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- The peculiarities of Ukrainian legislation brought about the phenomenon of dilutive share issues at deep discounts to market
- The positive side effect: since 2006, due to imperfect price adjustment, discounted share issues gave median 33% arbitrage return to subscribing shareholders over an average lock-in period of 108 days
- 17 share issues at a below market subscription price are pending or being conducted currently vs only two at market
- Top stories: 144% capital increase at Dzerzhinskogo Steel (DMKD), 154% at Energomashspetsstal (ENMA)

**Upcoming issues at par****Approved by shareholders**

	Ex-rights date	Capital Increase	Required correction*	MCap, \$ mln	FF, \$mn	Rec
ENMA	29.02.2008	154%	56%	93.5	9.5	N/R
UGZB	10.03.2008	20%	14%	673.3	67.3	HOLD
FORM	14.03.2008	45%	24%	943.0	94.3	BUY
SHMK	23.03.2008	22%	18%	79.2	2.0	SELL
DMPO	28.03.2008	256%	65%	44.4	3.1	BUY

**Awaiting shareholder approval**

	Ex-rights date	Capital Increase	Required correction*	MCap, \$ mln	FF, \$mn	Rec
HRTR	25.04.2008	2%	2%	1666.8	33.3	SELL
IGOK	25.04.2008	112%	26%	130.0	0.6	N/R
ENMZ	29.04.2008	2%	2%	962.5	132.8	BUY
DMKD	09.05.2008	144%	55%	1621.2	16.2	N/R

\* Based on closing market price of February 18

**SSEC registration pending**

	End of Subscription	Capital Increase	MCap, \$mn	Rec	Arbitrage
FLOT	19.12.2007	900%	141	N/R	72%
SVGZ	19.12.2007	200%	349	BUY	37%
KMED	28.12.2007	233%	243	N/R	0%
PGOK	15.01.2008	22%	2,129	U/R	7%
NFER	28.01.2008	411%	1,705	HOLD	54%
DMPZ	31.01.2008	157%	84	HOLD	0%
ALMK*	25.06.2008	139%	2,880	BUY	36%
SLAV**	30.08.2008	72%	630	BUY	15%

Note: Discount-to-market issues only

(\*) First-stage subscription over

(\*\*) First-stage subscription still running

**More than 70 additional share issues in 2006-2007**

Since 2006, more than 70 additional share issues have been conducted by Ukrainian open joint stock companies listed on the PFTS. With four exceptions, all of them were at par value, i.e. at a discount to the market. About 30 were conducted by relatively liquid names. Every third issue was by a commercial bank, while metals & mining account for another third.

**New share issues as opportunity for arbitrage return**

While subscription to cheap shares (at par) reduces the cost of the initial investment, the experience in Ukraine is that the market price does not make a complete adjustment on a fully diluted basis. The resulting arbitrage profit can be realized after the share issue is completed. 32 stocks with relatively liquid markets that made new share issues at discount prices over the last two years provided a median arbitrage return of 33% over an average registration period of 108 days. The effect is especially pronounced with undervalued stocks. We also found that the deeper the required price adjustment, the higher the arbitrage profit tends to be. The effect is hardly visible for capital increases below 20%.

**18-24 month window to play the game**

Since Jan 1, 2007, amended law encourages share issues at market price. So far, we only observed a few, but with more coming, arbitrage opportunities will be disappearing. We estimate the window of opportunity at 18-24 months. Monitor banking stocks, as banks conduct additional share issue at least on an annual basis.

**Risks to be aware of**

The regulatory procedure for share issues is rather drawn out and complicated. Two AGMs, two stages of subscription, and registration by the SSEC make the process vulnerable to **legal challenges** if conflicts exist between major shareholder groups. This risk can be detected in advance, and requires awareness of corporate governance practices. Additionally, in massively dilutive share issues, **free float** may shrink dramatically, due to non-subscribing "babushkas".

**Upcoming opportunities**

Our recommendation is to look closely at DMK Dzerzhinskogo Steel (DMKD) and Energomashspetsstal (ENMA), whose pending issues have similar characteristics. More than twofold capital increases, with required price correction of some 55% (at current market price) indicate relatively high arbitrage probability. We estimate these opportunities come with relatively low risk. Bank Forum can also generate extra return, though the size of the capital increase is not as significant. Subscription at Slavutych (SLAV) is still running – as of today, the arbitrage profit is 15%.

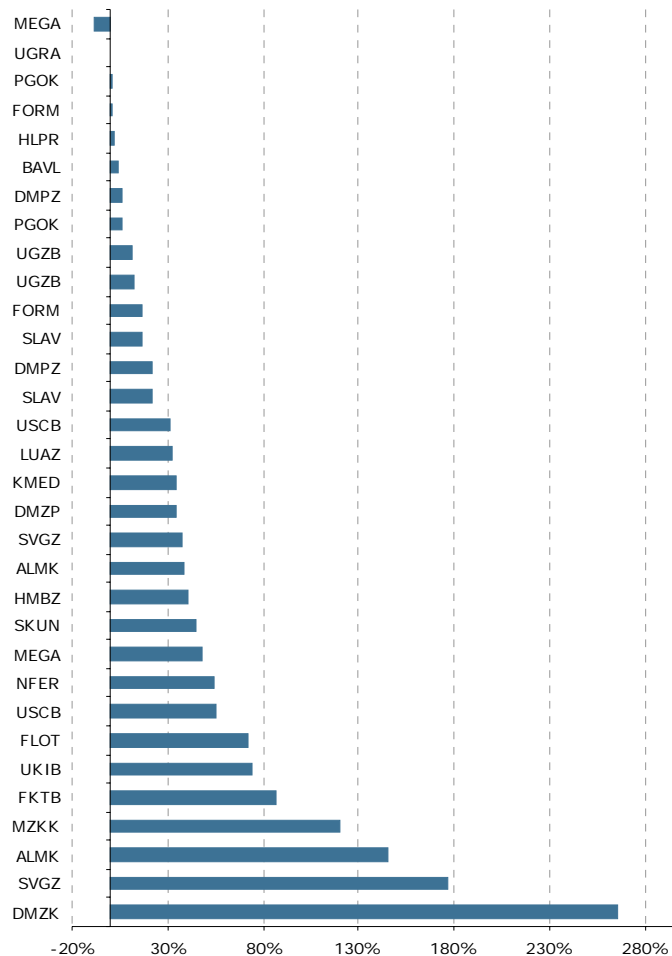
# SHARE ISSUES AT DISCOUNT AS A RETURN BOOSTER

A distinctive feature of the Ukrainian stock market is the phenomenon of additional share issues at deep discount to the market. This is rooted in controversial tax regulation prior to January 1, 2007, which treated proceeds from a share issue in excess of par value as taxable income for the issuer.

