



CONCORDE CAPITAL

Ukraine / Ferroalloys

# Nikopol Ferroalloy

Owners feel more at home

February 27, 2008

Current price: USD 1.98  
12M Target: USD 2.00

## HOLD

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On Friday the Ukrainian Securities and Exchange Commission registered Nikopol Ferroalloy's additional share issue. With this approval, we believe the probability of reprivatization is diminished. Given lower ownership-related risks, expected improvement in financial disclosure and booming global ferroalloy prices, we revise our valuation and upgrade our target price from USD 1.35 per share to USD 2.00, which only justifies a HOLD recommendation.

### Tickers

Bloomberg NFER UZ

### Market information

Market price, USD	1.98
MCap, USD mln	3,072.3
Chg YTD	-30%
52 Wk H/L, USD	3.47/1.10
No of shares, mln	1,551.5
Avg M Tr Vol 6M, USD mln	338.5
Free float	2%
Free float, USD mln	61.45

Prices as of Feb. 22, 2008

### Corporate Governance

Concorde Rating\* P

\* The rating is based on Concorde Capital's corporate governance survey. Q denotes quality corporate governance standards, AA - above average standards, A - average, BA - below average and P - poor.

### Shareholders\*

Privat Group	23%
Interpipe	75%
Other	2%

### Reprivatization risks waning

The Ukrainian Securities and Exchange Commission said on Friday it registered Nikopol Ferroalloy's additional share issue. With this fivefold charter fund increase, the privatized 50%+1 stake disputed by the state was diluted to 9.8%. The state would now face more legal obstacles should it persist in attempts to regain control: it must first get back the 9.8% stake and then seek to cancel the additional share issue. In addition, we think the government would find it problematic to muscle the necessary political will (see our note of January 15, 2008).

### Market welcomes share issue registration, liquidity improves

The market was fast to react to registration of the share issue: the stock's price jumped 30% on the day. Trading in NFER on the PFTS resumed last Wednesday for the first time since subscription for the share issue began on January 10. The spread squeezed from 70% to 20%; we expect it to shrink to under 10% in the next few weeks.

### Subscribing shareholders seized 54% arbitrage profit

Another example of arbitrage taking in the course of a discount-to-market share issue (the concept is elaborated upon in our February 21, 2008 report). The day after SEC registration, NFER traded at USD 1.98 per share, implying a return of 218% over a 45 day period on a fully diluted basis, which includes a 54% arbitrage profit.

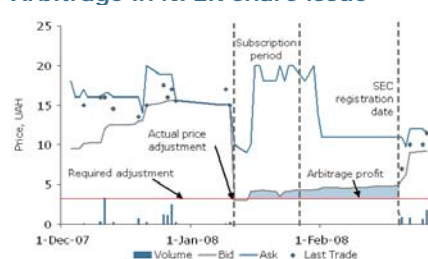
### Favorable market condition on the fundamental side

Global prices for ferroalloys have risen on shortages due to power failures in South Africa, snowstorms in China and floods in Australia. Spot ferroalloy prices in China and Europe have already increased by 20-35% YTD, putting upward pressure on contract prices next quarter. We upgrade our 2008 price outlook by 5% to USD 1,835 for FeMn and USD 1,790 for SiMn.

### We revise our target up to USD 2.0, HOLD

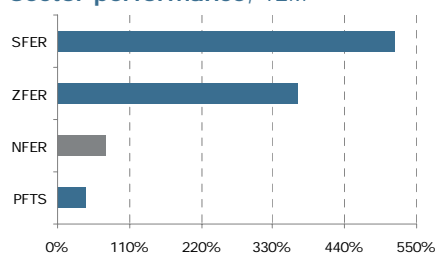
We see the company transitioning toward more transparency, which we believe the market will be receptive to. To capture that change, we change our approach to valuing NFER. We give more weight to the DCF-implied price based on our estimates of the full value of the business (80%) than on reported financials (20%, see page 2). Our upgraded target price of USD 2.0 only justifies a HOLD recommendation.

