



CONCORDE CAPITAL

# Ukraine/ Oil & Gas Concern Galnaftogaz

Rising Oil Retailer

**BUY**

05 Mar 2005

USD 0.0081

12m Target

USD 0.0105

**Andriy Gostik**  
+380 44 206 8370  
ag@con-cap.com

#### Market Information

PFTS GLNG

No of Shares, mn\* 16,000

\*13,000 mn shares are currently registered. The subscription for an additional 3,000 mn share issue has been completed and will be registered by the Ukrainian SEC shortly.

Market price, USD 0.008125

MCap, USD mn 130.0

Free Float, % 24.2%

#### Stock Ownership\*\*

Financial & Investment Energy Holding and related companies	70.7%
Mr Antonov & Mrs. Antonov	5.1%
Other	24.2%

\*\*Ownership structure as of Oct 18, 2004

#### Ratios 2004E

EBITDA Margin	3.9%
EBIT Margin	2.6%
Net Margin	1.2%
Net Debt/Equity	0.58

Ukraine's largest independent oil product distributor, Galnaftogaz, derives its value from diversification into non-oil products and services, exemplary corporate governance and cooperation with international finance institutions. The company is run by a western-minded management team and has embarked on a strategy to create a chain of European-style service-stations. We believe the company's operations are set for success. Our 12-month target price at USD 0.0105, providing a 29% upside. BUY

Galnaftogaz is the first Ukrainian oil products retailer to recognize **benefits of diversification** into non-oil products and services. Unlike other oil product distributing chains in Ukraine, Galnaftogaz focuses on providing full range of non-oil goods and services. Its stations are positioned as 'service stations'. This **strategy will allow the company to both secure a market niche of well-off customers as well as to mitigate the risk of 'price scissors'** stemming from the absence of in-house refining capacities.

**Independence from major business groups** coupled with western management style ensure the company's enhanced transparency and corporate governance. **The company has adopted a corporate governance code, conducts international audits of its financials** (using Ernst & Young) and has loan agreements with EBRD and Black Sea Trade & Development Bank (Greece).

The company's domain is western Ukrainian oblasts. Being a **regional market leader**, Galnaftogaz is aggressive in its expansion in Ukraine's eastern and central oblasts. The company's **OKKO brand is well-recognized** for both fuel and services quality.

#### KEY FINANCIAL DATA, USD mn

	Net Revenue	EBITDA	Net Income	DPS, USD
2003	176.7	3.1	2.1	0.000
2004E	244.3	9.4	3.0	0.000
2005F	279.3	20.9	10.4	0.000
Spot Exch Rate		5.30		

#### KEY RATIOS

	P/S	P/E	EV/EBITDA	Div Yield
2003	0.74	62.53	47.55	0.0%
2004E	0.53	43.80	16.48	0.0%
2005E	0.47	12.51	7.93	0.0%

## Highlights

- The only public retail and wholesale oil product distributor in Ukraine
- Operates a network of 164 gas stations, making it the Ukraine's fourth largest gas retailer chain
- Ninety-seven of the company's gas stations bear the brand name, OKKO, well-known in Ukraine
- With a 6% share of the Ukrainian oil product market, ranks sixth in terms of volume sold
- The company will spend USD 130 mn on the expansion of its retail network by 148 additional gas stations in 2005-2008
- Plans to capture 8-11% of the Ukrainian oil product market in 2008
- By 2014, its retail network will expand more than two times
- A pioneer in the Ukrainian oil product retail market, focusing on high quality service gas stations with a range of non-oil products and services
- Reduced dependency on Ukrainian refineries through supply diversification. Oil products are purchased from Mazeikiu Nafta (Lithuania), Samara refinery (Russia) and Mozyr refinery (Belarus) in addition to Ukrainian refineries Ukrtatnafta, LiNOS, Galychyna and Kherson
- Superb credit history, with focus on loans from international institutions such as the EBRD, IFC, Black Sea Trade & Development Bank and Raiffeisenbank
- The company's public debt is among Ukraine's most liquid corporate bonds
- In 2005, the EBRD and IFC expected to become Galnaftogaz' minority shareholders, purchasing a 15% stake

Galnaftogaz will post an increase in its 2004 audited consolidated net sales of 37.9% to USD 244.2 mn, according to management estimates. The company's adjusted EBITDA will be USD 9.4 mn, or three times more than in 2003. Galnaftogaz is expected to report a net income of USD 3.0 mn for 2004, a 42.9% yoy increase.

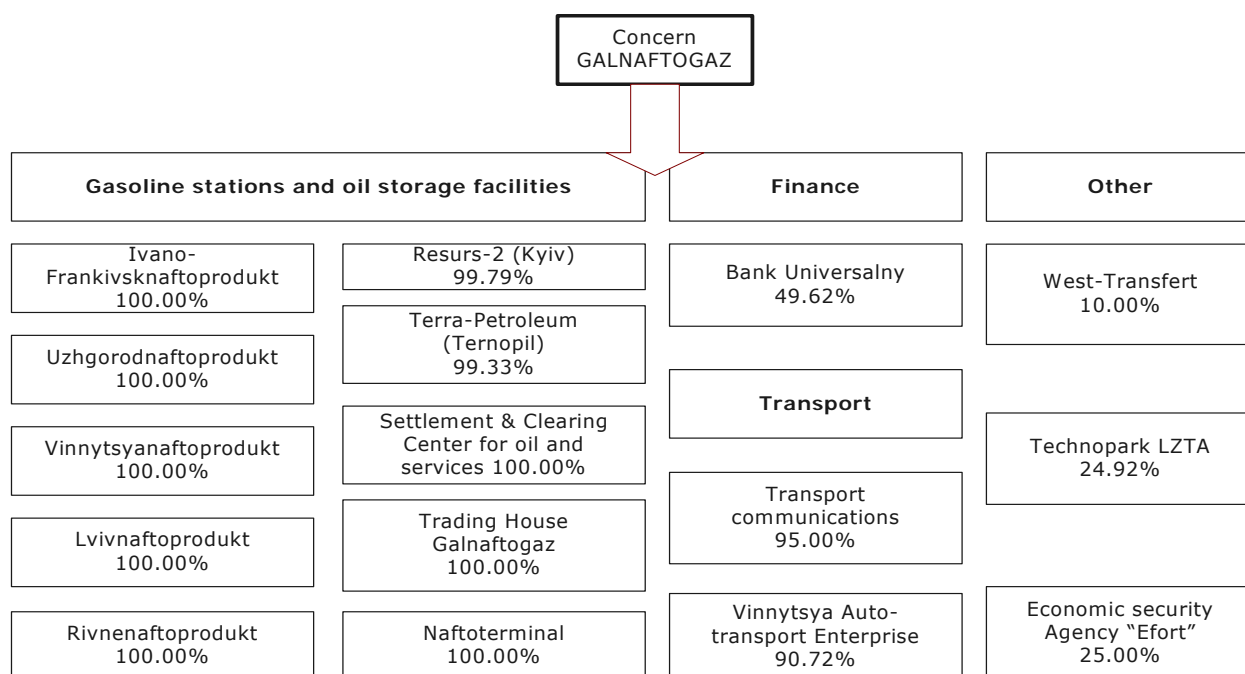
## Retail Oil Gem

**Ukraine's largest independent oil products retailer...**

Concern Galnaftogaz is Ukraine's largest independent retail oil products trader - it is not related to any of the Ukraine's major business groups or Russian oil majors who control Ukrainian refineries. The company's distance from Ukrainian/Russian tycoons encourages Galnaftogaz to increase its competitive advantages through business transparency, high corporate governance standards and cooperation with international finance institutions. The company has adopted a corporate governance code, conducts international audits of its financials (using Ernst & Young) and has loan agreements with EBRD and Black Sea Trade & Development Bank (Greece).

