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Coal

Growth In The Pipeline

Komsomolets Donbassa (SHKD: BUY)

Market Price, USD	0.25
12M Target, USD	0.60
Upside/Downside	140%

Krasnoarmiyska-Zakhidna (SHCHZ: BUY)

Market Price, USD	0.40
12M Target, USD	0.80
Upside/Downside	100%

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Investment Case

Company	Bloomberg	XETRA
Komsomolets Donbassa	SHKD UZ	n/a
Krasnoarmiyska-Zakhidna	SHCHZ UZ	n/a

	Price USD	12M TP USD	Upside	Rec.
SHKD	0.25	0.60	140%	BUY
SHCHZ	0.40	0.80	100%	BUY

Note: Prices set for blocks available on the market as coal stocks are highly volatile and exposed to manipulation due to their low liquidity.

	# of sh., mln	MCap, USD mln	Free Float %	USD mln
SHKD	334.9	83.7	2.5	2.1
SHCHZ	848.5	339.4	2.1	7.1

Production Forecasts, mln mt:

	2006E		2007E	
	New	Old	New	Old
SHKD	3.10	2.96	3.35	3.13
SHCHZ	6.82	6.86	7.50	7.51

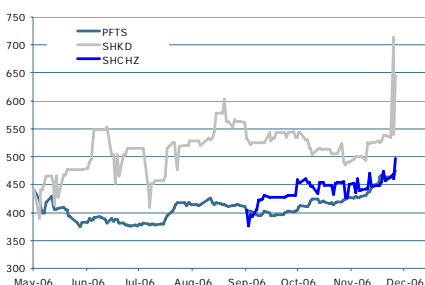
The IPO of Russia's Raspaskaya Mine in mid November set an appealing benchmark for the sector and Ukrainian coal mining stocks responded by gaining nearly 20% over the last month lifting the segment into the group of top performers in the metals & mining sector this year. Both SHKD and SHCHZ still have substantial upside potential, trading currently at undeserved discounts to Russian and global peers. Encouraged by robust industry fundamentals and strong market momentum, we upgrade both stocks with new targets implying three-digit upsides.

Growth Leaders In 9M06. SHKD outperformed total steam coal sector growth of 8% yoy with a 16% yoy increase to 2.6 mln mt (6% of steam coal output). SHCHZ expanded its production by 10% yoy to 5.1 mln mt notwithstanding production drop in coking coal segment and accounts currently for 22% in total Ukrainian coking coal output.

Komsomolets Donbassa will benefit from growing domestic demand for lean coal due to its affiliation with SCM, who is likely to lobby shipments to state-owned electricity generating companies. Moreover, the quality of SHKD's lean coal makes it competitive in CIS as well. After the company opens a new coal seam in late 2006 it will increase output by 8% yoy to 3.35 mln in 2007. The market has welcomed transparency improvement as evidenced by its surged margins in 9M06: 29.2% EBITDA margin and 14.4% net margin compared to 17.5% and 1.4% in 9M05, respectively.

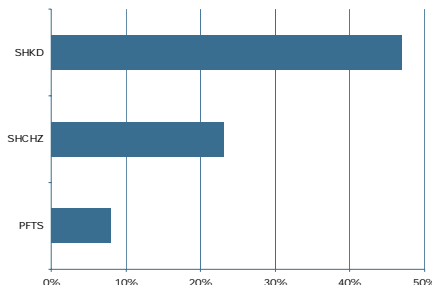
Krasnoarmiyska-Zakhidna, a producer of hard coking coal of comparable to Russia in terms of quality and competitive mining cost, will benefit from the deficit of hard coking coal in Ukraine estimated at 14-16 mln mt. We forecast SHCHZ to increase its output by 8% yoy in 2007 to 7.5 mln mt. The company's investment program launched in 2006, suggests coal production will increase to 10 mln mt per annum by 2010. The deterioration of financial reporting observed since the beginning of this year limits upside to a modest 100%. Recalculated for real-life economics, the upside would at least double.

Market*

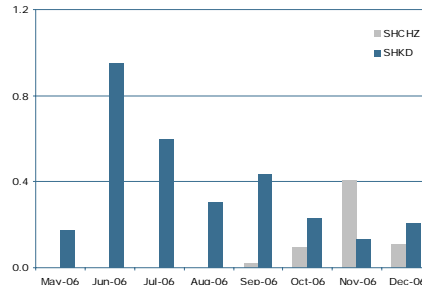


Source: PFTS. Note: SHCHZ was listed on the PFTS in mid-September; SHKD became liquid on the PFTS in May

Performance YTD*



Monthly Volumes (PFTS), USD mln



Price Ratios

	MCap USD mln	EV/S		EV/EBITDA		P/E		EV/Output, USD/mt
		2006E	2007E	2006E	2007E	2006E	2007E	2006E
Komsomolets Donbassa	83.7	0.79	0.71	2.74	2.38	5.67	4.76	27.0
Krasnoarmiyska-Zakhidna	339.4	1.24	1.08	3.35	2.84	7.28	5.99	49.9

Source: PFTS, Concorde Capital. Note: Multiples are calculated based on reported financials.

Industry Snapshot

Sector Performance 9M06: Private Mines Lead

Steam Coal Output Up: SHKD Outperforms the Sector

Ukrainian steam coal output grew by 8.9% yoy in 9M06 to 36.3 mln mt on the back of growing demand from electricity generation companies (GenCos). SCM-owned Komsomolets Donbassa (SHKD), with a 16% yoy increase in coal extraction, was among the sector's growth leaders and by itself contributed ~1% to total steam coal production growth.

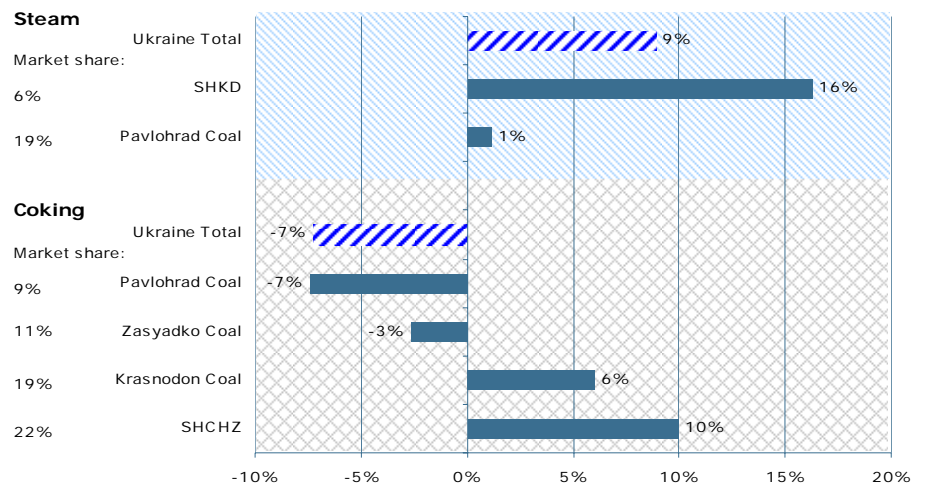
SCM-related Steam Coal Mines Have Friends in High Places

We attribute the growth of output at Komsomolets Donbassa to the fact that the mine got the green light to increase shipments to state owned GenCos after the Party of Regions, associated with SCM owner Rinat Akhmetov, won a majority in parliamentary following the March Rada elections. Moreover, Vostok Energo (generator), controlled by SCM, is on the rise filling the order books of related Pavlohrad Coal and Komsomolets Donbassa. Thanks to SCM's lobbying power, we expect these mines to increase deliveries to state electricity generators in the mid-term.

Coking Coal: Two Private Mines Save Sector From a Larger Drop

Coking coal production decreased 7.3% yoy to 22.8 mln mt in 9M06, due to lower extraction by state owned mines. While aggregate private mine extraction grew by 2.4% yoy, output at state mines slowed by 9.7% yoy. Two major private producers of hard and semi hard coking coal, Krasnoarmiyska-Zakhidna (SHCHZ) and Krasnodon Coal, increased production by 10% and 6% in 9M06, respectively. Together, these mines, which made up 41% of total domestic output, saved the coking coal sector from a large drop in production.

