

04 October 2011

# Kryukiv Wagon

## We lower our target price by 40% based on order outlook

- We lower our DCF-based target price to USD 3.51 per share (from USD 5.79), which implies 51% upside. We retain a BUY rating
- We raise the cost of equity from 15.0% to 17.5% in 2011-20F due to the rise in the yield of Ukraine's Eurobond maturing in 2020 to 7.5% and increase the equity risk premium by 1 pp to 7% due to volatility on the Ukrainian stock market
- We decrease our projections for output of freight railcars by 3% to 69,900 in 2011-19E, passenger railcars by 50% to 541 units and subway railcars by 64% to 80 units, based on 8M11 output and improved order visibility
- We reduce our projections of average freight railcar prices for 2012-15E by 6% on average based on our expectations of CIS market saturation, but we slightly increase our projections for end-2011 by 5% to USD 73,000, based on 9M11 results
- The stock has steep upside relative to prices implied by railcars manufacturer peers: 49% on 2012E EV/EBITDA and 102% on 2012E P/E

### Peer multiples

	EV/EBITDA			P/E		
	10	11E	12F	10	11E	12F
<b>Kryukiv Wagon</b>	<b>3.1</b>	<b>1.8</b>	<b>2.8</b>	<b>7.1</b>	<b>2.8</b>	<b>4.2</b>
<b>Railcar peers</b>						
American Railcar Industries	42.2	6.1	3.3	n/m	206.7	12.5
Freightcar America	n/m	29.7	3.7	n/m	306.8	13.6
Greenbrier Companies Inc	9.5	7.7	4.8	77.9	24.9	6.3
Construcc y Aux de Ferrocarr	6.0	5.1	4.4	10.2	8.8	8.0
UGL Ltd	7.1	6.0	5.4	12.0	10.1	9.2
<b>Median</b>	<b>7.1</b>	<b>6.1</b>	<b>4.4</b>	<b>10.2</b>	<b>24.9</b>	<b>9.2</b>
<i>Kryukiv Wagon price implied by peers median</i>	5.28	7.52	3.48	3.35	19.44	4.74
Upside (Downside)	126%	221%	49%	43%	730%	102%

Source: Bloomberg, UX, Concorde Capital

### Vitaly Gorovoy

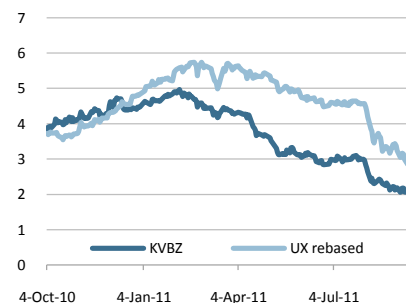
vg@concorde.com.ua

Bloomberg	KVBZ UK
Reuters	KVBZ=UA
<b>Recommendation</b>	<b>BUY</b>
Price (03 Oct 11), USD	2.33
12M price target, USD	3.51
Upside	51%

No of shares, mln	114.68
Market Cap, USD mln	267
52-week performance	-38%
ADT, 12M, USD mln	0.06
Free float, %	12.1%
Free float, USD mln	32

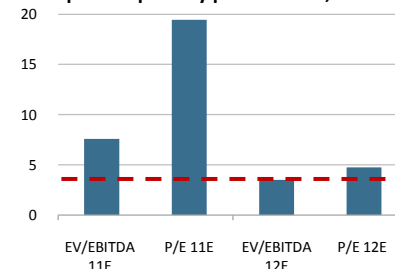
Prices as of Oct. 03, 2011

### Price performance vs. UX



Source: Bloomberg, UX

### KVBZ price implied by peer median, USD


 Note: Red dashed line indicates target price of KVBZ  
Source: Bloomberg, Concorde Capital