Since January 2007, this legal aberration was eliminated with amendment to the Law On Enterprise Profit Tax. Nevertheless, we only have seen four issues at market since then, while the majority of companies continue to conduct share issues at par. Partially, this could be chalked up to inertia. Partially the reason could be that discounted issues leave shareholders no other choice but subscribe - in a way guaranteeing successful placement at the expense of questionable corporate governance. At the same time, issues at deep discount still remain an efficient dilution instrument for a majority shareholder.

Those not subscribing during a significant capital increase, would be diluted, as the price falls overnight on the ex-rights date to adjust to the inflated number of shares. Nuisance as it could be, dilutive share issues have a useful side effect. Our analysis of statistical data revealed that the market tends to under-correct, bringing an arbitrage profit for those who subscribe.

## Arbitrage returns during discount-to-market share subscriptions, 2006-2008



Source: PFTS; Concorde Capital calculations

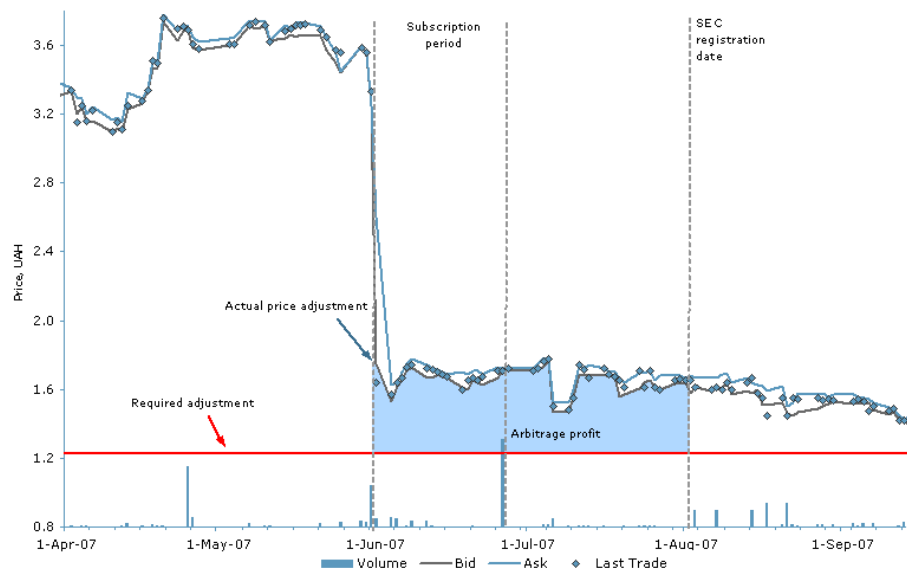
This is not arbitrage in its pure sense. The profit can only be realized after a lock-in period when new shares are registered and may be traded (see appendix for details). However, an investor with an open long position sees return on the stock, receiving a booster. The median lock-in period in completed share issues we analyzed was 108 days.

# ARBITRAGE PROFIT

## How an arbitrage emerges

On an efficient market, price would react to a dilutive share issue on the ex-rights date by adjusting downward to the level where the old market price and subscription price are blended according to the relative number of shares ("required adjustment"). As the cost of shares in the hands of a subscribing investor adjusts completely to the fully diluted basis, he receives an arbitrage profit should the market price find equilibrium above the required adjustment level.

## Ex-rights price usually does not adjust completely, creating an arbitrage USCB



Source: PFTS, Concorde Capital

The example in the chart above is a classic picture, due to the relatively high liquidity of Ukrsofsbank shares. A much more typical price behavior of Ukrainian stocks is a *protective spread* picture: since ex-rights date, the ask quote remains stable to reflect the old number of shares (accounting for the risk of share issue failure), while the bid drops in accordance with the new number of shares (you will find plenty examples in the charts on pp. 6-7).

## Our approach to analysis

The sample for our analysis includes discount-to-market share issues over the last two years (with ex-rights dates in January 2006 or later), excluding extremely illiquid stocks (no listing, no regular quotations or no trading).

We calculated returns on a fully diluted basis over the lock-in period: from ex-rights date to the date of share issue registration by the SSEC (or to the current date if the new share issue is not completed yet). Many stocks from the sample were rather illiquid around subscription, so in order to show the most conservative end in calculating returns we also used bid quotations in addition to market price estimations.

As the lock-in period is quite extended, market forces can begin driving prices up<sup>1</sup>. We take the bottom price levels during the lock-in period to gauge the arbitrage effect, as any upward movement is attributable to non-issue factors (like obvious examples, ALMK in 2007 or BAVL in 2006 - see the charts on pp. 6-7).

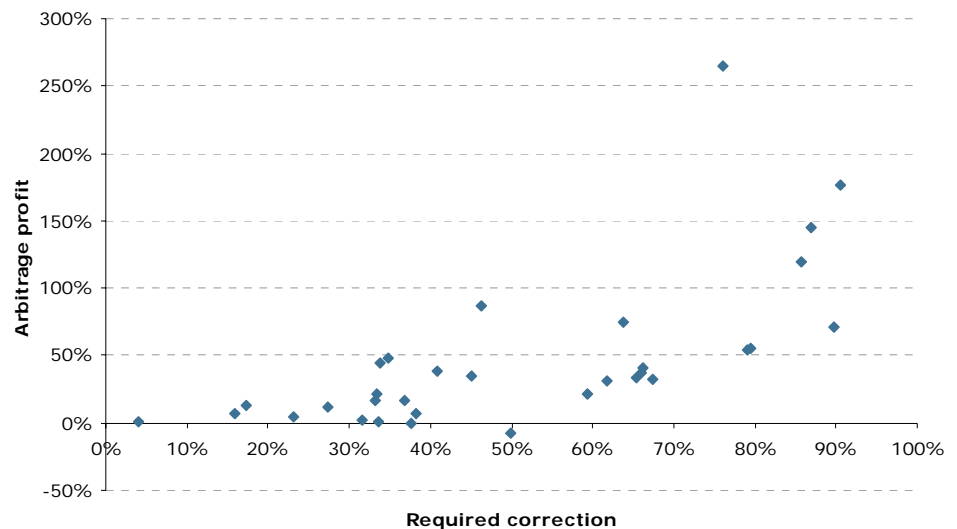
<sup>1</sup> Note: In some cases, trades were registered during a lock-in period at pre-ex-rights price levels (see for example ALMK in 2006). These are deals where a seller guarantees the buyer rights for the shares of the new issue in a special agreement.