Private mines vs. total production in 9M06, (growth yoy)



Source: Energobusiness, Concorde Capital estimates

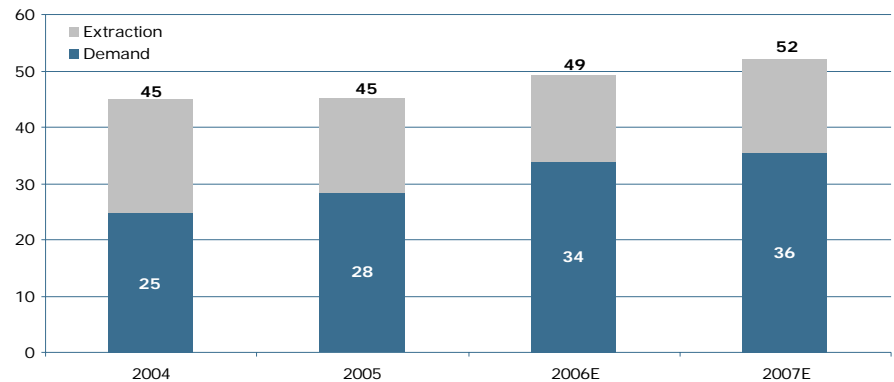
Note: Pavlohrad Coal produces high-grade steam and semi-soft coking coal.

Ukrainian Coal Market: Seeking Balance

Domestic Steam Coal Market Balanced

Ukraine consumes almost all of its domestic steam coal and is fairly balanced, with imports and exports each totaling less than 1% of the market. Production of domestic steam coal is enough to meet the 19% yoy growth in electricity generator's demand in 2006. Mines with higher calorific coal content, including SHKD, will be the major beneficiaries of a *gas for coal* substitution at thermal power plants, due to higher internal demand for their coal.

Domestic coal production vs. demand from GenCos, mln mt*

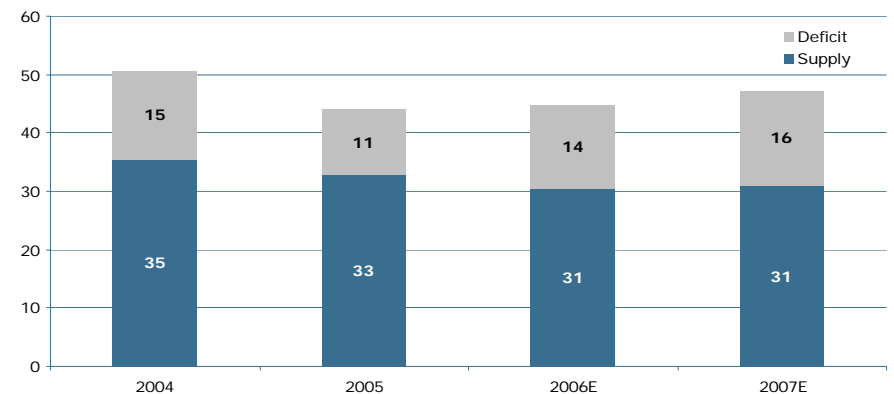


Source: Company data, Energobusiness, Concorde Capital estimates
 Note: The surplus is distributed between other users (including boiler plants)

Shortage of Coking Coal in Ukraine

Ukrainian coke makers have traditionally faced a deficit in the domestic supply of hard coking coal to meet production needs. In 2005, the deficit totaled 11 mln mt of coal, while this year we estimate this amount to grow to 14 mln mt due. In 2007, we forecast a deficit of 16 mln mt. Large unsatisfied domestic demand is favorable to private producers of high-quality coking coal, SHCHZ and Krasnodon Coal.

Domestic coking coal deficit vs. supply, mln mt



Source: Company data, Energobusiness, Concorde Capital estimates

Coking Coal Import is Exigency in 2006-2007

Domestic coke makers are dependent on imports of hard coking coal. Ukraine imported nearly 7–7.5 mln mt of concentrate in 2005, more than 95% of which came from Russia. After Mittal Steel bought the largest domestic vertically integrated steel mill, Kryvorizhstal (KSTL), the picture changed slightly as it started to import coal from its mines in Kazakhstan (12% of total Ukrainian imports in 10M06). According to the Ukrainian Coke Makers Association (Ukrkoks), Ukraine will import no less than 10 mln mt of coal concentrate in 2007.

Ukrainian coking coal imports*

Country	Volume, ths mt			Avg Price, USD/mt		
	10M06	10M05	Chg, Yoy	10M06	10M05	Chg, Yoy
Russia	5141.7	5309.4	-3%	77.1	99.8	-23%
Kazakhstan	706.8	11.3	6175%	105.6	135.2	-22%
Poland	2.5	26.8	-91%	108.5	138.8	-22%
USA	-	214.3	-	-	111.7	-
Georgia	0.2	-	-	74.8	-	-
Total	5851.2	5561.7	5%	-	-	-

Source: Energobusiness

* Ukraine imports hard and semi-hard coking coal concentrate.

Note: The conventional ratio of concentrate to coking coal is 1.65-1.7.

While in the mid-term we believe importing is unavoidable, in the long run, domestic producers of hard and semi-hard coking coal like SHCHZ, Zasyadko Mine and Krasnodon Coal will increase their shipments to domestic coke makers, cutting into imports.

Case Study: Ukrainian Mines Competitiveness

Ukrainian Coal a Quality Product

Despite the wide-spread opinion that Ukrainian coal is of low quality, we argue that some producers are, in fact, competitive with their CIS peers (to better understanding the table below please refer to appendix 2, 3).

CIS coal quality comparison

Region/Mine	Ash, %	Moisture, %	Sulphur, %	Calorific, CKal/kg	Caking, mm	Coal Grade	Price range*, USD/mt
<i>Russia/Kazakhstan</i>							
Vorkutaugol	32%	-	0.5-0.6%	-	19	Hard-coking	80-100
Kuzbassrazrezugol	14%	-	0.4-0.5%	-	10	Hard-coking	60-80
Yakutia	7%	-	0.3-0.4%	-	16	Hard-coking	100-120
Gukov Coal							
Kuzbassrazrezugol	10%	-	<1%	>5500	-	High-grade steam	45-65
Intaugol**	37%	12%	-	3500-4000	-	Sub-bituminous	10-15
	26%	10%	-	4000-4500	-	Low-grade steam	12-20
Ekibastuz	35%	-	-	3500-4000	-	Low-grade steam	12-20
<i>Ukraine</i>							
Komsomolets Donbassa	23.0%	5.0%	2.7%	>5500	-	High-grade steam	45-55
Krasnoarmiyska-Zakhidna	9.0%	9.9%	0.7%	-	13	Hard coking, semi hard-coking	75-90
Zasyadko Mine	8.7%	10.8%	2.0%	-	16-20	Semi hard-coking	60-70
Krasnodon Coal	8.4%	7.4%	3.0%	-	16-20	Semi hard-coking	60-70
Pavlohrad Coal	36.8%	9.9%	1.5%	>4100	-	High-grade steam	45-50

Source: Company data, Bloomberg, CentreInvest Group, Uralsib, Concorde Capital estimates

* Price range for the CIS

** Non-processed coal and concentrate

Note: The lower the sulfur, ash and moisture content and the higher the calorific value, the better the quality; caking characteristics are valuable for coking coal and vary from 3 to 20 mm (higher caking – higher coke quality)

Krasnoarmiyska-Zakhidna (SHCHZ) extracts coking coal with quality on par with the best in the CIS. Higher volumes of ash and moisture content in Komsomolets Donbassa's (SHKD) steam coal are not of key importance because CIS market requirements for them are low. The major factor that determines demand for steam coal in the CIS is calorific value.

Ukrainian Mines: Cost Competitive

The mining costs of major Ukrainian private coal producers are higher than in Russia (see the chart below). However, high railway transportation costs allow Ukrainian producers to be competitive on the domestic market (It takes from 25 USD/mt to 30 USD/mt to deliver the coal from Kuzbass region to the Ukrainian border). Moreover, SHCHZ exports hard coking coal to Russian steel smelters located in close proximity to the Ukrainian-Russian border (Novolipetsk Steel) and Slovakia (U.S. Steel Kosice).

Company/Mine	Mining Type	Mining cost, USD/mt
<i>Russia</i>		
Vorkutaugol	Underground	20
Gukovugol	Underground	20
Lenina Mine	Underground	16
Kirova Mine	Underground	10
Kuzbassrazrezugol	Open Pit	11-12
Yuzhny Kuzbass	Open Pit	12-14
Borodinsky	Open Pit	6-7
<i>Ukraine</i>		
Komsomolets Donbassa	Underground	22-24
Krasnoarmiyska-Zakhidna	Underground	21-25
Pavlohrad Coal	Underground	18-20

Source: Company data, CentreInvest Group, Energobusiness, Concorde Capital estimates

Methane Utilization: A Cost Cutting Opportunity

While domestic coal mines are currently spending to mechanize their production facilities by buying up-to-date mining equipment, they have room to cut mining costs by utilizing their methane deposits. Methane can be collected and sold as a gas, processed into electricity and sold, or used internally. Large coal mines presently consume ~10-25 MWh of electricity per annum and its share varies from 15% to 30% of mining costs. The installation of an in-house, combined heat & power unit that uses methane as the major feedstock will allow mines to significantly cut electricity costs. Estimated investments for one unit vary from USD 2 mln to USD 5 mln.

