



CONCORDE CAPITAL

Ukraine / Machinery

Motor Sich

Solid 3Q09 results warrant target upgrade

November 6, 2009

Current price: USD 175.7
Fair price: USD 220.0

BUY

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Tickers

PFTS/UX MSICH

Market information

Market price, USD	175.7
MCap, USD mln	365.2
52Wk Hi/Low, USD	175.7/33.1
No of shares, mln	2.0
Free float	35.8%
Free float, USD mln	123.4

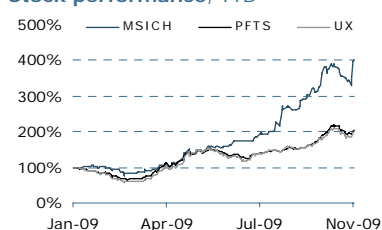
Shareholders

Management	61.3%
Treasury stock	4.7%
Bartence Alliance	9.7%
Other	24.3%

Key financials and ratios

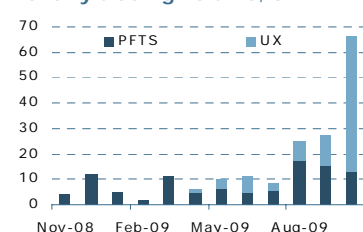
	Sales, USD mln	EBITDA, USD mln	Net income, USD mln
2007	346.5	79.0	41.0
2008	387.7	69.2	0.7
2009E	419.3	121.6	71.7
2010E	439.8	110.0	66.1

Stock performance, YTD



Source: Bloomberg, Concorde Capital

Monthly trading volume, UAH mln



Source: Bloomberg, Concorde Capital

- **Motor Sich released its 9M09 financial results earlier this week: net revenue rose 14% yoy to USD 323 mln and its EBITDA margin by 22 pp yoy to 33%**
- **In a conversation with us, Motor Sich's CFO clarified factors behind the company's growth in 9M09**
- **We revise our estimates upward: 2009 sales to USD 419 mln (9% higher than our previous projection) and EBITDA to USD 121.6 mln (up 77%)**
- **Based on new projections, we upgrade our target price for the stock to USD 220 per share, implying an upside of 25%. BUY**

Sales grew 14%, EBITDA more than tripled yoy in 9M09

We clarified the factors behind the company's solid growth with Motor Sich's CFO after the company released its 9M09 financials earlier this week:

- net revenue grew 14% yoy to USD 323 mln. Specifically, in 3Q09, sales were up 35% yoy to USD 156 mln, comparable to sales for 1H09. Motor Sich's CFO said the company raised its average contract prices in 3Q09 by ~10% in US dollar terms. We attribute this to improved demand from the Russian aviation industry, specifically, for helicopter engines.
- EBITDA margin grew by 22 pp yoy to 33% thanks to the effect of hryvnya devaluation (~50% of COGS and ~100% of SG&A are in hryvnias, while over 90% of sales are in foreign currencies), a 56% yoy decline in average steel purchase prices, and operational efficiency measures taken by the management. Specifically, Motor Sich's dollar COGS grew only 2% yoy and SG&A dropped 32% in 9M09.

Forecasts for 2009/10 revised upward on strong interim financials

Based on the company's 9M09 results, we upgraded our estimates of 2009E sales to USD 419 mln (9% higher than our previous projection) and EBITDA to USD 121.6 mln (up 77%).

For 2010, we conservatively assume 5% growth in sales, to USD 440 mln, even though Motor Sich's management is looking for 10-15% growth. We forecast the EBITDA margin next year to narrow to 25%, since no change in output prices is expected, while we see that COGS and SG&A can grow by as much as 10% due to expected growth in salaries and electricity prices.

