

9 September 2011

Galnaftogaz

Technical Downgrade to HOLD

Technical Downgrade to Hold: Galnaftogaz' performance, +10% since we included it in our June top picks report, has left a meager 14% upside. We technically downgrade our recommendation on Galnaftogaz to HOLD, reiterating our 12M target price of USD 0.027, and remove it from our list of top picks.

Sales in 2011 should partially offset growing costs/taxes: In 1Q11, revenues increased by 19% y-o-y to USD 438 mln, in line with our projections. However, operating income declined by 56% y-o-y to USD 6.5 mln due to increased oil prices and government pressure on selling prices. We maintain our 2011E net revenue forecast at USD 1.3 bln, +19% y-o-y. Given the September increase in fuel excise taxes by EUR 50 per mt, we expect its 2011E net margin to shrink by 0.3 pp y-o-y to 3.2% and forecast net income of USD 41.1 mln in 2011E, up only 7% y-o-y.

IFC, EBRD financing to support expansion: Last week Galnaftogaz signed a USD 190 mln financing agreement with IFC and EBRD. Proceeds will be used to expand its OKKO-branded fuel station network from 298 to over 500. The debt package consists of different USD-denominated loans with six to nine year maturities. We expect the effective rate on the loans of LIBOR+4-LIBOR+5%. Galnaftogaz also signed a USD 30 mln share purchase agreement with EBRD, which could raise the latter's stake in the company from 10% now to 19%. To finance working capital, Galnaftogaz has USD 65.5 mln in unsecured short-term loans from local banks, mostly UAH-denominated.

Proposed import duties threaten margins: Energy Minister Yuriy Boyko and Naftogaz CEO Yevhen Bakulin have spoken recently of reviving import duties on oil products that were abolished in 2005. If the government implements duties as proposed at EUR 130 per mt, while prohibiting fuel retailers from raising prices proportionately, we would revise our projections for Galnaftogaz` 4Q11, as the company imports 100% of its oil supplies: gross margin down from 7% to 4% and 2011E net income by USD 10.5 mln to USD 31.1 mln.

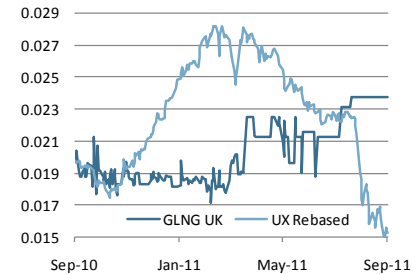
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Bloomberg	GLNG UK
Reuters	GLNG.UAX
Recommendation	HOLD
Price, USD	0.023
12M price target, USD	0.027
Upside	13.6%

No of shares, mln	19,526
Market Cap, USD mln	464
52-week performance	20.3%
ADT, 12M, USD mln	0.002
Free float, %	10%
Free float, USD mln	46.4

Prices as of Sept. 8, 2011

Price performance vs. UX



Source: Bloomberg, UX

Ownership structure

GNG Retail	63.8%
EBRD	10.3%
Other	15.0%
Free float	10.9%

Source: Company data, Concorde Capital estimates

Financial statements and forecasts, IFRS

Income statement summary, USD mln

	2005	2006	2007	2008	2009	2010	2011F	2012F
Net Revenues	379.8	514.7	635.4	1045.4	717.4	1091.7	1300.2	1495.3
Cost Of Sales	-357.6	-483.9	-591.9	-955.6	-634.8	-1000.9	-1209.4	-1360.7
Gross Profit	22.2	30.8	43.5	89.8	82.6	90.8	90.9	134.6
Other Oper. Income/Costs. net	-1.0	3.5	1.4	-21.4	-15.4	4.8	2.1	7.5
SG&A	-9.0	-13.0	-15.8	-25.7	-23.7	-30.5	-21.0	-37.4
EBITDA	16.0	26.2	36.4	54.4	56.8	79.3	87.0	123.1
<i>EBITDA margin. %</i>	<i>4.2%</i>	<i>5.1%</i>	<i>5.7%</i>	<i>5.2%</i>	<i>7.9%</i>	<i>7.3%</i>	<i>6.7%</i>	<i>8.2%</i>
Depreciation	3.7	4.9	7.2	11.7	13.2	14.2	14.9	18.4
EBIT	12.3	21.3	29.2	42.7	43.6	65.1	72.1	104.7
<i>EBIT margin. %</i>	<i>3.2%</i>	<i>4.1%</i>	<i>4.6%</i>	<i>4.1%</i>	<i>6.1%</i>	<i>6.0%</i>	<i>5.5%</i>	<i>7.0%</i>
Interest Expense	-4.4	-10.3	-14.3	-24.2	-22.1	-17.3	-18.0	-37.4
Financial income	0.2	0.0	0.1	0.1	0.4	0.3	0.0	0.0
Other income/(expense)	1.7	0.0	0.0	-125.4	-7.8	3.6	0.0	0.0
PBT	9.8	11.1	14.9	-106.8	14.1	51.8	54.1	67.3
Tax	-1.9	-2.7	-2.6	26.9	2.9	-13.3	-13.0	-13.5
Net Income	7.9	8.3	12.3	-79.9	17.0	38.5	41.1	53.8
<i>Net Margin. %</i>	<i>2.08%</i>	<i>1.61%</i>	<i>1.94%</i>	<i>-7.64%</i>	<i>2.36%</i>	<i>3.53%</i>	<i>3.16%</i>	<i>3.60%</i>

