

Initiating coverage

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Ekvin

Capturing The Growth

Bloomberg KVIN UZ

Market data

Market price, USD 105

Shares, mln 0.8

MCap, USD mln 84.3

Free float, shares 20.0%

FF MCap, USD mln 16.7

12M target

Price, USD 160.0

Upside 52%

Ownership

Management 80.0%

Institutional investors 20.0%

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INVESTMENT CASE

Bloomberg KVIN UZ

Market data

Market price, USD 105.0

Shares, mln	0.803
MCap, USD mln	84.3
Free float, shares	20.0%
FF MCap, USD mln	16.7

12M target

Price, USD	160.0
Upside	52%

Ownership

Management	80.0%
Institutional investors	20.0%

Indicators, 2006

# of outlets	51
Trading area, ths sq. m	19,127

Ekvin, operator of Ukraine's third largest consumer electronics chain – MKS, is on the verge of launching its ambitious expansion program. A 20% equity placement, which raised USD 14.5 mln in late 2006, geared up Ekvin to transform its 51-outlet retail chain into a full-fledged nation-wide franchise. In 2007 alone the company wants to open an additional 46 new outlets. In 2007-2009 MKS's trade area is planned to grow by more than 50% CAGR. We initiate coverage with BUY recommendation and set our twelve-month target at USD 150 per share.

Rapidly growing market

Ukraine's retail industry with a 23% CAGR over the past four years in real terms is the fastest growing CEE retail market. Consumer electronics' recent growth at 30% CAGR over 2003-2006 outpaced foods and the overall retail sector. Retail growth was boosted as real incomes increased by 16% CAGR and consumer lending jumped by 100% CAGR from 2001 to 2006. Low penetration will support further growth in consumer electronics by at least 25%-30% CAGR in the next three years.

MKS: Geared up for prompt expansion

Proceeds of USD 14.5 mln from a 20% stake placement in late 2006 gives MKS solid grounding to start realizing its 3-year retail chain expansion program. MKS is targeting new outlet expansion of 48% and growth in trading area of 57% CAGR over 2007-2009. MKS's diversified arsenal of trade formats (convenience stores, hypermarkets and supermarkets) will work to its advantage, as will nation-wide brand recognition. We expect MKS to see at least three years of growth above the market average.

PC and Audio/video segments major growth drivers

MKS is the #4 PC assembler in the country and generates more than half of its revenue from computers. Ukraine's low PC penetration level of nine PCs per every hundred residents leaves room for an attractive upside as the country catches up to other European countries. An aggressive push for laptops will bring about an acceleration in computer sales to 50% CAGR over the next four years. The Audio/Video segment will also be on the rise, driven by new global technologies as MP3 players and flat screen TVs lead consumers to replace old products *en masse*. We expect MKS's A/V revenues to accelerate by 68% CAGR in 2007-2010.

Key Financials, USD mln

	Net Revenue	EBITDA	Net Income
2006	115	2.5	neg
2007E	184	4.6	0.7
2008E	367	11.0	5.2

Spot exchange rate: 5.05

Price Ratios

	EV/S	EV/EBITDA	P/E
	0.9	40.7	Nm
	0.5	18.5	46.2
	0.3	8.7	14.8

2006 Results

Retail chain roll-out program set for launch

Having strengthened its investment power with an equity placement, the company is now set to start realizing its expansion project. According to management, the company has already negotiated thirty property lease agreements for new stores, which ensures execution of MKS's 2007 retail network expansion target by 65%. By the end of the month, MKS will already widen its network by adding four new stores.

Stronger sales

MKS's reported 2006 sales results came in 11% higher than we expected and reached USD 115 mln. Eight new outlets added to MKS's retail network in the last three months of 2006 arrived just in time to capitalize on the Christmas spending spree. The new additions appeared to be rather fertile and generated about 7% of the company's total 4Q06 revenues.

MKS's 2006 results

	2005	2006	chg., % yoy	2007E	chg., % yoy
Net Sales, USD mln	90.5	114.6	27%	183.6	60%
EBITDA, USD mln	2.2	2.5	13%	5.6	86%
Net Income, USD mln	0.1	-2.3		0.7	
EBITDA margin	2.4%	2.2%		2.5%	
Net margin	0.1%	neg		0.4%	

Source: Company data

Reshuffling product mix to sustain robust growth

In 2006 MKS intensified efforts to rearrange its product mix in favor of more promising segments: laptops and audio/video products, which were the company's major growth drivers. At the same, the low-margins for mobile phones and white goods, the most saturated consumer electronic segment in Ukraine, slowed growth last year.

Laptops secured higher PC sales

The company's PC sales grew by 21% yoy, beating our forecast of 8% yoy. Over the last year, a reshuffled PC product mix toward more in-demand laptops led it to continue strong growth in computer sales in 2006. Laptops sales grew by 62% yoy, increasing their share to 18% of MKS's total PC turnover in 2006 versus 13% one year ago.

Deeper penetration into brown goods

Brown goods and especially audio/video products were the company's growth leaders. Growth in audio/video sector accelerated 59% yoy last year, generating 18% of total revenues for the period, compared to 16% in 2005. We are encouraged by the company's strong overall brown goods growth- it is a high-margin segment for MKS. Over the next four years, we expect brown goods will be an important growth driver - the company is set to capitalize on a favorable product cycle for the segment with the central catalyst as acceleration in flat panel TV adoption and digital audio devices.

Opening up new markets drags profitability

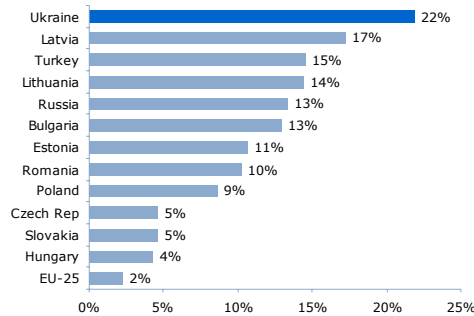
As we expected, MKS's earnings were negative in 2006. The company put the efficiency of its retail network under review and at the same time was active in entering new regional markets. In 2006 MKS got rid of sixteen poor-performing outlets and simultaneously added eleven new stores. This drove operational costs higher and, to greater extent, constrained growth in sales in 2006. Relatively high-cost borrowing that it had to use to finance its expansion last year depressed MKS's net margins further - financial expenses as a percentage of net sales doubled to 3.3% in 2006. In order to lower borrowing costs, the company changed its major lender in 2H06 to Russian VTB and incurred an additional one-time re-pricing charge. We expect this move will lead to a decrease in MKS's cost of borrowing rate by 4% in 2007.

UKRAINE'S RETAIL BOOM

Central & Eastern Europe's fastest growing market

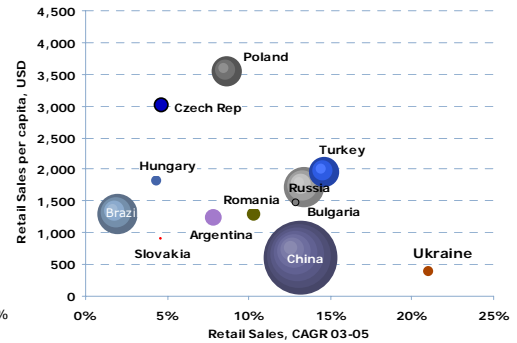
Ukraine's retail trade, at 22% CAGR in 2003-05 in real terms, was the fastest growing retail market in Central and Eastern Europe (CEE) and one of Ukraine's most dynamic sectors. In 2005, with total retail turnover of USD 18.4 bln, Ukraine became the #5 retail market in CEE (without Russia and Turkey). In 2006 Ukraine's retail sector growth accelerated to 25.3% yoy and expanded to USD 25.8 bln.

Retail sales in Europe, CAGR 03-05



Source: Bloomberg, National Statistic Agencies

Ukraine's retail sector vs. Global markets



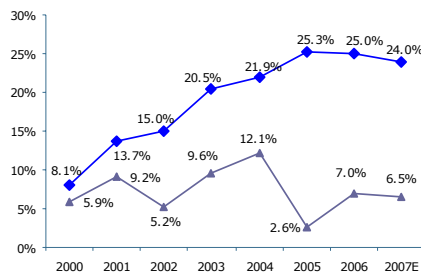
Bubble size represents retail turnover

After several years of strong growth, the Ukrainian retail sector is still in its infancy by global standards. Low retail sales per capita and a substantially low number of total retail outlets indicates that the local market is still years from saturation.

