

## Russian Oil Sector

# Sibneft and Transneft Upgraded to BUY

<b>SIBN</b>	<b>Buy</b>
Current Price	\$2.75
Fair Value	\$3.34
Upside	21%
Market Cap	\$13,039 mln
Average Daily Turnover	\$5 mln

<b>TRNFP</b>	<b>Buy</b>
Current Price	\$765
Fair Value	\$950
Upside	24%
Market Cap	\$4,755 mln
Average Daily Turnover	\$2 mln

*We are upgrading our recommendation on Sibneft from HOLD to BUY as the stock now has upside of 21% to our DCF fair value of \$3.34 per share. Unlike for YUKOS, we continue to use discounted free cashflow methodology to value Sibneft. While we are not trying to second guess what will happen with YUKOS' stake in the company, the shares are attractive from a fundamental point of view and minority Sibneft shareholders do seem to be protected from the "YUKOS risks".*

*We are also upgrading our recommendation on Transneft preferred shares from HOLD to BUY on price weakness; this stock now has upside of 24% to our fair value estimate, which remains unchanged at \$950 per share. We assume that it continues to trade cum-dividend, although there is no absolute clarity on this. The board will not meet until end May to determine an ex-dividend date; to judge from last year, it should be around May 20. We expect Transneft to pay \$36 per share to minority shareholders based on the company's 2003 RAS non-consolidated net profits of \$516 mln. At current prices, this translates into a healthy dividend yield of 4.7%.*

### Sibneft

Since Sibneft decoupled from YUKOS in mid December, it has underperformed LUKoil (by 29%) and Surgutneftegaz (by 14%), Russia's two other oil blue chips not burdened by tax allegations.

We believe that Sibneft minority shareholders are reasonably well shielded from the "YUKOS risks". Our DCF model points to a value for Sibneft of around \$16.1 bln, or \$3.37 per share. Moreover, the stock is currently trading at a 24% discount to LUKoil on 2004 EV/EBITDA and 53% discount on EV/FCF, despite the fact that Sibneft is expected to generate 1.65 times the EBITDA and 2.5 times the free cashflow of LUKoil per barrel of output. Sibneft's free cashflow yield presently stands at 15%, with an implied equity risk premium of 7%, against LUKoil's -1% and Surgutneftegaz' 6%. This premium looks rather high for a company that is not expected to deliver major earnings disappointments.

We fully recognize, however, that the company is not problem-free.

- The Tax Ministry has made mention of unspecified Sibneft tax liabilities, although these have yet to take substance as official claims.

- Sibneft's current management and board are unlikely to award dividends while the controlling stake rests in YUKOS' hands, increasing the corporate governance risks.
- Should YUKOS be allowed (or indeed forced) to sell 20% of Sibneft on the open market, price performance would suffer.

### **Transneft**

We expect Transneft to post yet another strong set of results for 2004, with IAS net profits of \$1.3 bln, up 32% y-o-y, and a top line of \$4.17 bln, up 22% on the back of strong 7.3% growth in throughput volumes to 446 mln tons. In addition, tariffs should grow by 14% this year in dollar terms (9% in ruble terms). However, uncertainties remain over 2004 dividends: according to the company, non-consolidated net profits are likely to be down by as much as 75% y-o-y, suggesting a similar fate for payouts to shareholders.

We continue to believe that Transneft combines the best of two worlds: value and growth. On an earnings basis, it remains the cheapest stock in our first-tier oil and gas universe, trading at a 2004 EV/EBITDA of 2. At the same time, the growth story is reflected in its sales trend: the top line is expected to grow over 2003-08 by a CAGR of around 11%, a function of the expansion in throughput volumes and supportive tariff environment.