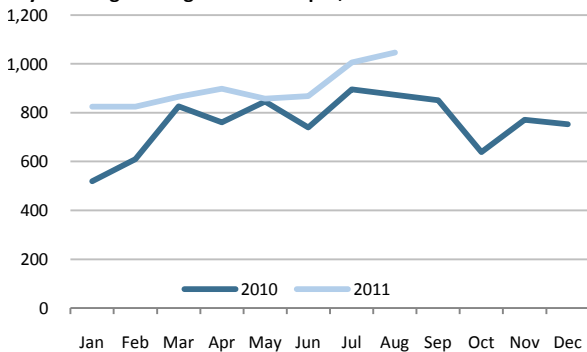
## Company update

Kryukiv Wagon produced 7,213 freight railcars in 8M11 (up 18% y-o-y) and five passenger railcars (down 2x y-o-y). The company's average freight railcar price in September 2011 was USD 75,000, up 92% from January 2010 and up 17% from January 2011.

Based on 8M11 output, we raise our freight railcar output estimates for 2011E by 27% to 10,782 units. We only slightly decrease our production projections for 2012-19E by 3% to 69.9 ths units (7,765 railcars annual average).

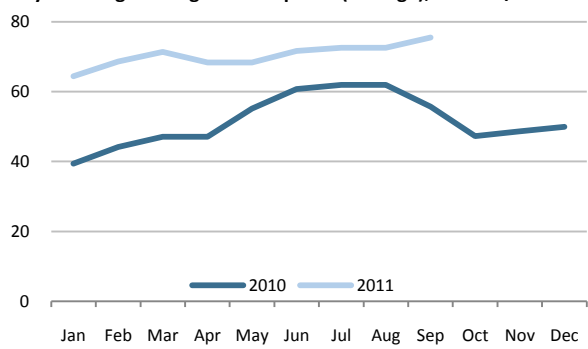
We cut our expectations for passenger railcars output by half in 2011-19E to 541 units, after First Deputy Minister of Infrastructure Konstantin Efimenko confirmed state plans to buy only 25 passenger railcars over the next four years. We do not believe Kryukiv Wagon will be able to compensate for the reduction in Ukrzaliznytsya orders from other potential buyers (Belarusian Railways, Kazakhstan Railways, etc.).

Kryukiv Wagon: freight railcar output, units



Source: Promishlennye gruzi

Kryukiv Wagon: freight railcar prices (average), USD ths/unit



Source: Promishlennye gruzi, Concorde Capital estimates

In a worst-case scenario like in 2008, we do not expect the plant to move to a shortened work week like it did then (for 13 months, it only operated for 3-day stretches), as Kryukiv Wagon has a full order book for next year.

### Forecast changes

	2011E	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
<b>Net Revenues, USD mln</b>										
New	864	603	595	601	652	677	733	789	830	893
Old	695	686	721	701	739	779	795	811	827	
Change (new/old, %)	24%	-12%	-17%	-14%	-12%	-13%	-8%	-3%	0%	
Change (y-o-y, %)	57%	-30%	-1%	1%	8%	4%	8%	8%	5%	8%
<b>EBITDA, USD mln</b>										
New	138	90	92	96	108	115	125	134	141	152
Old	128	127	115	97	105	112	115	117	119	
Change (new/old, %)	8%	-29%	-20%	-1%	3%	2%	9%	15%	18%	
Change (y-o-y, %)	89%	-35%	2%	4%	12%	7%	8%	8%	5%	8%
<b>EBITDA Margin, %</b>										
New	16.0%	15.0%	15.5%	16.0%	16.5%	17.0%	17.0%	17.0%	17.0%	17.0%
Old	18.5%	18.6%	16.0%	13.8%	14.1%	14.4%	14.4%	14.4%	14.4%	
Change (new/old, %)	-2.5%	-3.6%	-0.5%	2.2%	2.4%	2.6%	2.6%	2.6%	2.6%	
Change (y-o-y, %)	2.7%	-1.0%	0.5%	0.5%	0.5%	0.5%	0.0%	0.0%	0.0%	0.0%
<b>Freight Railcars Output, units</b>										
New	10,782	8,000	7,500	7,500	7,500	7,200	7,200	7,200	7,000	7,000
Old	8,500	8,000	8,000	7,200	7,200	7,200	7,200	7,200	7,200	
Change (new/old, %)	27%	0%	-6%	4%	4%	0%	0%	0%	-3%	
Change (y-o-y, %)	19%	-26%	-6%	0%	0%	-4%	0%	0%	-3%	0%
<b>Passenger Railcars Output, units</b>										
New	21	20	20	30	50	70	90	110	130	150
Old	50	60	75	100	125	150	150	150	150	
Change (new/old, %)	-58%	-67%	-73%	-70%	-60%	-53%	-40%	-27%	-13%	
Change (y-o-y, %)	-45%	-5%	0%	50%	67%	40%	29%	22%	18%	15%
<b>Subway Railcars Output, units</b>										
New	5	5	5	5	10	10	15	15	15	15
Old	25	25	25	25	25	25	25	25	25	
Change (new/old, %)	-80%	-80%	-80%	-80%	-60%	-60%	-40%	-40%	-40%	
Change (y-o-y, %)	-75%	0%	0%	0%	100%	0%	50%	0%	0%	0%