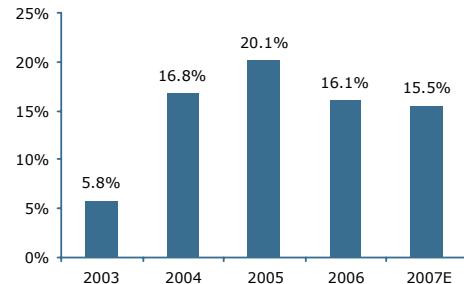
Macroeconomic environment favors further growth

Strong growth in the retail sector is a direct consequence of healthy economic performance as well as rapid growth in real income. Over the last five years, Ukraine's real GDP growth was 7.2% CAGR. Increased budget spending on salaries in the public sector and social payments supported real income growth of 16.0% CAGR between 2002 and 2006:

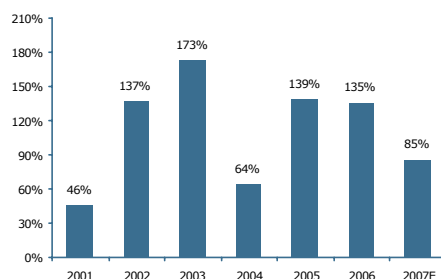
Growth: Retail turnover vs real GDP



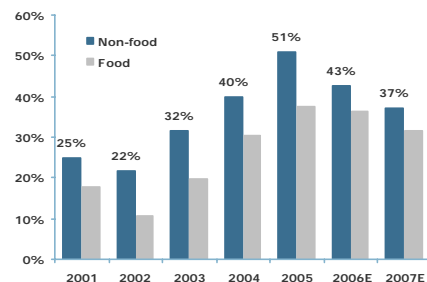
Growth in real disposable income



Consumer loan growth



Non-food vs food retail sales



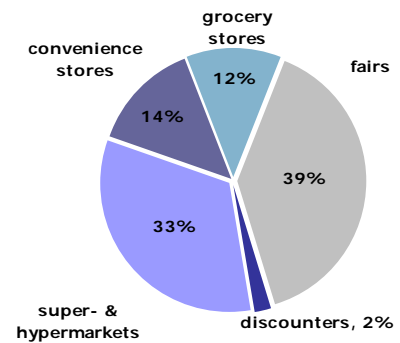
Source: Ukrainian State Statistics Committee

We expect that in the mid-term, the Ukrainian retail sector will continue to enjoy double-digit growth, even though the growth rate is likely to be slightly below the levels of recent years. We estimate that the retail sector will perform at 17-18% CAGR in real terms during the next four years. Our forecasted retail turnover is based on a sound outlook for real disposable income (15-16% p.a.), which will be propelled by strong GDP growth (6% p.a.), ongoing social spending increases and a modest inflation rate (8-9%).

Modern formats gain market share

The key trend over the last several years has been the rise of modern retail formats. Low prices, the main advantage of open markets, is not as crucial for consumers as it was before. Over the last few years, Ukrainians shifted their preferences toward civilized trade formats: unorganized trade accounted for 39% of total retail sales in 2006 against more than 50% in 2002-03. Soviet-style shops are gradually closing and more modern retail outlets are opening in Kyiv and other large urban areas, while open-air markets continue to dominate in the regions.

Ukraine's retail by trade channel



Source: Ukraine's Statistic Committee

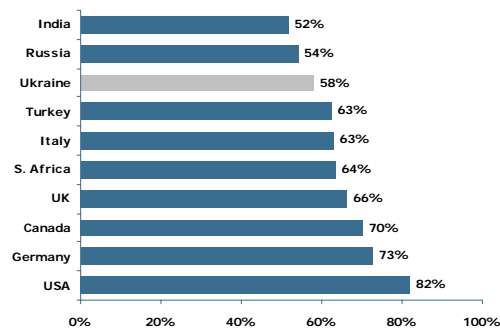
Super and hypermarkets have experienced the highest growth rates in terms of volume, expanding their market share to 33% in 2006 from 8-10% in 2002-03. However, only 25-30% of them are considered to use a real modern format, which implies that modern formats account for only 15% of the country's retail turnover.

Despite the success achieved by modern retail formats in gaining a market share, unorganized trade still retains a share in Ukrainian retail. We believe modern retail will continue to grow thanks to both overall market expansion and, more importantly, market share gains at the expense of unorganized trade.

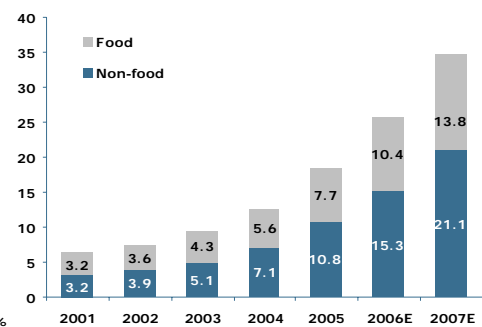
Higher share of non-food products

Following the improved welfare level of Ukrainian consumers, the structure of retail trade changed, with non-food sales gaining the major share of total sales in 2002. Record growth in consumer lending since 2000 was enough to fuel growth in non-food sales of 33% CAGR in 2001-05 versus 28% achieved by the market, which brought non-food products to 58% of total retail turnover.

Non-food portion in total retail sales



Food vs. non-food sales in Ukraine



Source: National Statistics Committees, Ukraine's Statistic Committee

Nevertheless, Ukraine's 42% share of food sales is still relatively high. In developed economies, food normally accounts for about one-third of the aggregate retail market. We expect the proportion of food sales to gradually fall with further improvements in the social sphere.

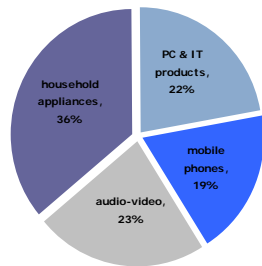
Regions become key growth engine

Regional markets are rapidly becoming a key source of growth for Ukrainian retailers due to low modern trade penetration in retail sales (retail chains account for only around 15% of total sales in regions vs. 30% in Kyiv) and fast growing disposable income. The combination of these two factors makes regional markets attractive for retailers in terms of growth opportunities. Top domestic retailers have aggressively started expanding in the regions to secure a share in the fast growing markets.

Ukraine's consumer electronics: Fast growing child

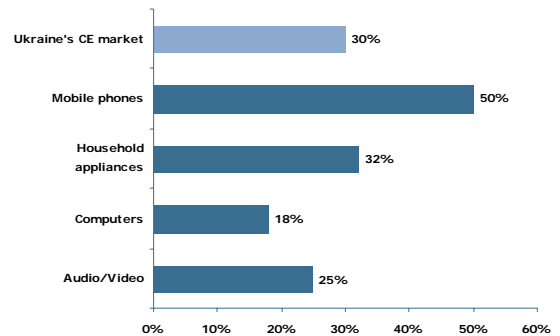
In the last few years, consumer electronics (CE) was the most dynamic segment in Ukraine's retail sector. The country's CE retail turnover has been expanding at 30% CAGR between 2003-2006, far above the overall retail sector average of 23%. The size of the CE market is estimated at USD 7.2 bln in 2006.

CE market breakdown by segment



Source: Ukraine's Statistic Committee

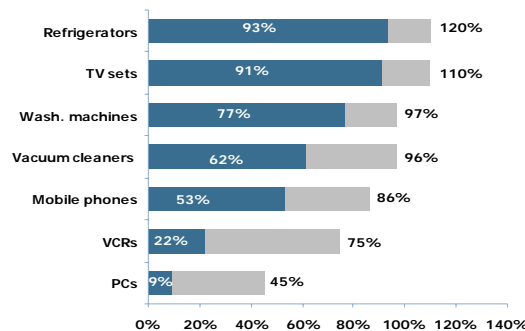
Ukraine's CE market CAGR 2003-06E



Household appliances currently account for around 36% of total CE sales. As more urgent products for most consumers, household appliances are better positioned to benefit from the higher incomes of Ukrainian consumers. As household appliances approach saturation, growth is expected to slow in the mid-term.