## Appendix 1. Sibneft

### Key data

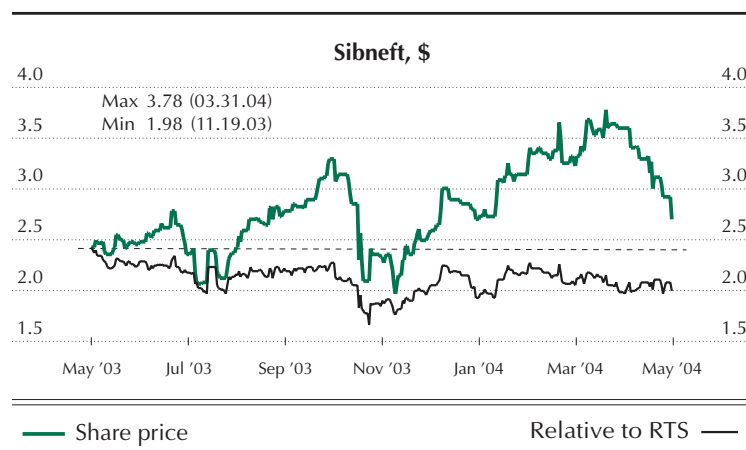
	2002	2003	2004E	2005F
<b>FINANCIALS, \$ mln</b>				
Sales	4,777	6,669	8,436	8,673
EBITDA	1,763	2,559	3,702	3,715
EBIT	1,353	2,069	3,166	3,136
Net profits	1,121	2,274	2,425	2,446
EPS, \$	0.24	0.48	0.51	0.52
Dividend payout	92%	49%	40%	37%
<b>MARGINS</b>				
EBITDA margin	37%	38%	44%	43%
EBIT margin	28%	31%	38%	36%
Net margin	23%	34%	29%	28%
<b>PRICE RATIOS</b>				
P/S	2.7	2.0	1.5	1.5
EV/EBITDA	8.4	5.8	4.0	4.0
P/E	11.6	5.7	5.4	5.3
P/CF	9.9	5.7	4.1	4.0

### Shared issued

Common	4,741,299,639
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### Share price performance and relative

	1 mo	3 mo	6 mo	1 yr
Price performance	-25.0%	-20.6%	18.9%	11.3%
Relative to RTS	-0.4%	-12.6%	5.5%	-26.5%



Source: Datastream

### Average Daily Turnover (ADT)

ADT, 30 days, \$ '000	5,214
ADT, 100 days, \$ '000	8,238
MCap/ADT, days	2,955

**Balance sheet (US GAAP), \$ mln**

	2002	2003E	2004E	2005F
Fixed assets and investments	5,169	6,350	6,819	7,232
Current assets	2,380	2,865	3,917	4,904
Stock and inventories	322	338	395	333
Accounts receivable	1,357	1,802	1,781	1,720
Cash and securities	621	644	1,662	2,771
Other current assets	80	80	80	80
<b>Total assets</b>	<b>7,548</b>	<b>9,214</b>	<b>10,736</b>	<b>12,137</b>
Current liabilities	1,441	1,888	1,798	1,750
Accounts payable	840	1,111	1,167	1,115
Short-term debt	579	755	609	613
Other current liabilities	22	22	22	22
Long-term liabilities	1,816	1,945	2,101	2,083
Long-term debt	1,658	1,787	1,944	1,925
Other long-term liabilities	157	157	157	157
Total liabilities	3,257	3,833	3,899	3,833
Equity	4,292	5,382	6,837	8,304
Share capital	861	861	861	861
Retained earnings	3,431	4,521	5,976	7,444
<b>Total liabilities and equity</b>	<b>7,548</b>	<b>9,214</b>	<b>10,736</b>	<b>12,137</b>

