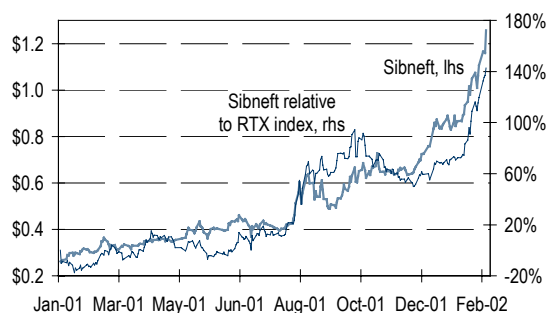


Sibneft – Upgrade to Strong Buy

The fastest-growing Russian oil company

Ordinary share price: **\$1.26**, price target **\$1.90**, implied upside **52%**

- Sibneft recently increased its production targets for 2002–05 and now hopes to expand 28.6% this year and 20% annually over 2003–05. This is substantially above our previous growth forecasts of 24% in 2002 and 5%–8% annually over 2003–05, and puts Sibneft significantly ahead of the pack in Russia.
- Our analysis of the key constraint—how much can the market absorb—concludes that Sibneft may be able to sell up to 40 m tons (292 m bbl) by 2005 given its current refining capacity. This is lower than the company's 2005–06 production target of 45 m tons (327 m bbl), but substantially above our previous forecast of 30 m tons in 2005. Our new target of 40 m tons (292 m bbl) implies a 2002–05E CAGR of 18%—by far the fastest organic growth rate in UBS Warburg's global oil universe (the global average is 4.2%).
- The company has also indicated that 2001 net profit will be around \$1,100 m, on EBITDA of \$1,600 m, 7% higher than our previous forecast. We therefore upgrade our 2001 earnings estimate from \$1,027 m to \$1,100 m and forecast slightly lower production costs in 2002 and onwards. We increase our 2002 profit forecast by 15% from \$831 m to \$954 m, and raise our 2003–05 forecasts 30% on average.
- We apply a target 2004E EV/DACF multiple of 4.0 to our 2004E EBITDA and net debt forecasts, and discount the resulting market capitalization back using a required rate of return of 10.7% (equal to the yield on the 2005 Eurobond yield and a 3.5% equity premium). After adjusting for dividend payments, we arrive at a one-year price target of \$1.9, up from our previous target of \$1.25. For comparison, our DCF model using a 14% discount rate suggests an NPV of \$3.2/share. At \$1.9, the company would trade at a 2004E P/E of 5.1, which we do not find excessive. We also raise our dividend forecasts for 2002–05, and predict a yield of 16.9%–39%. In the light of the above we upgrade the company from **Buy** to **Strong Buy**.



Ordinary share price:	\$1.26 (\$0.31–1.26)
No. of shares:	4,741 m
% of preferred:	0%
ADR ratio	1:10
Market Cap:	\$5,962 m
Freefloat:	12%

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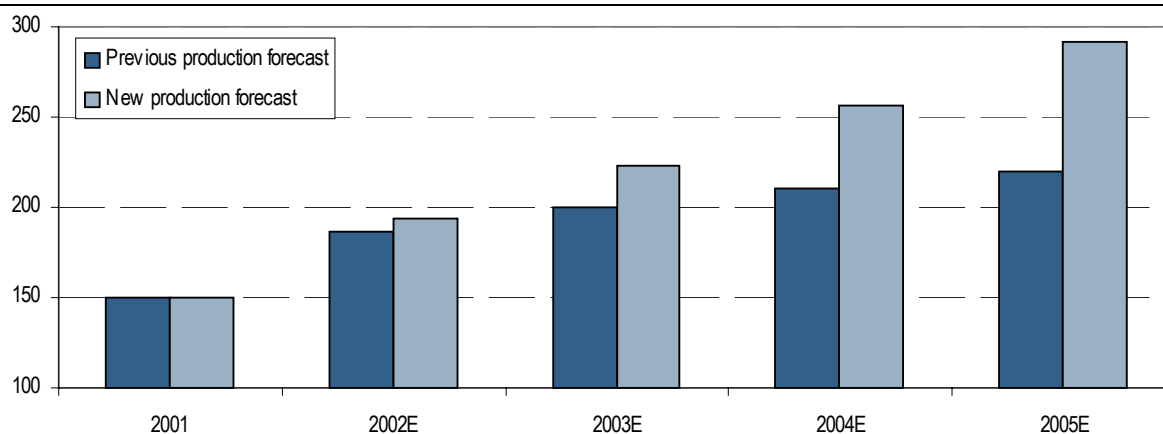
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How much can Sibneft grow?