Technically, coal seams cannot be mined when methane concentration is higher than the norm (4-5.5% in a seam). However, up until now Ukrainian mines have gotten around this by pumping out the gas, polluting the environment.

Pollution Quotas: An Alternative Source of Funds

According to the Kyoto protocol, coal mines can trade gas emission credits. In 2006, Ukrainian mine Zasyadko Coal sold some of its credits to Japan and Austria for EUR 2.5 mln. According to the deal, these countries will deliver special equipment (worth EUR 1-1.5 mln) for methane utilization and other equipment for a combined heat & power unit with an annual capacity of 10-12 MWh. Zasyadko Coal's management expects this technology to cover 100% of the mine's electricity needs. Recently, a few other domestic mines also announced plans to sell emissions credits.

Domestic Coal Price Expectations

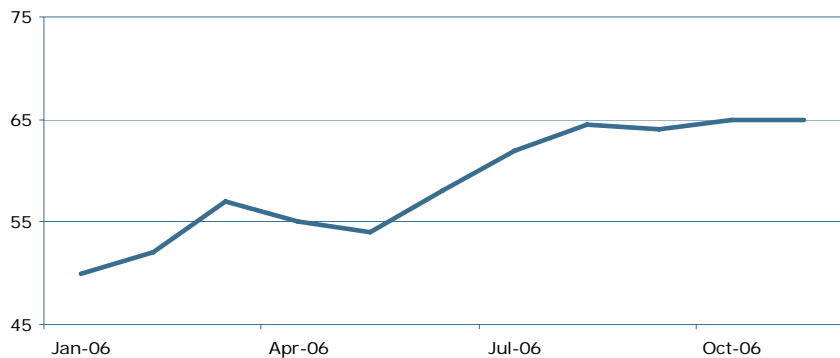
Steam Coal: Government Plans to Set New Rules

Recently the government, which sets the rules for the domestic steam coal sector, announced plans to implement a new pricing methodology for steam coal. According to the proposal, the price paid by state-owned GenCos will depend on the coal's calorific value (a major productivity factor for GenCos).

Favorable for SCM-related Mines

SCM-related coal mines Pavlohrad Coal and especially SHKD will benefit from the new rules as they produce high calorific coal (SHKD's calorific value is >5500 Kcal/kg). In the chart below, we use Russian prices for 6000 Kcal/kg steam coal to roughly estimate the price range for coal to state GenCos if the program is implemented.

Price of Baltic 6000 Kcal NAR FOB steam coal, USD per mt



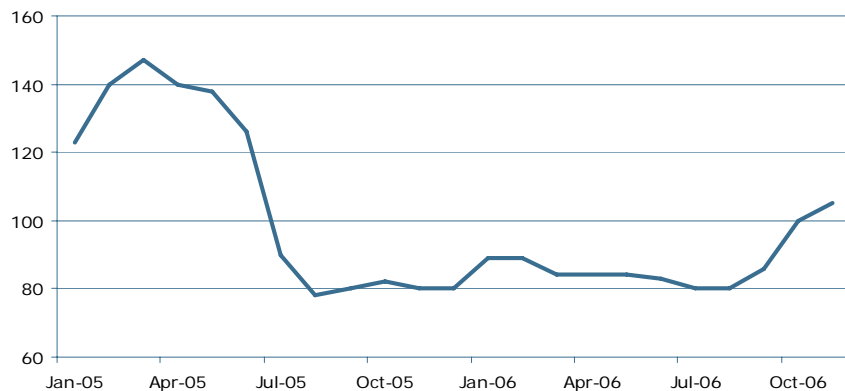
Source: Bloomberg

In January-October 2006, state GenCos purchased steam coal at USD 31-48 per mt, depending on the grade of the coal. The price for state-owned GenCos based on the new methodology will vary from USD 30 per mt for low calorific lignite to USD 65 per mt for lean coal, in our opinion.

Coking Coal: Prices Revive Slightly

The price for imports is the best indicator for domestic prices of high-grade hard and soft coking coal concentrate. In late 2006 import prices reversed on the back of reviving demand from coke makers, marking the beginning of an uptrend. The average price of USD 84 per mt in 11M06 is 27% yoy lower than in the same period last year. In the short-term, we estimate the domestic price of high grade coking coal concentrate will fluctuate between USD 85-100 per mt.

Russian import coking concentrate price DAF, USD/mt

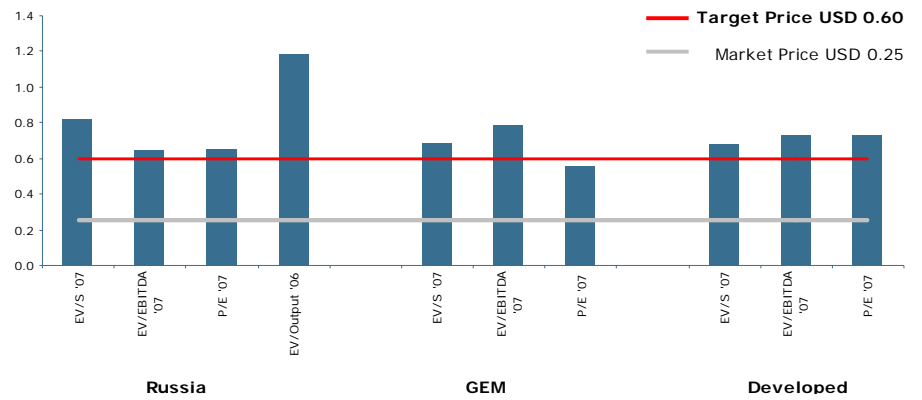


Source: Metal Magazine

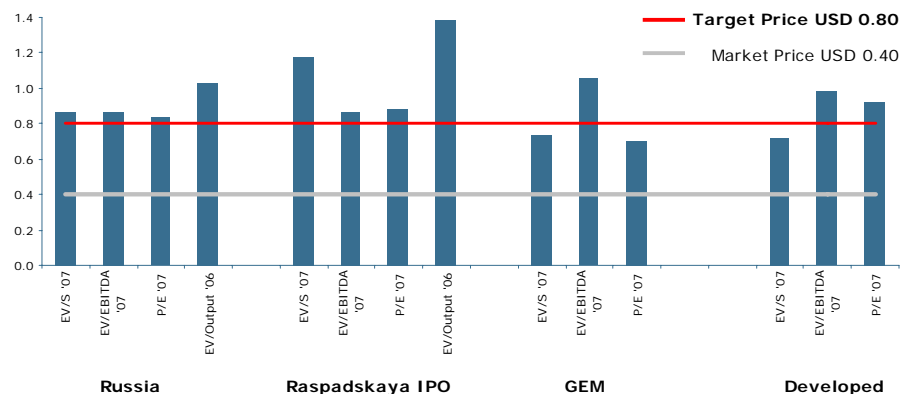
Valuation

Valuation Summary

Komsomolets Donbassa (SHKD), Upside: 140%, BUY



Krasnoarmiyska-Zakhidna (SHCHZ), Upside: 100%, BUY



IPO Rospadskaya Mine

The IPO of Rospadskaya, Russia's second largest coking coal mine, has been a hot story recently. Completed on Nov. 10, 2006 on the RTS, the IPO is quite opportune for Ukrainian coal stocks and provides us with a useful reference for measuring their value. We argue that a comparison to the Rospadskaya Mine IPO provides more accurate picture for SHCHZ, as it has similar production volume and coal quality. In regards to SHKD, we conducted this valuation primarily for illustrative purposes.