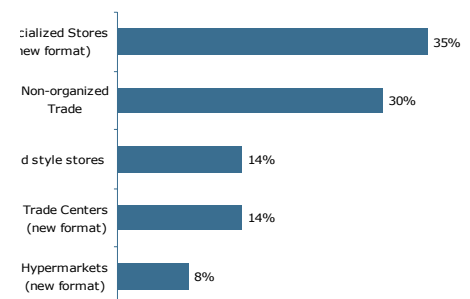
At the same time, PC & IT-related products, despite strong growth in the last few years (21% CAGR 2003-2006), still account for a small portion of total CE sales.

Ukraine's CE product penetration



Source: Ukraine's Statistic Committee, IDC Agency

CE sales breakdown by trade channel



The current level of market penetration clearly reveals the sector's future growth leaders. Striking under-penetration in the computer segment reveals an immense potential for growth. Mobile phone sales, due to frequent innovations and upgrades, are also expected to see further mid-term growth. Flat screen TVs and MP3 players should secure strong brown goods sales during the next three-four years as prices decline to levels that make them a mass consumption product.

Unlike food retail, unorganized trade formats account for a smaller share of total CE sales. Due to the sophisticated nature of CE products, in particular for IT-related products, specialized stores and supermarkets are the most appropriate trade formats. In Ukraine, the portion of consumer electronics sales through modern trade formats is currently estimated at 55-60%.

Market players

Market fragmentation remains high

The market for consumer electronics in Ukraine is highly fragmented, with about 25 retail chains operating some 600 stores. No market player accounts for more than 7% of the consumer electronics market. Most consumer electronics chains have strong exposure to the currently high-marginal household appliances segment, which posted strong growth in the last four years.

Only two consumer electronics retailers - Foxtrot and Eldorado - have a nationwide presence; other chains remain more regionally focused, with strong footprints in eastern and southern Ukraine - areas with the population has a higher net income.

Key Ukrainian CE retailers

	Eldorado	Foxtrot	MKS	Unitrade	City.com	Domotechnika	DiaWest
Product Focus	household appliances	household appliances & computing electronics	computer electronics	computer electronics	computer electronics	household appliances	computer electronics
Format	hyper-supermarkets	specialty store, hyper-supermarkets	specialty store, hyper-supermarkets	specialty store	cash&carry, hypermarkets	supermarket	specialty Store
Key operating indicators:							
2005 Revenues, USD mn	229	176	90	44	31	39	15
# of stores opened in '04-06	35	47	25	15	8	7	34
Current # of stores	75	150	51	31	8	19	56
Total area, sq.m. YE2005	50,000	93,000	34,023	6,587	8,800	33,000	3,280
Key financial indicators, 2005:							
Gross margin,%	4.8%	na	11.1%	11.0%	10.3%	6.7%	1.1%
Operating margin, %	na	na	1.6%	1.3%	3.1%	2.0%	0.3%
Net margin, %	na	na	0.1%	0.0%	2.1%	0.4%	0.1%

Source: Company data, State Statistic Committee. Note: City.com and Unitrade are operated by AVentures group.

Thin margins posted by Ukraine's CE retailers, quite a common thing for a rapidly expanding market, reflect the player's rush to carve the deepest market share possible with little regard to costs. Focus on operational efficiency will become topical at later stages of the market. Establishing a nationwide franchise and achieving strong brand recognition are the areas where management is adding the most value at the moment.

So far M&A and foreign interest has been sluggish

All local players have preferred to expand organically rather through M&A deals. Only three deals were posted: in December 2005, Russian retailer Euroset acquired the Ukrainian handset retailer Mobilka. In 2004, Greek Germanos acquired a 60% equity stake in consumer electronics retailer Mobitel, and Russian Mobitec Group acquired a majority stake in Ukrainian Mobiland.

The Russian retail chain Eldorado penetrated the Ukrainian market in 2001 as a green-field project. In 2005, the UK-based Dixons Group assumed an option to buy an initial 10 percent in Eldorado by 2008. If the option is exercised, Dixons Group will then have another option until 2011 to acquire full control of the Russian group.

As the market will continue to see double digit growth, international consumer electronics groups are expected to step into the Ukrainian retail sector. So far, German Karstadt-Quelle and Russian Divizion have announced plans to enter the Ukrainian market.

Local consolidation must also come after another one to two years of organic growth. We see AVentures Group, Foxtrot Group, Eldorado and MKS as the key candidates for the role of consolidator. With a similar product profile, format, and larger size AVentures is considered to be the major rival to MKS and is likely to be in the hunt for the same acquisition candidates.

Eldorado is dedicated to organic growth, but if Dixons Group exercises its option to buy 10% in 2008, it might make Eldorado more aggressive in their expansion and possibly takeovers.

Corporate wars among Foxtrot Group's shareholders might lead to the sale of the chain to an international strategic investor, which might present more competition to MKS's expansion plans.

PC & IT-related segment

The PC retail segment is currently occupied by 7 retail chains, operating 182 points-of-sale. Most computing electronics retailers started as PC assemblers that focused on sales to corporate clients. The increasing share of households in PC purchases forced them to diversify their distribution channels.

Penetration into retail allowed these retailers to better position themselves vis-à-vis smaller competitors - Ukrainian private entrepreneurs, which are capable of assembling up to 2,000 PCs. As a result, the market share of private entrepreneurs decreased from 67% in 2003 to an estimated 60% in 2006.

Ukraine's top PC assemblers

	Kvazar Micro	MKS	Inkom	Compass	Navigator	Diawest
Installed capacities, units	180,000	>87,600	84,000	72,000	60,000	42,000
Client sector	corporate and retail	retail and corporate	corporate	retail and corporate	corporate and retail	retail
# of own retail stores	none	51	none	12	none	54
Distribution channels	50% -corporate clients, 19% - retail stores of partners, 31% to dealers	70% - retail chain, 20% - corporate clients, 10% - dealers	through its regional branches	50% -its own and partner retail stores, 50% - corporate clients	65% - corporate clients, 20% dealers 5% retail, 10% to other assemblers	through its stores

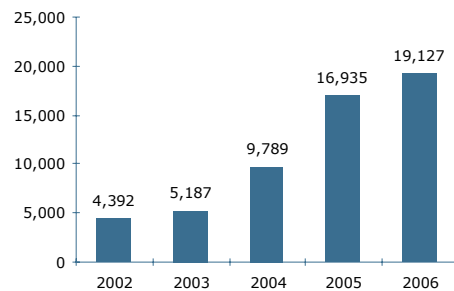
Source: Expert Ukraine

MKS franchise

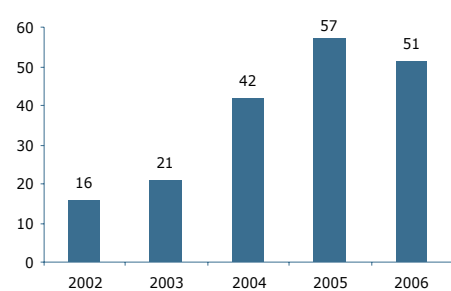
Profile

Kharkiv-based MKS started as a PC assembly company in 1990, and gradually evolved into the country's third largest consumer electronics retailer, in terms of sales. Although it is focused on PC & IT products, MKS has significant exposure to other top consumer electronics segments. Its network of 51 stores, with over 20 ths sq m of retail space, possesses a footprint in 12 regions of Ukraine, which makes MKS #4 in terms of national coverage. MKS operates three different retail formats: hypermarkets, supermarkets (CE supermarkets and computer supermarkets) and convenience stores.

