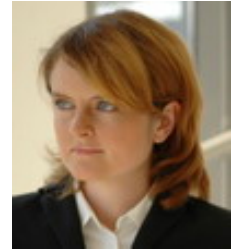




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Analyst's Notebook

Ukraine/Machine Building
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****Editor's Note:** The Analyst's Notebook is Concorde Capital's fast response tool for keeping our coverage of the Ukrainian market as up to date as possible. Unlike our more in-depth desk notes and reports, Analyst's Notebook provides rapid feedback on breaking news in the Ukrainian market. Analyst's Notebook gives you our analysts' first impressions of a situation and may set the table for further investigation. Our analysts will use their experience in their sectors to take a look at the situation and provide insight or speculate on possible scenarios. We want to emphasize however, this product consists mostly of the analyst's intuition and may require further analysis.

MSICH: Aviation With A Dash Of Politics

Motor Sich's (MSICH) net revenues were slightly higher than what we expected for 2005, while gross and net profitability margins were below our expectations. Based on information from the company's AGM, management interviews and multiples valuation, we see no reason to change our target price of USD **115** and **Buy** recommendation.

Sales up, profits down

Motor Sich's net revenues increased by 0.7% (in hryvnya terms) to USD 213.8 mln, which is slightly above our previous projection of USD 211.0 mln. However, gross profit declined by 7% to USD 71.3 mln (33% gross margin) due to the appreciation of the hryvnya by 5% in April 2005, and an increase in prices for energy.

The fact that the company, for the most part, has a monopoly in this segment, should allow it to adjust its contract prices in accordance with the appreciation of the national currency in 2006. Prices for energy supplies will continue to grow and are expected to make up 11% of production costs in 2006, up from 7.7% in 2005. In addition the company plans to increase salaries from their current level (~USD 200). However, this will be partially compensated by a decrease in social spending.

In general we expect gross and net profitability margins to slightly improve in 2006, but still not reach 2004 levels. The company's EBITDA grew by 23% to USD 22.5 mln in 2005 due to less losses in on currency operations, and a decrease in SG&A, while net income decreased by 8% to USD 9.7 mln (Net margin of 4.5%).

Growth ahead

Based on the company's order book Motor Sich's management projects a 12% increase in sales in 2006, in line with our projections. Russia is still the main consumer of MSICH products, accounting for over 50% of sales, but the company is also taking a look at China for possible future development. In April MSICH plans to sign a 3-year contract with China for USD 30 mln.

Russia: a long-term threat

Despite the statements made by the CEO of the plant, MSICH does not believe Russia will be able to start serial production of engines for military helicopters at the Klimov Plant. To this point no Russian officials have confirm this claim. According to MSICH's CEO Vyacheslav Boguslayev, this project would cost Russia USD 220 mln, and the government decided it was too expensive. Presently most of the spare parts used for assembling helicopters at the Klimov plant are delivered by MSICH.

Competition between Ukraine and Russia in helicopter and airplane engine production may grow fiercer in the long term – when a new generation of engines is developed. However, at present, Russia does not have capacities for the serial production of helicopter engines, making it more economically feasible to continue buying them from Ukraine's Motor Sich.

New plane, new orders

Orders for the An-148 new regional plane are increasing. The most recent number we heard was 24 planes in 2006-08. This would bring USD 67 mln of additional sales to Motor Sich. In 2006, the company plans to produce four engines for this plane.

From Dontesk To Kyiv

Vyacheslav Boguslayev, CEO of Motor Sich, is fifth on the Party of Regions election list. We believe he is a shoe-in for the Rada, as according to the most recent polls, Regions will get the largest share of votes - 26-31%. Thus, Boguslayev, and his party will be in a good position to push for more state support for state-owned aviation plants, meaning new orders for Motor Sich.

Multiples Valuation

	Sales			EBITDA Mgn		Net Mgn		MCap	P/S		EV/EBITDA			P/E				
	2004	2005	2006	2004	2005	2006	2004		2005	2006	2004	2005	2006	2004	2005	2006		
Motor Sich	204.3	213.8	239.5	15%	19%	18%	5%	5%	176.6	0.9	0.8	0.7	6.1	5.5	5.1	17.7	18.2	15.4
Rolls-Royce Group PLC	11,402.3	11,256.7	12,103.2	11%	15%	16%	3%	7%	13,133.7	1.2	1.2	1.1	10.9	8.1	7.0	33.5	16.3	13.7
United Technologies Corp.	36,700.0	45,754.5	48,246.6	15%	15%	16%	8%	8%	59,845.8	1.6	1.3	1.2	12.1	9.5	8.8	21.5	16.8	15.0
Sneema	9,258.8	8,490.1	8,971.8	10%	13%	n/a	3%	5%	8,329.3	0.9	1.0	0.9	8.8	7.5	n/a	26.2	20.3	n/a
Mitsubishi Heavy Industries Limited	22,813.9	23,585.7	23,886.7	7%	6%	8%	1%	1%	15,293.2	0.7	0.6	0.6	14.4	15.3	12.0	73.0	61.7	33.6
Honeywell International Inc	25,601.0	30,169.7	31,901.1	10%	13%	14%	5%	7%	31,864.7	1.2	1.1	1.0	13.8	8.9	7.9	24.9	15.3	13.4
Sequa Corp.	1,864.1	n/a	n/a	9%	n/a	n/a	1%	n/a	891.8	0.5	n/a	n/a	8.9	n/a	n/a	84.1	n/a	n/a
Mean				10%	12%	13%	3%	6%		1.01	1.03	0.98	11.48	9.84	8.90	43.86	17.17	14.03
Median				10%	13%	15%	3%	7%		1.03	1.06	1.00	11.47	8.99	8.34	29.86	16.54	13.70
Prem/discont to mean										-0.15	-0.20	-0.25	-0.47	-0.45	-0.43	-0.60	0.06	0.10
Prem/discont to median										-0.16	-0.22	-0.26	-0.47	-0.39	-0.39	-0.41	0.10	0.12
Implied Target Price at mean										99.6	106.2	112.8	167.35	190.4	164.2	211.1	80.2	77.6
Implied Target Price at median										100.8	108.7	115.1	167.33	172.0	152.5	143.7	77.2	75.8
Upside by mean										17%	25%	33%	97%	124%	93%	148%	-6%	-9%
Upside by median										19%	28%	35%	97%	102%	79%	69%	-9%	-11%

Source: Thomson Financials, Concorde Capital

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