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Analyst's Notebook

Ukraine/Banking
June 30, 2006

Banca Intesa/Ukrsotsbank Deal in Doubt?

Banca Intesa's plan to acquire Ukrsotsbank is running into obstacles because of a conflict between Ukrsotsbank's current owner, Viktor Pinchuk, and a minority shareholder, Cyprus-registered Tempsford Investments. Tempsford has obtained a court order blocking a planned share emission, which was assumed in the purchase agreement. The minority shareholder has also asked Italy's national bank not to permit the deal, and the Italian national bank has sent queries to Ukrsotsbank about the issue. Banca Intesa issued a statement this week saying it and Ukrsotsbank were jointly analyzing the situation. Our confidential sources confirm that Banca Intesa has warned that it could walk away from the deal.

According to the agreement, Banca Intesa would pay USD 1.16 bln for an 85.4% stake, which would then be increased to 88.1% through disproportional participation in the share emission. Cyprus-registered Tempsford, which owns about 7.3% of the bank, and other minority shareholders filed suit claiming they were illegally prevented from participating in the share emission. Ukrsotsbank said Tempsford and others showed up late. The court of first instance supported Tempsford and blocked the share emission. It is not completely clear who owns Tempsford. The woman who spoke to media on Tempsford's behalf earlier this year was an associate of one of Pinchuk's former partners, Mykhailo Shchegolevsky. However, Ukrsotsbank says all minority shareholders trying to block the deal represent the interests of the Privat business group, owner of rival Privatbank.

Nobody Interested in Killing the Deal

We think Tempsford, whoever it represents, is looking for money, not to kill the deal. If Banca Intesa were to back out, Ukrsotsbank could easily find another buyer. Intesa's rivals such as Societe Generale and Erste Bank would move in quickly. But by blocking the share emission, and thus putting Ukrsotsbank at risk of failing to meet capital adequacy requirements, Tempsford can demand from Intesa a premium to the deal price (USD 0.36) or the return of the disputed 2.7% stake, which is the amount by which the minority shareholders' stakes would be diluted if the share is completed.

We believe Banca Intesa will ultimately close the deal after renegotiating certain aspects of the purchase agreement. Since court battles over share emissions can drag on for years, Banca Intesa is actively looking for a way to settle. Presumably Banca Intesa is asking Pinchuk to slightly lower his price. The Italians might also reach a separate agreement with the minority shareholders. Banca Intesa is eager to gain a strong foothold in the Ukrainian market and there is no other comparable takeover target.

Should Portfolio Investors Worry?

We doubt any renegotiation would materially affect portfolio investors. If the share emission is canceled, a new one would be conducted, as Ukrsotsbank badly needs to increase its capital. Any shareholder who subscribed to the canceled emission would have to go through the process a second time. Shareholders who did not subscribe for whatever reason would benefit as they would get a second chance. Shareholders who bought in after the subscription might get a windfall, as the share emission's dilution effect has been priced into the stock since late January. However, it is very unlikely the share emission will be canceled.

In the meantime Pinchuk has found a way of temporarily covering Ukrsotsbank's shortage of capital. The holding company through which he owns the bank, Ferrotrade International, recently granted the bank a USD 19.3 mln loan on subordinated terms. This will allow the bank temporarily to avoid the risk of violating National Bank's capital adequacy requirements.

We maintain our BUY recommendation on the stock and our target price of USD 0.45.

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