**Share issues at discount to market since 2006**

Ticker	Company Name	Ex Rights	Capital increase	Pre Ex-Rights		Required adjustment		Actual adjustment (bid)			Actual adjustment (market price)			Lock-in period, days
				price, UAH	MCap USD min	Fully diluted price, UAH	Required correction	UAH	Arbitrage	Annualized arbitrage	UAH	Arbitrage	Annualized arbitrage	
USCB	Ukrsotsbank	19.01.2006	432%	4.63	636	0.95	79%	1.40	47%	106%	1.48	55%	124%	162
ALMK	Alchevsk Iron & Steel	08.02.2006	1290%	1.60	246	0.21	87%	0.50	140%	397%	0.51	145%	411%	129
LUAZ	Bohdan Automobile Plant	14.02.2006	352%	1.85	269	0.60	67%	0.70	16%	24%	0.80	33%	49%	242
PGOK	Poltava Iron Ore	06.04.2006	5%	68.93	1501	66.17	4%	50.00	-24%		66.50	1%	2%	82
MEGA	Megabank	07.06.2006	130%	8.75	87	4.38	50%	4.00	-9%		4.02	-8%		68
UGRA	Ukrgraphite	21.06.2006	184%	8.00	39	4.99	38%	4.00	-20%		5.00	0%	1%	115
FORM	Forum	21.06.2006	68%	60.00	440	39.79	34%	26.51	-33%		40.08	1%	3%	98
UGZB	Ukrgazbank	30.06.2006	50%	5.50	217	4.00	27%	4.00	0%	0%	4.47	12%	21%	208
BAVL	Raiffeisen Bank Aval	03.07.2006	40%	0.50	1480	0.38	23%	0.38	-1%	-3%	0.40	4%	8%	175
DMPZ	Donetsk Metal Rolling	14.07.2006	70%	0.14	16	0.09	38%	0.09	4%	14%	0.09	6%	22%	104
HMBZ	Svitlo Shakhtarya	14.08.2006	200%	1.63	36	0.55	66%	0.52	-5%		0.77	40%	194%	76
SLAV	Slavutych Brewery	09.11.2006	72%	4.90	481	3.26	33%	5.03	54%	50%	3.98	22%	20%	391
UKIB	Ukrinbank	01.12.2006	307%	0.07	65	0.02	64%	0.04	70%	312%	0.04	74%	331%	82
FORM	Forum	07.02.2007	81%	57.00	701	36.04	37%	40.10	11%	36%	42.05	17%	54%	113
SVGZ	Stakhaniv Wagon	27.02.2007	995%	290.00	66	27.44	91%	36.20	32%	99%	76.00	177%	547%	118
SKUN	Universalna Insurance	28.02.2007	67%	6.55	78	4.33	34%	6.05	40%	131%	6.25	44%	146%	111
FKTB	Factorial Bank	15.05.2007	155%	4.20	33	2.25	46%	3.86	71%	185%	4.20	86%	225%	140
USCB	Ukrsotsbank	31.05.2007	176%	3.25	2378	1.24	62%	1.58	27%	158%	1.63	31%	181%	63
DMZK	Kominmet	01.06.2007	538%	2.55	13	0.61	76%	2.22	264%	1528%	2.23	265%	1538%	63
MEGA	Megabank	07.06.2007	74%	5.50	125	3.59	35%	4.70	31%	202%	5.30	48%	311%	56
HLPR	Khlibprom	14.06.2007	65%	0.05	90	0.03	32%	0.03	-12%		0.04	2%	8%	105
ALMK	Alchevsk Iron & Steel*	13.07.2007	139%	0.34	717	0.20	41%	0.70	252%	415%	0.28	38%	63%	(222)
MZKK	Myroniv Feed and Cereal Plant	19.07.2007	823%	6.38	20	0.91	86%	2.00	119%	421%	2.01	120%	425%	103
DMZP	DMP Petrovskogo Steel	17.08.2007	118%	1.50	252	0.82	45%	1.10	33%	180%	1.11	35%	186%	68
UGZB	Ukrgazbank	31.08.2007	25%	7.30	578	6.04	17%	6.70	11%	23%	6.80	13%	27%	173
SVGZ	Stakhaniv Wagon*	15.11.2007	200%	105.09	262	35.73	66%	46.63	30%	116%	49.00	37%	141%	(96)
KMED	Kyivmedpreparat*	30.11.2007	233%	390.50	93	134.91	65%	115.00	-15%		181.00	34%	152%	(82)
DMPZ	Donetsk Metal Rolling*	30.11.2007	157%	0.34	66	0.14	59%	0.13	-7%		0.17	22%	96%	(82)
FLOT	Ukrflot*	07.12.2007	900%	90.05	141	9.32	90%	16.00	72%	349%	16.00	72%	349%	(75)
SLAV	Slavutych Brewery*	19.12.2007	72%	4.80	471	3.21	33%	3.50	9%	53%	3.75	17%	98%	(63)
PGOK	Poltava Iron Ore*	24.12.2007	22%	87.01	1988	73.13	16%	75.50	3%	21%	78.00	7%	43%	(57)
NFER	Nikopol Ferroalloy*	13.01.2008	411%	15.01	902	3.14	79%	4.82	54%	489%	4.84	54%	495%	(40)
<b>Median</b>			<b>147%</b>		<b>231</b>		<b>46%</b>		<b>22%</b>	<b>52%</b>		<b>33%</b>	<b>111%</b>	<b>108</b>

Source: Company data, PFTS, Concorde Capital calculations.