Concern Galnaftogaz incorporates seven regional oil products traders in western and central Ukraine (Lviv, Zakarpattia, Ivano-Frankivsk, Ternopil, Vinnytsia, Rivne and Kyiv), a trading house and a number of non-core businesses.

**Chart 1. Company Structure**

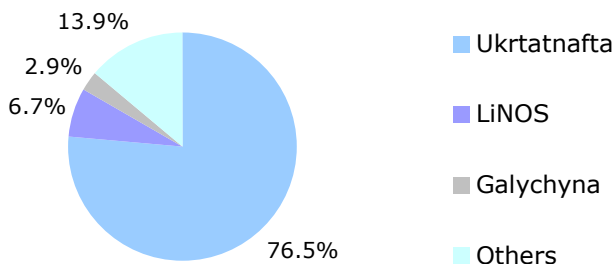


Source: Company Data

**The company enjoys a diversified feedstock supply**

Galnaftogaz' consolidated sales consist mostly of sales by its retail subsidiaries, while its parent company receives revenues from rent payments, trademark fees and wholesale oil product sales. The main suppliers of oil products to Galnaftogaz are Ukratnafta, LiNOS and Galychyna. In addition, Galnaftogaz buys oil products from Mazeikiu Nafta (Lithuania), Kherson refinery, Samara refinery (Russia) and Mozyr refinery (Belarus). The products are transported to the company's facilities by rail.

**Chart 2. Supplier Structure In 2004**



Source: Company Data

**Galnaftogaz owns a network of 164 gas stations**

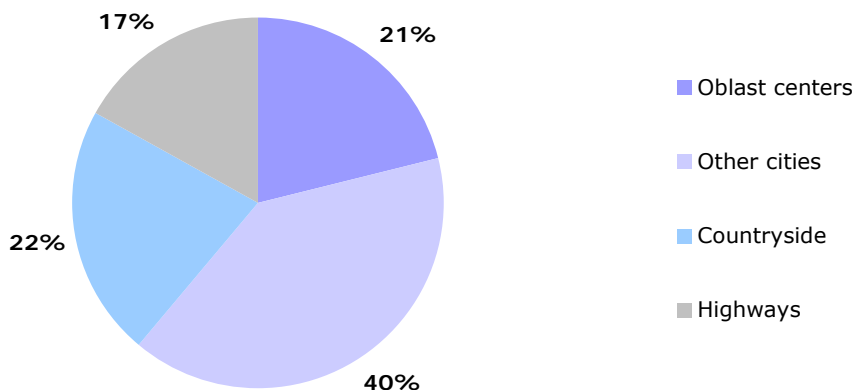
Galnaftogaz' retail network as of March 3, 2005 encompassed 164 gas stations, of which 97 stations bore the brand 'OKKO,' well recognized in western and central oblasts of Ukraine. Four stations were temporarily idling. The network's total retail capacity is estimated at over 730 ths mt annually. Also, in the company's possession are 15 tank storages, and two tank storage units under lease. Their total capacity is 196 ths cm. The availability of in-house tank storage allows Galnaftogaz to significantly save on transportation costs and enables continuous operation of its gas stations. Tank storages are also used to sell oil products in bulk to smaller retailers and agricultural companies. Galnaftogaz' transport fleet comprises 108 gasoline road tankers, 178 cars and 152 trucks. The company's employs over two ths people.

## Industry Background

About 6 ths gas stations operate in the Ukrainian market

The annual capacity of Ukraine's oil product market is 9.5 mn mt. As of April 1, 2004, Ukraine's gas stations network consisted of 5,948 stations. Their distribution by location was as follows:

**Chart 3. Distribution of Gas Stations by Location, 04.01.2004**



Source: Interfax

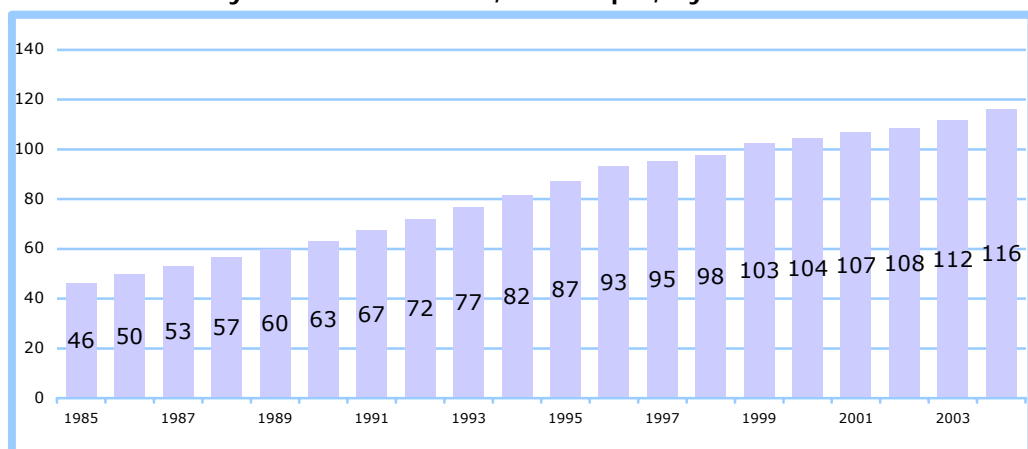
Ukraine's retail oil product market is characterized by a large number of low-yield gas stations

Ukrainian retail gas station sales in 1Q04 totaled USD 600.4 mn, including non-oil product sales (State Statistics Committee). While the estimated annual average sales per gas station amounted to USD 0.4 mn, we found that approximately 48% of all gas stations have sales of less than USD 0.1 mn (sales were below USD 19 ths in 1Q04). At the same time, 20 gas stations in 1Q04 had sales of USD 0.56–1.3 mn (USD 2.2–5.3 mn per year). Thus, in the Ukrainian market a small number of gas stations account for a major portion of sales, while a large number of gas stations generate low revenues. This suggests that the market will undergo further consolidation and only brand-name gas stations will thrive.

Demand for oil products is set to grow in Ukraine

This notwithstanding, we believe that the official data underestimates real revenues. Further, we forecast that the average annual sales per gas station will grow to at least USD 1.0 mn in the medium term, as inefficient gas stations will be closed and demand for automobiles will grow as a result of economic progression and a growing middle class.

