

YukosSibneft: Russian Oil Comes of Age

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Sibneft	Common:	BUY	\$2.40	Target price	\$3.2
Yukos	Common:	BUY	\$11.18	Target price	\$14.8

Figure 1. Yukos – Statistical Abstract, US GAAP

	Revenues	EBITDA	Net Income	EPS	P/S	EV/ EBITDA	P/CF	P/E	EV/Reserves	EV/ Production
	\$ mln	\$ mln	\$ mln						\$/boe	\$/boe
1999	4,093.6	1,645.5	1,129.4	0.52	5.9	14.6	22.9	21.3	2.06	72.07
2000	9,032.0	4,905.8	3,723.8	1.73	2.7	4.9	7.8	6.5	1.97	64.55
2001	9,461.1	3,904.1	3,156.1	1.46	2.5	6.2	7.7	7.6	1.80	55.22
2002E	11,304.8	4,543.3	3,331.8	1.55	2.1	5.3	7.3	7.2	1.80	46.13
2003E	13,486.3	5,200.8	3,835.5	1.78	1.8	4.6	6.4	6.3	1.80	37.59
52-week range: \$7.70 (03/25/02) - \$11.38 (5/20/02)				Common Shares Outstanding*		2,155.0 mln		Mcap	\$24,092.8 mln	

Note: Excluding 82 mln of shares held in treasury as of September 30, 2002

Sources: Company reports, Alfa-Bank estimates

Figure 2. Sibneft – statistical abstract, US GAAP

	Revenues	EBITDA	Net Income	EPS	P/S	EV/ EBITDA	P/CF	P/E	EV/ Reserves	EV/ Production
	\$ mln	\$ mln	\$ mln						\$/boe	\$/boe
1999	1,746.4	547.1	315.1	0.07	6.5	23.2	30.8	36.1	2.77	100.0
2000	2,397.9	1,027.4	674.8	0.14	4.7	12.4	12.4	16.9	2.74	94.6
2001	3,575.7	1,719.2	1,305.3	0.28	3.2	7.4	8.7	8.7	2.60	78.9
2002E	4,728.1	1,801.8	1,089.4	0.23	2.4	7.1	8.6	10.4	2.60	61.9
2003E	5,675.0	2,077.4	1,134.0	0.24	2.0	6.1	7.7	10.0	2.60	49.4
52-week range: \$1.56 (06/21/02) - \$2.40 (04/22/03)				Common Shares Outstanding		4,741 mln		Mcap	\$11,378.4 mln	

Source: Company reports, Alfa-Bank estimates

Investment Summary

- YukosSibneft would have the largest crude reserves among private oil companies of 18.4 bln bbl
- Estimated weighted average price offered for Sibneft stock is \$2.77 (17% premium to market)
- Prior to the deal Yukos is expected to pay out dividends of up to \$1.3/share, implying 12% yield

World's largest private oil company on crude reserves

World's fourth largest according to current 2.3 mmbpd crude output

Yesterday Yukos and Sibneft jointly announced a planned merger of the two companies into YukosSibneft Oil Company. The new entity would be the world's third-largest company according to crude oil and gas reserves (estimated at 19.4 boe bbl as of the end of 2001, of which 18.4 bln bbl is crude oil and 1 bln boe natural gas) and the fourth-largest based on crude oil production (currently at a level of 2.3 mmbpd this year). All of the deal's details will be worked out shortly, and the transaction is expected to be completed before year's end. In this report we set out the general structure of the deal and evaluate the transaction as well as its impact on the participants.

Deal is structured in three steps

Yukos will buy out 20% of Sibneft stock for \$3 bln cash

The deal is structured to be carried out in a number of steps. The first would involve Yukos buying out 20% of the stock currently in the hands of Sibneft's core shareholders (who are estimated to hold a 92% stake in the company) for \$3 bln. This would imply a valuation of the company's shares at \$3.16, representing a 33% premium to the closing price of the pre-announcement date and right on our \$3.2 target.