	MCap, USD mln	EV/S		EV/EBITDA		P/E		EV/Output, USD/mt
Ukraine		2006E	2007E	2006E	2007E	2006E	2007E	2006E
SHKD	83.7	0.79	0.71	2.74	2.38	5.67	4.76	27.0
SHCHZ (1)	339.4	1.24	1.08	3.35	2.84	7.28	5.99	49.9
SHCHZ (2)	339.4	0.78	0.67	1.46	1.29	2.35	2.11	49.9
	MCap at IPO, USD mln	2006E	2007E	2006E	2007E	2006E	2007E	2006E
Rospadskaya Mine	1 673.0	3.14	3.17	5.60	6.13	11.38	13.28	172.5
SHKD price								
Implied by Avg, USD		0.99	1.11	0.51	0.64	0.50	0.70	1.6
Upside/Downside by Avg		295%	345%	104%	157%	101%	179%	539%
SHCHZ price (1)								
Implied by Avg, USD		1.01	1.18	0.67	0.86	0.63	0.89	1.4
Upside/Downside by Avg		154%	195%	67%	116%	56%	122%	246%
SHCHZ price (2)								
Implied by Avg, USD		1.61	1.91	1.53	1.90	1.94	2.51	1.4
Upside/Downside by Avg		304%	377%	282%	374%	385%	528%	246%

Source: Company data, Thomson Financial, Bloomberg, CentreInvest Group, Concorde Capital estimates
 Note: The SHCHZ valuation is done both on reported (1) and estimated true (2) financials.

The comparison clearly indicates that SHCHZ is extremely undervalued based on all multiples, despite the weaker financial reporting standards of the Ukrainian mine. Depending on the multiple selected, the Rospadskaya Mine IPO comparison sets attractive upsides spanning from 56% to 528%.

Russian Peers

	MCap, USD mln	EV/S		EV/EBITDA		P/E		EV/Output, USD/mt
		2006E	2007E	2006E	2007E	2006E	2007E	2006E
Ukraine								
SHKD	83.7	0.79	0.71	2.74	2.38	5.67	4.76	27.0
SHCHZ (1)	339.4	1.24	1.08	3.35	2.84	7.28	5.99	49.9
SHCHZ (2)	339.4	0.78	0.67	1.46	1.29	2.35	2.11	49.9
Russian Market Peers								
Vorkuta Coal	965.0	1.87	1.79	5.15	4.84	8.22	7.65	128.7
South Kuzbass	2 201.0	2.23	2.01	6.99	6.92	12.58	12.51	129.5
Kuzbassrazrezugol	2 944.3	4.68	3.98	27.47	22.36	192.94	167.01	73.7
Raspadskaya Mine	1 673.0	3.15	3.19	5.62	6.15	11.38	13.28	173.2
Kirova	187.0	2.57	2.33	5.72	5.20	9.35	8.40	46.8
Average		2.45	2.33	5.87	5.78	10.38	10.46	110.4
Median		2.57	2.33	5.72	6.15	11.38	12.51	128.7
SHKD price								
Implied by Avg, USD		0.77	0.82	0.54	0.61	0.46	0.55	1.0
Implied by Median, USD		0.81	0.82	0.52	0.65	0.50	0.66	1.2
Upside/Downside by Avg		209%	226%	114%	143%	83%	120%	309%
Upside/Downside by Median		223%	227%	109%	159%	101%	163%	376%
SHCHZ price (1)								
Implied by Avg, USD		0.79	0.87	0.70	0.82	0.57	0.70	0.9
Implied by Median, USD		0.83	0.87	0.68	0.87	0.63	0.84	1.0
Upside/Downside by Avg		98%	116%	75%	104%	43%	75%	121%
Upside/Downside by Median		107%	117%	71%	117%	56%	109%	158%
SHCHZ price (2)								
Implied by Avg, USD		1.26	1.40	1.60	1.79	1.77	1.98	0.9
Implied by Median, USD		1.32	1.40	1.56	1.90	1.94	2.37	1.0
Upside/Downside by Avg		215%	250%	301%	347%	342%	395%	121%
Upside/Downside by Median		230%	251%	291%	376%	385%	491%	158%

Source: Company data, Thomson Financial, Bloomberg, CentreInvest Group, Concorde Capital estimates
 Note: The SHCHZ valuation is done both on (1) reported and (2) estimated true financials.

A comparison to Russian peers provides the most accurate valuation of Ukrainian coal mines, taking into account the quality of coal quality and mining technologies used by the companies. Ukrainian coal stocks trade at significant discounts to their Russian peers, suggesting strong upsides.

GEM Peers

	MCap, USD mln	EV/S		EV/EBITDA		P/E	
		2006E	2007E	2006E	2007E	2006E	2007E
Ukraine							
SHKD	83.7	0.79	0.71	2.74	2.38	5.67	4.76
SHCHZ (1)	339.4	1.24	1.08	3.35	2.84	7.28	5.99
SHCHZ (2)	339.4	0.78	0.67	1.46	1.29	2.35	2.11
GEM Peers							
China Shenhua (China)	35 783.5	5.12	4.49	9.25	8.07	15.19	13.29
Yanzhou Coal (China)	3 491.9	2.31	2.12	5.29	5.03	9.62	9.53
Banpu Public PCL (Thailand)	1 347.6	1.91	1.83	8.45	6.85	13.33	8.68
Tambang Batubara (Indonesia)	810.0	1.99	1.81	9.33	8.52	12.95	11.63
Average		2.83	2.56	8.08	7.12	12.78	10.78
Median		2.15	1.98	8.85	7.46	13.14	10.58
SHKD price							
Implied by Avg, USD		0.89	0.90	0.74	0.75	0.56	0.57
Implied by Median, USD		0.68	0.69	0.81	0.78	0.58	0.56
<i>Upside/Downside by Avg</i>		<i>257%</i>	<i>259%</i>	<i>195%</i>	<i>199%</i>	<i>125%</i>	<i>127%</i>
<i>Upside/Downside by Median</i>		<i>170%</i>	<i>177%</i>	<i>223%</i>	<i>213%</i>	<i>132%</i>	<i>122%</i>
SHCHZ price (1)							
Implied by Avg, USD		0.92	0.95	0.97	1.00	0.70	0.72
Implied by Median, USD		0.69	0.73	1.06	1.05	0.72	0.71
<i>Upside/Downside by Avg</i>		<i>129%</i>	<i>138%</i>	<i>141%</i>	<i>151%</i>	<i>75%</i>	<i>80%</i>
<i>Upside/Downside by Median</i>		<i>74%</i>	<i>83%</i>	<i>165%</i>	<i>163%</i>	<i>80%</i>	<i>77%</i>
SHCHZ price (2)							
Implied by Avg, USD		1.46	1.54	2.21	2.20	2.18	2.04
Implied by Median, USD		1.10	1.19	2.42	2.31	2.24	2.00
<i>Upside/Downside by Avg</i>		<i>264%</i>	<i>285%</i>	<i>452%</i>	<i>451%</i>	<i>444%</i>	<i>410%</i>
<i>Upside/Downside by Median</i>		<i>176%</i>	<i>197%</i>	<i>505%</i>	<i>477%</i>	<i>460%</i>	<i>400%</i>

Source: Company data, Thomson Financial, Bloomberg, CentreInvest Group, Concorde Capital estimates
 Note: The SHCHZ valuation is done both on (1) reported and (2) estimated true financials.

Developed Markets

	MCap, USD mln	EV/S		EV/EBITDA		P/E	
		2006E	2007E	2006E	2007E	2006E	2007E
Ukraine							
SHKD	83.7	0.79	0.71	2.74	2.38	5.67	4.76
SHCHZ (1)	339.4	1.24	1.08	3.35	2.84	7.28	5.99
SHCHZ (2)	339.4	0.78	0.67	1.46	1.29	2.35	2.11
Developed Market Peers							
		2006E	2007E	2006E	2007E	2006E	2007E
Peabody (USA)	12 396.6	2.57	2.01	12.98	8.80	20.75	15.10
Arch Coal (USA)	5 014.1	2.36	2.17	10.76	7.65	20.43	12.88
Consol (USA)	6 724.0	2.02	1.94	8.56	6.95	16.76	13.23
Massey (USA)	2 231.3	1.54	1.40	9.97	6.97	58.71	16.65
Macarthur (Australia)	653.7	2.06	1.83	4.95	6.82	7.65	11.01
Foundation Coal (USA)	1 686.5	1.59	1.49	7.36	5.89	23.58	15.20
Centennial Coal (Australia)	690.5	1.63	1.49	7.97	5.95	28.72	13.88
Felix Resources (Australia)	600.6	2.83	2.33	14.79	9.85	23.20	16.25
Gloucester Coal (Australia)	237.0	2.11	2.21	5.64	6.32	8.31	8.96
Average		2.08	1.87	9.22	7.25	23.12	13.68
Median		2.06	1.94	8.56	6.95	20.75	13.88
SHKD price							
Implied by Avg, USD		0.65	0.66	0.84	0.76	1.02	0.72
Implied by Median, USD		0.65	0.68	0.78	0.73	0.91	0.73
Upside/Downside by Avg		162%	162%	237%	204%	308%	187%
Upside/Downside by Median		160%	171%	213%	192%	266%	192%
SHCHZ price (1)							
Implied by Avg, USD		0.67	0.70	1.10	1.02	1.27	0.91
Implied by Median, USD		0.67	0.72	1.02	0.98	1.14	0.93
Upside/Downside by Avg		68%	74%	176%	156%	218%	129%
Upside/Downside by Median		67%	80%	156%	145%	185%	132%
SHCHZ price (2)							
Implied by Avg, USD		1.07	1.13	2.52	2.24	3.94	2.59
Implied by Median, USD		1.06	1.16	2.34	2.15	3.54	2.63
Upside/Downside by Avg		167%	182%	530%	460%	885%	547%
Upside/Downside by Median		165%	191%	485%	438%	784%	556%