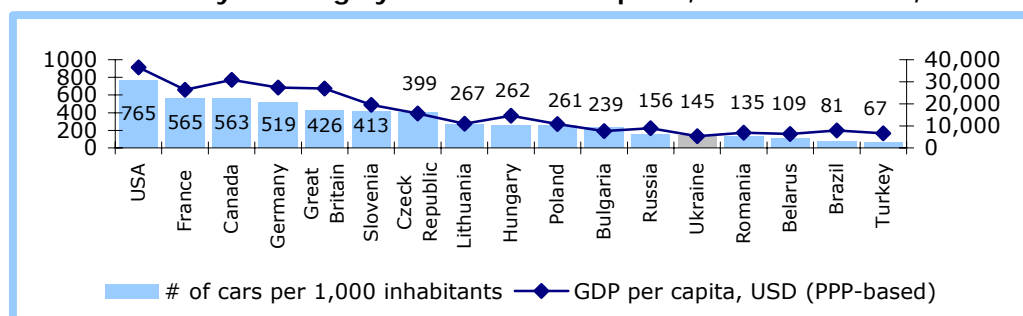
**Chart 4. Privately Owned Cars Per 1,000 People, Dynamics**



Source: State Statistics Committee; Ukrstatsbank

Ukraine is at the low end of country rankings for number of cars per 1,000 inhabitants:

**Chart 5. Country Ranking by Number of Cars per 1,000 Inhabitants, 2003**

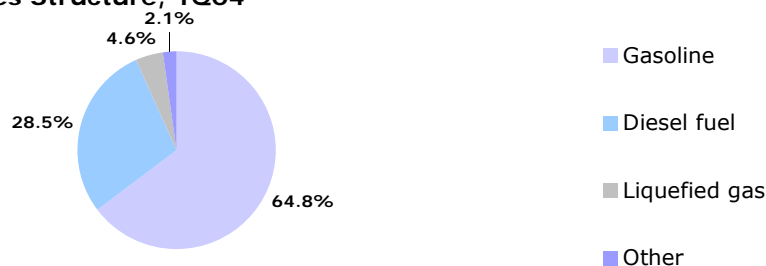


Source: RBK; IMF; Ukrstatsbank

98% of revenues from gas stations in Ukraine are generated by retail oil products

As the chart below indicates, sales of automotive fuel account for 98% of total sales by Ukraine's gas stations in 1Q04. This structure is different from that found in developed countries, where a significant portion of gas station revenue comes from non-oil products (e.g. consumer goods, services, restaurants, car washes, etc). Based on official quarterly data, we estimate current market capacity at over USD 2.5 bn p.a. and expect increasing demand for both oil and non-oil products due to rising household incomes.

**Chart 6. Retail Sales Structure, 1Q04**



Source: Interfax

Russian majors and Privat group dominate the retail market for oil products

The major players in the Ukrainian retail market are TNK-BP, Lukoil, Alliance group, Privat group (including Ukrnafta), Kontinium, Naftogaz, Ukratnafta and Galnaftogaz. All of them, except for Galnaftogaz, own Ukrainian refining capacities, thereby creating VIOCs. Light oil products in Ukraine are produced by six oil refineries and one gas condensate processing plant, with a total capacity of 390.7 mn bbls p.a.

**Table 1. Ukraine's Refining Capacities**

Crude oil	Key shareholders	Nameplate capacity, mn bbls/yr	Share in Ukraine's condensate capacities, %	Oil refined 2003, mn bbls	Capacity utilization level, 2003
Ukratnafta	Naftogaz(43%); Tatarstan (56%)	136.3	34.9%	48.6	35.6%
LiNOS	TNK-BP (78%+)	117.3	30.0%	45.5	38.8%
Kherson Refinery	Alliance Group (28%); Kazakhoil (20%)	52.0	13.3%	14.5	27.8%
Odesa Refinery	Lukoil (93%)	28.6	7.3%	20.8	72.6%
Galychyna refinery*	SPFU(25%); Privat (33%); Kontinium (40%)	31.5	8.1%	15.1	48.0%
Naftokhimyk Prykarpattya refinery	Privat (70%+); SPFU (26%)	19.1	4.9%	15.1	79.5%
<b>Gas condensate &amp; oil</b>					
Shebelynka GPP	Naftogaz (100%)	5.9	1.5%	5.6	95.6%
<b>Total</b>		<b>390.7</b>	<b>100%</b>	<b>165.2</b>	<b>42.3%</b>

\*SPFU stands for the State Property Fund of Ukraine

Most of Ukraine's refineries are owned/controlled by Russian oil majors (Ukratnafta, LiNOS, Kherson refinery, Odesa refinery) who feed them with Russian oil. Kazakh oil is supplied predominantly to the Kherson refinery. Overall, 90% of crude oil supplied to Ukrainian refineries is imported.

**Wide-spread franchising creates competition among brands while disguising the real owners**

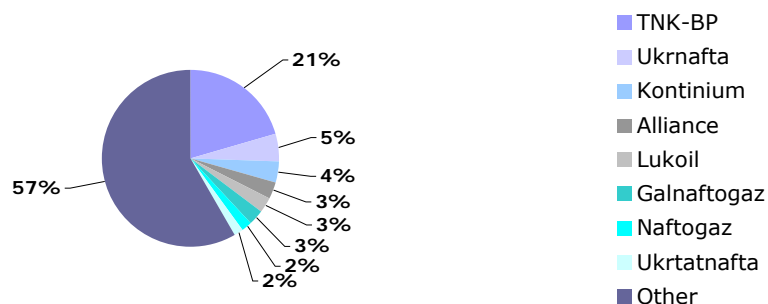
A common practice among Ukrainian oil product retailers is to operate under jobbing, or franchising agreements. Of the 1,220 gas stations in TNK-BP's network, only 40 stations are actually owned by TNK-BP. Among its jobbers are Sentoza, Avias and Alfa-Nafta (all three are associated with Privat bank), who have since sold a portion of their network to Ukrnafta. Currently, apart from Ukrnafta's 295 gas stations, Privat owns a network of over 400 gas stations, most of which operate under TNK-BP's brand.

**In western Ukraine, Galnaftogaz is a leading gas retailing chain**

Ukrainian Kontinium retails oil products from the Galychyna refinery through a network of roughly 240 outlets. Russian Alliance group operates around 170 gas stations. Lukoil's gas station network shrank from almost 200 (beginning 2004) to the current 170, as the company divested gas stations with low sales (below 10 cm per day). By 2007, Lukoil is planning to expand its network by 77%, to 300 stations. State-owned Naftogaz operates 127 gas stations that sell the products of Shebelinka GPP. Ukrtatnafta has jobbing agreements with 80-100 gas stations.

Galnaftogaz' network of 164 gas stations makes it a regional market leader. Galnaftogaz accounts for 3% of gas stations in Ukraine, enjoying a market share of around 6% in terms of sales. The company ranks fourth in Ukraine by number of gas stations and sixth in terms of overall stations, including stations operating under jobbing agreements.

**Chart 7. Retail Market Breakdown by Number of Gas Stations, 2004**



Source: Ukrainian News; RBK; Investgazeta; Dilova Stolytsia; Company Data

**Consolidation around strong brand names will shape the future**

While it seems there is a low concentration of gas stations on the market, (with 57% of gas stations controlled by minor players, "other") we believe the actual concentration is much higher, as many non-brand-name gas stations are associated with major Ukrainian business groups. We expect further consolidation of the market around the most well-known brand names. Competition in the market will also increase, as several players already declared their plans for network expansion in 2005 (e.g., Lukoil to 300 stations mostly by construction, and Ukrnafta will grow to 800 stations through acquisitions).

**The market is large enough to house independent retailers as well as VIOCs**

Ukrainian oil products market has enough room for both retailers associated with VIOCs and independent operators. By estimates of oil consulting company UPECO, 60% of all oil products produced at Ukrainian refineries are available for independent retailers who do not have access to refining capacities. Specifically, readily available is almost entire output of Ukraine's second largest refinery, Ukrtatnafta, and around 20% of output of Ukraine's largest one, LiNOS.

