	168.9	109.3	484.0	29.0	N/A	134.1	26.3	46.4	N/A	N/A
Working Capital, USD mln	2003	52.3	8.2	8.3	-18.0	707.2	1 042.4	979.0	253.7	125.8	184.0	32.3	76.8	21.8	67.2
	2004	42.6	5.2	13.5	-17.4	1 012.2	1 327.1	1 712.0	471.1	147.4	126.5	35.6	77.1	16.2	77.5
Total Assets, USD mln	2003	257.3	93.0	47.6	53.6	4 309.5	2 797.7	7 837.0	670.7	426.6	466.7	193.4	355.3	139.6	280.4
	2004	460.5	96.3	53.0	61.7	5 662.3	3 544.3	10 956.0	1 002.4	433.4	742.5	252.7	680.6	186.4	283.7
Total Fin. Debt, USD mln	2003	3.2	9.6	2.7	8.2	833.7	626.4	1 938.0	178.0	0.0	83.0	89.5	73.1	0.0	90.8
	2004	36.5	8.0	2.6	3.0	1 259.3	587.1	1 449.0	180.9	0.0	182.9	98.7	363.2	0.0	95.7
LT Fin. Debt, USD mln	2003	0.0	0.0	2.7	0.1	458.9	369.8	1 890.0	174.4	0.0	29.7	16.4	33.3	0.0	16.9
	2004	0.0	0.0	2.6	0.0	838.6	285.4	1 363.0	177.6	0.0	141.7	35.8	232.0	0.0	45.9
LT Fin. Debt to Equity	2003	0.0	0.0	0.1	0.0	0.2	0.8	1.7	0.5	0.0	0.1	0.3	0.1	0.0	0.1
	2004	0.0	0.0	0.1	0.0	0.2	0.6	0.3	0.3	0.0	0.4	0.6	1.0	0.0	0.3
ST Fin. Debt, USD mln	2003	3.2	9.6	0.0	8.1	374.8	256.6	48.0	3.5	0.0	53.3	73.1	39.8	0.0	73.9
	2004	36.5	8.0	0.0	3.0	420.8	301.7	86.0	3.3	0.0	41.2	62.9	131.2	0.0	49.8
ROA	2003	1.3%	2.2%	0.3%	-2.0%	4.9%	3.1%	-5.9%	3.4%	4.9%	12.8%	1.2%	2.2%	1.3%	1.4%
	2004	4.2%	0.4%	4.2%	0.6%	13.9%	8.8%	10.0%	19.3%	2.5%	9.5%	4.0%	0.3%	9.9%	5.7%
ROE	2003	2.0%	3.4%	0.4%	NEG	11.4%	11.2%	-42.4%	6.0%	8.4%	19.0%	4.4%	3.4%	2.7%	2.4%
	2004	10.4%	0.6%	5.7%	15.1%	31.5%	31.4%	27.5%	32.5%	4.1%	17.4%	17.5%	0.8%	22.2%	10.1%

## Ukrainian pipe mills have the following common characteristics:

- Low reported margins, ROA and ROE
- Low leverage
- Low CapEx

- Top-line numbers are low (sales per tonne are lower than for Russian peers despite significant overlap of markets and similar pricing)
- related party transactions with traders undercut sales

Source: Company data; Bloomberg

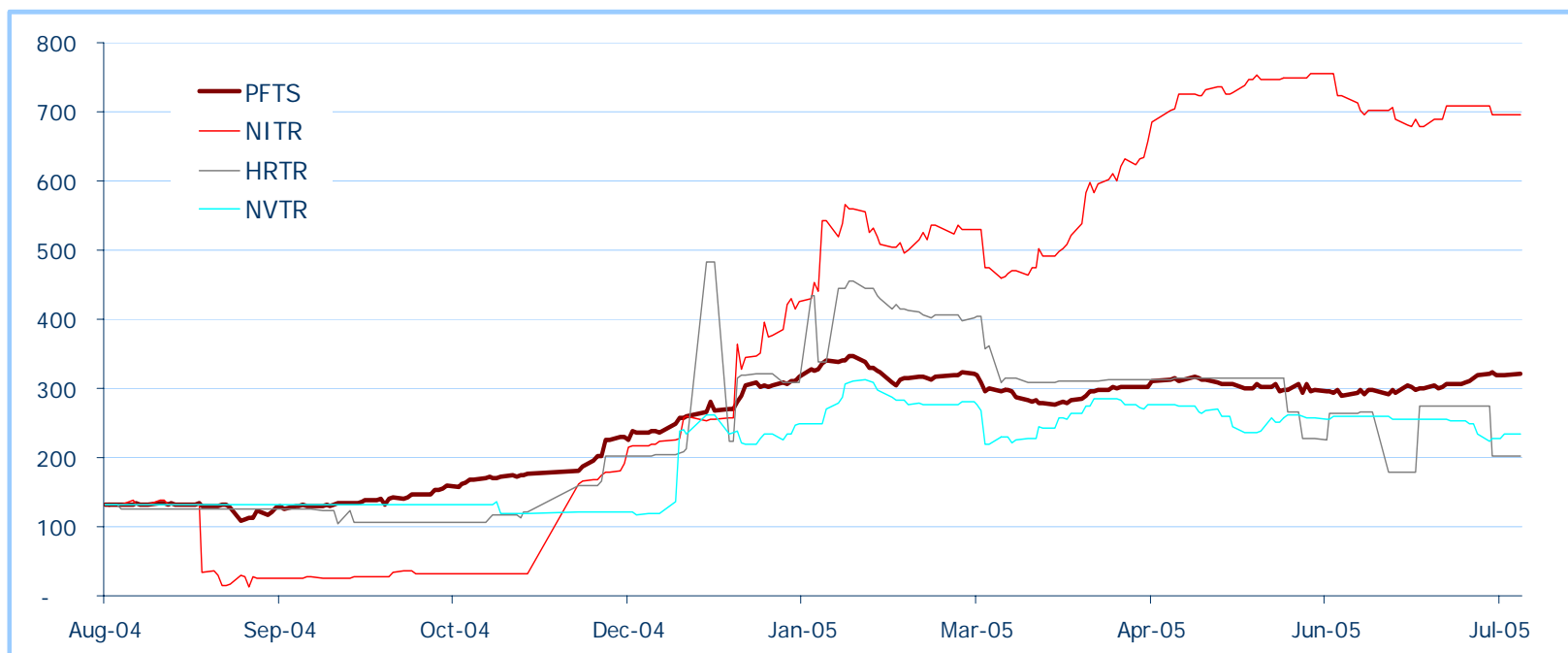
\* Significant portion of NTR's and Vyksa Steel Works' sales is railroad wheels & rims