### Arbitrage in NFER share issue

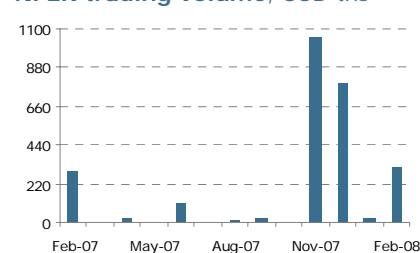


Source: PFTS, Concorde Capital calculations

### Sector performance, 12M



### NFER trading volume, USD ths



## Valuation

### Output revision

We upgrade our forecast of Nikopol Ferroalloy's output for 2008 onward, taking into account booming demand from steelmakers, and the company's reported 2007 figures (1,019 mt of alloys, 8.4% above our previous projection of 940 mt). We expect Nikopol to boost annual output to 1,180 mt by 2011.

#### Nikopol Ferroalloy output projection

	2007E	2008E	2009E	2010E
Old	940	1,006	1,056	1,056
New	1,019*	1,090	1,145	1,179

Source: Concorde Capital, Company data

\* Actual data

### Target upgrade

In order to ascertain the fair value of NFER's equity, we marked off the bottom and top of the range. The bottom (V1) could not be less than what officially reported (visibly distorted) financials imply. The top (V2) represents the full value of the business, currently only captured by controlling shareholders. We derive our 12-month target price, setting a higher weight (80%) for V2. We believe that, given the decreased risk of reprivatization and clarity in ownership, the transparency scenario will be increasingly discounted in NFER's market price.

- V1, 20% weight in valuation. Value as implied by reported financials.**  
 We assume profitability officially reported by the company "as is" (EBITDA margin of 7%) for valuation purposes. Our DCF model implies equity value of USD 490 mln or USD 0.3 per share.
- V2, 80% weight in valuation. Real value of the business.** We calculated the value of the company using our estimation of true profitability and cash generation. We estimate the company's true EBITDA margin at 32% in 2008. Our DCF valuation suggests a fair value for the company at USD 3.75 bln or USD 2.4 per share.

Weighting V1 and V2, we arrive at a target of USD 2.0.

# Valuation 1

	Sales, USD mln			EBITDA margin, %			Net margin, %		
	Old	new	chg. %	old	new	chg. p.p.	old	new	chg. p.p.
NFER	805	883	9.7%	7.0%	7.0%	0.0%	2.5%	3.2%	0.7%
2007E	805	883	9.7%	7.0%	7.0%	0.0%	2.5%	3.2%	0.7%
2008F	979	1,100	12.4%	15.2%	7.0%	-8.2%	9.8%	3.7%	-6.1%
2009E	1,146	1,254	9.4%	25.4%	7.0%	-18.4%	18.0%	4.2%	-13.8%
2010E	1,191	1,264	6.1%	27.6%	7.1%	-20.5%	19.7%	4.3%	-15.4%

## DCF Valuation

Valuation as of February

	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E
EBITDA	462	432	416	422	423	427	428	427	429
EBIT	420	390	374	381	383	387	389	389	391
Tax Rate	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBIT	315	293	280	286	287	290	291	292	294
Plus D&A	41	41	42	41	40	40	39	38	38
Less CapEx	(59)	(43)	(36)	(36)	(36)	(36)	(37)	(37)	(38)
Less change in OWC	(470)	16	33	(9)	(2)	(4)	(3)	(4)	2
FCFF	-	306	319	281	289	289	290	290	297
WACC	13.8%	13.3%	12.7%	12.3%	11.4%	11.4%	11.4%	11.5%	11.5%
Sum of discounted CFs		1,485							
PV of Terminal Value		1,238							
Firm Value		2,723							
Portion due to TV		45.5%							
Less Net Debt		(248)							
Equity Value		2,475							
Implied share price		0.32							
						WACC To Perpetuity			11.0%
						Terminal Value			2,996
						Perpetuity Growth Rate			1.0%
						Implied Exit EBITDA Multiple			7.0x

10-Year Discount Rates	Perpetuity Growth Rate				
	-0.5%	0.0%	0.5%	1.0%	1.5%
WACC-1.0%	2,484	2,547	2,616	2,693	2,779
WACC-0.5%	2,416	2,477	2,545	2,619	2,701
WACC+0.0%	2,351	2,410	<b>2,475</b>	2,547	2,626
WACC+0.5%	2,289	2,346	2,408	2,477	2,554
WACC+1.0%	2,228	2,283	2,344	2,410	2,485