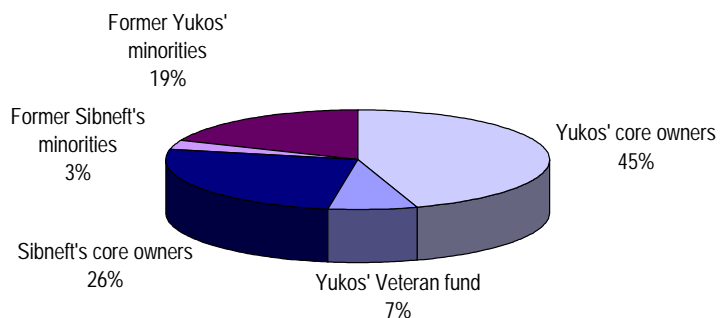
Remaining 80% of Sibneft stock will be exchanged into shares of new entity

The next step would involve an emission of shares by Yukos in order to consolidate the remaining 80% of Sibneft stock into Yukos. Assuming that all of Sibneft's shareholders (including the remaining 8% of minorities) will receive the same treatment as spelled out in the companies' joint press release (i.e. an exchange of each 1% of Sibneft for 0.36125% of the new YukosSibneft entity), Yukos would have to issue 876 mln new shares, assuming that the current number of shares outstanding is the issued 2,237 mln minus the 82 mln treasury shares. This would increase the total number of shares outstanding to 3,031 mln, which would represent the capital of the new joint entity.

Yukos' and Sibneft's core shareholders will own 45% and 26% of the new entity's stock

Step three would involve the exchange of Sibneft's shares for those of Yukos. Assuming that all of Sibneft's shareholders exchange their stock, they would end up with 876 mln shares of the joint company, or 28.9% of its equity capital (of which 26% would be in the hands of core shareholders) while Yukos' shareholders would retain the same number of shares (2,155 mln) with their share in the new entity's stock declining to 71.1% following the new emission (of this amount, 45% will be held by Yukos' core shareholders, 7.4% by Yukos' pension fund "Veteran" and the remaining 18.7% by Yukos' current minority shareholders). However, the breakdown of the new entity's shareholding structure could differ slightly from our estimates, as according to Yukos the company will likely use its cash for share buybacks. After the exchange is completed, Yukos will have 100% of Sibneft's shares on its balance sheet and have been officially transformed into the new entity – YukosSibneft Oil Company.

Figure 3. Proposed Structure of YukosSibneft Oil Company



Sources: Company data, Alfa Bank estimates

Weighted average acquisition price of Sibneft is \$2.77 per share

According to our estimates, the weighted average acquisition price of Sibneft (as implied by the terms spelled out in the joint press release) is \$2.77 per share, or \$13.13 bln for the entire company. This represents a 16.8% premium

to Sibneft's closing price prior to the announcement of the deal. We arrived at this number by taking the \$3.16 per share implied by the buyout price of 20% of Sibneft stock and \$2.67 per share implied by the proposed conversion terms for the remaining 80% of Sibneft stock. It should be noted that we assumed Sibneft's minorities will be able to swap at the same ratio as Sibneft's core shareholders. We also based our calculation on the closing prices of the pre-announcement date (April 21). However, as Sibneft's core shareholders received a cash-and-equity offer from Yukos, we believe that Sibneft's minority shareholders will either be treated in the same fashion or that their equity swap ratio will be more favorable than the one for core shareholders.

Figure 4. Summary of the Deal's Structure

	Sibneft	Yukos	YukosSibneft
Total shares outstanding at present, mln*	4,741	2,155	
Current Mcap**, \$ mln	11,237	23,812	35,048
Sibneft shares to be bought by Yukos:			
Cash sum, \$ mln	3,000		
Stake	20.0%		
Number of shares, mln	948		
Per share valuation, \$	3.16		
Subsequent share exchange:			
Sibneft shares remaining, mln	3,793		
New shares to be issued by Yukos, mln		876	
<i>Implied swap ratio</i>	<i>4.33</i>	<i>for 1</i>	
Total shares in new YukosSibneft Oil Co., mln	876	2,155	3,031
Respective stakes in new entity	28.9%	71.1%	
Implied value of stakes**, \$ mln	10,129	24,919	
Implied per-share valuation, \$	2.67	11.56	
Implied weighted average per share valuation of Sibneft, \$			
	2.77		
Total implied acquisition cost of Sibneft for Yukos, \$ mln		13,129	
Premium to Sibneft's current market valuation**		16.8%	