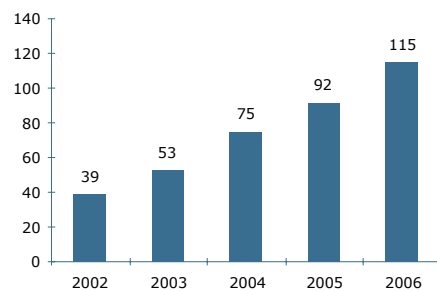
Total trading area, ths sq. m



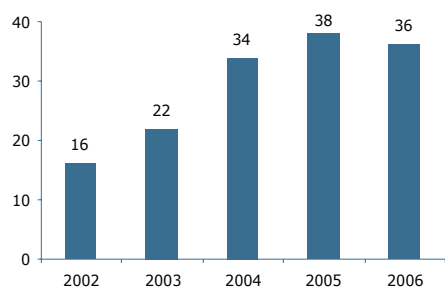
Number of outlets



Net sales dynamics, USD mln



MKS's PC assembling, units ths



Source: Company data, Concorde Capital

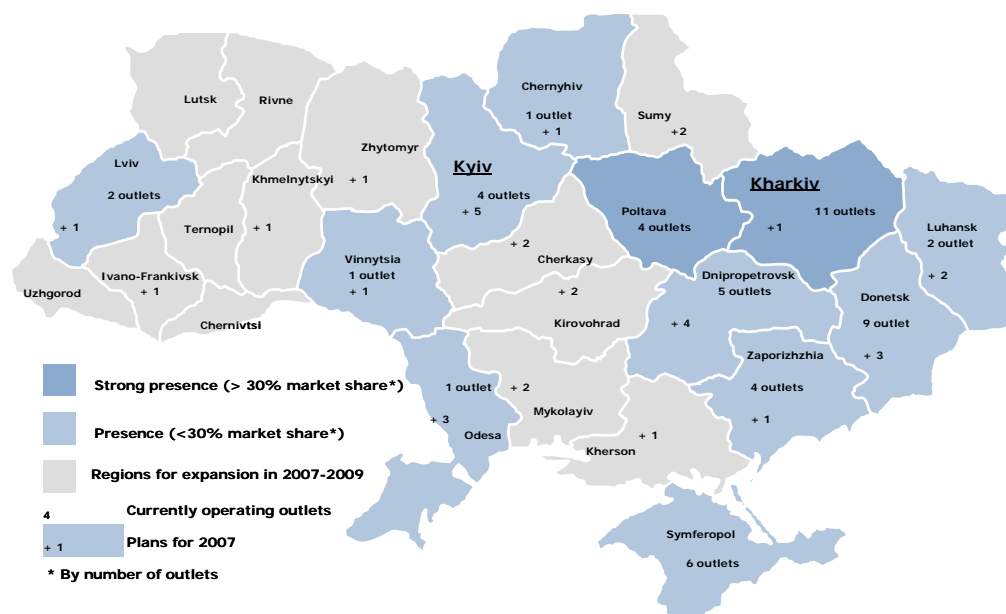
Light on its feet

MKS's multi-format approach has significantly expanded its market exposure. The company's convenience stores specializing in MKS branded PC products represent an efficient tool for exploring new market opportunities. Due to their relatively small size and low capital needs, they are able to provide quick exposure to the most promising market segments, both in terms of price and geographic location. These stores make up the bulk of the company's retail network.

Most of the company's trading space (~70%) is leased. The management views leases as the fastest and cheapest way to expand its network.

Focused on the right region

In terms of its geographic focus, MKS's expansion strategy is differentiated from those of other CE retailers in its early stages. While other competitors tended to set up outlets closer to Kyiv, MKS advanced into the regions, with a strong focus in Kharkiv and other industrially-developed eastern regions. More than half of MKS's stores are currently located in the six eastern regions, which is now Ukraine's biggest consumer market with 40% of total retail sales.



Source: Company data, Concorde Capital

Kyiv: Precision expansion

After years of growth, Kyiv leads Ukraine in retail market saturation. Nevertheless, the Ukrainian capital still has plenty of room for further growth. A sharp drop in suitable retail space for modern trade formats and the resulting high rental costs have hampered further development of retail chains. Moreover, intense competition and sophisticated consumers makes successful entry into Kyiv's market a challenging task. Conversely, Ukraine's capital remains retailers' most targeted market, as it offers exposure to the largest upper-middle class population in the country.

While entering Kyiv's market, MKS employed precise approach, focused only on its strongest product segment (PC & IT-related goods) and selected the most suitable trade format (convenience stores and later supermarkets). The ability to select premium locations for its outlets was another key factor that ensured the success of MKS branded stores. Currently, the company is operating four stores in Kyiv, which are MKS's top sales generators based on sq meters of retail space.

The roll-out program

In terms of creating a national franchise, MKS's management has worked out a 3-year network expansion program worth USD 26 mln. Nation-wide coverage is planned to be achieved during 2008.

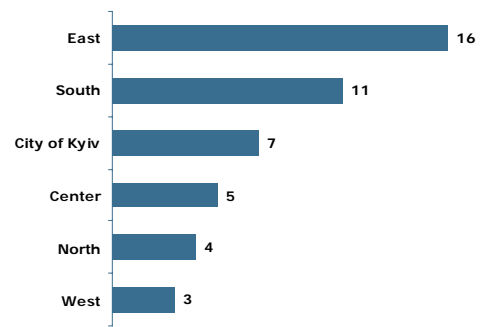
MKS's mid-term expansion plan

	investments per 1 outlet	2007		2008		2009	
		# of new outlets	total investments	# of new outlets	total investments	# of new outlets	total investments
Hypermarkets	665	7	4,655	4	2,660	8	5,320
CE supermarkets	246	7	1,722	0	0	7	1,722
Computer supermarkets	147	16	2,352	9	1,323	16	2,352
Computer stores	63	16	1,008	10	630	16	1,008
Renovation of existing outlets			569		105		105
Total investment for the year		46	10,306	23	4,718	47	10,507

Source: Company data, Concorde Capital

During the next three years, the company plans to triple its number of outlets to a total of 167 by the end of 2009. MKS is primarily seeking to strengthen its footprint in eastern Ukraine, its the core regional market, as well as underserved regions, especially in under-penetrated western and central Ukraine. The company plans to have nation-wide coverage by 2008.

Network expansion by region in 2007

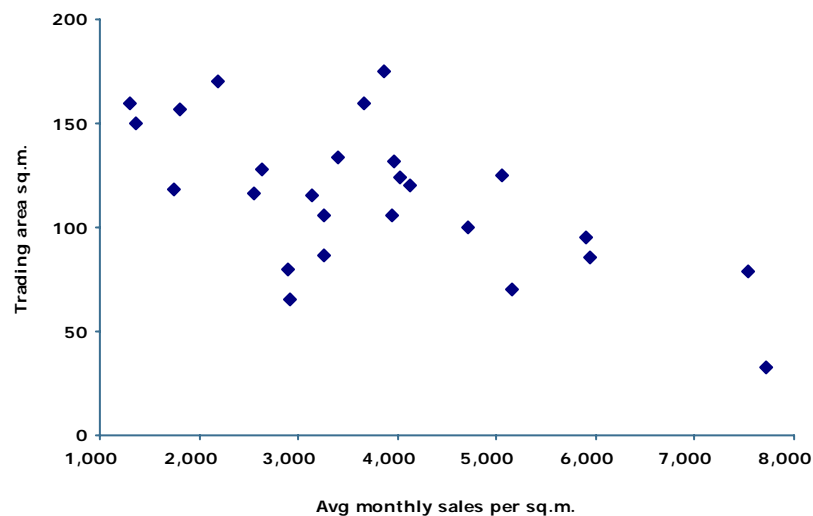


Source: Company data

The company will continue to rely on its core product group (PC and IT-related items) to capture the largest growth during the next three years.

MKS will stick with its multi-format expansion strategy (described in detailed in the next section). Hypermarkets and CE supermarkets will be a vehicle for establishing a strong footprint in key regions and cities, as well as a channel to serve higher-income customers. Specialized PC stores and computer supermarkets will provide the fastest way to enter new markets. A converse economy of scale works here: statistics prove that the smaller a computer store's trading space, the higher the sales per square meter, as shown in the diagram below. In a nutshell - you pay less to generate more sales per sq m.

Computer stores: Average sales per sq. m vs trading area



Source: Company data, Concorde Capital

Trading formats

High brand recognition

Unlike its domestic peers that use multiple brands, MKS uses multiple formats but relies on a single-brand. The commitment and development of its MKS brand materialized in the form of high brand recognition and awareness among customers, a significant competitive advantage. According to research conducted by the international agency TNS Ukraine, MKS branded desktops were recognized as the #3 best in spring 2006, and MKS's PC & IT-related stores were recognized as the best place to make a purchase.

Multi-format approach

MKS has built its network on three of the most important modern trade formats – hypermarkets, supermarkets and convenience stores. The multi-format strategy enables the company to have exposure to different market segments in terms of price and geographic location, in addition to increasing its flexibility in terms of the format for new stores. MKS always has the option of re-formatting old stores if needed. Converting its store formats over time will allow the company to increase the efficiency of its existing retail space and raise profitability.

On the other hand, the multi-format strategy calls for precise management execution and fine-tuned logistics. MKS's management has demonstrated their ability to manage growth in a multi-format framework. Only two other CE retailers follow a multi-format strategy, while others lag behind, unprepared to replicate their experience on a full scale at the moment.