\* Not registered issues, arbitrage calculated based on Feb. 18 prices, excluded from median lock-in period calculation

**The deeper the required adjustment, the higher the expected arbitrage**


Source: PFTS, Concorde Capital calculations

Case by case analysis of 32 share issues points to the following indications of a successful arbitrage:

- Absence of major corporate governance risks (privatization questions, conflicts among major shareholders, etc.)
- Deep required price adjustment

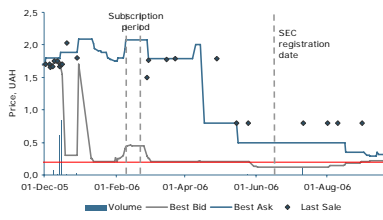
Risks to assume:

- Lock-in period may draw out in length. Four of 32 share issues had a lock-in period of more than six months. Two of them had long subscription periods, known at the outset, as decided at their AGMs; in two other cases, SSEC registration took too long.

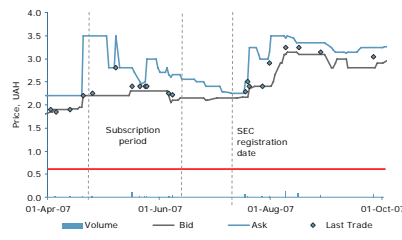
- Reversal of the share issue. The risk is relatively low and diminishing with the overall improvement of corporate governance in Ukraine. Since 2005, we could only detect one example of this action with Pivdenny Iron Ore's (PGZK) share issue. Results of the subscription to a threefold capital increase were not approved at several successive EGMs and finally canceled. The reason was disagreement between two major stakeholders – Privat and Smart groups. Fortunately, after abortion of the issue, the fundamentally undervalued stock, restricted from growth during the limbo period, shot up more than 500% over the next seven months, more than compensating shareholders for the trouble.
- A subscribing shareholder may encounter procedural hindrances. For example, during the recent Stakhaniv Wagon (SVGZ) subscription, there was a requirement that a shareholder (or representative) submit application documents in person at the company's headquarters. In extreme cases, a shareholder may struggle for their right to subscribe. In the recent subscription for Kyivmedpreparat's (KMED) issue, a group of investors who accumulated a significant block of shares failed to subscribe. Though they were turned down on legal grounds, there is an opinion that the majority shareholder considered share accumulation prior to the issue as an attempt at hostile attack, and acted in defensive way: other minorities were able to subscribe smoothly.

# SHARE ISSUES AT DISCOUNT TO MARKET 2006-2008

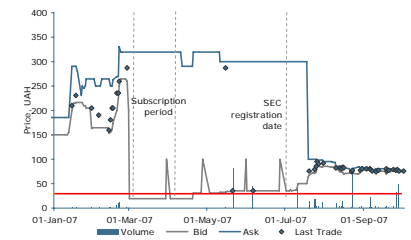
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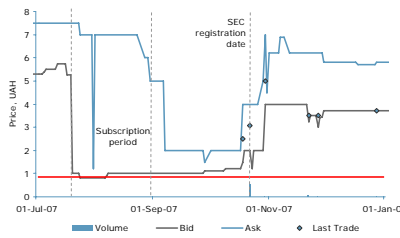
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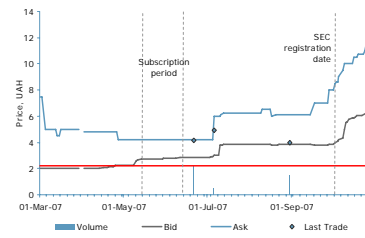
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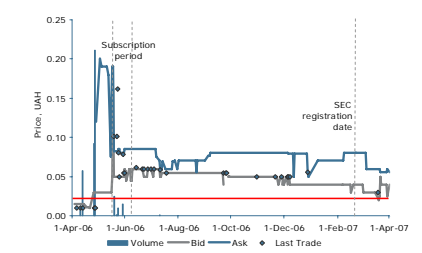
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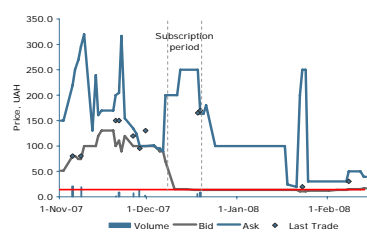
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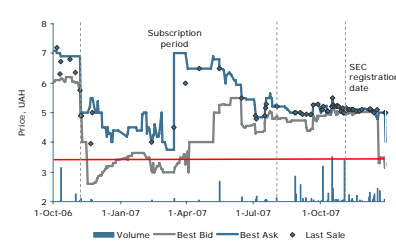
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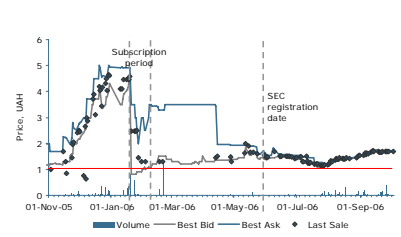
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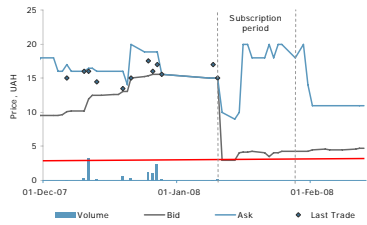
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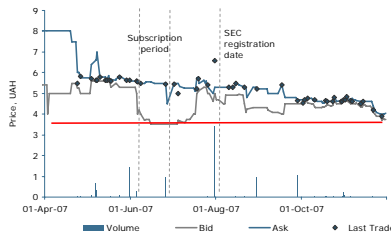
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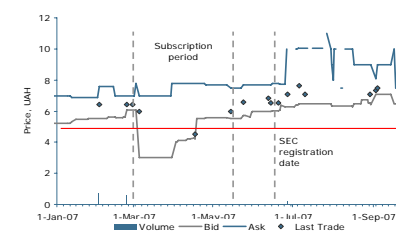
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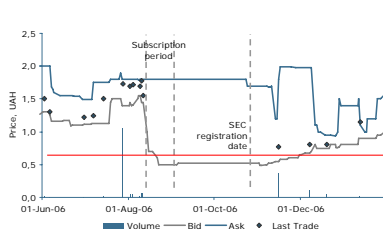
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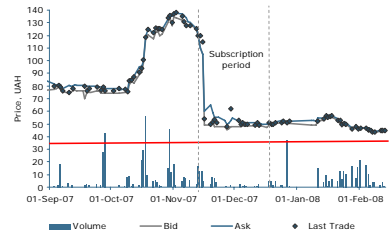
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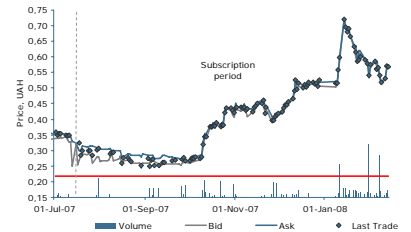
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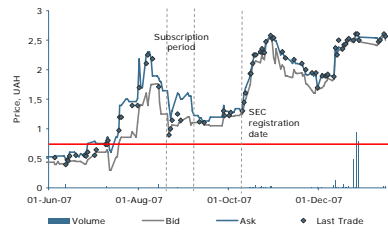
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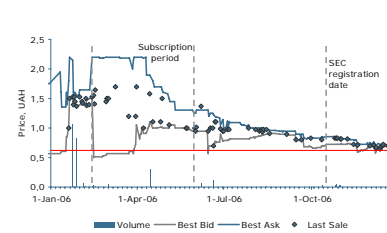
Note: Number in parentheses differentiates share issues, if a company had more than one