**Feedstock shortages and state regulation are major risk factors for independent oil products retailers**

Margins of independent oil products retailers are almost on a par with those typical of VIOCs. However, independent operators are at disadvantage, since they do not have guaranteed feedstock supply and are exposed to downtime risk during peaking demand periods. In this regard, Galnaftogaz possesses a competitive advantage through diversified supply. Another risk for independent operators is state regulation. Unlike oil products retailers combined into VIOCs, they have no safety margin in terms of retail markup. When retail prices are fixed, and bulk prices at refineries are rising, 'price scissors' hurt independent retailers most badly. In these conditions, only most efficient players with developed brand names can survive. This is the key reason why independent operators strive to focus on their brands, enhance quality of their services and diversify into non-oil products and services.

## Market Strategy And Investment Program

**Galnaftogaz' strategy envisages expansion to over 380 full service stations**

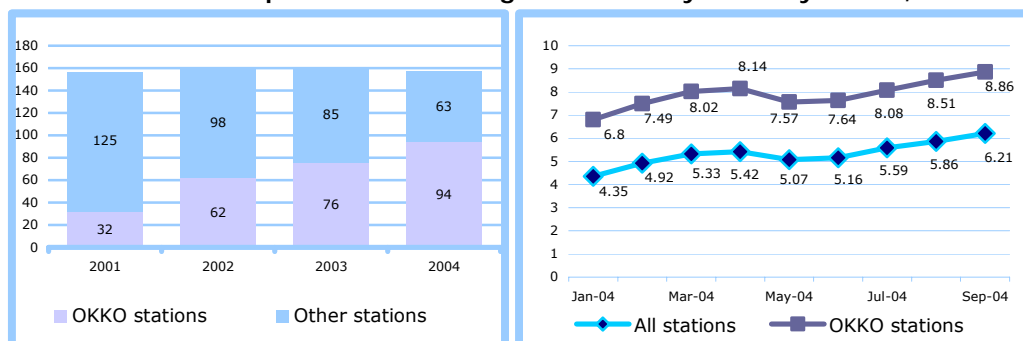
The company's business strategy is to create a network of over 380 brand gas stations with a focus on providing full range of non-oil goods and services, such as car washes, repair shops, motels, parking, grocery stores, fast food restaurants, etc. Galnaftogaz has successfully implemented a fuel smart card project 'OKKO card', which provides extra convenience in fuel payments. This clearing system covers the entire Ukraine's territory and can be found at gas stations operating under different brands, including those of TNK-BP and Lukoil. OKKO stations are positioned as 'service stations' rather than merely gas stations. This makes them similar to gas stations in Europe and the US. Conversely, most other Ukrainian oil product retailers concentrate solely on selling oil products, which they can get cheap from the refineries their owners control.

**Non-oil products & services will add the most value to the company in the mid-term**

Development of a western standard retail network with a full range of services, despite the current low usage of non-oil products and services in Ukraine, will endow Galnaftogaz with a competitive advantage in the mid-term. Market saturation, coupled with the rising purchasing power of Ukrainian car owners, will result in well-off car owners' shifting toward full-service gas stations in three to four years. This is the market niche targeted by Galnaftogaz. The company expects to capture 8-11% of the Ukrainian oil products market in 2008. In the long term, revenue from non-oil products may comprise as much as 15% of total retail sales, as it is now the case for BP's gas stations.

Branding has proven to be an efficient measure to increase sales of oil products. Thus, in the future Galnaftogaz plans to minimize number of non-brand stations.

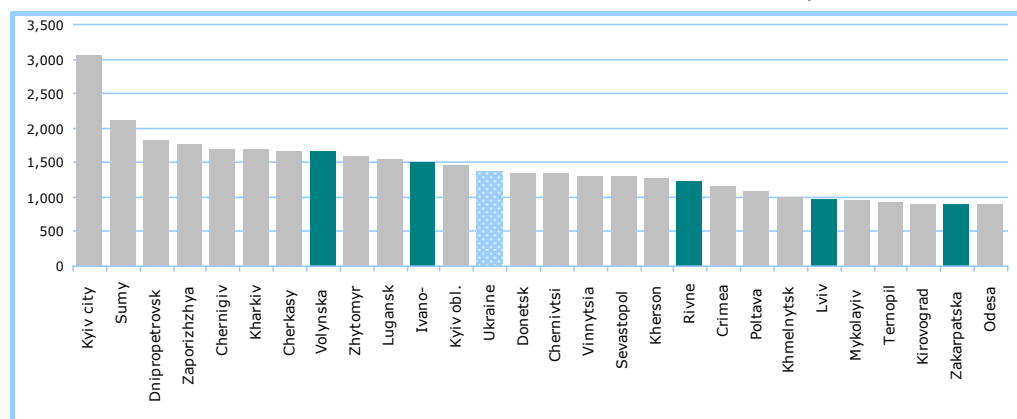
**Chart 8. Network Expansion & Branding** **Chart 9. Daily Sales Dynamics, mt**



Source: Company Data

Currently, Galnaftogaz' gas stations are concentrated primarily in five western oblasts – Lviv, Ivano-Frankivsk, Rivne, Zakarpatska and Ternopil, while overall the company's network covers 11 oblasts and the city of Kyiv.

**Chart 10\*. Number Of Automotive Vehicles Per Gas Station, 01.04.2004**



\*Regions where Galnaftogaz has most of its gas stations are highlighted in green

Source: State Statistics Committee

**Galnaftogaz will commit USD 130 mn to gas stations chain expansion in 2005-2008**

The company's management embraced a strategy of expanding into central and eastern regions, as well as into the capital city Kyiv. While Galnaftogaz will face stronger competition in these oblasts, turnover per every new station is expected to be higher due to a larger number of vehicles there. To this end, Galnaftogaz will commit about USD 130 mn in 2005–2008 for gas stations acquisition and reconstruction.

**Table 2. Galnaftogaz 2005 – 2008 Investment Plan**

<b>Region</b>	<b># of stations to be constructed/upgraded/acquired</b>	<b>Price per station, ths USD</b>
Kyiv – Odesa route	6	1,212
Kyiv - Kharkiv	2	1,037
Lviv	29	652
Kyiv – Chop route	4	1,168
City of Kyiv	7	782
Rivne	6	540
Zakarpattya	10	628
Kharkiv	6	743
Kyiv Oblast	3	750
Zaporizhzhya	5	836
Poltava	8	639
Zhytomyr	6	713
Volyn	11	728
Kirovograd	7	607
Chernivtsi	3	650
Chernigiv	5	635
Khmelnysky	14	598
Cherkasy	14	634
Ivano-Frankivsk	9	530
Vinnytsia	7	560
Ternopil	13	416
Other	18	683
<b>Total / average</b>	<b>193</b>	<b>669.5</b>

*Source: Company Data*

**CapEx will be used to upgrade stations to create a stronger brand image**

Apart from acquisitions, the second largest CapEx item will be expenses for upgrading and improving infrastructure at non-brand stations to make them into OKKO stations. Other CapEx will include reconstruction of tank storage units and acquisition of gas-tank trucks.