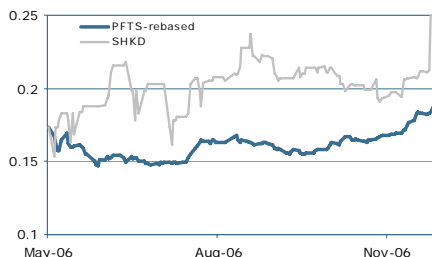
Source: Company data, Thomson Financial, Bloomberg, CentreInvest Group, Concorde Capital estimates
 Note: The SHCHZ valuation is done both on (1) reported and (2) estimated true financials.

Company Profiles

BUY

Current price	Target price
USD 0.25	USD 0.60

SHKD Mid-Market, USD



Market Information

Bloomberg Ticker	SHKD UZ
No of Shares, mln	334.9
Market price, USD	0.25
MCap, USD mln	83.7
Free float	2.5%
FF MCap, USD mln	2.1

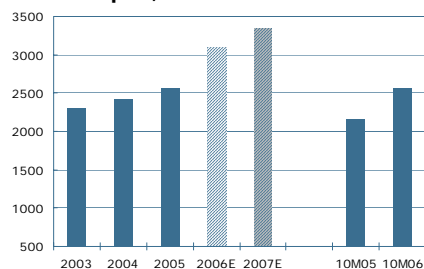
Stock Ownership

Avdiyvka Coke (SCM)	87%
Other	13%

Ratios, 2005

EBITDA Margin	17%
Net Margin	1%
Net Debt/ Equity	-0.02

Coal Output, ths mt



Source: Company data, Concorde Capital estimates

Revised Key Financials, USD mln

	Sales		EBITDA		Net Income	
	New	Old	New	Old	New	Old
2005	-	83.7	-	14.3	-	0.7
2006E	105.4	103.6	30.6	17.7	14.8	5.2
2007E	117.3	119.2	35.2	23.8	17.6	9.5

Spot exchange rate is 5.05

Komsomolets Donbassa

Target Price Upgraded. Robust growth and improved profitability provide the basis for a stock upgrade. We raise our target price from USD 0.3 per share to USD 0.6 per share, closer to the price implied by Russian peer EV/EBITDA ratios (average '07E x5.78). Our new target implies a 140% upside.

Strong Operational Performance. The company demonstrated a robust 16% yoy increase in output, which totaled 2.3 mln mt in 9M06, almost in line with our prior forecast for 2006 (15% yoy). In late November, the company launched a new coal seam equipped with modern extracting equipment (650 ths mt coal seam). According to management, the new seam will allow the mine to increase output to 3.35 mln mt in 2007 (up 8% yoy).

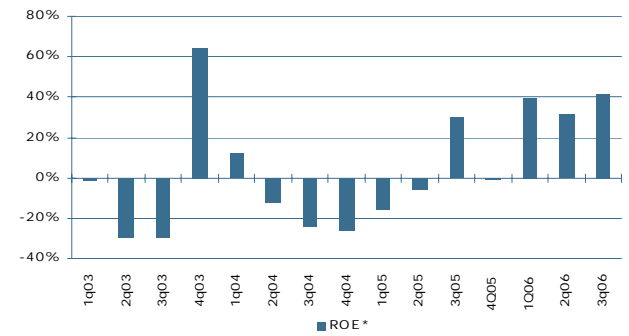
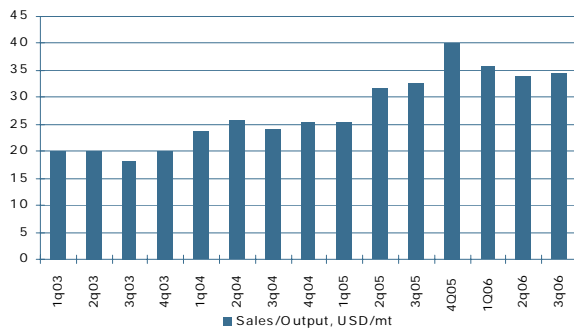
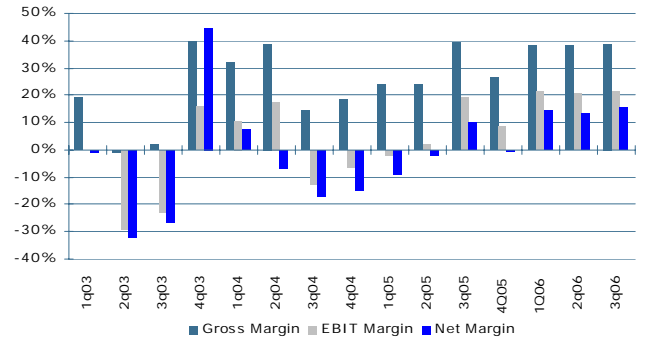
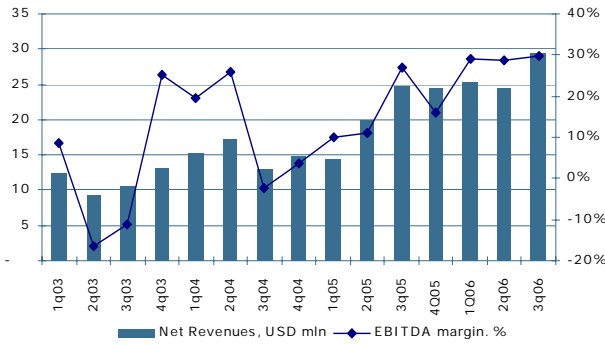
Financials Improved in 9M06. SHKD's interim financial results support our prior expectation of diminishing related-party transactions within the Donetsk Fuel Energy Company, which manages SCM energy assets. We think the improvement is part of the group's IPO strategy. Sales grew by 34% yoy to USD 79 mln in 9M06. Simultaneously, in 9M06 SHKD posted a 29.2% EBITDA margin and a 14.4% net margin compared to 17.5% and 1.4% in 9M05, respectively.

SCM Obtained Full Control. In July SCM bought a 26% stake in SHKD and now owns 87% of the mine. The stake in the mine had been owned by Ukrpodshipnyk (owned by the Klyuyev brothers, who are allies of SCM).

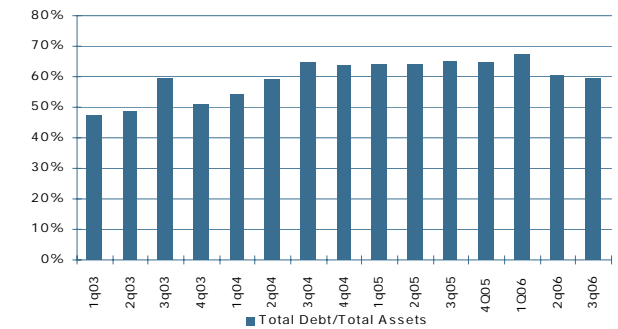
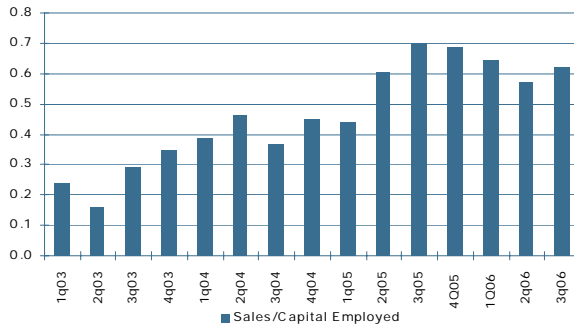
Price Ratios