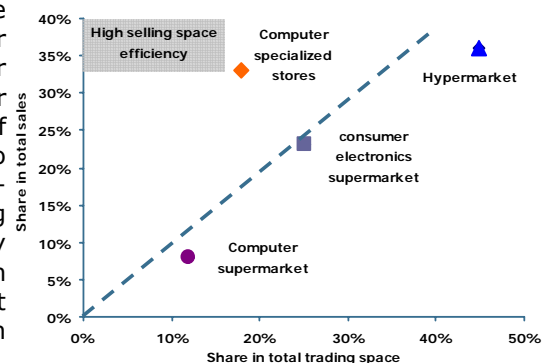
Hyper & Mini format interplay

Small size fits PCs best

In addition to being the most suitable format for rapid network rollout, MKS's computer stores and supermarkets are ideally suited for PC and IT-related products. The sophisticated nature of these products requires an individual approach, which is not possible in the larger-size formats.

PC & IT stores and supermarkets target the lower and middle income brackets by charging lower markups compared to other formats. However, due to their proximity and the recognition of the MKS brand, the stores are also attracting customers with above-average incomes. This pricing policy allows these stores to enjoy high customer traffic, which eventually will enable them to post superior sales per sq. meter. In terms of retail space utilization, small size formats rank the highest in sales per square meter.

Trade space efficiency by formats



Source: Company data, Concorde Capital

Hyper size

Hypermarkets and supermarkets that utilize premium product pricing mostly target customers with average and above-average incomes, which is where the markups are. Although they have a wider range of products and prices, they also cover the low income-segment. With their focus on the middle and upper middle-class brackets, these formats post higher margins, but sales per square meter are lower than in smaller formats.

Insight into the efficiency

The level of a retail outlet's efficiency and its sales generation capacities differs among MKS's retail network and is largely an interplay of two factors: age, location.

Age

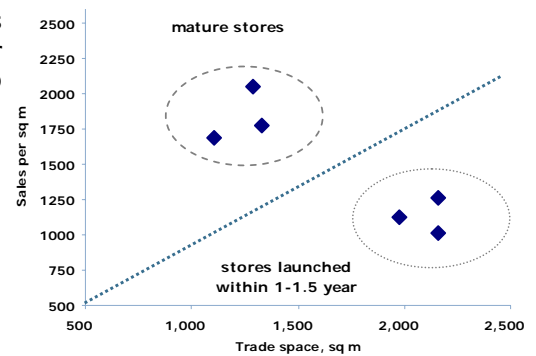
Currently, MKS's network is still far from its full sales potential because one-fourth of MKS's network was launched within a year and another 10% were launched 1.5 years ago (but are seeing growth).

Normally, it takes about a year for an outlet to reach substantial sales volumes. The time required to grow to the point where sales mature differs by format. Small-size and low-cost convenience stores usually have shorter terms - from 3 to 7 months, while a massive hypermarket can take up to two years to reach its target sales turnover.

Location

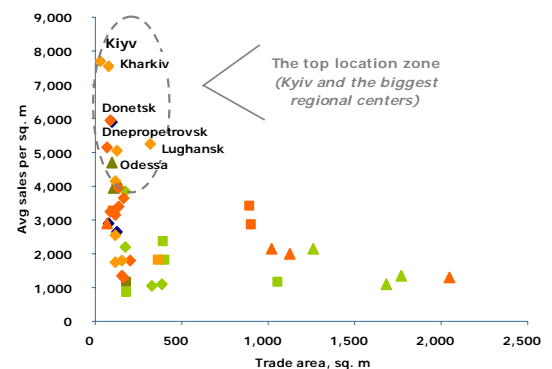
The choice of a suitable location is another important determinant of the success of a retail network. The right location can be a powerful sales booster and significantly shorten its maturation period. MKS's four outlets that operate in Kyiv are the best example of this. With a total retail space of 650 sq. m, these small retail outlets effectively utilize their premium location to generate the highest sales volumes per square meter in the company's entire network. MKS has often been a first-mover into regional markets, allowing it to secure favorable locations.

Hypermarkets at different maturity stages



Source: Company data, Concorde Capital

Formats' location and maturity stage



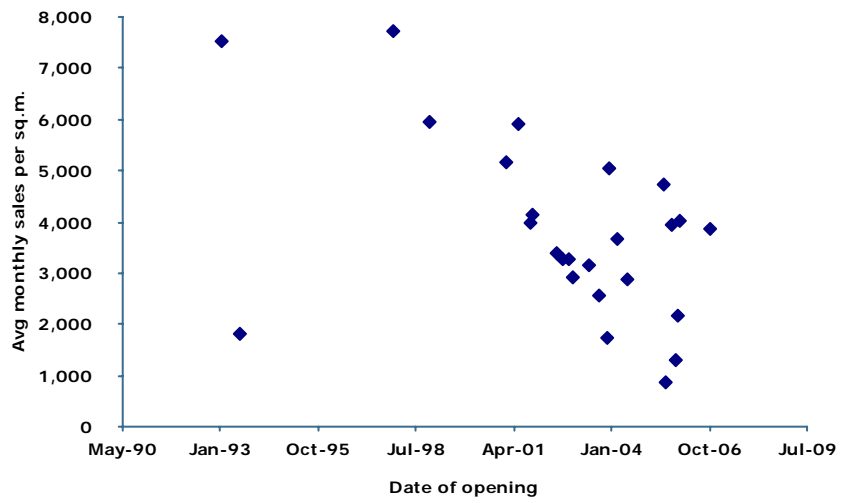
* Triangles indicate hypermarkets, squares - CE supermarkets, diamonds- others.
Green - launched within 1.5 yrs, Orange - older than 1.5 yrs.

Source: Company data, Concorde Capital

Brisk exploration of new markets

MKS's management is pursuing an aggressive policy of opening several new stores at once when testing locations in new markets and putting them to the test to see if they can survive. Within three to six months, some of these new stores might be shut down. There is an obvious correlation between age and sales per square meter, which is evident in the sample.

Computer stores: Average sales per sq. m & stage of maturity



Source: Company data, Concorde Capital

In our view, this “survival of the fittest” test is a plausible strategy when explosive growth must be achieved in many different regions without knowing the specifics of local markets. Of course, this strategy is a drag on profitability but it is a cost at which future quality sales are ensured.

Outlet profiles by format

Hypermarket



Typical trading space	1200-1500 sq m
Ownership/Renting	1/6
Total number	7
Typical locations	Regional centers and cities with a population of > 500 ths
Product offering	Full range of consumer electronic products
Pricing policy	Average & upper-average
Average sales per sq m of trading area	USD 2975

Electronics supermarket



Typical trading space	450-900 sq m
Ownership/Renting	3/4
Total number	7
Typical locations	Regional centers, cities & towns > 100-500 ths
Product offering	Consumer electronics, more limited assortment than in hypermarkets
Pricing policy	Average & upper-average
Average sales per sq m of trading area	USD 3698

Computer supermarket



Typical trading space	300-650 sq m
Ownership/Renting	1/3
Total number	4
Typical locations	Universal
Product offering	Full range of computer-related products
Pricing policy	Average & below average
Average sales per sq m of trading area	USD 3890

Computer store



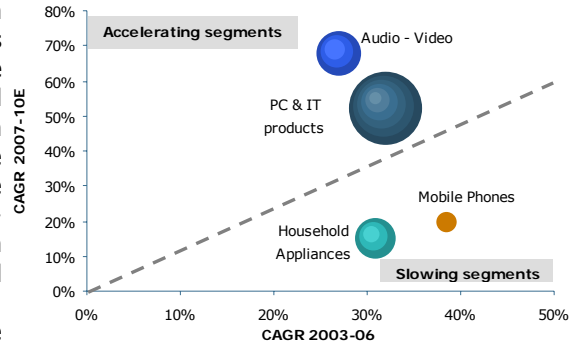
Typical trading space	100-250 sq m
Ownership/Renting	1/24
Total number	25
Typical locations	Most universal
Product offering	Computers & computer related products, selective offering
Pricing policy	Average & below average
Average sales per sq m of trading area	USD 6321

Segment outlook

PCs: Reshuffled product mix to sustain solid growth

MKS is Ukraine's top-4 desktop PC assembler with a total production capacity of more than 87 ths personal computers a year. The company is one of a limited number of PC assemblers with their own retail network. The strong growth posted by the company at 28% CAGR in 2003-2006 secured MKS's 5.5% share in one of the most highly-fragmented markets - PC-related products. Desktops assembled under the MKS brand account for 4% of the market and is the company's most profitable segment.