Galnaftogaz will tap both debt and equity sources to finance its investment program. In particular, the company plans to obtain new credit from the EBRD and IFC and go public on one of Europe's stock exchanges after 2005. It already utilizes a credit line from the Black Sea Trade & Development bank with total funds available of USD 23 mn (USD 8.8 mn used up in December and USD 5.0 mn – in January 2005). Galnaftogaz enjoys superb credit history in Ukraine, largely due to its continuous cooperation with Raiffeisenbank (Ukraine), and its bonds are among Ukraine's most liquid. The EBRD and IFC are expected to become minority shareholders of GLNG's in 2005 with a 15% stake.

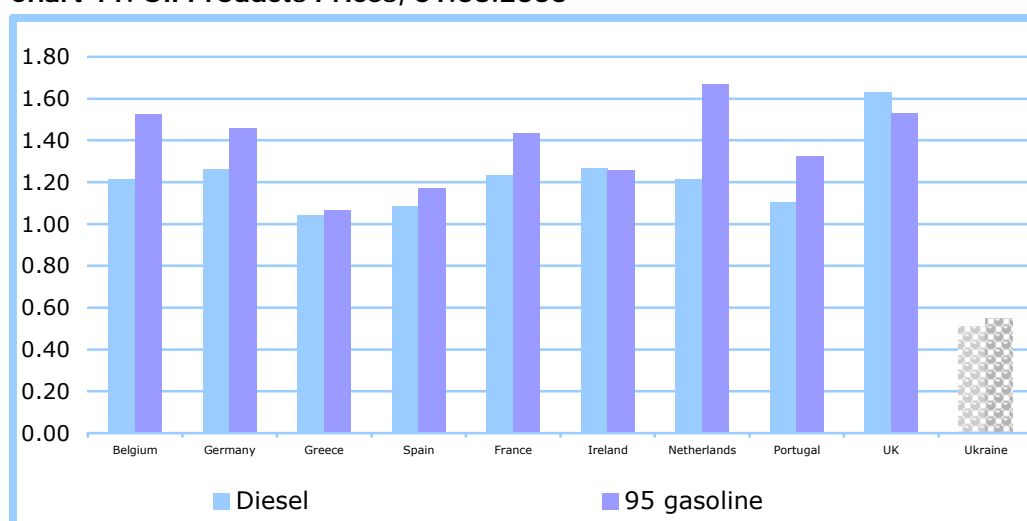
## Operations Modeling

In the model below, we have made the following assumptions:

- Galnaftogaz' retail network will reach 386 gas stations by 2014
- Marketing and infrastructure improvements will result in a daily sales increase to 9.8 mt of oil products for OKKO-brand stations
- Number of OKKO-brand stations will increase, while non-brand stations will keep diminishing
- Average price for oil products will rise with a CAGR of 4.5%

As Ukraine makes further advances towards EU accession/associated membership, domestic fuel prices are expected to rise, since their current levels are far below those in Europe. Administrative regulation, relatively cheap crude fed to Ukrainian refineries and competition will not allow the gap to disappear completely.

**Chart 11. Oil Products Prices, 01.03.2005**



Source: International Road Transport Union; UPECO

In our 2004 financials estimates we used the management's guidance. Specifically, we adjusted EBITDA – as it appears in Galnaftogaz' P&L prepared in accordance with the Ukrainian accounting standards – upwards to include a recurring item that pertains to the company's operating earnings, but was 'hidden' in the Other Income line.

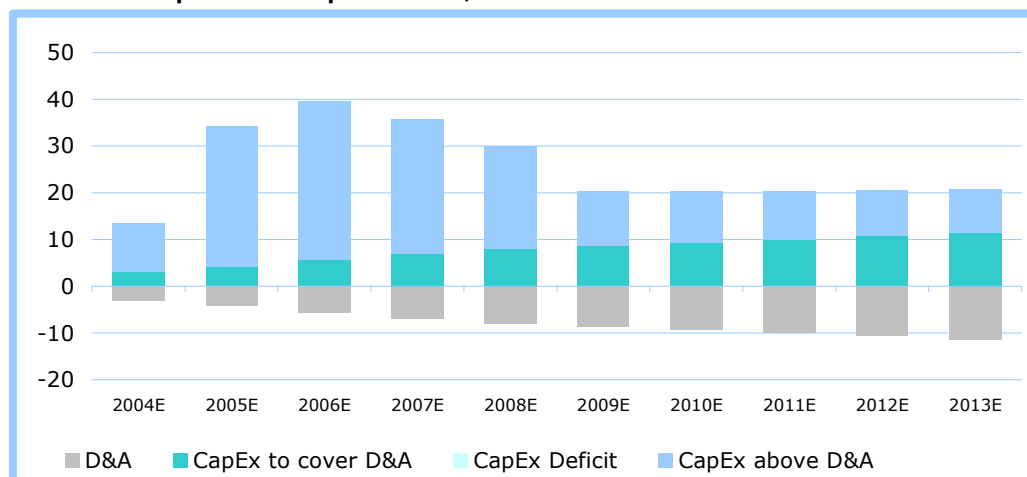
EBITDA margin spike in 2005 from 3.9% to 7.5% will result from the launch of a trading house in March 2005, which will help optimize bulk purchases. Currently, pure retail mark-up is around 13% in the Ukrainian market, while, by our estimates, in 2004 Galnaftogaz could only receive an effective mark-up of around 8%. This was due to the fact that Galnaftogaz' stations operated under commission agreements with bulk oil products traders and the company had to split its mark-up. Eventually the mark-up will decline due to both bulk price rise and competitive pressure. Our model projects that Galnaftogaz' EBITDA margin will stabilize at 5.5% by the end of our forecast horizon, which is close to the average figure for the oil products retail industry in the developing markets.