Note: * Number of Yukos shares is the number of shares outstanding (2,237 mln issued minus 82 mln held in treasury); ** Based on closing prices prior to the announcement date (April 21, 2003)
Sources: Company data, Alfa Bank estimates

Sibneft minorities should receive fair treatment

Sibneft minorities voting against the merger will be allowed to sell their shares. We estimate the fair range of buyout prices at \$2.67-2.77 per share and believe that companies with high corporate governance standards such as Yukos and Sibneft are unlikely to mistreat their minority shareholders.

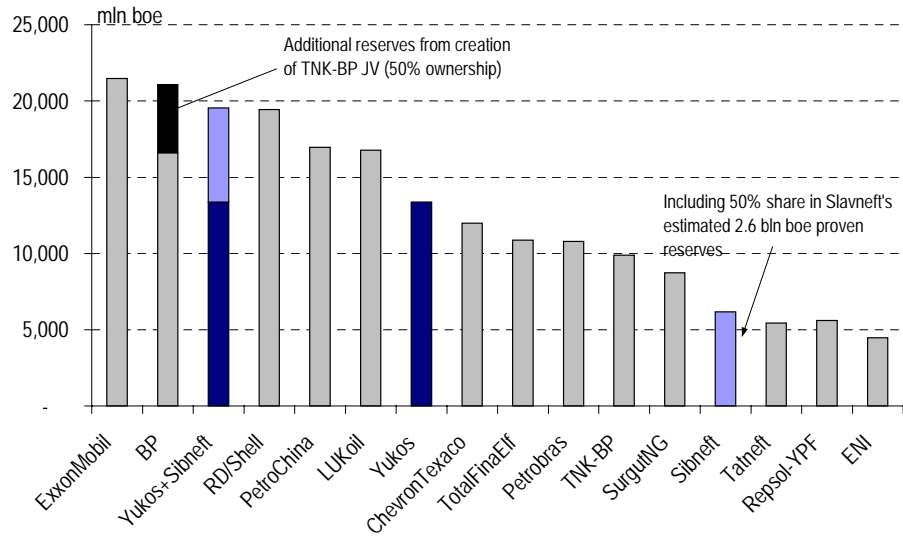
A giant with 19.4 bln boe of oil and gas reserves

World's largest private oil company based on crude reserves

By joining their assets the two companies would create a super oil major with 19.4-19.6 bln of proven oil and gas reserves (depending on the estimates of Slavneft's reserves, which have yet to be audited according to Western standards). This amount would exceed those of Russia's current leader LUKoil by 2.6-2.8 bln boe (or 15.6-16.6%) and rank third among the world's publicly traded companies, behind only ExxonMobil and BP (taking into account the 50% share to be received in the TNK-BP JV). We note that our valuation of Sibneft's reserves takes account of its 50% ownership of Slavneft's assets. The joint company would thus account for over 28% of the country's estimated reserve base. Based solely on crude reserves, YukosSibneft would become the world's largest private oil company.