MKS's growth by segment



Source: Company data, Concorde Capital.
Bubble size reflects \$-revenues of a segment

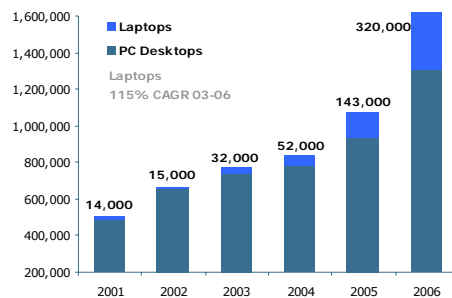
Laptop revolution

In 2004, the Ukrainian laptop market entered a phase of explosive growth: sales in the segment surged by more than five times over the past three years, as prices for laptops halved over the period. The evaporation of fat laptop premiums over desktops since 2004 was swift. Currently the average price for a laptop in Ukraine is USD 917, while in the rest of the world the average is USD 800. Laptops quickly gained around 20% of total computer sales in 2006 after holding a modest 6% of the market in 2004.

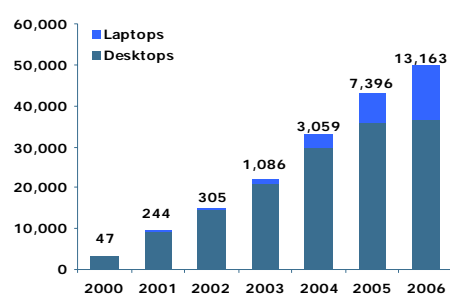
Strong response to the market challenge

As laptops were booming, MKS's branded PC sales grew at a steady 20% in physical terms. However, heavy price erosion in desktops resulted in diminished revenues across the sector. MKS promptly started selling third-party brand laptops and has outperformed the market.

Ukraine's PC sales, units



MKS's PC sales, units



Source: Company data, Concorde Capital

Reshuffling its PC product mix in favor of laptops will bring about an acceleration in computer sales next year. The share of laptops in the company's total trade turnover has already increased to 10.5% in 2006 versus 6.0% in 2004. Management is targeting for laptops to be around 20% of total sales by 2010. The effect of this new focus will already be visible in revenues as early as 2007.

We believe MKS's PC-related segment will keep outperforming the market in the mid-term, capitalizing on their expertise in the sector and the most suitable sales channel for this product - PC stores.

Desktops still extremely under-penetrated

All in all, we expect laptops to cannibalize desktop devices within a transitory period of 2-4 years, due to technology advances that make laptops increasingly acceptable alternatives to desktops. Nevertheless, increased pressure from laptops does not necessarily mean a pessimistic future for desktops in Ukraine. After years of stable growth, PCs (laptops and desktops) still remain the most under-penetrated consumer electronic good in Ukraine (9%), leaving room for growth in both devices.

Corporate sales to support desktops

The demand for desktops from corporate clients will support sound growth in the segment – the share of PCs sold to this demographic (30% in 2005) is steadily growing. MKS's respectable portfolio of corporate clients, which include railway operator Ukrzaliznytsya, fixed-line telephone monopoly Ukrtelecom, and some of Ukraine's top-10 banks, make it well-positioned to sustain corporate sales in the long run.

Growth rates of revenues by segment: MKS vs. the market

MKS, Growth	2003	2004	2005	2006E	CAGR 03-06	CAGR 07-10
PC & IT-related products	46%	40%	23%	21%	32%	52%
Audio - Video	17%	35%	13%	45%	30%	68%
Mobile Phones	30%	62%	39%	25%	22%	20%
Household Appliances	34%	44%	24%	23%	33%	15%

Market Growth	2003	2004	2005	2006E	CAGR 03-06	CAGR 07-10
PC & IT products	29%	7%	21%	30%	21%	30%
Audio - Video	25%	26%	24%	35%	27%	37%
Mobile Phones	90%	122%	88%	59%	90%	20%
Household Appliances	35%	35%	35%	22%	32%	13%

Source: Company data

White goods to slow as segment approaches saturation

Household appliances are the second largest segment for MKS, accounting for 18% of the company's revenue.

Over 2003-2006, household appliances and large white goods in particular experienced strong 32% CAGR. This dynamic growth from a segment that usually posts quite moderate increases was fuelled by Ukrainian consumers' rush to replace their obsolete Soviet-era household appliances. White goods were at the top of consumers' replacement lists.

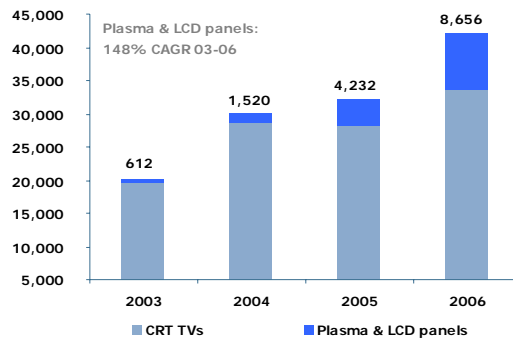
Today the segment seems to have approached saturation, and given that household appliance sales are seldom spurred by innovations and new technology, growth is expected to drop noticeably to 11%-13% CAGR in 2007-2010. MKS's white good sales are also set to slow over the next four years to 14-15% CAGR. The sector will be leapfrogged by Audio/Video brown goods.

Audio/Video sales: Growth to continue

Brown goods and especially audio/video products, show no signs of slowing down. With an expected 25-30% CAGR over the next four years, brown good sales promise to offset the slowdown in white goods.

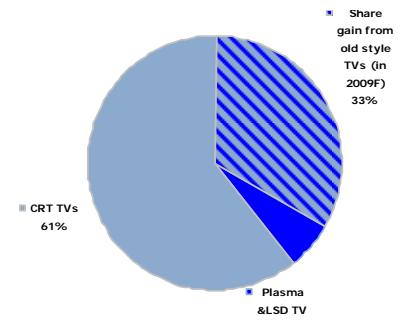
Previously robust growth was explained by low penetration. The sector is now set to capitalize on innovative technologies coming to the market. Currently, less than 5% of all Ukrainian households have a modern LCD or plasma TV, while worldwide penetration for these types of TVs is around 23%. Flat screen TVs, MP3 players, DVD and CD recorders are expected to see strong sales volumes in the near future, as prices have declined to more reasonable levels for consumers. We expect to see a big replacement rush as early as next year.

MKS: Plasma & LCD in total TV sales



Source: Company data

Plasma & LCD market share, 2009



Source: IDC Agency

Audio/Video currently generates around 18% of MKS’s revenues. More than 40% (6.6% of total sales) of MKS’s brown good sales are from modern audio/video devices, a substantial surge from 7% in 2003. We see MKS’s brown good sales accelerating to 65-68% CAGR in 2007-10.

Mobile handsets: Not impressive, but encouraging

MKS will complement its product portfolio by selling mobile handsets, a hot theme on the consumer electronics landscape. Mobile phone sales, with 48% CAGR in 2003-06, was the company’s most dynamic segment. This is lower than the market’s 90% CAGR in the same period, with a large share of handsets sold on the grey market.

As the share of grey market sales is decreasing, we assume that around 80% of all handsets will be sold through retail chains in 2008, putting an additional 5.7 mln handsets or USD 973 mln in sales in the hands of CE retailers.

As the market approaches the equator with 53% penetration, the major driving force for the market will remain replacements. Based on the performance of neighboring Russia’s handset market, we forecast that the period of replacement in Ukraine will accelerate from 18 months currently to 16.5 months by 2009, which together with the launch of 3G communications will result in 22-25% CAGR for the market in 2007-2010E.

Real estate: Extra gravy

A deeper look at the company's property is revealing, two key findings are described below.

Account for real estate to see real life book

The company owns 33% of the PP&E total 40,029 square meters it uses. MKS LLC owns four supermarkets, one hypermarket and one computer specialty store with a total area of 13,312 sq. m and total trading area of 3,696 sq. m. Even as Ukraine's real estate market was booming, MKS's real estate on the company's books has been kept at an artificially low cost, hiding the real appreciation in value.

An appraisal by independent auditors in April 2006, resulted in a one time revaluation of the property from USD 5.4 mln to USD 21.7 mln. This figure is reported in MKS LLC's managerial accounts. The company did not include the results of the revaluation in its financial accounts for the sake of optimizing tax payments, as appreciation on fixed assets is taxed according to Ukrainian legislation.