# Stock Market & Valuations

# Trading

Performance Of Pipe Stocks Relative to the PFTS (mid-market, re-based) \*



	Liquidity	Hist. Spread		Free Float	FF MCap USD mln	Avg. PFTS Monthly Trading		Annualized FF Turnover USD mln
		12-mo ago	Current			shares mln	USD mln	
<b>NITR**</b>	Blue chip	525%	12%	15.0%	50.5	0.27	1.01	24%
<b>HRTR</b>	Medium	36%	400%	2.0%	7.6	0.05	0.01	2%
<b>NVTR</b>	Low	650%	11%	36.5%	25.2	0.08	0.49	23%

\* DPTR is not listed on the PFTS

\*\* NITR's wide spread 12 months ago was due to share issue expectations

Source: PFTS; Concorde Capital estimates

# Recommendations

	Current Price, USD	Multiple-Based Value, USD		DCF-Based 12-Mo Value, USD		Upside/ (Downside)	Recom.
		EV/Output 2004	P/S 2005E	Scenario 2	Scenario 3 (Target)		
NITR	6.25	9.17	7.73	9.69	<b>8.34</b>	33.5%	<b>BUY</b>
HRTR	0.15	0.12	0.11	0.11	<b>0.09</b>	-38.0%	<b>SELL</b>
NVTR	5.75	12.50	8.40	9.86	<b>8.82</b>	53.4%	<b>BUY</b>
DPTR	N/A	114.85	81.31	95.68	<b>86.65</b>	N/M	<b>N/R</b>

Given a wide range of stock value estimates by comparison method, **we rely more on our DCF analysis.**

In our cash flow projections we assumed that in the future **pipe makers will abstain from transfer pricing schemes** due to both pressure from the new government and improving corporate governance.

DCF analysis assuming no transfer pricing to estimate a true value of pipe businesses is given on the page over. It corresponds to our **Scenario 1** when pipe makers start to report their **true financials already in 2005.**

However, with portfolio investors in mind, the **major issue** for our DCF analysis is **the timing** when Ukrainian pipe makers will start reporting their **true cash flows.**

**Scenario 2** refers to the case when pipe companies start reporting their **true financials in 2006.**

**Scenario 3** considers the case when **true financials are reported from 2007** going forward.

**We base our 12-month target prices on a more conservative Scenario 3.**



# Comparison Valuation

## Russian Peers

Company	Mcap, USD mln	Price, USD	EV/Output (USD/mt)
<b>2004</b>			
DPTR	N/A	N/A	N/A
NVTR	69.0	5.75	335.0
HRTR	382.3	0.15	868.9
NITR	336.8	6.25	419.7
<b>Median</b>			<b>419.7</b>
<b>Average</b>			<b>541.2</b>
Tagmet	265.9	0.6	522.6
Vyksa Steel Works	781.1	415.0	701.9
Chelyabinsk Pipe	374.4	0.8	826.7
Seversky Pipe	346.5	7.2	755.9
<b>Median</b>			<b>728.9</b>
<b>Peer Average</b>			<b>701.8</b>
<b>DPTR</b>			
Premium/ (Discount)			N/M
<b>Implied Price, USD</b>			<b>114.85</b>
Upside (Downside)			N/M
<b>NVTR</b>			
Premium/ (Discount)			-52%
<b>Implied Price, USD</b>			<b>12.50</b>
Upside (Downside)			117%
<b>HRTR</b>			
Premium/ (Discount)			24%
<b>Implied Price, USD</b>			<b>0.12</b>
Upside (Downside)			-18%
<b>NITR</b>			
Premium/ (Discount)			-40%
<b>Implied Price, USD</b>			<b>9.17</b>
Upside (Downside)			47%

As both Ukrainian and Russian pipe makers sell most of their products through intermediaries who accumulate a lion's portion of profits, **EV/Output** is, in our view, the **most appropriate multiple for valuation by comparison with Russian pipe companies**.

We included railroad wheels and rims in outputs of NITR and Vyksa Steel Works.

