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Analyst's Notebook

Ukraine / Oil & Gas
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Ukrnafta's Preliminary 1Q06 Results Meet Our Expectations

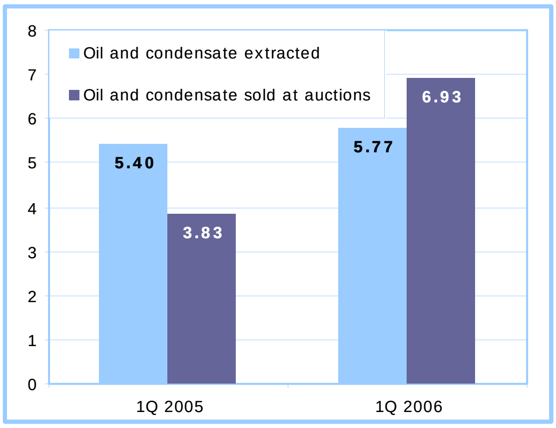
In 1Q06 Ukrnafta (**UNAF: HOLD**) reported 68% yoy increase in gross sales and 62% higher net revenue (hereafter, growth rates are in UAH terms). Net income grew an abnormal 127% yoy.

In general, the company's financial results are well in line with our forecasts for this year. In 2006 we expect 61% and 49% yoy growth of gross sales and net revenue respectively, building off the removal of tolling schemes, oil price growth and the company's further penetration into retail segment (see our research from May 15, 2006). We rate the most important factors contributing to better 1Q performance as follows:

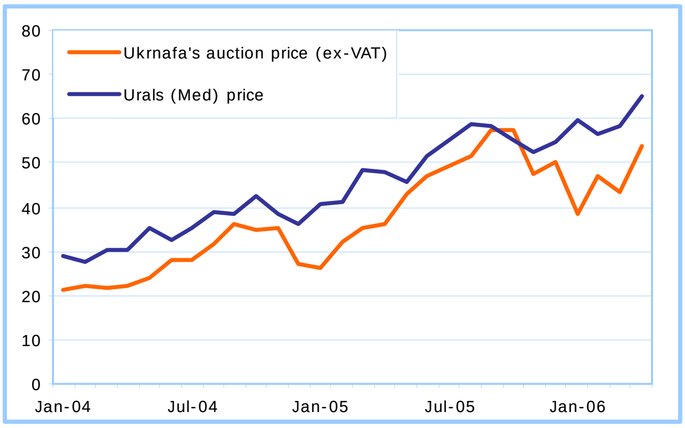
1. The End Of Tolling
We estimate that in 1Q06 Ukrnafta indeed sold all its extracted volume of crude at auctions, almost double the amount it sold in 1Q05, which supports our "no tolling" assumption for 2006.

2. Price Growth
Combined with the removal of tolling, a 32% yoy increase in Ukrnafta's oil auction price definitely contributed to the company's growth in 1Q 2006 in yoy terms. However, for the whole year we forecast Ukrnafta's auction price to lag behind the global trend, as everything points to Privat under-pricing oil at auctions to support profitability in its oil processing business. In our model, we assume the company's oil price will increase by a mere 7% yoy.

UNAF's Auction Sales*, mln bbls



Historical Oil Prices, USD / bbl



** excluding natural and oil gas*
Source: Ukrainian News, Bloomberg, Energobiznes, Concorde Capital estimates

3. Intensified Downstream Expansion
At the same time, compared to 1Q05, expansion of the company's retail network has intensified – during the first three months of 2006 it has put into operation 92 filling stations, almost the same amount the company put in operation during the whole 2005. We expect downstream sales to increase by 53% yoy in 2006, fueled by growth of its retail network and higher oil products prices.

Net Margin Hike To Vanish By Year-End

Ukrnafta's huge net income growth of 127% yoy in 1Q06 implied net margin of 46%, 12 p.p. higher than it was in 2005 and 25 p.p. higher than our forecast for 2006. We believe this increase stemmed from the peculiarities of local accounting and will be short-lived. Our 2006 forecast suggests that net income will decrease by 7% yoy, basically due to rapid retail expansion, which offers much lower margins than upstream operations.

Unfortunately, the company disclosed only a few lines of its financial statements. Once we get the full picture, we will follow up with a more detailed analysis of the company's 1Q06 results.

Income Statement Projections, USD mln

	2004	2005	2006F	2007F
Gross Sales	**978**	**1 628**	**2 620**	**3 217**
Change y-o-y	*N/M*	*66%*	*61%*	*23%*
Net Revenues	**736**	**1 088**	**1 623**	**2 074**
Change y-o-y	*N/M*	*48%*	*49%*	*28%*
Gross Profit	510	691	699	782
% of Net Revenues	*69%*	*64%*	*43%*	*38%*
EBITDA	**459**	**586**	**585**	**635**
EBITDA margin. %	62%	54%	36%	31%
Net Income	**253**	**365**	**343**	**356**
Net Margin. %	*34%*	*34%*	*21%*	*17%*

Source: Company data, Concorde Capital estimates