	EV/S	EV/EBITDA	P/E
2005	1.00	5.85	n/m
2006E	0.79	2.74	5.67
2007E	0.71	2.38	4.76

SHKD's Quarterly Analysis



*Quarterly ROE is annualized



Financial Statements

All financial statements according to Ukrainian Accounting Standards

Income Statement Summary, USD mln

	1Q03	2Q03	3Q03	4Q03	1Q04	2Q04	3Q04	4Q04	1Q05	2Q05	3Q05	4Q05	1Q06	2Q06	3Q06
Net Revenues	12	9	10	13	15	17	13	15	14	20	25	25	25	24	29
Gross Profit	2	(0)	0	5	5	7	2	3	3	5	10	7	10	9	11
Other Operating Income/Costs, net	(1)	(1)	(0)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(1)	(1)	(1)	(1)
SG&A	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)	(2)	(2)	(2)
EBITDA	1	(2)	(1)	3	3	4	(0)	1	1	2	7	4	7	7	9
<i>EBITDA margin, %</i>	<i>9%</i>	<i>-17%</i>	<i>-11%</i>	<i>25%</i>	<i>20%</i>	<i>26%</i>	<i>-2%</i>	<i>4%</i>	<i>10%</i>	<i>11%</i>	<i>27%</i>	<i>16%</i>	<i>29%</i>	<i>29%</i>	<i>30%</i>
Depreciation	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)	(2)	(2)	(2)	(2)	(3)
EBIT	(0)	(3)	(2)	2	2	3	(2)	(1)	(0)	0	5	2	5	5	6
<i>EBIT margin, %</i>	<i>0%</i>	<i>-29%</i>	<i>-23%</i>	<i>16%</i>	<i>10%</i>	<i>17%</i>	<i>-13%</i>	<i>-6%</i>	<i>-2%</i>	<i>2%</i>	<i>19%</i>	<i>9%</i>	<i>21%</i>	<i>21%</i>	<i>21%</i>
Interest Expense	(0)	(0)	(0)	(0)	(0)	(0)	(0)	(0)	-	-	-	(0)	(0)	(0)	(0)
Financial income/(expense)	-	-	-	-	-	-	-	-	-	-	0	0	-	0	0
Other income/(expense)	(0)	(0)	(0)	4	(0)	(4)	(0)	(1)	(0)	(0)	(0)	(0)	(0)	(0)	(0)
PBT	(0)	(3)	(3)	6	1	(1)	(2)	(1)	(1)	0	5	2	5	5	6
Tax	-	(0)	-	0	(0)	(0)	(0)	(1)	(0)	(1)	(2)	(2)	(2)	(2)	(2)
Net Income	(0)	(3)	(3)	6	1	(1)	(2)	(2)	(1)	(0)	3	(0)	4	3	5
<i>Net Margin, %</i>	<i>-1%</i>	<i>-32%</i>	<i>-26%</i>	<i>45%</i>	<i>8%</i>	<i>-7%</i>	<i>-17%</i>	<i>-15%</i>	<i>-9%</i>	<i>-2%</i>	<i>10%</i>	<i>0%</i>	<i>15%</i>	<i>13%</i>	<i>15%</i>

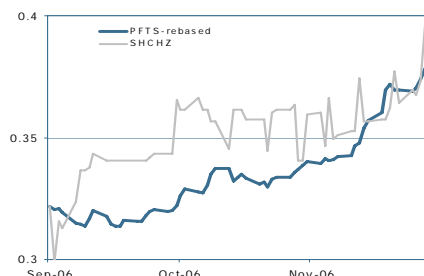
Balance Sheet Summary, USD mln

	1Q03	2Q03	3Q03	4Q03	1Q04	2Q04	3Q04	4Q04	1Q05	2Q05	3Q05	4Q05	1Q06	2Q06	3Q06
Current Assets	19	15	28	13	17	28	32	17	14	12	22	20	39	27	31
Cash & Equivalents	0	0	0	0	0	1	0	0	0	0	0	1	0	0	1
Trade Receivables	12	9	14	8	7	6	8	10	7	4	10	10	19	15	17
Inventories	6	5	12	3	3	3	13	4	5	4	3	4	5	4	3
Other current assets	1	1	3	3	7	18	10	2	1	4	8	5	15	7	10
Fixed Assets	59	59	60	63	67	63	67	72	78	79	79	81	80	80	82
PP&E, net	55	55	57	60	63	58	60	64	67	67	71	71	70	69	69
Other Fixed Assets	4	4	3	3	4	5	8	8	10	11	8	9	10	11	13
Total Assets	78	75	88	76	84	91	99	89	91	91	101	100	119	107	113
Shareholders' Equity	41	38	36	37	38	37	35	33	33	33	35	35	39	42	46
Share Capital	16	16	16	16	16	16	16	16	16	16	16	17	17	17	17
Retained Earnings and Other	(12)	(15)	(8)	(2)	(1)	(2)	(4)	(6)	(8)	(9)	(6)	(6)	(3)	1	4
Current Liabilities	26	16	52	38	45	54	64	56	58	58	65	65	79	65	66
ST Interest Bearing Debt	2	2	0	2	1	4	1	0	0	0	-	-	-	-	-
Trade Payables	22	11	49	34	35	36	45	38	42	45	45	46	48	42	43
Accrued Wages	1	1	1	1	1	1	1	1	2	2	2	2	2	2	2
Accrued Taxes	0	0	0	0	0	0	0	2	1	1	3	3	3	3	3
Other Current Liabilities	1	2	1	1	7	13	16	15	14	10	16	14	26	18	18
LT Liabilities	11	20	0	0	0	0	0	0	0	0	0	0	0	0	1
LT Interest Bearing Debt	10	19	-	-	-	-	-	-	-	-	-	-	-	-	-
Other LT	1	1	0	0	0	0	0	0	0	0	0	0	0	0	1
Total Liabilities & Equity	78	75	88	76	84	91	99	89	91	91	101	100	119	107	113

BUY

Current price	Target price
USD 0.40	USD 0.80

SHCHZ Mid-Market, USD



Market Information

Bloomberg Ticker	SHCHZ UZ
No of Shares, mln	848.5
Market price, USD	0.40
MCap, USD mln	339.4
Free float	2.1%
FF MCap, USD mln	7.1

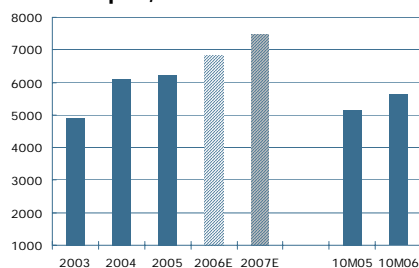
Stock Ownership

Donetskstal	46%
Investrozvytok LTD	41%
Other	13%

Ratios, 2005

EBITDA Margin	42%
Net Margin	23%
Net Debt/ Equity	-0.004

Coal Output, ths mt



Source: Company data, Concorde Capital estimates

Krasnoarmiyska-Zakhidna

Updated Target Price Yields an Upside. Visible benefits of an ongoing investment program outweigh some deterioration in the quality of financial reporting by SHCHZ. The recent IPO of Rapsadskaya Mine provides the benchmark for our new valuation. We upgrade our target price from USD 0.6 per share to USD 0.8 per share – closer to what our Russian peer comparison implies.

Leader of the Coking Coal Sector. The company boosted its coal extraction by 10% yoy in 9M06 to 5.1 mln mt, which is slightly higher than the 9% yoy increase we previously anticipated for the full year. We maintain our forecast of 6.8 mln mt for 2006 (9% yoy growth) and estimate coal output 2007 at 7.5 mln mt (up 10% yoy). We believe this growth is realistic due to high domestic demand and a well-designed investment program.

Large-Scale CapEx Program. SHCHZ plans to invest more than USD 230 mln to almost double its output to 10 mln mt by 2010. Specifically, the company will complete construction of groove #2 (diameter – 8 m, depth – 850m) and buy new mining equipment. A second refinery will be constructed, which will increase the production capacity of coking coal concentrate to ~6.5 mln mt (up 60%). Management also told us that SHCHZ is going to implement cost saving technologies during the construction of an in-house combined heat & power unit with methane gas as a feedstock. The generator (10-15 MWh annual capacities) will make SHCHZ self-sufficient in electricity.