Sibneft has made a number of positive statements over recent weeks. First, the company increased its 2002 production target from 24% to 28.6%, or to 26.5 m tons (191 m bbl), up from 20.6 m tons (150 m bbl) in 2001. Going forward, the company now expects organic growth in excess of 20% per year up to 2005, and targets 45 m tons (329 m bbl) in 2005–06. This would translate into 123% growth over 2001–05 to 45.8 m tons (334 m bbl). These forecasts do not include Sibneft's stake in Onako—we estimate the company will end up with 33% of the consolidated Onako, which has 2001 production of 8 m tons (58 m bbl).

Production growth, m bbl



Source: Company data, Brunswick UBS Warburg estimates

We have every faith in management's production forecasts—the company delivered a 19.6% increase last year and 23.8% year-on-year in January, and has never to our knowledge been overoptimistic with its estimates. We believe the bottleneck comes on the refining and retail side, rather than production. Based on the refining capacity the company itself owns and currently has access to, we estimate it can increase output 14.7% per year after 2002, to 40 m tons (292 m bbl) in 2005. Although lower than the company's own forecast, this is a 33% increase on our previous 2005 estimate of 30 m tons (220 m bbl).

The company has contracted French oil services company Pride Forasol to drill six horizontal wells this year for \$60 m. Last week the company showed the drilling of the first well to investors, where production is currently 2,000 tons (14,600 bbl/d)—equivalent to levels in the Middle East. Pride Forasol estimates that all six wells should produce at this level, and although horizontal wells have a more unstable profile, if these estimates prove correct they would together yield 4.4 m tons (32.1 m bbl) per year, or 21% of total 2001 production.

Production and crude flows, m tons

	2001E	2002E	2005E
Total production	20.6	26.5	40
exports	7.3	9.0	16
refining at Omsk Refinery	13.3	13.5	17
refining at Moscow Refinery	0.0	4.0	7

Source: Company data, Brunswick UBS Warburg estimates

Substantial earnings upgrades for 2001–02 and beyond

On the back of these new production targets, we have substantially upgraded our financial forecasts for Sibneft. We also expect Sibneft to process more crude at the Moscow Refinery and that retail volumes will double by 2005 (the company plans have 2,500–3,000 gas stations by 2005, up from 1,000 currently). We estimate that throughput at the Omsk Refinery will rise to full capacity of 17 m tons (124 m bbl) by 2005. On the cashflow side we believe the company paid \$200 m for various acquisitions last year, including an undisclosed sum for the 35% stake in Moscow Refinery (36.8% of votes). Conservatively, we have not included any contribution from Onako, as the company is not yet consolidated; however, we estimate that Onako may be able to contribute a further \$50–70 m annually in cashflow going forward.

As a result of these changes, we increase our 2001 net profit forecast by 7%, 2002 by 15% and 2003 by 30%. Capex for 2002 is forecast at \$700 m, although the company says this number could be reduced if the recent successes continue. Sibneft broadly agrees with our 2002 net profit forecast of \$954 m.