Estimate revisions, USD mln

	2009E		2010E	
	old forecast	new forecast	old forecast	new forecast
Net revenue	383.9	419.3	438.3	439.8
yoy	-1.0%	8.1%	14.2%	4.9%
EBITDA	68.6	121.6	87.7	110.0
mgn	17.9%	29.0%	20.0%	25.0%
Net income	31.2	71.7	46.9	66.1
mgn	8.1%	17.1%	10.7%	15.0%

Source: Company data, Concorde Capital

Valuation: target price upgraded

We upgrade our target price for Motor Sich to USD 220 per share from USD 175, an upside of 25%, and rate the stock as a BUY. The stock is trading at EV/EBITDA '10E of 3.7x. We base the target price on the average EV/EBITDA '10E for two peer groups, aircraft engine manufacturers and aerospace companies (currently 5.6x), to which we apply a discount of 20%. We argue that the stock deserves a discount to its peers since we think Motor Sich's high projected EBITDA margin of 25% is hardly sustainable in the medium-term and expect it to normalize at some 20%, which is about the company's average EBITDA margin in 2002-2008.

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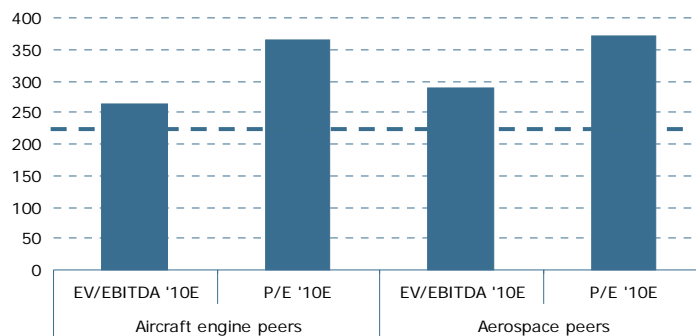
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Motor Sich peer valuation

	MCap		EV/S		EV/EBITDA		P/E	
	USD mln	09E	10E	09E	10E	09E	10E	
Motor Sich	365	1.0	0.9	3.6	3.7	5.1	5.5	
Aircraft engine peers								
IHI Corporation	2,769	0.4	0.4	7.8	6.8	30.5	19.5	
Ufimskiye Motors	120	1.1	1.0	8.5	5.3	17.1	4.6	
Magellan Aerospace Corp	24	0.4	0.4	3.5	4.0	1.7	6.3	
Sichuan Chengfa	426	n/a	n/a	n/a	n/a	31.7	29.6	
MTU Aero Engines	2,424	0.7	0.7	5.4	5.5	10.9	11.5	
Median		0.6	0.6	6.6	5.4	17.1	11.5	
Price MSICH, USD per share								
Implied by engines peer median		86.7	102.6	353.5	264.3	589.0	364.3	
<i>Upside/Downside</i>		-51%	-42%	101%	50%	235%	107%	
Aerospace peers								
Boeing Co	34,949	0.6	0.6	10.3	6.2	32.5	11.4	
Lockheed Martin	26,426	0.7	0.6	5.6	5.5	8.9	9.5	
Cobham	4,191	1.5	1.4	7.8	7.0	13.0	11.9	
EADS	15,598	0.2	0.2	2.9	3.1	12.9	12.8	
Finmeccanica	9,913	0.6	0.5	4.6	4.3	9.1	8.1	
Meggitt PLC	2,670	2.1	2.1	7.4	7.0	11.0	10.5	
Safran SA	6,806	0.6	0.5	5.3	5.1	11.0	12.8	
Dassault Aviation	7,590	n/m	n/m	5.7	5.5	17.8	15.4	
Textron	5,018	0.7	0.6	9.2	6.6	962.5	22.8	
Zodiac SA	1,909	0.9	0.9	6.3	6.7	8.3	10.4	
Median		0.7	0.6	6.0	5.8	12.0	11.6	
Price MSICH, USD per share								
Implied by aerospace peer median		98.5	108.1	318.9	288.6	413.2	370.4	
<i>Upside/Downside</i>		-44%	-38%	81%	64%	135%	111%	
Global machinery peers								
United Technologies Corp	59,252	1.2	1.2	8.3	7.7	15.5	14.1	
Honeywell International Inc	27,508	1.0	1.0	7.1	6.9	12.5	13.3	
ABB	43,677	1.2	1.2	8.1	8.3	15.9	17.2	
Siemens	81,744	0.9	0.9	7.4	7.6	13.5	14.1	
Median		1.1	1.1	7.4	8.4	13.4	14.4	
Price MSICH, USD per share								
Implied by global peer median		195.0	208.6	418.6	386.6	499.3	449.2	
<i>Upside/Downside</i>		11%	19%	138%	120%	184%	156%	