## International Peers

Company	Mcap, USD mln	Price, USD	P/S		EV/EBITDA		P/E	
			2004	2005E	2004	2005E	2004	2005E
DPTR	N/A	N/A	N/M	N/M	N/M	N/M	N/M	N/M
NVTR	69.0	5.75	0.6	0.4	13.2	1.7	31.4	2.7
HRTR	382.3	0.15	3.5	0.8	44.4	4.7	979.7	6.9
NITR	336.8	6.25	0.7	0.5	6.9	1.7	17.4	3.0
<b>Median</b>			<b>0.7</b>	<b>0.5</b>	<b>13.2</b>	<b>1.7</b>	<b>31.4</b>	<b>3.0</b>
<b>Average</b>			<b>1.6</b>	<b>0.6</b>	<b>21.5</b>	<b>2.7</b>	<b>342.8</b>	<b>4.2</b>
Borusan	280.1	8.2	0.8	0.6	7.4	6.6	8.8	10.4
Tubacex	312.6	2.4	0.7	0.5	9.2	5.5	18.6	8.6
<b>Median</b>			<b>0.7</b>	<b>0.6</b>	<b>8.3</b>	<b>6.1</b>	<b>13.7</b>	<b>9.5</b>
<b>Peer Average</b>			<b>0.7</b>	<b>0.6</b>	<b>8.3</b>	<b>6.1</b>	<b>13.7</b>	<b>9.5</b>
<b>DPTR</b>								
Premium/ (Discount)			N/M	N/M	N/M	N/M	N/M	N/M
<b>Implied Price, USD</b>			<b>101.57</b>	<b>81.31</b>	<b>17.83</b>	<b>181.11</b>	<b>4.67</b>	<b>191.48</b>
Upside (Downside)			N/M	N/M	N/M	N/M	N/M	N/M
<b>NVTR</b>								
Premium/ (Discount)			-23%	-32%	59%	-72%	129%	-71%
<b>Implied Price, USD</b>			<b>7.49</b>	<b>8.40</b>	<b>3.54</b>	<b>19.85</b>	<b>2.51</b>	<b>20.13</b>
Upside (Downside)			30%	46%	-38%	245%	-56%	250%
<b>HRTR</b>								
Premium/ (Discount)			373%	33%	433%	-23%	7055%	-28%
<b>Implied Price, USD</b>			<b>0.03</b>	<b>0.11</b>	<b>0.03</b>	<b>0.20</b>	<b>0.00</b>	<b>0.21</b>
Upside (Downside)			-79%	-25%	-83%	32%	-99%	38%
<b>NITR</b>								
Premium/ (Discount)			-8%	-19%	-17%	-73%	27%	-69%
<b>Implied Price, USD</b>			<b>6.80</b>	<b>7.73</b>	<b>7.34</b>	<b>20.54</b>	<b>4.90</b>	<b>19.99</b>
Upside (Downside)			9%	24%	18%	229%	-22%	220%

While comparing to other international peers, we focus on **forward-looking 2005E multiples based on projected true financials** of Ukrainian pipe makers rather than reported figures.



# Company Profiles



# Historical Financials

Income Statement Summary, USD mln	NITR		HRTR		NVTR		DPTR	
	2003	2004	2003	2004	2003	2004	2003	2004
<b>Net Revenues</b>	<b>316</b>	<b>495</b>	<b>75</b>	<b>109</b>	<b>84</b>	<b>121</b>	<b>48</b>	<b>85</b>
Change y-o-y	26%	57%	71%	45%	77%	44%	158%	79%
Gross Profit	48	75	25	20	12	13	2	8
% of Net Revenues	15%	15%	33%	19%	14%	11%	4%	9%
Other Operating Income/Costs, net	(1)	(1)	(1)	(2)	(1)	(1)	1	1
SG&A	(33)	(32)	(8)	(10)	(8)	(7)	(2)	(6)
% of Net Revenues	10%	6%	11%	9%	10%	6%	5%	7%
<b>EBITDA</b>	<b>14</b>	<b>43</b>	<b>15</b>	<b>9</b>	<b>2</b>	<b>5</b>	<b>1</b>	<b>3</b>
EBITDA margin, %	4.4%	8.6%	20.2%	8.0%	2.6%	4.5%	1.3%	3.0%
<b>EBIT</b>	<b>7</b>	<b>35</b>	<b>10</b>	<b>4</b>	<b>1</b>	<b>3</b>	<b>(1)</b>	<b>1</b>
EBIT margin, %	2.1%	7.1%	13.6%	3.5%	0.6%	2.9%	-2.2%	1.1%
Interest Expense	(1)	(2)	(2)	(1)	(0)	(0)	(0)	(0)
Financial income/(expense)	0	0	-	-	-	-	-	-
Other income/(expense)	(0)	(3)	(2)	(1)	-	-	-	-
<b>PBT</b>	<b>6</b>	<b>30</b>	<b>7</b>	<b>2</b>	<b>0</b>	<b>3</b>	<b>(1)</b>	<b>0</b>
Tax	(3)	(11)	(5)	(2)	(0)	(1)	-	-
Effective tax rate	46%	36%	68%	79%	72%	36%	0%	0%
<b>Net Income</b>	<b>3</b>	<b>19</b>	<b>2</b>	<b>0</b>	<b>0.1</b>	<b>2</b>	<b>(1)</b>	<b>0</b>
Net Margin, %	1.1%	3.9%	2.8%	0.4%	0.2%	1.8%	-2.3%	0.4%
<b>Dividend Declared</b>	<b>0.6</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Balance Sheet Summary, USD mln</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>	<b>2004</b>
<b>Current Assets</b>	<b>104</b>	<b>185</b>	<b>35</b>	<b>38</b>	<b>18</b>	<b>25</b>	<b>33</b>	<b>42</b>
Cash & Equivalents	1	26	0	1	0	0	0	1
Trade Receivables	48	34	7	15	8	14	20	19
Inventories	40	52	11	11	7	8	10	17
Other current assets	15	73	16	11	4	3	4	5
<b>Non-Current Assets</b>	<b>153</b>	<b>278</b>	<b>58</b>	<b>58</b>	<b>29</b>	<b>28</b>	<b>20</b>	<b>20</b>
PP&E, net	81	80	54	53	23	24	16	16
Other Fixed Assets	72	198	5	6	6	4	4	4
<b>Total Assets</b>	<b>257</b>	<b>463</b>	<b>93</b>	<b>96</b>	<b>48</b>	<b>53</b>	<b>54</b>	<b>62</b>
<b>Shareholders' Equity</b>	<b>166</b>	<b>186</b>	<b>61</b>	<b>62</b>	<b>34</b>	<b>39</b>	<b>2</b>	<b>2</b>
Share Capital	10	10	5	5	0	3	16	16
Retained Earnings and Other	157	176	56	57	34	36	(14)	(14)
<b>Current Liabilities</b>	<b>52</b>	<b>141</b>	<b>27</b>	<b>33</b>	<b>10</b>	<b>11</b>	<b>51</b>	<b>59</b>
ST Interest Bearing Debt	3	37	10	8	0	0	8	3
Trade Payables	44	97	13	21	8	11	39	19
Other Current Liabilities	6	8	4	4	2	1	5	38
<b>LT Liabilities</b>	<b>39</b>	<b>135</b>	<b>5</b>	<b>1</b>	<b>3</b>	<b>3</b>	<b>0</b>	<b>0</b>
LT Interest Bearing Debt	-	-	-	-	3	3	0	-
Other LT	39	135	5	1	1	0	0	0
<b>Total Liabilities &amp; Equity</b>	<b>257</b>	<b>463</b>	<b>93</b>	<b>96</b>	<b>48</b>	<b>53</b>	<b>54</b>	<b>62</b>
<b>Cash Flow Statement Summary, USD mln</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>	<b>2004</b>
Net Income	3	19	2	0	0	2	(1)	0
Depreciation	7	7	5	5	2	2	2	2
Non-operating and non-cash items	2	11	1	(0)	0	(0)	(0)	0
Changes in working capital	44	(11)	8	5	(2)	(5)	(1)	5
<b>Operating Cash Flow</b>	<b>56</b>	<b>26</b>	<b>16</b>	<b>10</b>	<b>(0)</b>	<b>(2)</b>	<b>(1)</b>	<b>7</b>
Capital Expenditures, net	(6)	(3)	(3)	(6)	(1)	(1)	(0)	(1)
Other Investments, net	(50)	(128)	2	(0)	0	(0)	0	0
<b>Investing Cash Flow</b>	<b>(56)</b>	<b>(131)</b>	<b>(1)</b>	<b>(6)</b>	<b>(0)</b>	<b>(2)</b>	<b>(0)</b>	<b>(1)</b>
Net Borrowings/(repayments)	(0)	130	(3)	(2)	(1)	-	1	(5)
Dividends Paid	(0)	(1)	-	-	(0)	(0)	-	-
Other	-	(0)	(12)	(2)	2	3	(0)	(0)
<b>Financing Cash Flow</b>	<b>(0)</b>	<b>129</b>	<b>(15)</b>	<b>(4)</b>	<b>1</b>	<b>3</b>	<b>1</b>	<b>(5)</b>
<b>Net Cash Inflows/Outflows</b>	<b>(0)</b>	<b>25</b>	<b>0</b>	<b>1</b>	<b>0</b>	<b>(0)</b>	<b>(0)</b>	<b>1</b>