Revised forecasts, \$ m

	2001E	2002E	2003E	2004E	2005E
Old forecasts					
Revenues	3,253	3,033	3,620	3,926	4,239
EBITDA	1,519	1,369	1,735	1,951	2,145
Operating profit	1,163	954	1,283	1,470	1,649
Pretax profit	1,208	1,021	1,315	1,516	1,707
Net profit	1,027	831	1,071	1,235	1,391
Production, m bbl	150	186	200	210	220
New forecasts					
Revenues	3,306	3,149	4,081	4,842	5,658
EBITDA	1,600	1,524	2,108	2,593	3,110
Operating profit	1,244	1,110	1,656	2,112	2,615
Pretax profit	1,289	1,172	1,702	2,161	2,666
Net profit	1,096	954	1,387	1,762	2,175
Production, m bbl	150	194	223	256	292
% change					
Revenues	2%	4%	13%	23%	33%
EBITDA	5%	11%	21%	33%	45%
Operating profit	7%	16%	29%	44%	59%
Pretax profit	7%	15%	29%	43%	56%
Net profit	7%	15%	30%	43%	56%
Production	0%	4%	12%	22%	33%

Source: Brunswick UBS Warburg estimates

Leveraged positions

In contrast to companies such as Surgutneftegaz [\$0.321, **Buy**, PT under review] Sibneft runs a leveraged operation, and prefers to hand over excess cash to shareholders as dividends. We estimate that the company had net debt of \$1,100 m as of end-2001, of which \$1,000 m was long-term debt with an average maturity of 3.5 years. We expect the company to finance further growth partly with debt, and if the 19.68% government stake in Slavneft comes up for privatization this year, we anticipate Sibneft would bid, sourcing the funds through a Eurobond issue of roughly \$300–400 m.

Oil price sensitivity – risk is now on the upside

Our global oil strategy team now believes the risk to our 2002 average Brent price forecast of \$18/bbl is on the upside. We estimate that a \$1.50/bbl increase to our 2002 Brent forecast would raise Sibneft's 2002 profits 5.5% (not all of the rise would filter through to the bottom line, as we believe the average 2002 export tariff would go up from \$0.53/bbl to \$1.05/bbl). With Brent averaging \$19.5/bbl in 2002, Sibneft would be trading at a 2002E P/E of 5.9 at current prices, or 8.9 at our new price target of \$1.90. On the downside, we believe Sibneft is well protected by its low cost base—the company maintains it would be profitable on the bottom line with Brent down as low as \$8/bbl, and cashflow positive down to \$10/bbl.

Oil price sensitivity

	At current 2002 Brent forecast of \$18/bbl	Assuming Brent at \$19.5/bbl	% difference
EBITDA	1,524	1,587	4.1%
Net profit	954	1,006	5.5%

Source: Brunswick UBS Warburg estimates

The icing on the cake—dividend payouts that put other companies in the shade

Sibneft runs a relatively tight ship, with the aim of paying back all free cashflow to shareholders, on top of any funds the company cannot invest in acquisitions, which translates into generous dividends (see table below). There is a caveat—under Russian legislation, companies cannot pay out more than their recorded net profit in dividends. This creates uncertainties for the 2001 dividend, as technically the 2000 dividend payout of \$612 m was an “interim 1H01 dividend” for tax reasons. Subsequently the company paid out \$370 m as an “interim 3Q01 dividend.” Interim dividends are no longer allowed, and we believe that there is limited scope for dividends on full-year 2001 results (to be paid out in 2002)—we forecast a further payout for 2001 of \$135 m, bringing the total to \$1,117 m. While Sibneft may try to circumvent this legislation and pay a higher dividend on 2001 results, we remain conservative with our forecasts. Going forward, we expect dividends to return to higher levels in 2002 (payable in 2003), with yields of 16.9%–39% over 2002–05E.