Source: Sibneft, Troika Dialog estimates

**Income statement (US GAAP), \$ mln**

	2002	2003E	2004E	2005F
Sales	4,777	6,669	8,436	8,673
Operating costs	3,424	4,599	5,270	5,537
EBIT	1,353	2,069	3,166	3,136
Depreciation	410	489	537	579
EBITDA	1,763	2,559	3,702	3,715
Net interest expenses	(115)	(141)	(154)	(129)
FX gain (loss)	4	(11)	(6)	9
Net other expenses	33	759	185	203
EBT	1,274	2,675	3,190	3,219
Tax	(163)	(401)	(766)	(773)
Profits before minority interest	1,111	2,274	2,425	2,446
Minority interest	10	–	–	–
<b>Net profits</b>	<b>1,121</b>	<b>2,274</b>	<b>2,425</b>	<b>2,446</b>

Source: Sibneft, Troika Dialog estimates

**Cashflow statement, \$ mln**

	2002	2003E	2004E	2005F
<b>EBITDA</b>	<b>1,763</b>	<b>2,559</b>	<b>3,702</b>	<b>3,715</b>
Provisions and non-cash items	73	(46)	(581)	(530)
Taxes	(174)	–	–	–
(Increase)/decrease in working capital	(295)	(187)	24	69
Increase in other assets	(46)	(23)	8	(14)
<b>Operating cashflow</b>	<b>1,322</b>	<b>2,303</b>	<b>3,153</b>	<b>3,241</b>
Capital expenditures	(959)	(1,006)	(1,027)	(1,030)
Other investments	27	(219)	34	50
<b>Free cashflow</b>	<b>390</b>	<b>1,079</b>	<b>2,160</b>	<b>2,261</b>
Increase/(decrease) in debt	1,314	250	–	–
Interest paid	(75)	(122)	(172)	(173)
Dividends	(1,098)	(1,184)	(970)	(979)
<b>Net cashflow</b>	<b>530</b>	<b>23</b>	<b>1,018</b>	<b>1,109</b>
<b>Change in cash position</b>	<b>530</b>	<b>23</b>	<b>1,018</b>	<b>1,109</b>

Source: Sibneft, Troika Dialog estimates

## Appendix 2. Transneft

### Key data

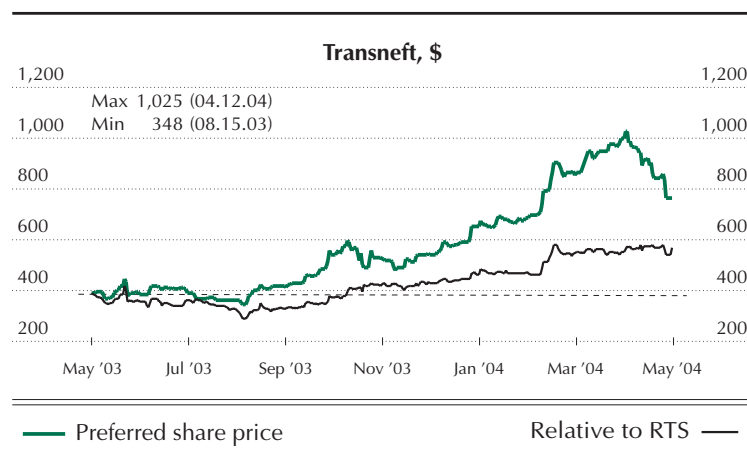
	2002	2003	2004E	2005F
<b>FINANCIALS, \$ mln</b>				
Sales	2,905	3,730	4,542	4,947
EBITDA	1,608	2,062	2,441	2,605
EBIT	1,203	1,566	1,886	1,984
Net profits	827	993	1,307	1,375
EPS, \$	133.0	159.6	210.1	221.2
Dividend payout	10.4%	11.5%	10.0%	10.0%
<b>MARGINS</b>				
EBITDA margin	55%	55%	54%	53%
EBIT margin	41%	42%	42%	40%
Net margin	28%	27%	29%	28%
<b>PRICE RATIOS</b>				
P/S	1.6	1.3	1.0	1.0
EV/EBITDA	3.0	2.4	2.0	1.9
P/E	5.7	4.8	3.6	3.5
P/CF	3.9	3.3	2.5	2.2