In the company profiles, we address the transfer pricing issue that distorts official financial statements.

To this end, we show:

the key financials that the companies reported in 2004 and are likely to report in 2005 - 2006;

our estimates of true financials that reflect the economics of respective businesses.

# Nyzhnyodniprovsky Pipe Rolling (NITR)

## BUY

Target price **USD 8.34**

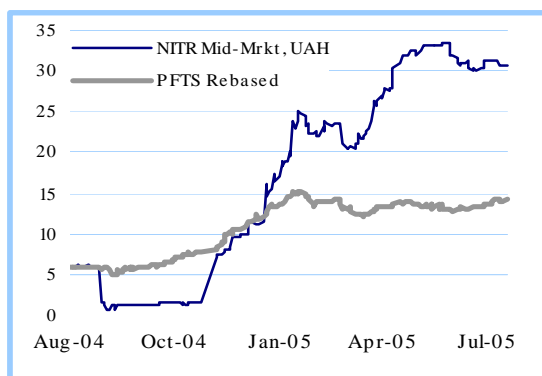
### Market Information

No of Shares, mln	53.9
Par Value, USD	0.05
<b>Market price, USD</b>	<b>6.25</b>
MCap, USD mln	351.9
Free Float, %	15%
FF MCap, USD mln	50.5

### Stock Ownership

Interpipe & management	85%
Minorities	15%

# of employees 9,609



**Profile:** Ukraine's largest pipe maker by output (22.4% share in 2004) and #3 by design capacity (900 ths mt p.a.). The only producer of railroad wheels, tires & rings in Ukraine and one of three in the CIS able to make up to 256 ths mt of wheels and 70 ths mt of tires and rings p.a. The company's pipe business is focused on high quality seamless OCTG pipes. Welded pipes are also present in product assortment. NPR possesses open hearth steel making capacities that enable it to both save on raw material costs and produce customized railroad wheels & tires from in-house steel. Designed steel capacity is 700 ths mt p.a. NPR's location in industrialized Dnipropetrovsk oblast endows the plant with logistical benefits – proximity to raw material suppliers (mainly DMK Dzerzhynskogo) and transportation links.

**Products & Markets:** The company exports over 70% of its pipes, and 50% of pipe sales (in terms of tonnage) are to non-CIS markets. NPR's railroad wheels sales are shifting from domestic markets to abroad (in 2003, 56% of wheels & tires were sold in Ukraine, while in 10M04 over 60% of wheels & tires were sold to Russia). The plant's 12–377 mm OD product range includes:

- casing and production pipes and couplings, heavy-weight drill pipes
- hot-rolled and cold-drawn general purpose tubes, boiler plant pipes and tubing
- bearing tubes
- high precision tubes
- electric-welded round and shaped tubes

NPR's pipes are in conformity to local UkrSEPRO and GOST systems, certified by the API and the TÜV NORD Certification Center.