**Table 3. Key Projections**
*For the purposes of forecasting local currency is used*

	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F	CAGR 5Y	CAGR 10Y
GDP growth	12.0%	8.0%	6.0%	5.0%	4.5%	4.0%	4.0%	4.0%	4.0%	4.0%	7.1%	5.5%
Industrial production growth	12.5%	9.0%	6.5%	5.5%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	7.7%	6.3%
# of operating gas stations	157	193	237	281	312	325	338	351	366	386	14.1%	9.1%
-OKKO gas stations	94	142	196	248	286	306	326	346	366	386	30.3%	17.6%
-Other gas stations	63	51	41	33	26	19	12	5	0	0	-21.1%	-100.0%
Avg daily sales by OKKO station, mt	7.9	8.2	8.4	8.7	8.9	9.1	9.3	9.5	9.7	9.8	2.9%	2.4%
Avg daily sales by non-brand station, mt	2.5	2.7	2.9	3.1	3.4	3.4	3.4	3.4	-	-	6.5%	-
Oil products retailed, ths mt	305.4	411.3	566.8	746.8	906.4	1,011.1	1,091.9	1,175.6	1,267.0	1,345.0	28.5%	17.9%
Avg oil products price, ths UAH/mt	3.00	3.69	3.86	4.03	4.21	4.40	4.60	4.81	5.02	5.25		
Retail oil products revenue, UAH mn	969	1,606	2,313	3,184	4,039	4,708	5,313	5,978	6,732	7,468	40.0%	25.8%
Sales of ancillary products, UAH mn	69	91	109	135	172	200	226	254	286	318	27.5%	20.1%
Wholesale oil products revenue, UAH mn	303	81	83	86	89	93	95	96	98	101	-5.8%	-1.7%
Other revenues, UAH mn	237	-	-	-	-	-	-	-	-	-		
<b>Net revenue, UAH mn</b>	<b>1,299</b>	<b>1,482</b>	<b>2,088</b>	<b>2,838</b>	<b>3,583</b>	<b>4,168</b>	<b>4,695</b>	<b>5,274</b>	<b>5,931</b>	<b>6,573</b>	<b>30.6%</b>	<b>21.4%</b>
Gross margin, %	6.3%	10.0%	10.7%	10.5%	10.5%	10.2%	10.0%	9.6%	9.2%	8.9%		
<b>Gross profit, UAH mn</b>	<b>82</b>	<b>148</b>	<b>223</b>	<b>298</b>	<b>376</b>	<b>425</b>	<b>470</b>	<b>506</b>	<b>546</b>	<b>585</b>	<b>55.3%</b>	<b>30.2%</b>
EBITDA margin, %	3.9%	7.5%	8.1%	7.8%	7.7%	7.4%	7.0%	6.4%	6.0%	5.5%		
<b>EBITDA, UAH mn</b>	<b>50</b>	<b>111</b>	<b>169</b>	<b>221</b>	<b>276</b>	<b>308</b>	<b>329</b>	<b>338</b>	<b>356</b>	<b>361</b>	<b>76.0%</b>	<b>36.3%</b>
EBIT margin, %	3%	6%	7%	7%	7%	6%	6%	5%	5%	5%		
EBIT, UAH mn	33	88	139	185	234	262	279	284	299	301	103.6%	46.4%
NI margin, %	1.2%	3.7%	4.2%	4.1%	4.2%	4.2%	4.1%	3.8%	3.6%	3.4%		
<b>Net Income, UAH mn</b>	<b>16</b>	<b>55</b>	<b>88</b>	<b>117</b>	<b>149</b>	<b>173</b>	<b>192</b>	<b>201</b>	<b>215</b>	<b>220</b>	<b>68.2%</b>	<b>34.8%</b>
Dividend Declared, UAH mn	-	-	-	-	44.8	60.5	67.2	70.3	86.0	88.1	nm	nm

Source: Concorde Capital Projections

Projected CapEx dynamics generally follow our forecast for the number of gas stations constructed/ acquired each year.

**Chart 12. CapEx and Depreciation, USD mn**


Source: Company data; Concorde Capital Projections

## Valuation

### DCF APPROACH

DCF analysis conducted below suggests that GLNG's stock fair value per share is currently USD 0.0087, with a 12 month fair value of USD 0.0105.

**Table 4. Discounted Cash Flow Valuation**

Valuation date	Mar 5, 2005									
<i>For the purposes of forecasting local currency is used (UAH mn)</i>										
	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F
<b>EBITDA</b>	<b>50</b>	<b>111</b>	<b>169</b>	<b>221</b>	<b>276</b>	<b>308</b>	<b>329</b>	<b>338</b>	<b>356</b>	<b>361</b>
EBIT	33	88	139	185	234	262	279	284	299	301
Tax Rate	12%	17%	18%	20%	22%	22%	22%	22%	22%	22%
Taxed EBIT	29	73	114	148	182	205	218	222	233	235
Plus D&A	17	23	30	37	42	46	50	53	57	60
Less CapEx	(72)	(182)	(210)	(190)	(159)	(108)	(108)	(108)	(109)	(110)
Less change in OWC	(53)	(6)	(24)	(25)	(17)	(4)	(20)	(22)	(24)	(24)
<b>FCFF</b>	<b>-</b>	<b>(91)</b>	<b>(90)</b>	<b>(30)</b>	<b>48</b>	<b>138</b>	<b>139</b>	<b>145</b>	<b>157</b>	<b>162</b>
Avg. est. interest rate	12.7%	12.6%	11.8%	10.9%	10.9%	11.2%	10.2%	9.9%	10.6%	10.6%
Cost of equity	21.0%	18.7%	17.5%	16.1%	15.4%	14.4%	14.1%	14.1%	14.1%	14.1%
WACC	16.5%	15.2%	13.7%	12.7%	12.7%	12.5%	12.4%	12.8%	13.2%	13.4%
WACC to Perpetuity	11.0%	Terminal Value								<b>2,080</b>
<b>Firm Value</b>	<b>877</b>		Portion due to TV							79.8%
Less Net Debt	(143)		Perpetuity Growth Rate							3.0%
<b>Equity Value</b>	<b>734</b>		Implied Exit EBITDA Multiple							5.8 x
<b>Fair Value per Share</b>	<b>USD 0.0087</b>		<b>12-mo Fair Value per Share</b>							<b>USD 0.0105</b>

Source: Concorde Capital forecasts

**Table 5. Sensitivity Analysis: Implied 12-Month Share Price, USD**

10-Year Discount Rates	Perpetuity Growth Rate				
	2.0%	2.5%	3.0%	3.5%	4.0%
<b>WACC – 3.0%</b>	0.0120	0.0127	0.0134	0.0143	0.0152
<b>WACC – 2.0%</b>	0.0111	0.0117	0.0124	0.0132	0.0140
<b>WACC – 1.0%</b>	0.0102	0.0107	0.0114	0.0121	0.0130
<b>WACC + 0.0%</b>	0.0093	0.0099	<b>0.0105</b>	0.0112	0.0119
<b>WACC + 1.0%</b>	0.0086	0.0091	0.0096	0.0103	0.0110
<b>WACC + 2.0%</b>	0.0079	0.0083	0.0089	0.0095	0.0101
<b>WACC + 3.0%</b>	0.0072	0.0076	0.0081	0.0087	0.0093

Source: Concorde Capital calculations

**Table 6. Sensitivity Analysis: Implied 12-Month Share Price, USD**

WACC to perpetuity	Perpetuity Growth Rate				
	2.0%	2.5%	3.0%	3.5%	4.0%
<b>8.0%</b>	0.0134	0.0146	0.0161	0.0178	0.0200
<b>9.0%</b>	0.0117	0.0126	0.0136	0.0148	0.0163
<b>10.0%</b>	0.0104	0.0110	0.0118	0.0127	0.0137
<b>11.0%</b>	0.0093	0.0099	<b>0.0105</b>	0.0112	0.0119
<b>12.0%</b>	0.0085	0.0090	0.0094	0.0100	0.0106
<b>13.0%</b>	0.0079	0.0082	0.0086	0.0091	0.0095
<b>14.0%</b>	0.0073	0.0076	0.0079	0.0083	0.0087