Source: Company data, Concorde Capital

## Valuation

### DCF model output, USD mln

	2011E	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
<b>PBT</b>	<b>125</b>	<b>81</b>	<b>83</b>	<b>87</b>	<b>97</b>	<b>104</b>	<b>113</b>	<b>122</b>	<b>128</b>	<b>138</b>
Tax Rate	23%	21%	19%	16%	16%	16%	16%	16%	16%	16%
<b>Net Income</b>	<b>96</b>	<b>64</b>	<b>67</b>	<b>73</b>	<b>82</b>	<b>88</b>	<b>95</b>	<b>102</b>	<b>108</b>	<b>116</b>
+ D&A	8	6	5	6	6	6	7	7	8	8
- Change in the OWC	(63)	(38)	(26)	(22)	(23)	(19)	(19)	(13)	(15)	(6)
- CapEx	(10)	(7)	(7)	(7)	(7)	(8)	(8)	(8)	(9)	(9)
<b>FCFF</b>	<b>0</b>	<b>24</b>	<b>39</b>	<b>49</b>	<b>58</b>	<b>67</b>	<b>75</b>	<b>89</b>	<b>92</b>	<b>110</b>
<b>WACC</b>	<b>17.2%</b>	<b>17.4%</b>	<b>17.4%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>
Sum of disc't'd CF's	200									
Terminal Value	924									
Disc'd TV	187									
Portion due to TV	48.4%									
<b>Firm Value</b>	<b>387</b>									
Less Net Debt	16									
<b>Equity Value</b>	<b>403</b>									
Implied exit EBITDA Multiple	6.1x									
Perpetuity Growth Rate	3%									
<b>Fair value of ord. share</b>	<b>3.51</b>									

Source: Concorde Capital

### Sensitivity Analysis (implied share price, USD)

	Perpetuity Growth Rate					WACC	Exit Multiple (EBITDA)				
	2.0%	3.5%	3.0%	3.5%	4.0%		4.1x	5.1x	6.1x	7.1x	8.1x
<b>WACC</b>											
-2.0%	4.15	4.24	4.34	4.44	4.56	-2.0%	3.38	3.70	4.02	4.34	4.66
-1.0%	3.74	3.81	3.89	3.98	4.07	-1.0%	3.17	3.47	3.76	4.05	4.34
0.0%	3.39	3.45	3.51	3.58	3.65	0.0%	2.98	3.25	3.51	3.78	4.05
+1.0%	3.09	3.14	3.19	3.25	3.31	+1.0%	2.80	3.05	3.29	3.54	3.78
+2.0%	2.84	2.88	2.92	2.96	3.01	+2.0%	2.63	2.86	3.09	3.31	3.54

Source: Concorde Capital

We raise the cost of equity from 15.0% to 17.5% in 2011-20F due to the rise in the yield of Ukraine's Eurobond maturing in 2020 to 7.5% and increase the equity risk premium by 1 pp to 7% due to volatility on the Ukrainian stock market.