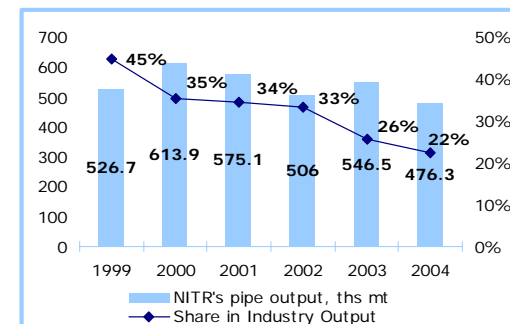
**Transfer pricing:** NITR's top-line is undercut by transfer pricing schemes (at least by 15 – 20%), as the company's export operations are carried out through Interpipe-related traders. We do not see any evidence of artificial cost inflation, though.

**Ownership issues:** Intended sale of Interpipe by current owners may be an additional driver of the stock's future appreciation.

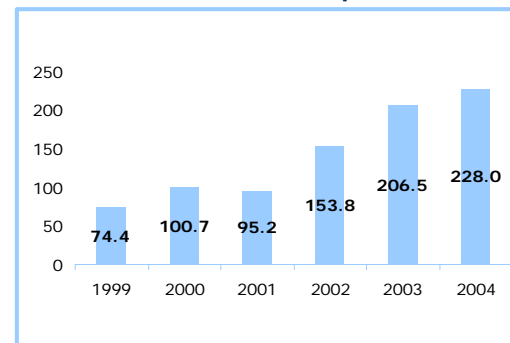
	P/S	P/S True	P/E	P/E True	EV/EBITDA	EV/EBITDA True
<b>2004</b>	0.7	0.5	17.5	2.8	11.3	2.6
<b>2005E</b>	0.6	0.5	8.6	3.0	5.8	2.3
<b>2006E</b>	0.5	0.5	21.2	3.6	10.4	2.4

	Reported Sales USD mln	True Sales USD mln	EBITDA margin		Net margin	
			Reported	True	Reported	True
<b>2004</b>	494.8	641.2	8.6%	29.5%	3.9%	19.8%
<b>2005E</b>	596.5	702.6	11.4%	24.8%	6.6%	16.2%
<b>2006E</b>	624.4	735.5	5.3%	19.6%	2.5%	13.7%

### Pipe Output, '000 mt



### Rail Wheels & Rims Output, '000 mt







# Khartsyzk Tube (HRTR)

## SELL

Target price **USD 0.09**

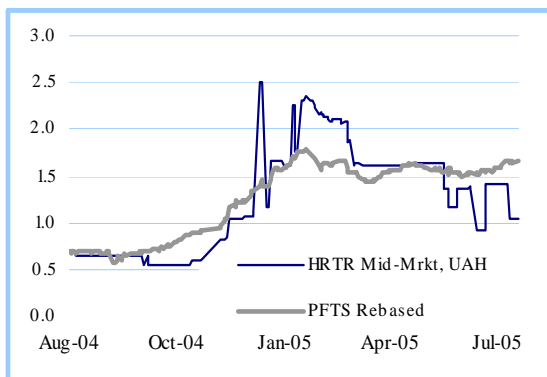
### Market Information

No of Shares, mln	2,548.8
Par Value, USD	0.01
<b>Market price, USD</b>	<b>0.15</b>
MCap, USD mln	382.3
Free Float, %	2%
FF MCap, USD mln	7.6

### Stock Ownership

SCM	98%
Minorities	2%

# of employees **6,613**



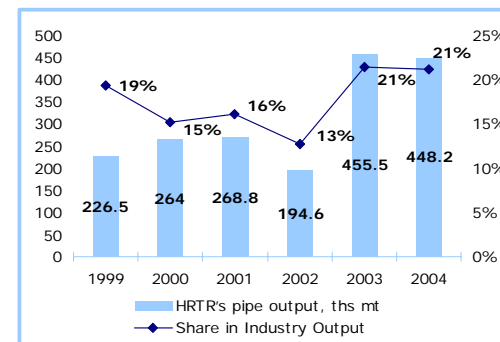
**Profile:** The largest Ukrainian pipe maker in terms of installed capacity (1.6 mln mt of pipes annually) and second largest by output (21.1% share in 2004). Its product assortment encompasses over 500 items.

**Products & Markets:** HRTR's core product is large diameter steel pipes, with corrosion-proof coating, used for construction of oil and gas-main pipelines. Its pipes were used in construction of trunk oil & gas pipelines in Russia, Turkmenistan, Azerbaijan, Uzbekistan, Kazakhstan as well as in the construction of international trunk oil pipelines Druzhba and Urengoy-Pomary-Uzhgorod. Current demand for pipes manufactured in Khartsyzk stems chiefly from the new needs of the reviving oil & gas sector in the CIS and from previously constructed pipelines repair & maintenance. The key consumer of HRTR's pipes is Gazprom accounting for ~60% of HRTR's tonnage sales. Gazprom buys mostly Ø1,420 mm pipes.

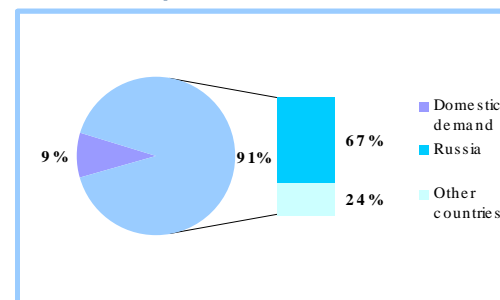
**Transfer pricing:** The company heavily engages in transfer pricing, selling nearly all of its pipes through operators related with its key shareholder, SCM, such as Leman Pipe and Azovstal. We estimate that its sales are undercut by at least 70%. On the other hand, cost of raw materials reported on HRTR's P&L is also severely understated due to a tolling scheme HRTR is involved in with its main strip supplier, Azovstal. In addition, HRTR's reported top line includes revenue from sales of steel and railcars produced by plants under SCM's control.