Source: Concorde Capital calculations

**PEER COMPARISON**

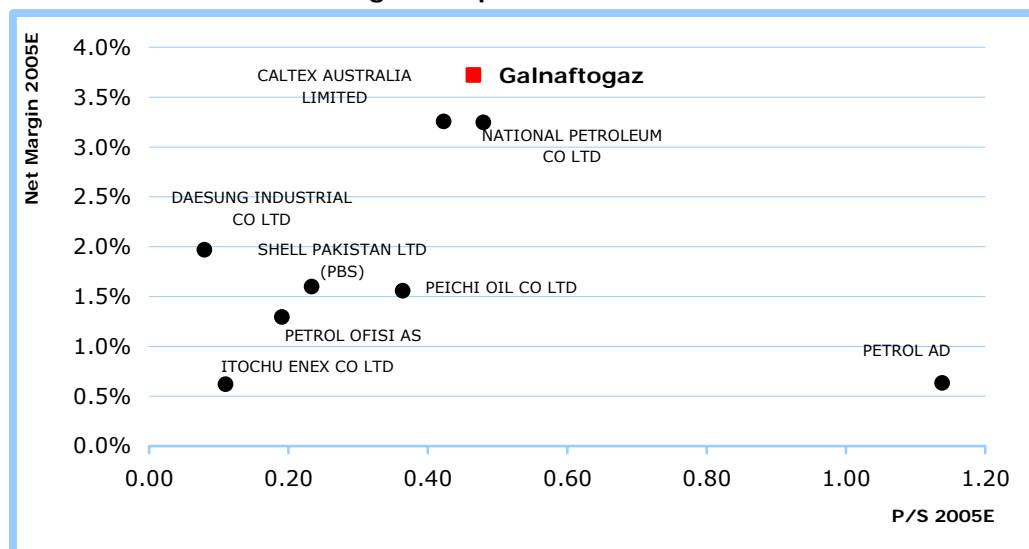
A comparison valuation below shows mixed results. GLNG looks overpriced in terms of average P/S, but undervalued on an EV/EBITDA and P/E basis. Importantly, Galnaftogaz looks significantly undervalued compared to its Bulgarian peer, Petrol. The latter is much similar to Galnaftogaz in terms of both business environment and strategy pursued. It owns a chain of 450 gas stations in Bulgaria, over 100 of which are constructed according modern European standards, 80 tank storages and 3 seaport terminals.

**Table 7. Comparative Valuation**

Company	Country	MCap, USD mn	P/S		EV/EBITDA		P/E	
			2004E	2005F	2004E	2005F	2004E	2005F
<b>Galnaftogaz</b>	<b>Ukraine</b>	<b>130.0</b>	<b>0.5</b>	<b>0.5</b>	<b>16.5</b>	<b>7.9</b>	<b>43.8</b>	<b>12.5</b>
PETROL AD	Bulgaria	300.3	1.2	1.1	26.9	25.9	187.5	180.3
CALTEX AUSTRALIA LIMITED	Australia	2,618.8	0.4	0.4	6.0	7.4	9.8	13.0
DAESUNG INDUSTRIAL CO LTD	South Korea	103.1	0.1	0.1	5.3	5.1	4.2	4.0
PETROL OFISI AS	Turkey	1,252.6	0.2	0.2	8.3	8.5	42.0	14.7
SHELL PAKISTAN LTD (PBS)	Pakistan	336.6	0.2	0.2	7.6	7.3	15.2	14.6
PEICHI OIL CO LTD	Taiwan	37.7	0.4	0.4	13.4	12.9	24.3	23.4
NATIONAL PETROLEUM CO LTD	Taiwan	253.7	0.5	0.5	16.7	16.0	15.5	14.8
ITOCHU ENEX CO LTD	Japan	611.0	0.1	0.1	7.7	7.8	159.5	17.7
<b>Median</b>			<b>0.3</b>	<b>0.3</b>	<b>8.0</b>	<b>8.2</b>	<b>19.9</b>	<b>14.7</b>
<b>Peer Average</b>			<b>0.4</b>	<b>0.4</b>	<b>11.5</b>	<b>11.4</b>	<b>57.2</b>	<b>35.3</b>
Premium/ (Discount) to Avg			23%	43%	-30%	-23%	-65%	23%
Implied Price, USD			0.0066	0.0052	0.0126	0.0106	0.0229	0.0066
Upside (Downside)			-19%	-36%	55%	31%	182%	-19%
<b>Comparison with Petrol AD:</b>								
Premium/ (Discount) to Petrol AD			-55%	-59%	-39%	-69%	-77%	-93%
Implied Price, USD			0.0182	0.0199	0.0143	0.0317	0.0348	0.1171
Upside (Downside)			125%	145%	76%	290%	328%	1341%

Source: Concorde Capital calculations; Bloomberg

**Chart 13. P/S And Net Margin Comparison**



Source: Concorde Capital calculations; Bloomberg

### COMPARATIVE DEAL METHOD

We decided to focus on one deal, which we think is relevant to infer a possible acquisition price for Galnaftogaz. In 2H04, Lukoil bought 37 gas stations in St. Petersburg from Balt-Trade for an estimated USD 40 mn, which implies an average price of USD 1.08 mn per station. Based on this price, Galnaftogaz' chain of 164 stations would cost about USD 177 mn (USD 0.0111). Certainly, this is a rough estimate, as Galnaftogaz' OKKO stations must cost, on average, more than USD 1.1 mn, due to their developed infrastructure and higher turnover. Other stations located in non-industrial regions are definitely cheaper than the stations in St. Petersburg city.

On the other hand, Ukrnafta purchases gas stations located predominantly in central and western Ukraine for an average price of USD 0.9–1.0 mn, which gives an estimated acquisition price for Galnaftogaz' chain of USD 148–164 mn (or USD 0.0092–0.1025 per share). It is essential that Ukrnafta not seek to develop its non-oil goods and services segment, which means its stations must cost less than Galnaftogaz' OKKO-brand ones.

### CONCLUSION

Taking into account all three valuation methods, we have determined the DCF-based value to be the most reliable and have determined a 12 month target price of USD 0.0105 for GLNG. Thus, the implied 12 month upside to the current market price of USD 0.0081 is 29%. **BUY**

Financial statements are reported according to IFRS

**Income Statement Summary, USD mn**

	2003	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F
<b>Net Revenues*</b>	<b>177</b>	<b>244</b>	<b>279</b>	<b>394</b>	<b>535</b>	<b>675</b>	<b>786</b>	<b>885</b>	<b>994</b>	<b>1,118</b>	<b>1,239</b>
<i>Change y-o-y</i>	-54%	38%	14%	41%	36%	26%	16%	13%	12%	12%	11%
Cost Of Sales*	(169)	(229)	(251)	(351)	(479)	(604)	(705)	(796)	(899)	(1,015)	(1,129)
Gross Profit*	8	15	28	42	56	71	80	88	95	103	110
Other Operating Income/Expenses, net	(1)	(1)	-	-	-	-	-	-	-	-	-
SG&A	(4)	(6)	(7)	(10)	(14)	(19)	(22)	(27)	(32)	(36)	(42)
<b>EBITDA*</b>	<b>3</b>	<b>9</b>	<b>21</b>	<b>32</b>	<b>42</b>	<b>52</b>	<b>58</b>	<b>62</b>	<b>64</b>	<b>67</b>	<b>68</b>
<i>EBITDA margin, %</i>	1.7%	3.9%	7.5%	8.1%	7.8%	7.7%	7.4%	7.0%	6.4%	6.0%	5.5%
Depreciation	(2)	(3)	(4)	(6)	(7)	(8)	(9)	(9)	(10)	(11)	(11)
<b>EBIT*</b>	<b>1</b>	<b>6</b>	<b>17</b>	<b>26</b>	<b>35</b>	<b>44</b>	<b>49</b>	<b>53</b>	<b>54</b>	<b>56</b>	<b>57</b>
<i>EBIT margin, %</i>	0.7%	2.6%	6.0%	6.7%	6.5%	6.5%	6.3%	5.9%	5.4%	5.0%	4.6%
Interest Expense	(1)	(3)	(4)	(6)	(7)	(8)	(8)	(6)	(5)	(4)	(4)
Financial Income	3	-	-	-	-	-	-	-	-	-	-
Other income/(expense)*	-	-	-	-	-	-	-	-	-	-	-
<b>PBT</b>	<b>2</b>	<b>3</b>	<b>13</b>	<b>20</b>	<b>27</b>	<b>36</b>	<b>42</b>	<b>46</b>	<b>49</b>	<b>52</b>	<b>53</b>
Tax	(0)	(0)	(2)	(4)	(5)	(8)	(9)	(10)	(11)	(11)	(12)
<i>Effective tax rate</i>	12%	12%	17%	18%	20%	22%	22%	22%	22%	22%	22%
<b>Net Income</b>	<b>2</b>	<b>3</b>	<b>10</b>	<b>17</b>	<b>22</b>	<b>28</b>	<b>33</b>	<b>36</b>	<b>38</b>	<b>41</b>	<b>42</b>
<i>Net Margin, %</i>	1.2%	1.2%	3.7%	4.2%	4.1%	4.2%	4.2%	4.1%	3.8%	3.6%	3.4%
<b>Dividend Declared</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>8</b>	<b>11</b>	<b>13</b>	<b>13</b>	<b>16</b>	<b>17</b>