Source: Bloomberg, Concorde Capital

MSICH price implied by peer median and target price, USD


Source: Bloomberg, Concorde Capital

Income statement summary, cumulative USD mln

	3M07	6M07	9M07	2007	3M08	6M08	9M08	2008	3M09	6M09	9M09
Net Revenues	57.8	139.4	223.6	346.5	87.4	166.8	282.9	387.3	55.8	165.6	322.0
<i>Change y-o-y</i>	52.5%	72.2%	64.1%	41.4%	51.2%	19.6%	26.5%	11.8%	-36.2%	-0.7%	13.8%
Cost Of Sales*	(27.6)	(67.2)	(111.6)	(176.1)	(49.4)	(96.8)	(168.5)	(229.4)	(30.2)	(86.4)	(172.5)
Gross Profit	30.2	72.2	112.0	170.4	38.0	70.0	114.4	157.9	25.6	79.2	149.6
<i>Gross Margin, %</i>	52.3%	51.8%	50.1%	49.2%	43.5%	42.0%	40.4%	40.8%	45.8%	47.8%	46.4%
<i>Change y-o-y</i>	15.7%	29.7%	22.5%	7.5%	-16.9%	-19.0%	-19.3%	-17.1%	5.5%	13.9%	14.9%
Other Operating Income/Costs, net	(1.9)	(4.4)	(6.9)	(12)	(2.0)	(8.3)	(16.1)	(11)	0.2	(0.2)	1.7
SG&A	(13.5)	(28.2)	(50.7)	(78.9)	(25.3)	(45.0)	(66.9)	(82.2)	(13.8)	(28.6)	(45.7)
<i>Change y-o-y</i>	38.7%	40.6%	62.2%	32.7%	87.1%	59.4%	31.9%	4.2%	-45.4%	-36.5%	-31.7%
<i>% of Net Revenues</i>	23.4%	20.2%	22.7%	22.8%	29.0%	27.0%	23.6%	21.2%	24.8%	17.2%	14.2%
EBITDA	14.8	39.6	54.4	79.0	10.6	16.8	31.4	65.2	11.9	50.4	105.5
<i>Change y-o-y</i>	152.4%	246.5%	179.9%	98.7%	-28.4%	-57.6%	-42.3%	-17.5%	12.5%	200.6%	236.2%
<i>EBITDA margin, %</i>	25.6%	28.4%	24.3%	22.8%	12.1%	10.1%	11.1%	16.8%	21.4%	30.4%	32.8%
Depreciation	(3.9)	(8.3)	(12.7)	(18.8)	(5.1)	(10.6)	(16.0)	(20.5)	(3.4)	(6.8)	(10.7)
EBIT	10.9	31.3	41.7	60.2	5.6	6.2	15.4	44.7	8.5	43.6	94.8
<i>Change y-o-y</i>	520.9%	864.1%	513.3%	177.6%	-49.0%	-80.2%	-63.1%	-25.7%	53.9%	606.5%	516.0%
<i>EBIT margin, %</i>	18.8%	22.4%	18.6%	17.4%	6.4%	3.7%	5.4%	11.5%	15.3%	26.3%	29.4%
Interest Expense	(1.8)	(3.6)	(5.5)	(7.4)	(1.9)	(4.3)	(7.3)	(10.1)	(2.4)	(5.0)	(7.8)
Financial income/(expense)	0.1	0.6	2.2	3.3	0.5	1.7	1.8	2.5	(0.2)	(0.2)	(0.2)
Other income/(expense)	0.1	(0.1)	(0.1)	(0.5)	(0.2)	2.5	3.6	(32.1)	1.3	0.4	(3.4)
PBT	9.3	28.1	38.2	55.6	3.9	6.1	13.6	5.1	7.2	38.8	83.4
Tax	(0.3)	(4.0)	(5.3)	(14.6)	(0.0)	(5.1)	(9.3)	(3.6)	(2.1)	(5.6)	(16.6)
<i>Effective tax rate</i>	3.4%	14.2%	13.8%	26.3%	0.5%	83.4%	68.0%	70.4%	28.5%	14.6%	19.9%
Net Income	8.9	24.1	32.9	41.0	3.9	1.0	5.4	4.5	8.2	40.1	78.8
<i>Change y-o-y</i>	6588.4%	4632.4%	8804.7%	450.5%	-56.3%	-95.8%	-83.7%	-89.0%	109.6%	3885.0%	1371.0%
<i>Net Margin, %</i>	15.5%	17.3%	14.7%	11.8%	4.5%	0.6%	1.9%	1.2%	14.7%	24.2%	24.5%