MKS's property valuation

City	Format	The area, sq m		Net book value, USD ths					Net book value for 1 sq m, USD
		Total area	Trading area	30-Nov-05	31-Dec-05	31-Jan-06	31-May-06	31-Oct-06	31-Oct-06
<i>Accounted for revaluation</i>									
Kramatorks	PC store	183	70	58	58	58	57	55	303
Kharkiv	PCr supermarket	305	202	0	6,894	7,207	8,920	8,766	28,742
Kharkiv	CE supermarket	3,179	895	4,096	4,078	4,061	3,991	3,903	1,228
Kharkiv	CE supermarket	974	369	1,346	1,341	1,335	1,714	1,685	1,730
Kharkiv	Hypermarket	7,422	1,257	0	0	4,585	4,508	4,412	595
Kharkiv	CE supermarket	1,249	903	1,733	1,726	1,718	2,514	2,477	1,983
Total		13,312	3,696	7,233	14,097	18,964	21,704	21,299	1,600
<i>As reported in financial statements</i>									
Total net book value		40,029	19,808	4,949	4,949	4,949	5,440	8,858	221

Source: Company's data; Averse Standard LLC, Granula Vostok LLC (independent appraisers)

As of Oct. 31, 2006, the net book value of the real estate amounted to USD 21.3 mln (USD 1,600 per sq. m).

The book value reported by MKS in their financial statements must be adjusted upward to correctly account for the market value of the company's property. A negative USD 0.6 mln equity on the balance sheet as of Oct. 1, 2006 is misleading and corrects to USD 16.3 mln (as of Oct. 1, 2006, financial statements reported property value at USD 6 bln). For our DCF modeling we factor in the true market value of the real estate owned by the company.

The hedge and value booster

MKS's 30% ownership of its trading space gives it a hedge against inflation in lease costs in the mid term and enables a strategy of aggressive expansion via renting of trading space. The company finished its last construction in January 2006 and the mid-term development plan does not foresee any further construction or acquisition of trading space. We consider this strategy the best solution at the moment to grab market share.

At later stages, with real estate inflation subsiding, MKS can benefit from its real estate ownership by implementing a Sell & Lease Back program. This can be a powerful growth multiplier and serve as a value booster. MKS will have to make an important decision though, as sale of their property will lead to substantial tax obligations, as described above. Nevertheless, our analysis indicates this is an economically feasible option after accounting for all related costs.

A supermarket with total area of 3.2 ths sq m is a feasible candidate for an SLB project. Proceeds from the sale of an estimated USD 4.2 bln (including transaction costs and taxes) would allow MKS to open some 60+ computer specialty store outlets. This format, is the best sales per sq. meter generator of any MKS formats. With 60+ openings on top of those already scheduled next year, the program would be realistic when implemented over a four to five year period. We calculated that augmented sales generated by the project would increase the value of the business by approx. 10% in a stable real estate cost environment.

Valuation summary

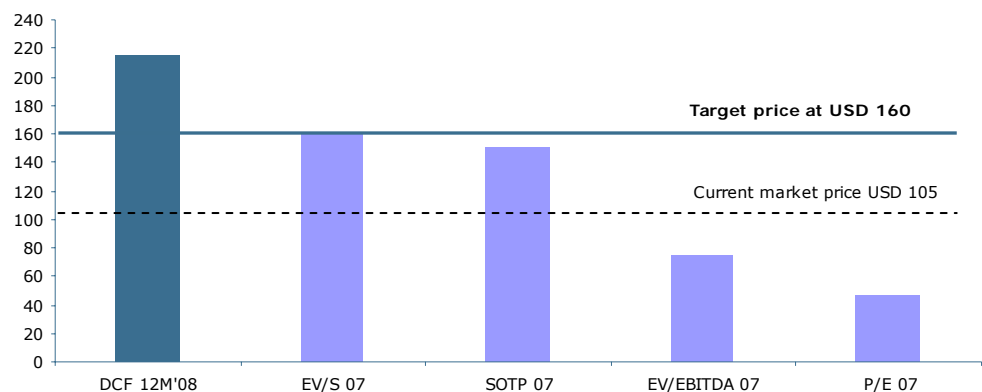
We value MKS from two angles – discounted cash flow and a peer multiple analysis.

Since MKS is a story of capturing market share in the early stage of an emerging industry and not a story of fat margins, applying EV/EBITDA and P/E metrics is inappropriate for relative valuation, in this case. We rely on EV/Sales 2007E as the most relevant market multiple.

The multiples-based valuation range is quite narrow: USD 150 to 160 per share. The upper end is implied by MKS's 2007 forward-looking EV/S. Additionally, we identified companies focusing exclusively on household appliances, mobile phones and computer electronics to gauge MKS' value on a sum-of-the-parts basis. SOTP valuation results in a price of USD 150 per share.

In our DCF analysis we explicitly factored in the management's program of outlet roll-out by year, accounting for a maturing stage in each of the four trading formats. Sales generation capacity and gross margin evolution of each of the four main trade formats is accounted for. The DCF valuation yields a price of USD 163 per share.

We set the twelve-month target at USD 160 per share, which implies a 52% upside to the current market price.



DCF Valuation

Model Assumptions

	2006	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E
Trade formats											
Hypermarkets											
New outlets added	1	7	4	8	7	6	3	2	2	2	2
# outlets, eop	6	13	17	25	32	38	41	43	45	47	49
Trade space added, '000 sq m	1.7	9.5	5.4	10.8	9.5	8.1	4.1	2.7	2.7	2.7	2.7
Trade space, '000 sq m, eop	8.9	18.4	23.8	34.6	44.0	52.1	56.2	58.9	61.6	62.9	65.6
Supermarket of electronics											
New outlets added	1	7	0	7	6	4	3	3	3	2	2
# outlets, eop	8	15	15	22	28	32	35	38	41	43	45
Trade space added, sq m	0.7	4.7	0.0	4.7	4.1	2.7	2.0	2.0	2.0	1.4	1.4
Trade space sq m, eop	4.9	9.7	9.7	14.4	18.4	21.1	23.2	25.2	26.5	27.9	29.2
Computer supermarket											
New outlets added	6	16	9	16	9	7	5	4	3	2	2
# outlets, eop	8	24	33	49	58	65	70	74	77	79	81
Trade space added, sq m	2.0	7.6	4.3	7.6	4.3	3.3	2.4	1.9	1.4	1.0	1.0
Trade space sq m, eop	2.9	10.5	14.7	22.3	26.6	29.9	32.3	34.2	35.6	36.6	37.5
Computer store											
New outlets added	3	16	10	16	14	10	8	8	5	3	2
# outlets, eop	29	45	55	71	85	95	103	111	116	119	121
Trade space added, sq m	0.4	2.8	1.8	2.8	2.5	1.8	1.4	1.4	0.9	0.5	0.4
Trade space sq m, eop	4.9	7.7	9.5	12.3	14.7	16.5	17.9	19.3	20.1	20.7	21.0
Number of outlets, eop	51	97	120	167	203	230	249	266	279	288	296
<i>Growth, %</i>	<i>-11%</i>	<i>90%</i>	<i>24%</i>	<i>39%</i>	<i>22%</i>	<i>13%</i>	<i>8%</i>	<i>7%</i>	<i>5%</i>	<i>3%</i>	<i>3%</i>
Revenue by Trade Formats, USD mln:											
Hypermarkets	46	60	103	151	213	275	327	362	393	411	429
Supermarket of electronics	30	49	73	101	131	178	214	243	272	294	311
PC Supermarket	7	39	129	194	293	358	410	451	491	511	525
PC Store	32	36	62	85	116	144	165	184	205	214	219
Total	115	184	367	531	754	955	1,116	1,240	1,361	1,429	1,484
Gross Profit Margin	12.2%	13.0%	14.0%	15.0%	16.0%	17.0%	18.0%	19.1%	19.3%	19.5%	19.5%
EBITDA Margin, %	2.4%	2.2%	3.0%	3.0%	3.0%	3.0%	2.8%	2.9%	2.9%	3.0%	3.2%
Net Margin, %	0.1%	-2.0%	0.4%	1.4%	1.4%	1.6%	1.5%	1.7%	1.9%	2.0%	2.3%