# SHARE ISSUES AT DISCOUNT TO MARKET 2006-2008 (CONT.)

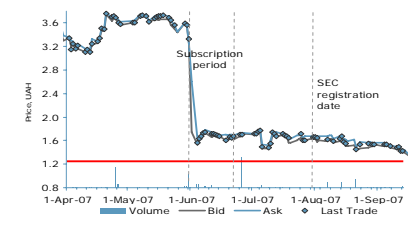
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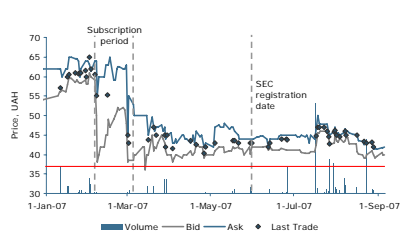
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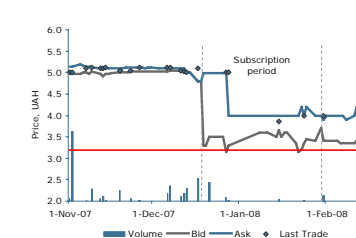
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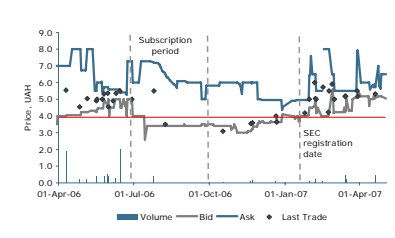
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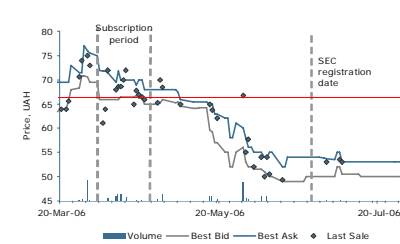
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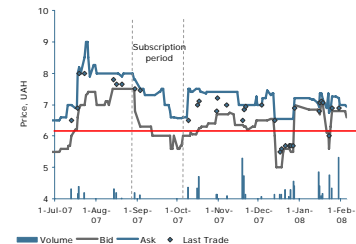
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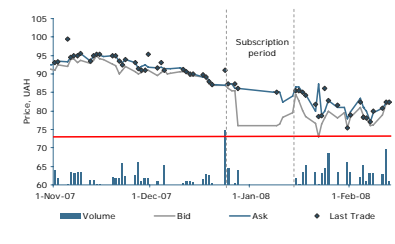
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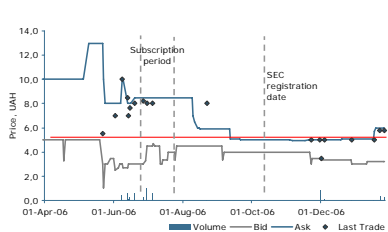
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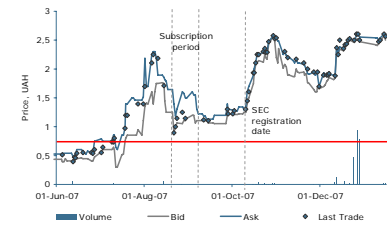
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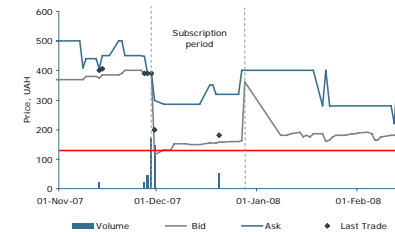
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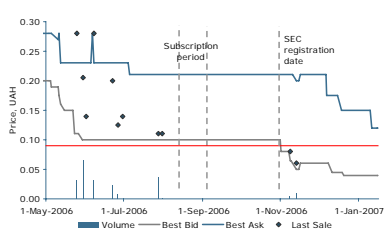
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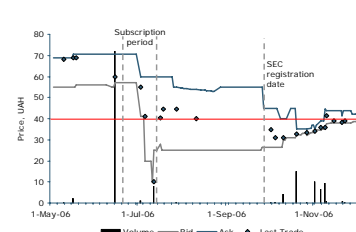
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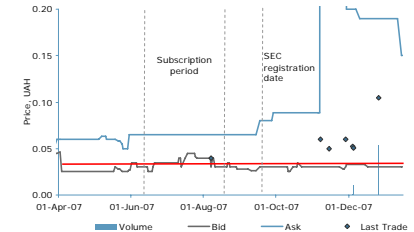
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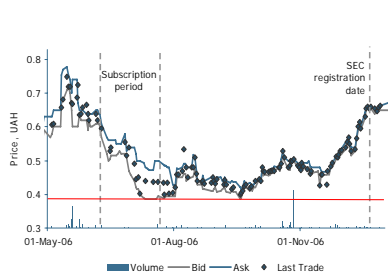
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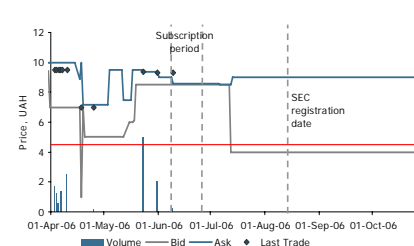
HLPR