WACC to perpetuity	Perpetuity Growth Rate				
	-0.5%	0.0%	0.5%	1.0%	1.5%
9.5%	2,459	2,530	2,609	2,697	2,796
10.0%	2,403	2,467	2,539	2,618	2,706
10.5%	2,351	2,410	<b>2,475</b>	2,547	2,626
11.0%	2,305	2,359	2,418	2,483	2,555
11.5%	2,262	2,312	2,366	2,425	2,491

## Valuation 2

		Sales, USD mln			EBITDA margin, %			Net margin, %		
		old	new	chg, %	old	new	chg, p.p.	old	new	chg, p.p.
NFER	2007E	805	883	9.7%	7.0%	7.0%	0.0	2.5%	3.2%	0.7
	2008F	979	1,319	34.7%	15.2%	32.2%	17.0	9.8%	22.9%	13.1
	2009E	1,146	1,901	65.9%	25.4%	32.2%	6.8	18.0%	23.3%	5.3
	2010E	1,191	1,823	53.1%	27.6%	32.4%	4.8	19.7%	23.4%	3.7

## DCF Valuation

Valuation as of February

	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E
EBITDA	2,124	3,030	2,864	2,819	2,847	2,827	2,813	2,798	2,655
EBIT	2,083	2,988	2,822	2,778	2,806	2,786	2,772	2,758	2,615
Tax Rate	25%	25%	25%	25%	25%	25%	25%	25%	25%
Taxed EBIT	1,562	2,241	2,117	2,083	2,104	2,090	2,079	2,068	1,961
Plus D&A	41	41	42	41	41	41	41	40	40
Less CapEx	(53)	(47)	(44)	(44)	(44)	(44)	(44)	(44)	(40)
Less change in OWC	(408)	(431)	65	(2)	11	(2)	(2)	(2)	16
FCFF	-	1,804	2,179	2,078	2,113	2,085	2,074	2,063	1,977
WACC	14.1%	13.5%	12.8%	12.4%	11.5%	11.5%	11.5%	11.5%	11.5%
Sum of discounted CFs		10,180							
PV of Terminal Value		8,219							
Firm Value		18,399							
Portion due to TV		44.7%							
Less Net Debt		708							
Equity Value		19,107							
Implied share price		2.44							
						WACC To Perpetuity			11.0%
						Terminal Value			19,967
						Perpetuity Growth Rate			1.0%
						Implied Exit EBITDA Multiple			7.5x

10-Year Discount Rates	Perpetuity Growth Rate				
	-0.5%	0.0%	0.5%	1.0%	1.5%
WACC-1.0%	19,180	19,600	20,061	20,571	21,138
WACC-0.5%	18,725	19,130	19,576	20,068	20,615
WACC+0.0%	18,286	18,677	<b>19,107</b>	19,582	20,111
WACC+0.5%	17,861	18,239	18,654	19,113	19,623
WACC+1.0%	17,451	17,816	18,217	18,660	19,153

WACC to perpetuity	Perpetuity Growth Rate				
	-0.5%	0.0%	0.5%	1.0%	1.5%
9.5%	19,001	19,472	19,994	20,579	21,236
10.0%	18,626	19,054	19,527	20,052	20,640
10.5%	18,286	18,677	<b>19,107</b>	19,582	20,111
11.0%	17,976	18,334	18,728	19,160	19,638
11.5%	17,692	18,022	18,383	18,778	19,213

# Appendix – Disclosures

## Analyst Certification

I, Andriy Gerus, 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.

### NFER

Date	Target price, USD	Market Price, USD	Recommendation	Action
10-Jun-05	0.013	0.010	SELL	Initiate
22-Mar-06	N/A	1.33	N/R	Suspend
21-Jan-08	1.35	0.81	HOLD	Reinstate
27-Feb-08	2.00	1.98	HOLD	Upgrade

NFER recommendation history, USD per share



## 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.

### Concorde Capital ratings distribution

Buy	46	44%
Hold	28	27%
Sell	13	12%
Under Review	18	17%
Total	105	100%

### Investment banking clients\*

Buy	9	100%
Hold	0	0%
Sell	0	0%
Under Review	0	0%
Total	9	100%

\* Within the last twelve month period, Concorde Capital has obtained compensation from these companies for investment banking services.

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