Figure 5. Proven Oil and Gas Reserves among International Companies, 2001

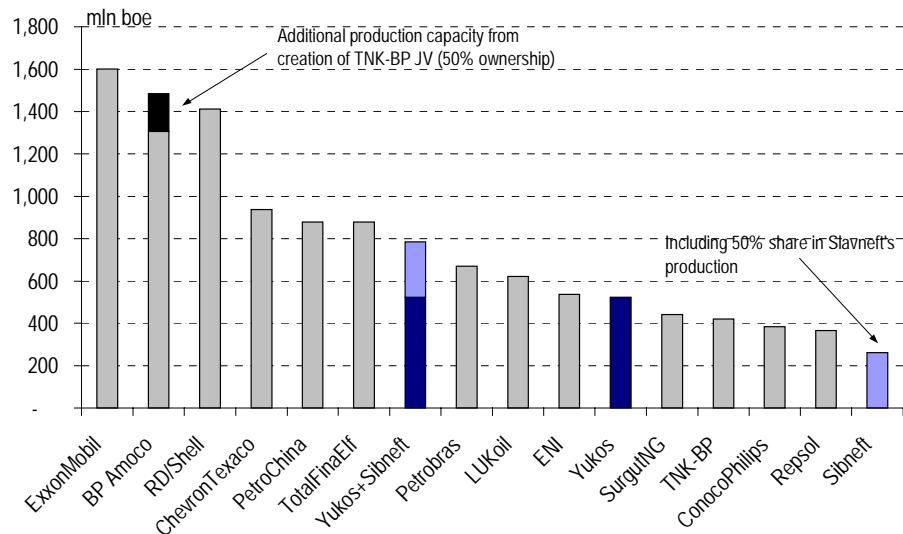


Source: Company data, Alfa Bank estimates

Production of YukosSibneft is expected to reach 2.6 mmbopd in 2003

The estimated production capacity of the new company would be around 900 mln bbl of crude and over 50 mln boe of natural gas (or 2.6 mmbopd in total) based on projected 2003 volumes. Crude production would account for about 30% of the total volume expected to be produced in Russia this year.

Figure 6. Crude Oil and Gas Production among International Companies, 2002



Sources: Company data, Alfa Bank estimates

1.9 mmbpd of refining capacities and over 2,600 gasoline stations

On the downstream side the company would consolidate six fully-owned refineries on Russian territory (Omsk, Angarsk, Achinsk and three facilities in Samara region) and be able to utilize the capacities of Slavneft's refineries (Yaroslavl and Mozyr, which are currently jointly owned by Sibneft and TNK) as well as part of those of Moscow refinery (proportional to Sibneft's 38.5% ownership stake). In addition, the holding would control a refinery abroad – Lithuania's Mazeikiu Nafta, which was consolidated by Yukos last year. This amounts to a total of nearly 100 mln tons (1.9 mmbpd) of joint refining capacity, with an impressive, geographically diversified structure. The

company's retail network would number over 2,600 stations, which would be the largest domestic retail network under any single owner.

The estimated revenues of the consolidated entity could amount to around \$20.8 bln in 2003E, EBITDA \$7.7 bln and net income \$5.2 bln. This does not account for likely synergies from the merger of the two businesses, the inclusion of which should to boost revenue and earnings forecasts even further. Yukos and Sibneft are currently the industry's most efficient producers, with respective lifting costs of \$1.4/bbl and \$1.62/bbl compared to the \$2.5/bbl industry average. By joining their efforts, they can reach even higher levels of operating efficiency.

Synergies will be created

Synergies are based on optimization of refinery load and joint development of Eastern Siberian reserves

We feel that additional value in this merger could be created from the following:

(1) **Economies of scale.** The larger size of the company alone will permit greater access to debt markets as well as opportunities to engage in larger scale projects than otherwise would have been possible. In addition, the large capitalization of the new company (currently estimated at over \$35 bln) would make it one of the world's ten largest traded oil and gas stocks. This implies a better chance that it will be included in global portfolios.

(2) **Protection from possible competition** in the form of a new international super major entering the Russian market.

(3) **Synergy effects.** Synergies could lie in optimizing the utilization of downstream assets. For example, Yukos could provide crude to the underloaded Yaroslavl and Mozyr refineries. In addition, the companies will be able to jointly develop their Eastern Siberian reserves: Yukos holds a dominant position through reserves at its Tomskneft subsidiary and a stake in Eastern Siberian Oil Company, while Sibneft is likely to receive licenses from Slavneft's subsidiary Krasnoyarskneftegaz.

As for Yukos' shareholders, we feel the offered 16.8% premium to Sibneft's April 21 closing price is quite reasonable. The positive effects of consolidation via further cost-cutting and optimization of refining capacity utilization should justify this premium. Moreover, given Yukos' intention to raise its Debt-to-Equity ratio to a moderate level from the currently low 6%, we expect good dividends on Yukos stock prior to completion of the merger. Assuming that Yukos can raise its debt to a level corresponding to a D/E ratio of 25% (or the Russian average), we estimate that Yukos would have close to \$5.9 bln in cash and equivalents. Of this amount, \$3 bln would be paid for 20% of Sibneft while the remainder of up to \$2.9 bln would be left for dividend payments. Thus, our valuation implies a potential dividend of up to \$1.3 per Yukos share, or about a 12% dividend yield.