BAVL



MEGA



Note: Number in parentheses differentiates share issues, if a company had more than one

## UPCOMING SHARE ISSUES

Five PFTS-listed stocks have already scheduled new share issues at par over the coming months. Among them, we recommend looking at DMK Dzerzhinskogo Steel (DMKD) and Energomashspetsstal (ENMA): more than a double capital increase, with required price correction of 55% (to current market) creates the prerequisites to expect an arbitrage profit. Parameters of Dniprometiz' (DMPO) share issue are attractive for arbitrage, but beware of low free float. Bank Forum (FORM) can also generate extra return, though the size of the capital increase is not as significant.

The share issue at Inguletsky Iron Ore, with very attractive technical parameters, is marred by stock illiquidity. Issues at Shostka Milk (SHMK) and Khartsyzk Pipe (HRTR) are not of a size to hope for any significant price corrections.

As always, in the course of the year, banks will provide a flow of share issues to be considered.

### Scheduled share issues at par

#### Approved by shareholders

	Ex-rights date	Capital Increase	Depth of correction	MCap, USD mln	FF, USD mln	Inv. Rating
ENMA	29.02.2008	154%	56%	94	10	N/R
UGZB	10.03.2008	20%	14%	673	67	HOLD
FORM	14.03.2008	45%	24%	943	94	BUY
SHMK	23.03.2008	22%	18%	79	2	SELL
DMPO	28.03.2008	256%	65%	44	3	BUY

#### Share issues pending AGM consent

	Ex-rights date	Capital Increase	Depth of correction	MCap, USD mln	FF, USD mln	Inv. Rating
HRTR	25.04.2008	2%	2%	1 667	33	SELL
IGOK	25.04.2008	112%	26%	130	1	N/R
ENMZ	29.04.2008	2%	2%	963	133	BUY
DMKD	09.05.2008	144%	55%	1 621	16	N/R

Source: [www.smida.gov.ua](http://www.smida.gov.ua), Company data, Concorde Capital calculations

### Investment Cases

#### Shostka Milk

PFTS ticker: SHMK  
 XETRA ticker: n/a  
 Industry: Food  
 MCap, \$ mln: 79.2  
 FF, \$ mln: 2.0  
 12m target, \$: 41.40  
 Investment rating: SELL

**Ex-rights date: 21 Mar 2008**

**Charter fund increase: 22%**

CorpGovernance rating\*: **N/A**

Shareholders voted for a 22% charter fund increase at their EGM on January 22. Subscription stage (1): March 24 to April 11; stage (2): April 12 to April 29. Required correction to the market price (as of February 18): 18%. Major shareholder French Bel Fromageries (97.5%) conceded its subscription stake to EBRD. Minorities will be able to subscribe on a pro-rata basis. We estimate related risks as insignificant. Low trading volumes on the PFTS.

Fifth largest hard cheese manufacturer, with 5.5% of domestic production in 2006. Ninth in terms of processed raw milk, with a 3% market share in 2006. Plans to double cheese production by 2010 to 21 ths mt. Strong brand. We project sales growth at 35% CAGR over 2006-2009.

\* 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.



### Khartsyzk Pipe

PFTS ticker: HRTR  
 XETRA ticker: LB5 GR  
 Industry: Metals & Mining  
 MCap, \$ mln: 1666.8  
 FF, \$ mln: 33.3  
 12m target, \$: 0.44  
 Investment rating: SELL  
**Ex-rights date: 27 Apr 2008**  
**Charter fund increase: 2%**  
 CorpGovernance rating\*: **A**

Shareholders will vote for a 2% charter fund increase at their AGM on March 14. The first stage of subscription is scheduled for April 28 to May 12; the second from May 13 to May 14. Required correction to the market price (as of February 18): 2%. The share issue seems to be technical (2%), we do not think it carries risks for minorities.

Ukraine's #2 largest pipe maker by volume (508.9 ths mt, 19.5% share of domestic production in 2007). Capacity: 1.5 mln mt of pipes/yr. Core product - large diameter steel pipes with corrosion-proof coating, used in construction of oil and gas main pipelines. Exports over 90% of total output, mainly to Russia. Medium risk of losing position on the Russian market in near-term, as Russia plans to increase its LD pipe manufacturing by 2010. Parent company, Metinvest, is a 2009 IPO candidate.

### Enakievo Steel

PFTS ticker: ENMZ  
 XETRA ticker: n/a  
 Industry: Metals & Mining  
 MCap, \$ mln: 962.5  
 FF, \$ mln: 132.8  
 12m target, \$: 120.00  
 Investment rating: BUY  
**Ex-rights date: 29 Apr 2008**  
**Charter fund increase: 2%**  
 CorpGovernance rating\*: **P**

Shareholders will vote on a 1.7% charter fund increase at their EGM on March 21; subscription schedule: (1) from April 30 to May 14, (2) from May 15 to May 16. Required correction to the market price (as of February 18): 2%. We do not see risks for minorities: the issue seems to be of a technical nature.

Sector leader by sales growth: 46.5% yoy in 2007. 6.5% of Ukrainian steel output in 2007. Integration into Metinvest provides immunity from global raw materials price hikes. Planned merger with Metalen would boost Enakievo's value 25-50%. Enakievo-Metalen produces pig iron, steel channels, billets, steel angles, railway rails, round steel bars, rolled products, etc. Key export markets: CIS & Baltics, Europe, the Middle East, Africa and South America. In 2007, produced 2.4 mln mt of pig iron (up 11.3% yoy) and 2.8 mln mt of steel (up 8.1% yoy).