Disappointing 9M06 Financials. In 9M06, Krasnoarmiyska-Zakhidna's top line stayed at its 9M05 level (USD 205 mln), while margins decreased: EBITDA margin to 32% in 9M06 from 48% in 9M05, net margin to 13% in 9M06 from 29% in 9M05. This decrease is directly attributable to poor corporate governance. We calculated SHCHZ underreported 40% of its top line in 9M06, selling coal concentrate to related companies at the price of ordinary coal (USD ~80 per mt vs. USD ~45 per mt). Estimated true sales in 2006 are USD 437 mln vs. reported USD 280 mln.

Revised Key Financials, USD mln

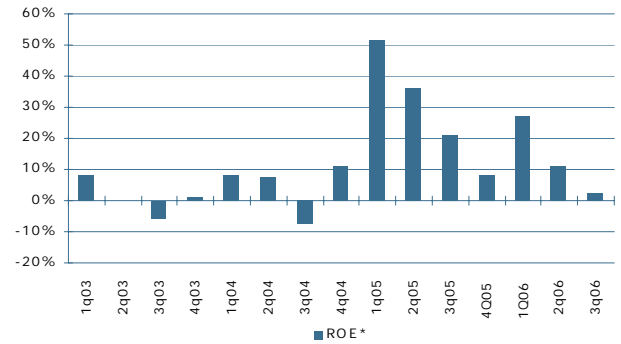
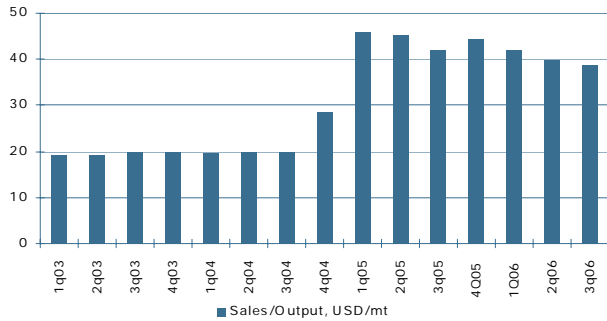
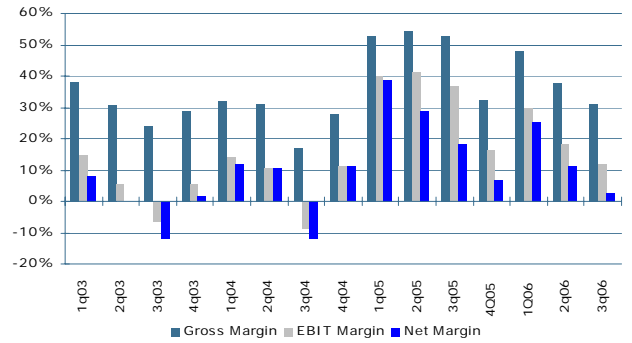
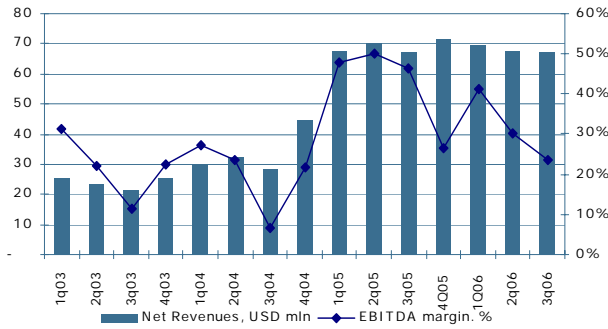
	Sales		EBITDA		Net Income	
	New	Old	New	Old	New	Old
2005	-	276.7	-	117.5	-	63.6
2006E	274.2	302.1	101.4	120.8	46.6	60.4
2007E	315.0	332.3	119.7	132.9	56.7	66.5

Spot exchange rate is 5.05

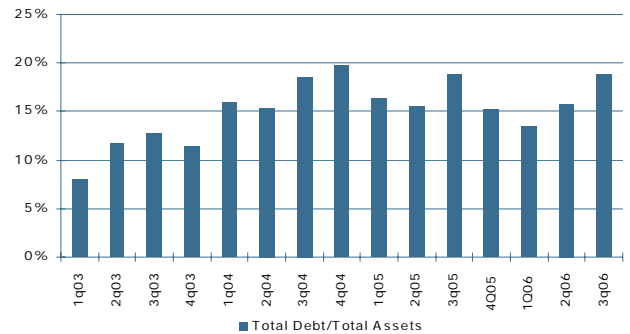
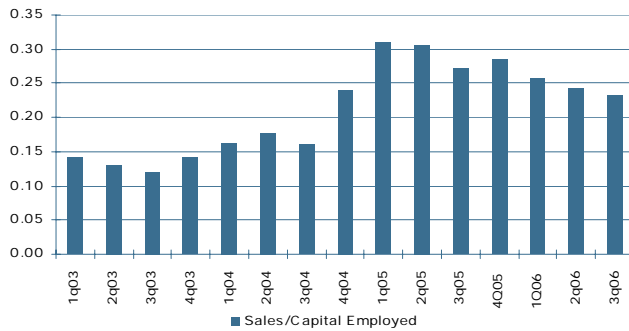
Price Ratios

	EV/S	EV/EBITDA	P/E
2005	1.23	2.89	5.34
2006E	1.24	3.35	7.28
2007E	1.08	2.84	5.99

SHCHZ's Quarterly Analysis



*Quarterly ROE is annualized



Financial Statements

All financial statements according to Ukrainian Accounting Standards

Income Statement Summary, USD mln

	1Q03	2Q03	3Q03	4Q03	1Q04	2Q04	3Q04	4Q04	1Q05	2Q05	3Q05	4Q05	1Q06	2Q06	3Q06
Net Revenues	25	23	21	26	30	32	28	45	68	70	67	72	70	68	67
Gross Profit	10	7	5	7	10	10	5	13	36	38	36	23	33	26	21
Other Operating Income/Costs, net	(1)	(1)	(2)	(1)	(0)	(1)	(2)	(2)	(2)	(1)	(2)	(2)	(1)	(2)	(2)
SG&A	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(2)	(2)	(2)	(2)	(3)	(4)	(3)
EBITDA	8	5	2	6	8	8	2	10	32	35	31	19	29	20	16
<i>EBITDA margin, %</i>	<i>31%</i>	<i>22%</i>	<i>11%</i>	<i>22%</i>	<i>27%</i>	<i>23%</i>	<i>6%</i>	<i>22%</i>	<i>48%</i>	<i>50%</i>	<i>47%</i>	<i>26%</i>	<i>41%</i>	<i>30%</i>	<i>24%</i>
Depreciation	(4)	(4)	(4)	(4)	(4)	(4)	(4)	(5)	(5)	(6)	(6)	(7)	(8)	(8)	(8)
EBIT	4	1	(1)	1	4	3	(3)	5	27	29	25	12	21	12	8
<i>EBIT margin, %</i>	<i>15%</i>	<i>5%</i>	<i>-7%</i>	<i>5%</i>	<i>14%</i>	<i>11%</i>	<i>-9%</i>	<i>11%</i>	<i>40%</i>	<i>41%</i>	<i>37%</i>	<i>17%</i>	<i>30%</i>	<i>18%</i>	<i>12%</i>
Interest Expense	(0)	(0)	(0)	(0)	(0)	(0)	(0.1)	(0)	(0)	(0)	(0)	(0)	(0)	(0)	(0)
Financial income/(expense)	0	0	0	0	0	0	0	(0)	0	0	0	0	0	0	0
Other income/(expense)	(1)	(0)	(1)	(2)	(0)	(0)	(0)	(0)	(0)	(0)	(0)	(0)	(1)	(1)	(4)
PBT	3	1	(2)	(1)	4	3	(3)	5	27	28	24	12	20	12	4
Tax	(1)	(1)	(0)	2	(0)	0	(0)	0	(1)	(8)	(12)	(7)	(2)	(4)	(4)
Net Income	2	0	(3)	0	4	3	(3)	5	26	20	12	5	18	7	2
<i>Net Margin, %</i>	<i>8%</i>	<i>0%</i>	<i>-12%</i>	<i>2%</i>	<i>12%</i>	<i>11%</i>	<i>-12%</i>	<i>11%</i>	<i>39%</i>	<i>29%</i>	<i>18%</i>	<i>7%</i>	<i>25%</i>	<i>11%</i>	<i>3%</i>