Sale to an international major is unlikely

Taking into account the large size of the newly created entity, it would be hard to imagine Russia's authorities allowing the sale of a blocking, let alone a controlling, stake to an international strategic investor. However, considering the reasonable premium that Sibneft's shareholders would receive for their stake, there is no guarantee they would have gotten a better deal from an international oil and gas major.

YukosSibneft trades at discounts to EMs and international oil majors

Looking at the new super oil major's multiples, we see that the company still trades at discounts to international oil majors and emerging market companies based on both financial and operating multiples. The company's 2003E EV/EBITDA of 4.8 represents a 28.7% discount to Super Majors and a 6.1% discount to EMs. We again stress that the new company's projected financials do not include synergy effects, the inclusion of which would make the company even cheaper compared to internationals. Moreover, YukosSibneft's

discounts based on EV/Reserves and EV/Production are even more substantial, ranging from 39-80%.

Figure 7. Financial and Operating Multiples

	P/E		P/CF		EV/EBITDA		EV/2002 Production	EV/2001 Reserves
	2002E	2003E	2002E	2003E	2002E	2003E	\$/boe	\$/boe
Russian Companies								
YukosSibneft		6.8		6.4		4.8	47.0	1.9
LUKoil	7.0	4.8	4.6	3.5	4.2	4.1	25.1	0.9
Surgutneftegaz (without treasury)	5.5	5.8	3.6	3.4	4.1	4.1	23.1	1.2
Surgutneftegaz (with treasury)	10.3	10.8	6.7	6.4	6.2	6.2	35.3	1.8
Yukos	7.2	6.3	7.3	6.4	5.3	4.6	46.1	1.8
Tatneft	3.2	3.7	2.2	2.5	2.4	2.5	14.2	0.5
Sibneft	10.4	10.0	8.6	7.7	7.1	6.1	61.9	2.6
Sibneft + 50% of Slavneft		8.4		6.4		5.1	48.6	2.1
International Companies								
BP Amoco	21.1	17.5	8.9	7.9	9.5	7.3	138.1	10.9
Exxon Mobil	21.0	16.6	11.2	10.3	10.3	8.6	150.1	11.2
ChevronTexaco	15.5	11.9	7.0	6.0	6.8	5.4	87.6	6.8
TotalFina Elf	14.2	11.9	7.7	6.8	5.9	5.6	117.9	9.5
Emerging Markets								
Sinopec (China)	8.7	7.4	3.0	2.7	7.5	6.8	160.6	12.8
Perez Companc (Argentina)	(3.9)	17.5	8.8	4.1	5.5	7.4	60.8	3.9
Petrobras (Brasil)	7.0	3.6	4.5	2.3	5.3	2.9	36.3	2.3
PetroChina (China)	6.2	6.5	3.4	3.6	3.4	3.4	51.5	2.7
<i>International company average</i>	<i>17.9</i>	<i>14.5</i>	<i>8.7</i>	<i>7.8</i>	<i>8.1</i>	<i>6.7</i>	<i>123.5</i>	<i>9.6</i>
<i>Emerging markets average</i>	<i>7.3</i>	<i>8.7</i>	<i>4.9</i>	<i>3.2</i>	<i>5.4</i>	<i>5.1</i>	<i>77.3</i>	<i>5.4</i>

Note: multiples are based on April 22, 2003 closing prices

Source: I/B/E/S, Company data, Alfa Bank estimates

To summarize, we expect Sibneft shares to appreciate to a level of \$2.7 until the two companies announce the swap conditions for minority shareholders of Sibneft. Thereafter, the shares will be converted into Yukos stock, which also has good upside potential. We currently expect dividends and share buybacks from Yukos, which should boost the company's valuation in the short term. Prior to the deal, we set a target price for Yukos at \$14.8 per share, which implies 32% upside from yesterday's closing price. As a result of the merger, we expect an even greater upside for YukosSibneft given the deal's economies of scale and synergy effects.

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