Dividend yields

	2000	2001E	2002E	2003E	2004E	2005E
Yield, %	10.2%	8.5%	16.9%	27.3%	34.4%	39.3%
Total payout on current year's earnings, \$ m	612	505	1,008	1,630	2,056	2,346
Payout per share, ¢	12.9	10.7	21.3	34.4	43.4	49.5

Note: dividends are actually paid for the year following the relevant results—for example, the 2000 dividend of \$612 m was paid in 2H01 and booked as a 1H01 dividend. The 2001 dividend of \$370 m was announced in 3Q01 and was paid in the beginning of 2002. We estimate that the final 2001 dividend will be announced this summer and be around \$135 m. Under Russian law a company cannot pay out more in dividends than it books in net profit under RSA, thus Sibneft may not be allowed to pay out any further dividends on 2001 earnings. Further, recent changes to the Law on Joint-Stock Company's have ruled out interim dividends, thus dividends on this year's earnings may only be payable in 2003.

Source: Brunswick UBS Warburg estimates

Conclusion and rating

In the light of the company's new production targets and track record of meeting them, as well as its generous dividend policy, we raise our one-year price target from \$1.25 to \$1.90 and upgrade the company from **Buy** to **Strong Buy**. Further, we expect the company to start producing biannual financial accounts in the near future, which should increase transparency.