### WACC assumptions

	2011E	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
Debt/Equity eop	0.05	0.03	0.03	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Average Interest Rate	14.1%	16.2%	15.0%	12.4%	11.0%	11.8%	12.0%	11.0%	11.0%	10.0%
Ukr Eurobonds 2020 YTM	7.5%	7.5%	7.5%	7.5%	7.5%	7.5%	7.5%	7.5%	7.5%	7.5%
Equity premium	7%	7%	7%	7%	7%	7%	7%	7%	7%	7%
Comp.-specif. Prem/Disc	3%	3%	3%	3%	3%	3%	3%	3%	3%	3%
<b>Cost of Equity</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>	<b>17.5%</b>
<b>WACC</b>	<b>17.2%</b>	<b>17.4%</b>	<b>17.4%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>17.3%</b>
<b>WACC to Perpetuity</b>	<b>17.3%</b>									

Source: Concorde Capital

Our new DCF-based target price is USD 3.51 per share (from USD 5.79), which implies 51% upside. We retain a BUY rating.

## Key risks

- **State order for Euro-2012 prototypes.** Kryukiv Wagon already produced two high-speed passenger trains for Euro-2012 at its own cost (unit cost estimated at USD 20-25 mln). If the Ukrainian government will not buy these trains, Kryukiv Wagon will be stuck with the cost. We expect a government decision in the next 6-8 months: *Medium Risk*
- **Business cyclicality.** We forecast strong demand for freight railcars in the CIS in 2011-12 and assume that demand will peak in 2Q12 before gradually declining in 2013, based on Kryukiv Wagon's current order book and the expected launches of new railcar manufacturing facilities in Russia. If freight railcar demand reaches the saturation point earlier (in 4Q11-1Q12), then revenues could fall short of our forecast. But we do not believe Russian plants will come on line sooner and expect demand for freight railcars to decrease only if global economic slowdown gets measurably worse: *Low Risk*