### DMK Dzerzhinskogo Steel

PFTS ticker: DMKD  
 XETRA ticker: n/a  
 Industry: Metals & Mining  
 MCap, \$ mln: 1621.2  
 FF, \$ mln: 16.2  
 12m target, \$: N/A  
 Investment rating: N/R  
**Ex-rights date: 9 May 2008**  
**Charter fund increase: 144%**  
 CorpGovernance rating\*: **P**

Subscription for share issue is scheduled for May 12 to December 5. Required correction to the market price (as of February 18): 55%. This share issue has a significantly longer than the average lock-in period - SSEC registration is expected not earlier than the end of 2008. This and poor corporate governance rating gives medium risk to the issue.

Ukraine's sixth largest steel producer in terms of output, with 8.8% of total domestic steel production in 2007. Product mix: pig iron, sinter, steel, hot-rolled long and flat products for machine-building and transport industries. Controlled by the Industrial Union of Donbas. In 2007, output of finished steel grew 4.2% yoy to 3.78 mln mt, pig iron production was up 3.2% to 3.45 mln mt.

### Inguletsky Iron Ore

PFTS ticker: IGOK  
 XETRA ticker: n/a  
 Industry: Metals & Mining  
 MCap, \$ mln: 130.0  
 FF, \$ mln: 0.6  
 12m target, \$: N/A  
 Investment rating: N/R  
**Ex-rights date: 25 Apr 2008**  
**Charter fund increase: 112%**  
 CorpGovernance rating\*: **P**

EGM is scheduled to vote on 112% capital increase on March 21. Subscription schedule: stage one from April 28 to May 12 and stage two from May 13 to May 14. Required correction to the market price (as of February 18): 26%. Corporate governance issues in the past (in 2005, the company twice changed its legal structure) and scarce free-float of 0.5% lead us to assign medium risk to this issue.

Produces the most Ukrainian sinter feed, which it delivers to local steel mills with their own sintering factories. Located in Ukraine's largest iron ore basin, Kryviy Rih. Capacity: 36 mln mt of iron ore, 14 mln mt of sinter feed p.a. Uses cost-efficient open-pit mines.

\* 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.

**Dniprometiz**

PFTS ticker: DMPO  
 XETRA ticker: n/a  
 Industry: Metals & Mining  
 MCap, \$ mln: 44.1  
 FF, \$ mln: 3.1  
 12m target, \$: 154.00  
 Investment rating: BUY  
**Ex-rights date: 28 Mar 2008**  
**Charter fund increase: 256%**  
 CorpGovernance rating\*: **N/A**

On January 10 the company's shareholders OKed a 256% capital increase. Subscription schedule: (1) from March 31 to April 08, and (2) from April 9 to April 11. Required correction to the market price (as of February 18): 65%. We think that the share issue might be purposed to dilute "babushkas", while institutional investors will be not diluted. We estimate the risks associated with the issue as relatively low due to Severstal-Metiz' high corporate governance profile.

Largest producer of wire in Ukraine. Acquired by Severstal-Metiz, a wing of Russian steel giant Severstal Group, in 2006. Three-year development plan foresees increasing production capacity by 30% to 200 ths mt per year. More shipments to the capacious European market via Severstal-Metiz's dealer network.

**Bank Forum**

PFTS ticker: FORM  
 XETRA ticker: B5F GR  
 Industry: Banking  
 MCap, \$ mln: 943.0  
 FF, \$ mln: 94.3  
 12m target, \$: N/A  
 Investment rating: BUY  
**Ex-rights date: 14 Mar 2008**  
**Charter fund increase: 45%**  
 CorpGovernance rating\*: **Q**

Subscription for a 45% additional share issue will take place from March 17 to April 14, 2008. Required correction to the market price (as of February 18): 24%. Traditionally, banking share issues have proved to be low-risk. Forum is ranked among the best companies in Ukraine in terms of corporate governance.

In Sept. 2007, German Commerzbank acquired a 60% stake in the bank; acquisition-related positives are already showing up: 2007 earnings growth accelerated to 89% yoy vs. a moderate increase of 29% yoy in 1H07. Ukraine's #12 largest bank with USD 2,855 mln in assets as of January 1, 2008. In 2007, its gross loan portfolio surged 89% yoy to USD 1.9 bln.

**Ukrgazbank**

PFTS ticker: UGZB  
 XETRA ticker: n/a  
 Industry: Metals & Mining  
 MCap, \$ mln: 673.3  
 FF, \$ mln: 67.3  
 12m target, \$: 11.50  
 Investment rating: HOLD  
**Ex-rights date: 10 Mar 2008**  
**Charter fund increase: 20%**  
 CorpGovernance rating\*: **BA**

20% charter fund increase was approved at the company's EGM on February 1. Subscription will take place from March 11 to March 31. Required correction to the market price (as of February 18): 14%. Historically, all eleven of the bank's share issues within the last ten years have gone off without a hitch.

Net income more than tripled in 2007 to USD 19.9 mln. 2007 asset growth of 131% yoy, to USD 2.0 bln, was twice the sector average. Rapidly diversifying into retail: loans to individuals grew 2.4x yoy in 2007. Owners are in talks to sell the bank. Ukraine's #17 largest bank by assets (USD 2.0 bln), with a 1.8% market share as of January 1, 2008.

**Energomashpetsstal**

PFTS ticker: ENMA  
 XETRA ticker: n/a  
 Industry: Metals & Mining  
 MCap, \$ mln: 93.5  
 FF, \$ mln: 9.5  
 12m target, \$: N/A  
 Investment rating: N/R  
**Ex-rights date: 29 Feb 2008**  
**Charter fund increase: 154%**  
 CorpGovernance rating\*: **BA**

Subscription will last from March 3 to March 26. Required correction to the market price (as of February 18): 56%. We assign low risk to the issue: minority shareholders of IUD-owned companies have not suffered from share issue-related conflicts.

Produces castings and forgings for machine-building, metallurgic, iron ore and other industries. Exports to: the United Kingdom, Italy, the U.S.A., Germany, Hungary, Turkey, Bulgaria, Thailand and the Dominican Republic. In 1H2007, net revenues of USD 46.2 mln (up 45% yoy). Plans to invest USD 80 mln in modernization by 2009.