International valuation comparison

	Price 4-Mar	Curr.	M. Cap, \$ bn	EV/DACF					P/CEPS				P/E			
				00	01E	02E	03E	04E	00	01E	02E	03E	00	01E	02E	03E
BP	590	GBP	188.0	10.7	10.5	12.0	11.3	10.8	9.7	11.1	10.4	10.0	13.9	20.6	18.8	17.6
ExxonMobil	42.0	USD	282.8	12.3	11.7	12.4	11.7	11.2	11.7	12.4	11.6	11.1	18.3	20.4	18.8	17.7
Royal Dutch	59.7	EUR	107.7	10.4	10.0	9.6	9.1	8.7	9.6	9.3	8.7	8.2	15.8	17.9	16.5	15.5
Shell	496	GBP	68.1	9.8	10.2	9.1	8.6	8.2	9.7	8.8	8.2	7.7	16.0	17.0	15.6	14.6
TotalFinaElf	170	EUR	97.7	7.0	9.3	8.9	8.2	7.8	9.0	8.6	7.8	7.4	15.1	18.0	16.3	15.3
ChevronTexaco	85.5	USD	84.1	7.4	8.9	10.4	9.0	8.5	7.4	9.0	7.7	7.2	12.9	18.2	15.9	15.3
Conoco	27.9	USD	17.5	6.1	7.0	7.8	7.1	6.6	4.9	5.1	4.7	4.4	10.0	16.7	13.6	11.9
Eni	15.7	EUR	52.2	5.5	6.7	7.0	6.5	6.2	5.8	6.0	5.8	5.5	10.6	11.5	10.7	10.1
Repsol YPF	14.9	EUR	14.3	6.8	6.7	7.6	7.1	6.4	3.0	3.9	3.5	3.1	7.5	13.6	10.9	8.3
Phillips	59.3	USD	22.0	5.3	6.1	8.0	7.3	6.4	4.0	5.7	5.2	4.6	10.1	19.9	15.3	11.9
Norsk Hydro	378.5	NKR	11.0	4.2	4.8	4.8	4.9	4.6	4.4	4.0	3.8	3.5	10.4	10.9	9.8	8.7
Amerada Hess	71.9	USD	6.4	3.3	5.0	5.2	5.2	4.7	2.8	3.1	3.2	2.9	6.9	14.2	13.6	12.7
Occidental	27.6	USD	10.3	4.9	5.5	7.4	6.6	6.3	3.8	5.5	4.9	4.7	7.3	22.1	16.1	14.4
Murphy	86.2	USD	3.9	4.5	5.8	7.2	6.1	5.7	5.1	6.4	5.3	4.9	12.7	39.0	24.3	21.7
Imperial Oil	46.0	CAD	11.1	7.8	7.8	11.0	9.5	9.3	8.1	11.4	9.7	9.0	13.6	20.9	16.4	15.3
Petro-Canada	38.3	CAD	6.5	4.5	6.2	6.8	6.1	5.9	6.1	6.5	5.9	5.7	12.2	16.3	14.2	13.4
Shell Canada	52.4	CAD	9.4	6.7	7.4	13.1	9.5	8.1	7.6	13.3	9.8	8.7	11.9	22.3	17.5	15.0
Suncor	54.8	CAD	7.9	11.4	18.6	10.2	9.3	8.2	11.9	8.6	8.1	7.3	30.3	17.7	16.6	15.0
CEPSA	15.0	EUR	3.5	5.4	5.4	6.9	5.5	4.6	4.3	5.5	4.4	3.8	7.5	10.5	8.5	7.4
OMV	98	EUR	2.4	4.7	4.1	4.6	4.7	4.4	2.4	2.8	2.7	2.5	6.0	7.7	8.0	7.6
MOL	5,400	HUF	1.9	7.6	7.8	3.9	3.5	3.1	6.6	2.8	2.6	2.4	0.0	5.2	5.3	4.7
Global integrated average				8.5	9.0	9.7	9.0	8.5	9.2	9.8	9.1	6.7	15.0	18.6	16.8	15.7
Emerging markets																
Perez Companc	2.32	ARS	2.1	8.8	7.3	8.1	7.6	6.7	5.5	4.3	3.6	3.0	9.7	-8.5	5.0	7.9
Petrobras	57.90	BRL	26.8	5.2	6.4	6.8	5.6	5.1	4.7	4.8	3.9	3.4	6.0	6.0	4.8	4.3
Petrochina	1.45	HKD	32.7	n/a	3.5	4.8	4.7	4.5	n/a	3.8	3.7	3.5	n/a	10.7	10.4	9.6
Sasol	11,180	ZAR	6.1	4.6	7.5	5.3	5.4	4.8	6.9	5.2	5.7	5.5	9.0	7.0	7.6	7.3
Sinopec Corp	1.18	HKD	13.1	4.1	4.4	4.1	3.7	3.3	2.5	2.3	2.2	2.0	7.1	7.4	6.2	5.5
PTT E&P	118	THB	1.8	8.3	5.9	6.2	6.7	5.7	6.3	6.8	7.7	7.7	7.1	8.4	9.8	9.6
Tupras	8,900	TRL	1.6	2.9	13.3	5.5	4.7	5.3	7.4	4.7	4.0	4.6	n/m	8.7	6.7	7.9
GEM universe				5.6	6.9	5.8	5.5	5.0	5.5	4.6	4.4	4.3	7.8	5.7	7.2	7.4
Russia, US GAAP																
Lukoil	12.6	USD	10.7	3.0	3.2	5.4	4.5	4.0	2.6	2.9	4.7	4.0	3.2	4.1	8.0	6.3
Surgutneftegaz	0.32	USD	8.8	2.0	1.0	1.9	1.2	0.6	2.8	2.4	3.9	3.3	3.4	3.0	4.9	4.1
Sibneft	1.26	USD	6.0	2.0	1.7	4.3	3.2	2.6	1.6	1.5	4.3	3.2	2.2	2.0	6.3	4.3
Tatneft	0.52	USD	1.2	1.9	1.5	2.2	1.2	0.6	1.2	1.1	1.9	1.4	1.5	1.4	3.5	2.2
Russian average				2.2	1.9	3.4	2.5	2.0	2.0	2.0	3.7	3.0	2.6	2.6	5.7	4.2
Sibneft premium/(discount) to emerging market average				-65%	-76%	-27%	-42%	-48%	-71%	-67%	-2%	-25%	-72%	-64%	-13%	-42%
Sibneft premium/(discount) to integrated average				-77%	-82%	-56%	-65%	-69%	-83%	-85%	-53%	-53%	-86%	-89%	-63%	-73%

Note: Based on historic average market capitalization for past years

Source: UBS Warburg; Brunswick UBS Warburg estimates

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