Peer comparison

Global CE Retailers

Company	Country	Mkt price, USD	Mcap, USD mln	EV/Sales		EV/EBITDA		P/E	
				2007E	2008E	2007E	2008E	2007E	2008E
Gome	Hong-Kong	1.5	3,379	0.6	0.5	20	16	26	22
China Paradise	Hong-Kong	0.3	663	0.2	0.2	15	13	28	20
Fone Zone Group	Australia	0.5	62	0.7	0.3	10	3	18	4
JB Hi-FI	Australia	5.8	602	1.5	0.5	39	8	91	16
Avenir	France	3.4	316	0.4	0.3	8	7	14	16
Best Buy	United States	47.1	22,602	1.7	1.7	16	16	30	27
Circuit City	United States	19.5	3,397	0.2	0.2	8	7	30	22
DSG	UK	3.4	6,184	0.5	0.4	8	7	15	13
Elektroniki Athinon	Greece	7.2	124	0.6	0.7	9	9	32	33
Germanos	Greece	181.1	2,064	1.2	1.1	12	11	18	16
Kesa	UK	6.7	3,528	0.4	0.4	7	7	17	16
Mobilezone	Switzerland	6.1	220	0.9	0.8	8	6	14	13
Rex Stores	United States	16.9	175	0.5	0.5	20	15	26	32
Radioshack	United States	24.0	3,265	0.7	0.7	9	8	24	17
Plasio Computers	Greece	9.2	203	0.5	0.5	10	9	16	14
Staples	United States	26.1	18,976	1.0	0.9	10	9	20	18
PC Depot	Japan	324.4	71	0.2	0.2	na	na	8	7
Average				0.7	0.6	13.0	9.5	25.1	18.1
MKS	Ukraine	105	84.3	0.5	0.2	15.1	7.9	56.2	14.8
Implied MCap, USD mln				129	209	60	102	38	100
Implied share price, USD				160	260	74	127	47	125
Premium/(Discount)				-35%	-59%	16%	-17%	124%	-18%

Source: Bloomberg, PFTS, Concorde Capital

Sum-of-the-parts valuation

In addition to the peer comparison, for deriving MKS's value we applied a sum-of-the-parts valuation to provide a better reflection of MKS's multi-segment business model and diversified product mix. We defined three major segments for its business: PC & IT-related products, Household appliances & audio/video and Mobile phones, which generate 58%, 36% and 6% of the company's total revenues respectively.

Household appliances & audio-video retailers

Company	Country	Mkt price, USD	Mcap, USD mln	EV/Sales	
				2007E	2008E
Gome	Hong-Kong	1.5	3,379	0.6	0.5
China Paradise	Hong-Kong	0.3	663	0.2	0.2
JB Hi-FI	Australia	5.8	602	1.5	0.5
Elektroniki Athinon	Greece	7.2	124	0.6	0.7
Average				0.8	0.5

Mobile phones retailers

Company	Country	Mkt price, USD	Mcap, USD mln	EV/Sales	
				2007E	2008E
Fone Zone Group	Australia	0.5	62.2	0.7	0.3
Avenir	France	3.4	315.9	0.4	0.3
Germanos	Greece	181.1	2064	1.2	1.1
Mobilezone	Switzerland	6.1	219.9	0.9	0.8
Average				0.8	0.6

PC & IT-related products retailers

Company	Country	Mkt price, USD	Mcap, USD mln	EV/Sales	
				2007E	2008E
Plasio Computers	Greece	9.2	203.5	0.5	0.5
Staples	United States	26.1	18976.3	1.0	0.9
PC Depot	Japan	324.4	71.4	0.2	0.2
Average				0.6	0.5

MKS: SOTP Valuation Summary

	2007E	2008E
Implied EV by sectors, USD mln		
<i>Household appliances & audio/video</i>	49.4	64.7
<i>Mobile phones</i>	9.7	13.8
<i>PC & IT-related</i>	61.2	110.7
Implied MCap, USD mln	120.1	186.2
Implied price, USD	150	236
Implied upside	42%	124%

Financial statements

All financial statements were prepared according to Ukrainian Accounting Standards

Income Statement Summary, USD mln

	2005	2006	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E
Net Revenues	90	115	185	367	531	754	955	1,116	1,240	1,347	1,415	1,469
<i>Change y-o-y</i>	27%	27%	62%	98%	45%	42%	27%	17%	11%	9%	5%	4%
Cost Of Sales	(81)	(101)	(161)	(316)	(451)	(633)	(793)	(915)	(1,003)	(1,088)	(1,139)	(1,183)
Gross Profit	10	14	24	51	80	121	162	201	237	259	275	286
Other Operating Income/Costs. net	0.3	(0.2)	-	-	-	-	-	-	-	-	-	-
SG&A	(8)	(11)	(19)	(40)	(64)	(98)	(136)	(168)	(201)	(220)	(231)	(239)
EBITDA	2	2	6	11	16	23	27	32	36	40	45	46
<i>EBITDA margin. %</i>	2.4%	2.2%	3.0%	3.0%	3.0%	3.0%	2.8%	2.9%	2.9%	3.0%	3.2%	3.2%
Depreciation	(0.7)	(1.0)	(1.5)	(1.4)	(1.4)	(1.3)	(1.2)	(1.1)	(1.0)	(1.0)	(0.9)	(0.9)
EBIT	1	1	4	10	15	21	26	31	35	39	44	46
<i>EBIT margin. %</i>	1.6%	1.3%	2.2%	2.6%	2.7%	2.8%	2.7%	2.8%	2.8%	2.9%	3.1%	3.1%
Interest Expense	(1)	(4)	(3)	(3)	(5)	(6)	(7)	(7)	(6)	(5)	(4)	(2)
Financial income	-	-	-	-	-	-	-	-	-	-	-	-
Other income/(expense)	(0)	(0)	-	-	-	-	-	-	-	-	-	-
PBT	0.1	(2.4)	1.0	6.6	9.7	15.2	18.7	24.3	28.7	34.0	40.3	43.6
Tax	(0)	0	(0)	(2)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
<i>Effective tax rate</i>	9%	3%	25%	24%	23%	22%	21%	20%	20%	20%	20%	20%
Extraordinary Income/(loss)	-	-	-	-	-	-	-	-	-	-	-	-
Net Income	0.1	(2.3)	0.8	5.0	7.5	11.9	14.8	19.4	23.0	27.2	32.2	34.8
<i>Net Margin. %</i>	0.1%	-2.0%	0.4%	1.4%	1.4%	1.6%	1.5%	1.7%	1.9%	2.0%	2.3%	2.4%
Dividend Declared	-	-	-	-	-	-	-	-	-	-	-	-

Balance Sheet Summary, USD mln

	2005	2006	2007E	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E
Current Assets	28	34	55	107	152	210	264	305	336	368	390	418
Cash & Equivalents	4	3	7	15	21	30	38	45	51	58	66	81
Trade Receivables	3	7	9	18	24	30	38	44	47	51	53	55
Inventories	17	20	33	65	93	131	164	189	208	225	236	245
Other current assets	3	4	5	9	13	19	24	28	31	34	35	37
Fixed Assets	7	22	22	22	22	22	22	22	22	22	22	22
PP&E. net	5	21	21	21	21	21	21	21	21	21	21	21
Other Fixed Assets	2	1	1	1	1	1	1	1	1	0	0	0
Total Assets	35	56	77	129	174	232	286	327	358	389	412	439
Shareholders' Equity	1	11	32	39	48	62	78	98	121	148	181	216
Share Capital	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Reserves and Other	1.0	11.2	32	38	48	62	78	98	121	148	181	216
Current Liabilities	28	25	38	84	119	164	202	223	231	235	230	223
ST Interest Bearing Debt	8	-	1	11	19	23	26	24	23	15	10	-
Trade Payables	18	23	35	69	95	133	166	188	201	212	211	214
Accrued Wages	0	0	-	-	-	-	-	-	-	-	-	-
Accrued Taxes	0	0	-	-	-	-	-	-	-	-	-	-
Other Current Liabilities	1	2	2	4	5	8	10	11	7	8	8	9
LT Liabilities	6	19	7	6	6	6	6	6	6	6	1	0
LT Interest Bearing Debt	6	19	7	6	6	6	6	6	6	6	1	0
Other LT	-	-	-	-	-	-	-	-	-	-	-	-
Total Liabilities & Equity	35	56	77	129	174	232	286	327	358	389	412	439

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