Balance sheet summary, USD mln

	2005	2006	2007	2008	2009	2010	2011F	2012F
Current Assets	79.3	98.6	110.2	108.0	205.1	240.4	273.2	291.8
Cash & Equivalents	3.2	10.4	11.2	9.9	21.1	12.9	39.0	44.9
Trade Receivables	47.4	41.5	31.0	25.9	38.8	19.3	39.0	44.9
Inventories	14.3	20.8	29.3	28.3	44.7	38.4	65.0	74.8
Other current assets	14.3	25.8	38.7	43.9	100.5	169.8	130.2	127.3
Fixed Assets	84.5	150.1	292.8	448.7	447.1	471.8	564.9	662.3
PP&E, net	80.4	146.4	278.3	420.7	427.6	429.3	520.1	613.1
Other Fixed Assets	4.2	3.7	14.5	28.0	19.5	42.5	44.8	49.2
Total Assets	163.8	248.6	403.0	556.7	652.2	712.2	838.1	954.1
Shareholders' Equity	62.0	89.2	162.8	194.2	221.0	260.0	325.8	398.6
Share Capital	31.7	31.7	31.7	23.1	24.5	24.5	24.4	24.4
Retained earnings	16.9	25.2	37.9	-30.4	-12.3	26.1	65.2	119.1
Reserves and Other	13.5	32.3	93.3	201.5	208.9	209.4	236.2	255.1
Current Liabilities	65.6	75.9	101.6	90.1	149.9	212.1	243.5	255.5
ST Interest Bearing Debt	34.9	48.3	57.1	57.6	55.0	103.2	137.5	150.0
Trade Payables	30.5	27.4	44.3	32.5	94.0	107.7	104.0	104.7
Accrued Taxes	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Other Current Liabilities	0.0	0.0	0.2	0.0	1.0	1.2	2.0	0.9
LT Liabilities	36.1	83.5	138.6	272.3	281.2	240.1	268.8	300.0
LT Interest Bearing Debt	30.8	70.3	115.6	212.2	234.6	191.0	250.0	275.0
Other LT	5.3	13.3	23.1	60.1	46.6	49.0	18.8	25.0
Total Liabilities & Equity	163.8	248.6	403.0	556.7	652.2	712.2	838.1	954.1

UAH/USD exchange rates

	2005	2006	2007	2008	2009	2010	2011F	2012F
Average	5.12	5.05	5.05	5.27	7.79	7.94	8.0	8.0
Year-end	5.05	5.05	5.05	7.58	7.98	7.96	8.0	8.0

Selected ratios

	2005	2006	2007	2008	2009	2010	2011F	2012F
Net debt/EBITDA	3.9	4.1	4.4	4.8	4.7	3.5	4.0	3.1
Net debt/Equity	1.0	1.2	1.0	1.3	1.2	1.1	1.1	1.0
Total debt/Assets	0.4	0.5	0.4	0.5	0.4	0.4	0.5	0.4
ROE	13%	9%	8%	-41%	8%	15%	13%	14%

Source: Company data, Concorde Capital projections

Appendices

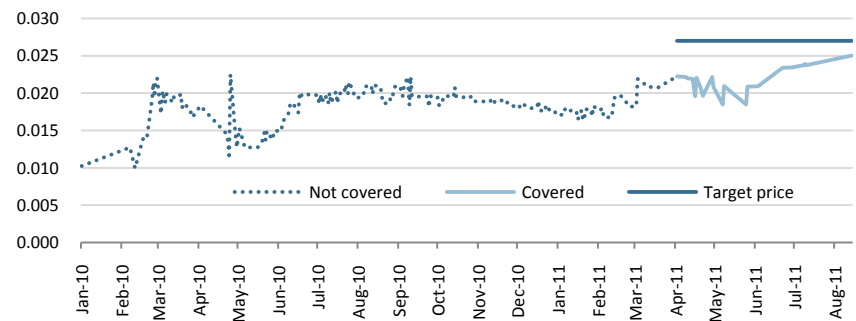
Analyst certification

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Galnaftogaz ratings history

Date	12M target price, USD	Market price, USD	Rating	Action
26-Apr-11	0.027	0.021	BUY	Maintain
10-Jun-11	0.027	0.022	BUY	Maintain
9-Sep-11	0.027	0.024	HOLD	Downgrade

Galnaftogaz: Target Price vs. Share Performance



Covered by Antonina Davydenko since April 2011

Source: Bloomberg, UX, Concorde Capital

Investment ratings

The time horizon for target prices in Concorde Capital's research is 12 months unless otherwise stated. Concorde Capital employs three basic investment ratings: Buy, Hold and Sell. Typically, Buy recommendation is associated with an upside of 15% or more from the current market price; Sell is prompted by downside from the current market price (upside <0%); Hold recommendation is generally for limited upside within 15%. Though investment ratings are generally induced by the magnitude of upside, they are not derived on this basis alone. In certain cases, an analyst may have reasons to establish a recommendation where the associated range given above does not correspond. Temporary discrepancies between an investment rating and its upside at a specific point in time due to price movement and/or volatility will be permitted; Concorde Capital may revise an investment rating at its discretion. A recommendation and/or target price might be placed Under Review when impelled by corporate events, changes in finances or operations. Investors should base decisions to Buy, Hold or Sell a stock on the complete information regarding the analyst's views in the research report and on their individual investment objectives and circumstances.

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