**Share issue:** In early 2005, HRTR increased its charter fund 4.6 times raising USD 19.8 mln. The proceeds will be used to construct a new production line for manufacturing single-weld pipes with an outer diameter of 711 – 1,420 mm. Project cost is estimated at USD 18.5 mln and its completion is expected in 2006. Single-weld large diameter pipes are superior in quality to double-weld pipes HRTR was able to make before and enjoy a strong demand from Gazprom.

### Pipe Output, '000 mt



### HRTR's Export Structure, 2003



	P/S	P/S True	P/E	P/E True	EV/EBITDA	EV/EBITDA True
<b>2004</b>	3.5	1.0	N/M	8.3	44.4	5.4
<b>2005E</b>	2.7	0.8	N/M	6.9	20.0	4.7
<b>2006E</b>	3.2	1.0	N/M	8.8	23.3	5.5

	Reported Sales USD mln	True Sales USD mln	EBITDA margin		Net margin	
			Reported	True	Reported	True
<b>2004</b>	109.1	403.4	8.0%	18.0%	0.4%	11.5%
<b>2005E</b>	144.2	485.0	14.1%	18.0%	1.6%	11.5%
<b>2006E</b>	118.3	397.7	14.1%	17.7%	1.6%	11.0%



# Novomoskovsk Pipe (NVTR)

## BUY

Target price **USD 8.82**

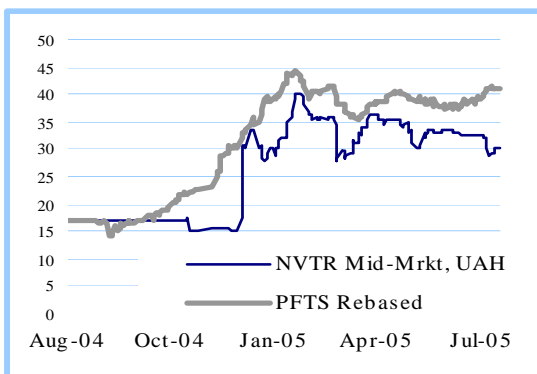
### Market Information

No of Shares, mln	12.0
Par Value, USD	0.05
<b>Market price, USD</b>	<b>5.75</b>
MCap, USD mln	69.0
Free Float, %	36.5%
FF MCap, USD mln	25.2

### Stock Ownership

Interpipe	63.5%
Minorities	36.5%

# of employees 3,632



**Profile:** One of the largest producers of welded pipes for oil- and gas-main pipelines in the CIS. Its pipes were used in the construction of the Odesa-Brody oil pipeline, the Druzhba gas-main pipeline and pipelines in Siberia and Turkmenistan. NVTR ranks #2 in Ukraine by pipe capacity (1,337 ths mt pipes annually). It also ranks 3<sup>rd</sup> by pipe output (10.1% share in 2004). NVTR purchases around 70% of strip for its pipes from domestic suppliers (Azovstal, Illich Metal, Zaporizhstal). Russian Novolipetsk Iron & Steel Mill and Severstal provide most of the balance.

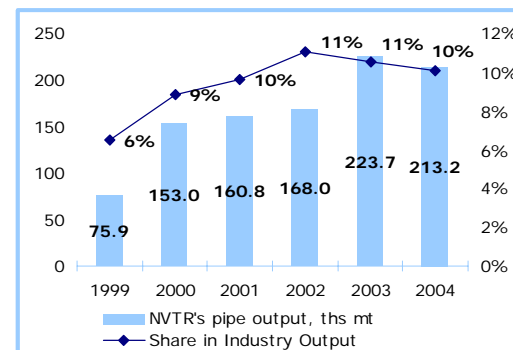
**Products & Markets:** NVTR's core product is large-diameter (Ø1,020 mm) and middle-diameter (Ø159 - 529 mm) welded pipes for oil & gas and general purpose pipelines. Russian Transneft traditionally places orders for this type of pipe. Apart from Russia, the company's largest consumer is Turkmenistan. NVTR also supplies other CIS countries, specifically, Uzbekistan and Kazakhstan. Plant's installed capacity for manufacturing of large- & middle-diameter pipes comprises 98% of its total installed capacity. In addition, the plant produces welded pipes for water and gas steam communications, food and machine building industries. These are mostly small-diameter pipes (Ø20-75 mm).

NVTR is a monopoly producer of middle-diameter welded pipes in the CIS, as its competition focuses mostly on seamless middle-diameter pipes, which are more expensive. NVTR's pipes are certified according to UkrSEPRO and GOST systems as well as by the API and the TÜV NORD CERT Certifying Body.

In addition to pipes, NVTR produces enamelled and galvanized dishware which accounts for a minor portion of its revenues.

**Transfer pricing:** Like NITR, NVTR practices related-party transactions when a large share of profits is accumulated by trading companies associated with NVTR's controlling shareholder, Interpipe. We estimate that NVTR's reported sales are underestimated by at least 10%. Possible sale of Interpipe talked about vastly since year beginning should result in a substantial improvement of NVTR's reported financials to reflect its true sales and earnings.

Pipe Output, '000 mt



	P/S	P/S True	P/E	P/E True	EV/EBITDA	EV/EBITDA True
<b>2004</b>	0.6	0.5	31.4	5.5	13.2	3.6
<b>2005E</b>	0.5	0.4	5.5	2.7	3.3	1.7
<b>2006E</b>	0.4	0.4	6.6	2.9	3.8	1.8

	Reported Sales USD mln	True Sales USD mln	EBITDA margin		Net margin	
			Reported	True	Reported	True
<b>2004</b>	121.3	136.1	4.5%	14.8%	1.8%	9.2%
<b>2005E</b>	151.7	170.1	13.6%	22.9%	8.3%	15.0%
<b>2006E</b>	157.0	176.1	11.2%	20.8%	6.6%	13.5%



# Dnipropetrovsk Pipe (DPTR)

## Not Rated

Target price **USD 86.65**

### Market Information

No of Shares, mln	1.06
Par Value, USD	16.28
<b>Market price, USD</b>	<b>N/A</b>
MCap, USD mln	N/A
Free Float (est.), %	5%
FF MCap, USD mln	N/M

### Stock Ownership

IUD group (est.)	95%
Minorities	5%

# of employees **4,371**

**Profile:** Ranks 4<sup>th</sup> in Ukraine by design capacity (583 ths mt of pipes annually) and 5<sup>th</sup> by output (8.1% share in 2004).