## Financial statements, UAS

### Income statement summary, USD mln

	2009	2010	2011E	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
<b>Net Revenues</b>	<b>182</b>	<b>551</b>	<b>864</b>	<b>603</b>	<b>595</b>	<b>601</b>	<b>652</b>	<b>677</b>	<b>733</b>	<b>789</b>	<b>830</b>	<b>893</b>
Change, y-o-y	-70.5%	202.4%	57.0%	-30.2%	-1.3%	1.1%	8.4%	3.9%	8.3%	7.7%	5.2%	7.6%
Cost Of Sales	(158)	(451)	(706)	(492)	(486)	(491)	(532)	(553)	(599)	(645)	(678)	(730)
Gross Profit	24	99	158	110	109	110	119	124	134	144	152	163
Other Operating Income/Costs. net	5	(10)	(1)	2	8	14	19	25	28	30	34	36
SG&A	(10)	(16)	(19)	(22)	(25)	(28)	(30)	(34)	(37)	(41)	(44)	(48)
<b>EBITDA</b>	<b>18</b>	<b>73</b>	<b>138</b>	<b>90</b>	<b>92</b>	<b>96</b>	<b>108</b>	<b>115</b>	<b>125</b>	<b>134</b>	<b>141</b>	<b>152</b>
EBITDA Margin. %	10.0%	13.3%	16.0%	15.0%	15.5%	16.0%	16.5%	17.0%	17.0%	17.0%	17.0%	17.0%
Depreciation	(4)	(5)	(8)	(6)	(5)	(6)	(6)	(6)	(7)	(7)	(8)	(8)
<b>EBIT</b>	<b>14</b>	<b>68</b>	<b>130</b>	<b>85</b>	<b>87</b>	<b>91</b>	<b>102</b>	<b>109</b>	<b>118</b>	<b>127</b>	<b>134</b>	<b>144</b>
EBIT Margin. %	7.7%	12.4%	15.1%	14.1%	14.6%	15.1%	15.6%	16.1%	16.1%	16.1%	16.1%	16.1%
Interest Expense	(2)	(9)	(2)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Financial Income	1	1	2	1	2	2	2	2	2	2	2	3
Other Income/(expense)	(1)	(3)	(6)	(4)	(4)	(4)	(5)	(6)	(6)	(6)	(7)	(7)
<b>PBT</b>	<b>12</b>	<b>58</b>	<b>125</b>	<b>81</b>	<b>83</b>	<b>87</b>	<b>97</b>	<b>104</b>	<b>113</b>	<b>122</b>	<b>128</b>	<b>138</b>
Tax	(3)	(20)	(29)	(17)	(16)	(14)	(16)	(17)	(18)	(19)	(20)	(22)
Effective Tax Rate	22%	35%	23.0%	21.0%	19.0%	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%
<b>Net Income</b>	<b>9</b>	<b>38</b>	<b>96</b>	<b>64</b>	<b>67</b>	<b>73</b>	<b>82</b>	<b>88</b>	<b>95</b>	<b>102</b>	<b>108</b>	<b>116</b>
Net Margin. %	5.0%	6.8%	11.1%	10.6%	11.3%	12.1%	12.6%	13.0%	13.0%	13.0%	13.0%	13.0%

Source: Company data, Concorde Capital

### Balance sheet summary, USD mln

	2009	2010	2011E	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
<b>Current Assets</b>	<b>144</b>	<b>265</b>	<b>267</b>	<b>293</b>	<b>316</b>	<b>345</b>	<b>368</b>	<b>395</b>	<b>416</b>	<b>436</b>	<b>450</b>	<b>265</b>
Cash & Equivalents	8	35	24	24	24	26	27	30	32	34	36	35
Trade Receivables	26	10	7	7	7	7	8	8	9	9	10	10
Inventories	66	106	74	73	74	80	83	90	97	102	109	106
Other Current Assets	44	115	162	189	211	232	250	267	278	291	294	115
<b>Fixed Assets</b>	<b>52</b>	<b>78</b>	<b>78</b>	<b>86</b>	<b>92</b>	<b>101</b>	<b>108</b>	<b>116</b>	<b>122</b>	<b>128</b>	<b>132</b>	<b>78</b>
PP&E, Net	38	51	52	57	61	67	71	77	81	84	87	51
Other Fixed Assets	14	26	26	29	31	34	36	39	41	43	45	26
<b>Total Assets</b>	<b>196</b>	<b>343</b>	<b>346</b>	<b>378</b>	<b>408</b>	<b>447</b>	<b>476</b>	<b>510</b>	<b>537</b>	<b>563</b>	<b>582</b>	<b>343</b>
<b>Shareholders' Equity</b>	<b>151</b>	<b>246</b>	<b>278</b>	<b>312</b>	<b>341</b>	<b>374</b>	<b>400</b>	<b>428</b>	<b>449</b>	<b>470</b>	<b>482</b>	<b>246</b>
Share Capital	11	11	11	11	11	11	11	11	11	11	11	11
Reserves and Other	140	235	267	301	330	363	389	418	438	460	471	235
<b>Current Liabilities</b>	<b>46</b>	<b>97</b>	<b>68</b>	<b>67</b>	<b>67</b>	<b>73</b>	<b>76</b>	<b>82</b>	<b>88</b>	<b>93</b>	<b>100</b>	<b>97</b>
ST Interest Bearing Debt	6	12	8	8	8	9	9	10	11	11	12	12
Trade Payables	7	7	5	5	5	5	6	6	6	7	7	7
Accrued Wages	1	4	3	3	3	3	3	4	4	4	4	4
Accrued Taxes	0	3	2	2	2	2	2	2	2	2	3	3
Other Current Liabilities	31	71	50	49	50	54	56	60	65	68	74	71
<b>LT Liabilities</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
LT Interest Bearing Debt	0	0	0	0	0	0	0	0	0	0	0	0
Other LT	0	0	0	0	0	0	0	0	0	0	0	0
<b>Total Liabilities &amp; Equity</b>	<b>196</b>	<b>343</b>	<b>346</b>	<b>378</b>	<b>408</b>	<b>447</b>	<b>476</b>	<b>510</b>	<b>537</b>	<b>563</b>	<b>582</b>	<b>343</b>