Balance Sheet Summary, USD mln

	1Q03	2Q03	3Q03	4Q03	1Q04	2Q04	3Q04	4Q04	1Q05	2Q05	3Q05	4Q05	1Q06	2Q06	3Q06
Current Assets	45	53	52	47	55	51	46	35	36	34	49	26	38	48	51
Cash & Equivalents	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0
Trade Receivables	30	37	33	26	22	19	16	6	5	4	17	5	12	18	24
Inventories	5	5	6	7	19	14	14	14	15	14	16	17	20	23	23
Other current assets	10	11	13	13	14	16	16	15	16	15	16	4	5	6	4
Fixed Assets	149	149	150	153	158	165	172	196	226	238	253	271	273	282	307
PP&E, net	130	129	127	130	135	141	146	160	176	182	188	210	206	213	225
Other Fixed Assets	19	20	23	23	23	24	27	35	50	56	65	61	67	69	82
Total Assets	194	202	202	199	213	215	219	231	262	272	302	297	311	330	358
Shareholders' Equity	178	178	177	177	179	183	178	185	219	230	246	252	270	278	290
Share Capital	40	40	40	40	40	40	40	40	40	40	42	42	42	42	42
Retained Earnings and Other	49	49	46	47	49	52	49	55	83	94	107	109	126	133	134
Current Liabilities	15	23	24	20	31	33	40	45	43	42	57	45	42	52	67
ST Interest Bearing Debt	5	6	9	6	4	2	2	0	0	-	-	-	-	-	-
Trade Payables	5	13	11	9	20	23	30	37	31	27	38	30	28	40	56
Accrued Wages	2	2	2	2	2	2	2	2	3	3	4	4	4	5	4
Accrued Taxes	1	1	0	0	1	1	0	1	3	4	6	3	2	1	1
Other Current Liabilities	2	3	2	3	4	5	5	4	6	8	9	8	7	7	6
LT Liabilities	0	0	2	3	3	0	0	0	0	0	0	0	0	0	-
LT Interest Bearing Debt	0	0	2	3	3	-	-	-	-	-	-	-	-	-	-
Other LT	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
Total Liabilities & Equity	194	202	202	199	213	215	219	231	262	272	302	297	311	330	358

Appendix 1: Key Financials

	<i>in USD mln, unless otherwise stated</i>						
	Sales		EBITDA mgn, %		Net mgn, %		Output, mln mt
	2006E	2007E	2006E	2007E	2006E	2007E	2006E
Ukraine							
SHKD	105.4	117.3	29%	30%	14%	15%	3.1
SHCHZ (1)	274.2	315.0	37%	38%	17%	18%	6.8
SHCHZ (2)	436.5	510.0	53%	51%	33%	31%	6.8
Russian Peers	2006E	2007E	2006E	2007E	2006E	2007E	2006E
Vorkuta Coal	517.3	540.6	36%	37%	23%	23%	7.5
South Kuzbass	989.0	1 093.0	32%	29%	18%	16%	17.0
Kuzbassrazrezugol (KRU)	662.2	716.1	17%	18%	2%	2%	42.0
Kirova	72.8	80.1	45%	45%	27%	28%	4.0
Raspadskaya Mine	533.0	527.0	56%	52%	28%	24%	9.7
GEM Peers	2006E	2007E	2006E	2007E	2006E	2007E	
China Shenhua (China)	7 958.2	9 079.1	55%	56%	30%	30%	
Yanzhou Coal (China)	1 512.9	1 644.9	44%	42%	24%	22%	
Banpu Public PCL (Thailand)	876.7	918.5	23%	27%	12%	17%	
Tambang Batubara (Indonesia)	407.4	447.1	21%	21%	15%	16%	
Developed Markets	2006E	2007E	2006E	2007E	2006E	2007E	
Peabody (USA)	5 360.9	6 846.7	20%	23%	11%	12%	
Arch Coal (USA)	2 532.8	2 755.8	22%	28%	10%	14%	
Consol (USA)	3 644.7	3 800.7	24%	28%	11%	13%	
Massey (USA)	2 161.5	2 383.5	15%	20%	2%	6%	
Macarthur (Australia)	320.7	361.3	42%	27%	27%	16%	
Foundation Coal (USA)	1 459.8	1 563.0	22%	25%	5%	7%	
Centennial Coal (Australia)	727.8	796.8	20%	25%	3%	6%	
Felix Resources (Australia)	221.1	268.6	19%	24%	12%	14%	
Gloucester Coal (Australia)	120.7	115.1	37%	35%	24%	23%	

Source: Company data, Thomson Financials, Bloomberg, CentreInvest Group, Concorde Capital estimates
 Note: The SHCHZ data includes (1) reported and (2) estimated true financials.

Appendix 2: Coal Quality Parameters

Steam Coal – (Power Generation)

Calorific value:

The core factor affecting efficiency of electricity generators. The calorific value of steam coal may vary from 2000–3500 Kcal/kg for lignite to 3500–6500 Kcal/kg for hard steam coal. The most scarce grades of high quality anthracites may reach 7000 Kcal/kg.

Ash:

Ash content is another important factor. The best quality steam coal has ash content below 10%, while the worst grades have ash content of more than 40%.

Sulphur:

Steam coal sulphur content varies from below 1% to more than 4%. The Standard European Coal Agreement mandates sulphur of below 1% for steam coal.

Moisture:

The moisture level is an influential parameter, primarily for lignite, which suffers from excess moisture content. A high moisture level results in decreased efficiency for a power generator.

Coking Coal – (Metallurgical Coke Production)

Caking:

The main characteristic of coking coal is caking capability, which indicates whether it can be used as a core component in coke manufacturing. Calorific value is irrelevant here. In CIS coal specifications, caking characteristics are defined by the plastic layer thickness of heated coal (in mm).

Sulphur & Phosphorus:

High sulphur and phosphorus content in coke adversely affects the quality of steel. Based on requirements of Japanese steel manufacturers, sulphur content must be below 0.8% for hard coking coal and below 1% for semi-hard and semi-soft coking coal.

Ash:

A sizable ash content results in higher operating costs of coke manufacturers. Ash content must be below 7.5% for hard coking coals, below 10% for semi-hard coking coals, and 12% for semi-soft coking coals.

Appendix 3: Coal Classification

International	Ukraine	Domestic Private Producers
Anthracite	High-grades anthracite (A)	
Bituminous:		
Hard coking coal	Coking (K), Fat (Zh) coal	Krasnoarmiyska-Zakhidna (K)
Semi-hard and semi-soft coking coal	Coking (K), Fat (Zh) with high sulfur content and ash, plus high-grade gas (G) and poorly caking (OS) coal	Krasnoarmiyska-Zakhidna (K) , Krasnodon Coal (Zh, K), Zasyadko (Zh), Pavlohrad Coal (G)
High-grade steam coal	Low-grade anthracite (A), lean (T), poorly caking (SS), gas (G), high-grade candle (D) coal	Komsomolets Donbassa (T) , Pavlohrad Coal (G)
Sub-Bituminous	Candle (D), plus high-grade brown (B) coal	
Lignite	Brown (B) coal	

Analyst Certification

I, Eugene Cherviachenko, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report.

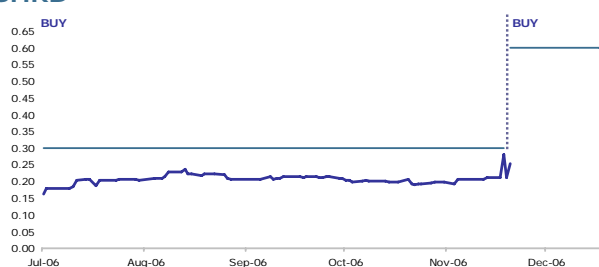
Komsomolets Donbassa

Date	Target price, USD	Market Price, USD	Rec'	Action
25-Jul-06	0.30	0.18	BUY	Initiating
15-Dec-06	0.60	0.25	BUY	Maintain

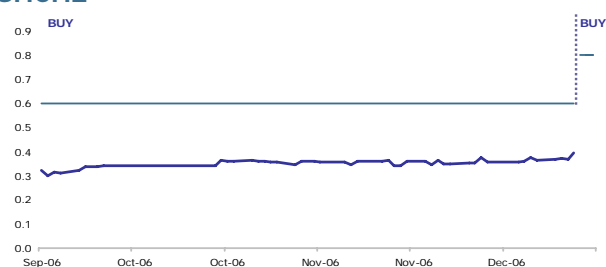
Krasnoarmiyska-Zakhidna

Date	Target price, USD	Market Price, USD	Rec'	Action
25-Jul-06	0.60	0.32	BUY	Initiating
15-Dec-06	0.80	0.40	BUY	Maintain

SHKD



SHCHZ



Concorde Capital Rating Universe

Buy	39	53%
Hold	16	22%
Sell	13	18%
Pending/Suspended	6	8%
Total	74	100%

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