Most steel feedstock (strip for welded pipes and billets for seamless pipes) is purchased from domestic suppliers (strip from Zaporizhstal and MMK Illich Metal, tubular billets from DMK Dzerzhynskogo and DMK Petrovskogo).

**Products & Markets:** The company has a lesser exposure to OCTG segment than its peers NITR, NVTR and HRTR. Therefore, its pipes are relatively cheaper and markets are more diversified industry-wise. DPTR caters to construction industry, agriculture and utilities (boiler, water & gas pipes), machine building and petrochemical industry. Although also export-driven, it sells a larger portion of its pipes domestically than NITR, HRTR and NVTR. DPTR's product range includes:

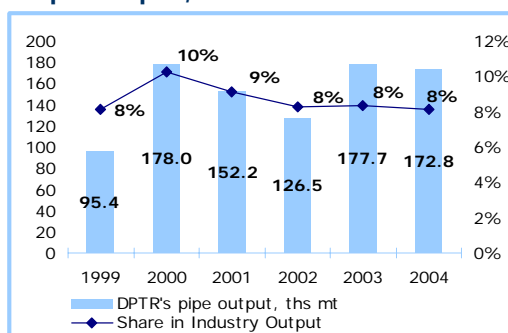
- **hot-rolled seamless steel pipes**  
for oil refining and petrochemical industry; for gas tube lines of gas lift systems; for steam-boilers and conduits
- **welded pipes**  
general purpose and water and gas steel pipes
- **cold-drawn seamless steel pipes**  
for oil refining and petrochemical industry; for shipbuilding; precision steel pipes; square and rectangular profile seamless steel pipes; bimetallic tubes for bearings and machine parts.

**Transfer pricing:** DPTR sells a portion of its output through a number of traders associated with its holding company, IUD. We estimate that DPTR's sales are under-reported by ~10%, a significantly lower percentage than that for HRTR or NITR.

**CapEx:** DPTR embarked on a major technical re-equipment in 2004 with a total cost of USD 2.6 mln. It will be completed in 2005, to which end USD 1.0 mln will be spent this year. In addition, in 2005-2006 the company will reconstruct its rolling and reduction mills, which will allow DPTR to expand its product assortment. These works will be primarily financed by debt. DPTR plans to raise EUR 6-8 mln in loans to accomplish this project.

	Reported Sales	True Sales	EBITDA margin		Net margin	
	USD mln		USD mln	Reported	True	Reported
<b>2004</b>	85.2	103.7	1.1%	20.3%	0.4%	12.8%
<b>2005E</b>	130.8	144.8	14.8%	21.9%	8.8%	14.7%
<b>2006E</b>	135.4	149.9	11.3%	18.7%	6.0%	12.1%

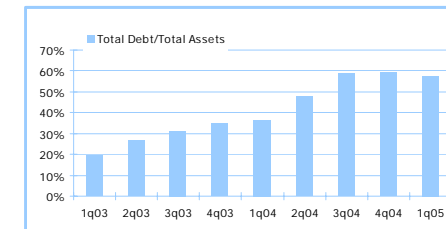
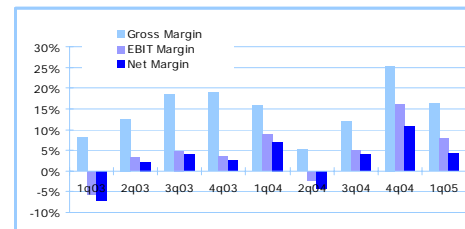
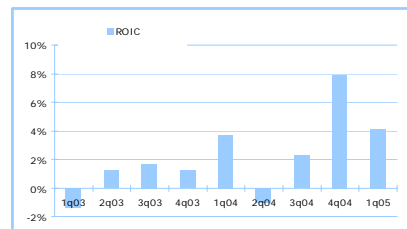
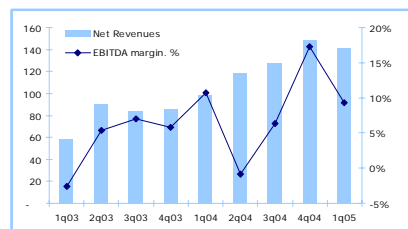
Pipe Output, '000 mt





# Ratio Analysis Quarter By Quarter

## NITR: profitability improved, debt grew in 2004



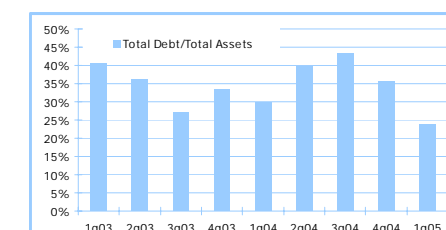
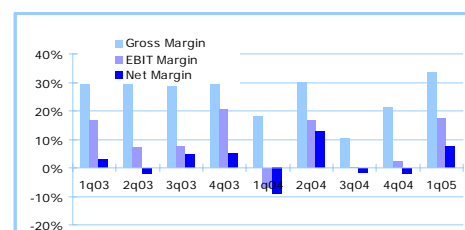
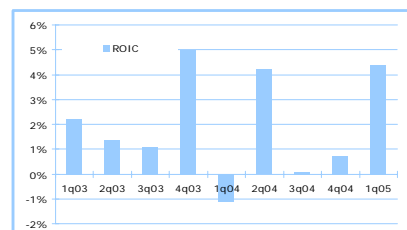
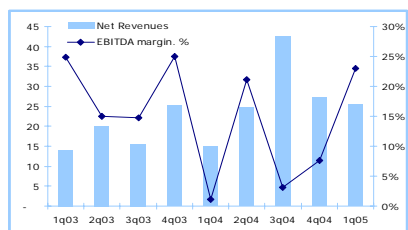
Revenue, margins and ROIC grew in 2004. We attribute this to two factors:

- Interpipe's attempt to reduce transfer pricing and make its business more transparent;
- High ferroalloy prices, as NITR exported ferroalloys produced by Interpipe's another company, Nikopol Ferroalloy.