Source: Company data, Concorde Capital

### UAH/USD exchange rates

	2009	2010	2011E	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2020F
Average	7.90	7.94	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00
Year-end	7.99	7.96	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00

Source: NBU, Concorde Capital

## Appendices

### Analyst certification

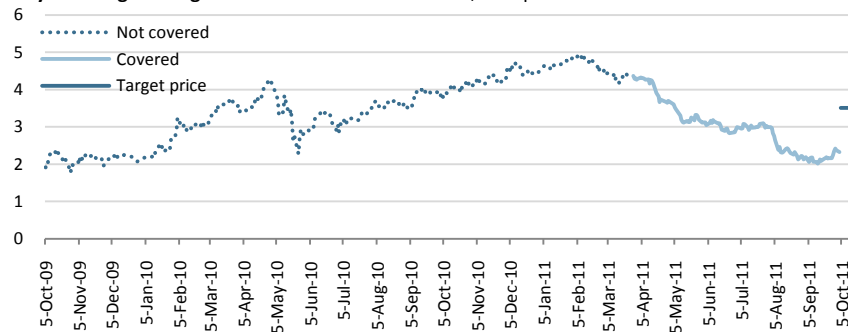
I, Vitaly Gorovoy, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views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

#### Kryukiv Wagon target price history

Date	12M target price, USD	Market price, USD	Rating	Action
04-Oct-11	3.51	2.33	BUY	Maintain

Source: Concorde Capital

#### Kryukiv Wagon: Target Price vs. Share Performance, USD per share



Covered by Vitaly Gorovoy since April 2011

Source: 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.

## Contacts

### CONCORDE CAPITAL

2 Mechnikova Street, 16th Floor  
 Parus Business Centre  
 Kyiv 01601, Ukraine  
 Tel.: +380 44 391 5577  
 Fax: +380 44 391 5571  
 www.concorde.ua  
 Bloomberg: TYPE CONR <GO>

#### CEO

Igor Mazepa im@concorde.com.ua

#### SALES

##### Head of Sales & Trading

Luba Yurchyk ly@concorde.com.ua

##### International Sales & Trading

Katerina Shevchenko ksh@concorde.com.ua  
 Marina Martirosyan mm@concorde.com.ua  
 Rostyslav Shmanenko rs@concorde.com.ua  
 Dasha Vasilieva vd@concorde.com.ua

#### RESEARCH

##### Head of Research

Andriy Gerus ga@concorde.com.ua

##### Utilities, Agriculture, Consumer

Yegor Samusenko syg@concorde.com.ua

##### Basic materials

Andriy Gerus ga@concorde.com.ua

##### Energy, Chemicals

Antonina Davydenko ada@concorde.com.ua

##### Equity strategy, Industrial machinery

Vitaly Gorovoy vg@concorde.com.ua

##### Economics, Financials

Svetlana Rekrut sr@concorde.com.ua

##### Fixed income

Andriy Gerus ga@concorde.com.ua  
 Svetlana Rekrut sr@concorde.com.ua

##### Politics

Brad Wells bw@concorde.com.ua

##### Editor

Brad Wells bw@concorde.com.ua

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