\* 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.

## APPENDIX

## UNDERSTANDING NEW SHARE ISSUES

**Decision on an additional share issue** is taken at the general shareholder meeting by simple majority of voting shares present. Quorum at a shareholder meeting is 60%+1 votes. The shareholder meeting defines the terms and time period for the placement, which among other things include the ex-rights date and duration of the subscription.

**The form of the issue can be private (closed) or public (open).** Private share issues limit the number of investors, other than existing shareholders, who can subscribe, to 100 predefined participants. Public issues are not limited in the number of new investors.

In both cases, existing shareholders shall be guaranteed priority subscription rights. This results in a two-stage subscription procedure: (1) existing shareholders subscribe on a pro-rata basis, (2) subscription for unsubscribed remaining shares is open to other investors. Terms for stage one are defined by the shareholder meeting. According to law, during private share issues, stage one of a subscription period may not be shorter than 15 calendar days.

**Ex-rights date.** By law, the list of shareholders entitled to subscribe to new shares on a pro-rata basis, is formed from the shareholder register on the day preceding the ex-rights date. For closed share placements, the ex-rights date must always be the first date of stage one of subscription. For open share placements, the decision on ex-rights date is taken by the AGM – most typically, it coincides with the day stage one of subscription begins.

In practical terms, presence in the shareholder register at the end of the working day preceding the ex-rights date is required for subscription rights.

**First stage of subscription.** During this stage, existing shareholders realize their priority right to subscribe for new shares. In rare cases, the applicant may be burdened by special requirements. For example, a shareholder (or representative) might be demanded to submit application documents in person at the company's headquarters. On the first working day after the completion of stage one, existing shareholders have the right to request a report from the company on the number of shares placed.

**Second stage of subscription.** The pro-rata principle is not applicable during the second stage; shares are placed on a 'first come first serve' basis (additional methods can be approved by shareholders but are rare). In real life, this means that the main shareholder subscribes for shares remaining after stage one subscription and dilutes those who did not subscribe. In many cases, this is the goal of the subscription – massive dilution of minorities like employees, retired employees, etc who received shares for free during privatization and do not have the ability to pay for new shares (or are just not well informed). An example is Ukrichflot, where widely fragmented ownership was consolidated via a dilutive share issue in December 2007 after the new owner took over control of the company.

**Approval of subscription at EGM.** A shareholder meeting must approve the results of subscription, and corresponding amendments to the company's by-law must be approved by  $\frac{3}{4}$  of the voting shares present at the EGM. If main shareholder groups disagree on subscription, the deal could fall through at this point. This case was with Pivdenny Iron Ore, where a new share emission launched at an AGM on April 26, 2005 was finally canceled as several successive shareholder meetings failed to approve the results of subscription.

**Registration by the SSEC.** The share issue must be registered with the Ukrainian Securities and Exchange Commission. Usually, the registration process concludes 4-7 weeks after approval of subscription results at the shareholder meeting.

## THE EXTRA RETURN MATH

### Price adjustment

Share issues conducted at discount to the market force the market price to fall on the ex-rights date to adjust for the new number of shares. Under the assumption of the efficient market and cash contributions by all shareholders, the adjusted price should be:

$$P_{adj} = ( P_{pre-ex} * N_{old} + P_{subscr} * N_{add} ) / ( N_{old} + N_{add} )$$

where:

$P_{pre-ex}$	Closing market price on the trading day preceding the ex-rights date
$P_{subscr}$	Price of subscription
$N_{old}$	Number of shares before subscription
$N_{add}$	Number of new shares being issued

### Arbitrage profit

If the market price,  $P_{act}$ , does not adjust perfectly, the investor who bought shares prior to subscription and subscribed for new shares receives an arbitrage profit  $\delta$ :

$$\delta = ( P_{act} - P_{adj} ) / P_{adj}$$

## SHARE ISSUES NOT INCLUDED IN OUR ANALYSIS

Ticker	Company	Ex-Rights	Registration	Comments
HLPR	Khlibprom	09.02.2006	04.05.2006	no listing
YAMZ	Yasynuvatsky Machinery	10.02.2006	29.05.2006	no listing
SGOK	Pivnichny Iron Ore	11.02.2006	27.04.2006	illiquid
CGOK	Centralny Iron Ore	13.02.2006	27.04.2006	no listing
BKOK	Bagliy Coke	03.03.2006	05.10.2006	illiquid
CHIM	Chernigiv Khimvolokno	25.03.2006	26.06.2006	no listing
BXRK	Khreschatyk Bank	31.03.2006	19.08.2006	illiquid
DMPO	Dniprometiz	24.05.2006	01.09.2006	no listing
NADR	Nadra Bank	02.06.2006	29.11.2006	no listing
AKRB	Autokrazbank	30.06.2006	12.04.2007	illiquid
VKDV	VK Development	01.08.2006	08.11.2006	illiquid
KGST	Kyivmiskbud	22.09.2006	14.09.2006	illiquid
BXRK	Khreschatyk Bank	13.10.2006	11.10.2006	illiquid
GRMA	Grand Market	19.04.2007	03.04.2007	no listing
ODEN	Odessaoblenergo	18.05.2007	pending	no listing
RODB	Rodovid Bank	31.05.2007	11.10.2007	placed at market price
OGAZ	OdessaGaz	22.06.2007	19.07.2007	illiquid
BAVL	Raiffeisen Bank Aval	02.07.2007	15.11.2007	placed at market price
UROS	Ukrros	24.07.2007	pending	not listed prior to issue
KMOL	Kovelmoloko	24.08.2007	pending	illiquid
DNEN	Dniproenergo	27.09.2007	28.09.2007	participation restricted
CHIM	Chernigiv Khimvolokno	28.09.2007	06.12.2007	illiquid
HLPR	Khlibprom	24.11.2007	pending	participation restricted
GLNG	Galnaftogaz	29.11.2007	pending	placed at market price
SKUN	Universalna Insurance	25.01.2008	pending	placed at market price
UNIV	Universalna Life	27.01.2008	pending	illiquid

Source: Company data, PFTS, Concorde Capital calculations

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