Despite a general growing trend, profitability measures were volatile in 2003 - 2004

Debt / Assets ratio kept growing throughout 2003 – 2004, as NITR borrowed funds from its holding company Interpipe to engage in acquisitions of Nikopol Ferroalloy and Kryvorizhstal as a Variable Interest Entity

## HRTR: profitability and debt/assets volatile



Despite growing quarterly revenues, in 2004 profitability measures were vastly volatile and generally lower than in 2003.

Lower profitability has to do with HRTR operating under tolling with Azovstal, its key strip supplier, who accumulated a large share of HRTR's profits.

Debt / Assets ratio fluctuated around the level of 30%, which indicates the company's financial stability.

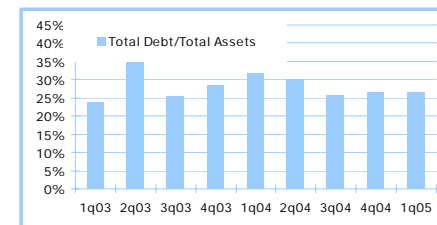
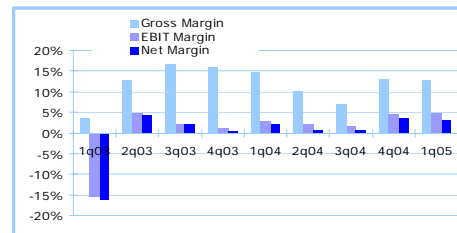
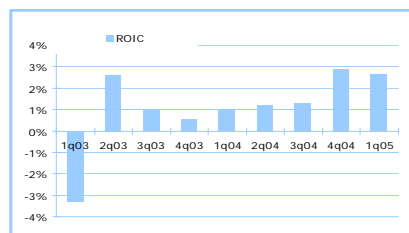
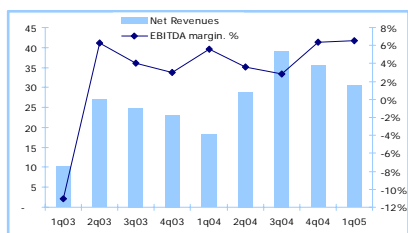
In 3Q04 - 1Q05, Debt / Assets ratio exhibited a declining pattern, but we believe it will grow by year end due to new financial debt HRTR will assume in 2005 to finance its CaPEX.

Financials according to Ukrainian Accounting Standards; quarterly ROIC is not annualized



# Ratio Analysis Quarter By Quarter(Cont-ed)

## NVTR: profitability volatile, debt flat

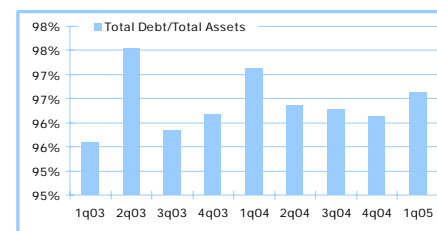
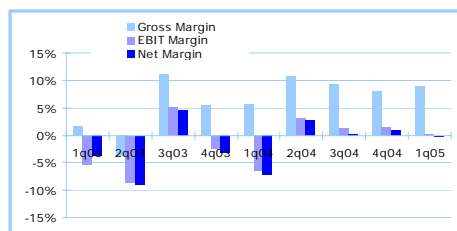
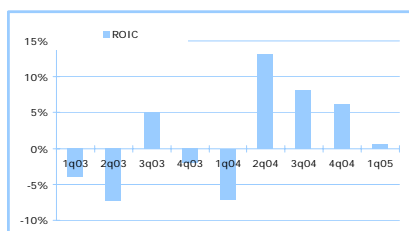
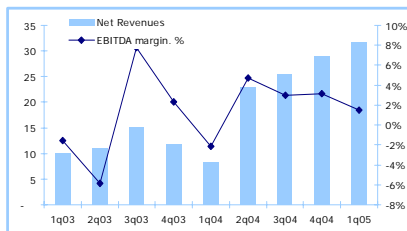


In 2004, the company's revenue grew and profitability improved. On a quarterly base, however, profitability was highly volatile in 2003 – 2004.

The company appears financially stable, as indicated by its flat Debt / Assets ratio.

In our view, top-line improvement was due more to Interpipe cutting its transfer pricing than just to favorable market for pipes.

## DPTR: profitability on the upward trend, debt/assets ratio high and volatile



Revenue exhibited a clear upward trend on the back of a favorable market situation in 2004. Profitability metrics slightly improved.

The company's Debt / Assets ratio is enormously high.

Apparently, efforts by the company's owner, IUD group, to recover the company from its previously near-to-bankrupt state are starting to pay off.

This is explained by the fact that the company bore losses up until 2004, which resulted in a negative equity.

Positive market outlook in 2005 should result in both top-line and bottom-line improvements this year.

We expect DPTR's financial debt to increase in 2005, as the company will borrow to finance its CapEx.

*Financials according to Ukrainian Accounting Standards; quarterly ROIC is not annualized*



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