### Shared issued

Total	6,219,502
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### Share price performance and relative

	1 mo	3 mo	6 mo	1 yr
Price performance	-22.1%	14.7%	53.8%	104.1%
Relative to RTS	2.4%	22.7%	40.3%	66.2%



Source: Datastream

### Average Daily Turnover (ADT)

ADT, 30 days, \$ '000	1,959
ADT, 100 days, \$ '000	2,301
MCap/ADT, days	2,849

**Balance sheet (IAS), \$ mln**

	2002	2003E	2004E	2005F
Fixed assets and investments	7,145	8,611	9,732	10,572
Current assets	1,205	1,444	2,028	2,739
Stock and inventories	190	253	324	364
Accounts receivable	569	775	934	981
Cash and securities	424	394	747	1,372
Other current assets	22	22	22	22
<b>Total assets</b>	<b>8,350</b>	<b>10,055</b>	<b>11,759</b>	<b>13,311</b>
Current liabilities	669	784	997	1,101
Accounts payable	387	502	629	679
Short-term debt	283	282	368	422
Long-term liabilities	1,083	1,757	2,062	2,254
Long-term debt	110	810	1,146	1,370
Other long-term liabilities	973	947	917	884
Total liabilities	1,752	2,541	3,059	3,355
Interest of minorities	270	295	324	354
Equity	6,328	7,219	8,376	9,601
Share capital	10	10	10	10
Retained earnings	6,319	7,209	8,366	9,592
<b>Total liabilities and equity</b>	<b>8,350</b>	<b>10,055</b>	<b>11,759</b>	<b>13,311</b>

Source: Transneft, Troika Dialog estimates

**Income statement (IAS), \$ mln**

	2002	2003E	2004E	2005F
Sales	2,905	3,730	4,542	4,947
Operating costs	1,702	2,164	2,656	2,963
EBIT	1,203	1,566	1,886	1,984
Depreciation	404	497	555	621
EBITDA	1,608	2,062	2,441	2,605
Net interest expenses	(82)	(78)	(129)	(151)
FX gain (loss)	(3)	–	(8)	2
Monetary gain (loss)	(19)	–	–	0
EBT	1,110	1,497	1,758	1,850
Tax	(264)	(479)	(422)	(444)
Profits before minority interest	846	1,018	1,336	1,406
Minority interest	(18)	(25)	(29)	(31)
<b>Net profits</b>	<b>827</b>	<b>993</b>	<b>1,307</b>	<b>1,375</b>

Source: Transneft, Troika Dialog estimates

**Cashflow statement, \$ mln**

	2002	2003E	2004E	2005F
<b>EBITDA</b>	<b>1,608</b>	<b>2,062</b>	<b>2,441</b>	<b>2,605</b>
Provisions and non-cash items	96	34	34	41
Taxes	(287)	(505)	(452)	(476)
(Increase)/decrease in working capital	(203)	(153)	(104)	(36)
Increase in other assets	(6)	–	–	–
<b>Operating cashflow</b>	<b>1,208</b>	<b>1,439</b>	<b>1,918</b>	<b>2,133</b>
Capital expenditures	(835)	(1,988)	(1,700)	(1,487)
Other investments	4	–	–	–
<b>Free cashflow</b>	<b>378</b>	<b>(549)</b>	<b>218</b>	<b>647</b>
Increase/(decrease) in debt	48	680	398	314
Interest paid	(76)	(78)	(129)	(151)
Dividends	(70)	(102)	(150)	(150)
<b>Net cashflow</b>	<b>280</b>	<b>(50)</b>	<b>336</b>	<b>659</b>
FX and monetary effects on cash	(35)	20	16	(34)
<b>Change in cash position</b>	<b>245</b>	<b>(30)</b>	<b>353</b>	<b>625</b>

Source: Transneft, Troika Dialog estimates

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