* net of D&A

Balance sheet summary, USD mln

	3M07	6M07	9M07	2007	3M08	6M08	9M08	2008	3M09	6M09	9M09
Current Assets	266.0	293.5	318.4	347.9	380.3	418.1	424.5	298.5	328.2	350.0	354.8
Cash & Equivalents	5.8	11.1	13.9	16.6	13.6	15.8	11.0	6.4	5.4	6.5	16.7
Trade Receivables	30.8	26.0	20.5	23.0	28.1	16.6	17.9	25.3	20.3	24.5	26.7
Inventories	183.9	197.1	216.9	227.7	253.9	296.7	310.9	197.7	228.0	233.2	207.5
Other current assets	45.5	59.3	67.1	80.6	84.6	89.0	84.7	69.1	74.4	85.8	103.9
Fixed Assets	209.5	214.9	221.7	229.4	234.9	249.1	256.7	161.1	163.5	166.5	165.2
PP&E, net	142.6	142.2	146.7	155.7	155.8	163.7	165.6	109.8	109.2	109.4	105.7
Other Fixed assets	67.0	72.7	75.0	73.7	79.1	85.4	91.1	51.3	54.3	57.1	59.5
Total Assets	475.5	508.4	540.1	577.3	615.2	667.2	681.2	459.6	491.7	516.5	520.0
Shareholders' Equity	285.1	318.3	344.8	354.4	360.0	371.1	373.3	234.4	239.2	269.5	289.8
Share Capital	52.6	53.6	54.6	54.6	88.5	92.3	92.0	58.1	58.1	58.6	55.9
Retained Earnings & Other	232.5	264.7	290.3	299.9	271.5	278.9	281.3	176.3	181.1	210.9	233.9
Current Liabilities	178.9	178.2	183.7	202.3	234.6	273.1	285.4	208.4	235.4	226.6	210.6
ST Interest Bearing Debt	77.1	70.4	75.9	70.9	77.5	88.0	88.9	76.5	73.6	71.9	71.8
Trade Payables	32.3	29.7	30.3	42.2	45.1	50.2	48.3	33.2	29.0	25.9	21.9
Accrued Wages	4.0	3.7	4.6	5.1	5.5	6.7	6.2	3.9	4.0	4.1	4.2
Accrued Taxes	0.8	4.1	1.2	4.3	1.1	1.3	3.2	0.8	1.6	3.6	7.6
Other Current Liabilities	64.6	70.3	71.7	79.9	105.4	126.9	138.8	94.0	127.1	121.1	105.2
LT Liabilities	11.5	11.9	11.6	20.6	20.7	22.9	22.1	16.3	16.0	20.4	19.6
LT Interest Bearing Debt	-	-	-	4.0	4.0	5.0	5.0	8.9	8.5	12.3	12.3
Other LT	11.5	11.9	11.6	16.5	16.7	17.9	17.1	7.5	7.5	8.1	7.2
Total Liabilities & Equity	475.5	508.4	540.1	577.3	615.2	667.2	680.9	459.1	490.5	516.5	520.0

Source: Company data

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