**Balance Sheet Summary, USD mn**

	2003	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F
<b>Current Assets</b>	<b>20</b>	<b>41</b>	<b>46</b>	<b>63</b>	<b>83</b>	<b>101</b>	<b>114</b>	<b>128</b>	<b>144</b>	<b>162</b>	<b>180</b>
Cash & Equivalents	2	2	3	4	5	7	8	9	10	11	12
Trade Receivables	11	26	28	37	48	57	63	71	80	89	99
Inventories	3	6	7	10	13	17	20	22	25	28	31
Other current assets	4	7	8	12	16	20	24	27	30	34	37
<b>Fixed Assets</b>	<b>43</b>	<b>55</b>	<b>85</b>	<b>120</b>	<b>150</b>	<b>165</b>	<b>178</b>	<b>190</b>	<b>201</b>	<b>212</b>	<b>222</b>
PP&E, net	34	43	71	104	133	156	169	180	190	200	209
Other Fixed Assets	10	12	15	16	17	9	9	10	11	12	13
<b>Total Assets</b>	<b>63</b>	<b>96</b>	<b>131</b>	<b>183</b>	<b>233</b>	<b>267</b>	<b>292</b>	<b>318</b>	<b>345</b>	<b>374</b>	<b>402</b>
<b>Shareholders' Equity**</b>	<b>31</b>	<b>43</b>	<b>62</b>	<b>79</b>	<b>101</b>	<b>121</b>	<b>142</b>	<b>165</b>	<b>190</b>	<b>214</b>	<b>239</b>
Share Capital	26	35	43	43	43	43	43	43	43	43	43
Reserves and Other**	6	9	19	36	58	77	99	122	147	171	196
<b>Current Liabilities*</b>	<b>15</b>	<b>25</b>	<b>31</b>	<b>46</b>	<b>63</b>	<b>80</b>	<b>92</b>	<b>100</b>	<b>112</b>	<b>126</b>	<b>133</b>
ST Interest Bearing Debt	2	1	4	8	11	14	16	13	15	17	12
Trade Payables	12	22	25	35	48	61	71	80	89	101	111
Accrued Wages	-	-	-	-	-	-	-	-	-	-	-
Accrued Taxes	0	0	0	0	0	0	0	0	0	0	0
Other Current Liabilities**	1	2	2	3	4	5	6	7	8	9	9
<b>LT Liabilities</b>	<b>16</b>	<b>28</b>	<b>38</b>	<b>58</b>	<b>69</b>	<b>66</b>	<b>57</b>	<b>53</b>	<b>43</b>	<b>33</b>	<b>29</b>
LT Interest Bearing Debt	15	26	35	54	64	60	50	44	33	22	16
Other LT	1	2	3	4	5	7	8	9	10	11	12
<b>Total Liabilities &amp; Equity</b>	<b>63</b>	<b>96</b>	<b>131</b>	<b>183</b>	<b>233</b>	<b>267</b>	<b>292</b>	<b>318</b>	<b>345</b>	<b>374</b>	<b>402</b>

**UAH/USD Exchange Rates**

	2003	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F
Average	5.33	5.32	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31
Year-end	5.33	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31

Financial statements are reported according to IFRS

**Cash Flow Statement Summary, USD mn**

	2003	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F
Net Income	2	3	10	17	22	28	33	36	38	41	42
Depreciation	2	3	4	6	7	8	9	9	10	11	11
Non-operating and non-cash items	(2)	0	1	0	0	0	0	0	0	0	0
Less Changes in working capital	1	(10)	(1)	(5)	(5)	(3)	(1)	(4)	(4)	(5)	(5)
<b>Operating Cash Flow</b>	<b>3</b>	<b>(3)</b>	<b>14</b>	<b>18</b>	<b>25</b>	<b>33</b>	<b>41</b>	<b>42</b>	<b>44</b>	<b>47</b>	<b>49</b>
Capital Expenditures, net	(20)	(14)	(34)	(40)	(36)	(30)	(20)	(20)	(20)	(21)	(21)
Other Investments, net	(5)	(1)	-	-	-	8	-	-	-	-	-
<b>Investing Cash Flow</b>	<b>(25)</b>	<b>(14)</b>	<b>(34)</b>	<b>(40)</b>	<b>(36)</b>	<b>(22)</b>	<b>(20)</b>	<b>(20)</b>	<b>(20)</b>	<b>(21)</b>	<b>(21)</b>
Net Borrowings/(repayments)	(1)	10	11	23	13	(1)	(8)	(8)	(9)	(9)	(10)
Dividends Paid	-	-	-	-	-	(8)	(11)	(13)	(13)	(16)	(17)
Other	23	9	9	-	-	-	-	-	-	-	-
<b>Financing Cash Flow</b>	<b>23</b>	<b>19</b>	<b>20</b>	<b>23</b>	<b>13</b>	<b>(9)</b>	<b>(19)</b>	<b>(21)</b>	<b>(23)</b>	<b>(25)</b>	<b>(27)</b>
Beginning Cash Balance	1	2	2	3	4	5	7	8	9	10	11
Ending Cash Balance	2	2	3	4	5	7	8	9	10	11	12
<b>Net Cash Inflows/Outflows</b>	<b>1</b>	<b>1</b>	<b>0</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>

**Ratio Analysis and Per Share Data**

	2003	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F
<b>Liquidity Ratios</b>											
Current Ratio	1.30	1.64	1.46	1.36	1.32	1.27	1.23	1.29	1.29	1.29	1.35
Receivables Collection DOH (est.)	23	28	35	30	29	29	28	28	28	28	28
Inventories Processing DOH (est.)	6	7	9	9	9	9	9	9	9	9	9
Payment Period (est.)	26	27	34	31	32	33	34	34	34	34	34
Cash Conversion Cycle	4	8	10	7	6	5	3	3	3	3	3
<b>Operating Efficiency Ratios</b>											
Total Asset Turnover	2.80	3.06	2.45	2.50	2.57	2.70	2.81	2.90	3.00	3.11	3.20
Fixed Asset Turnover	4.10	4.97	3.97	3.83	3.96	4.28	4.58	4.81	5.09	5.42	5.71
<b>Operating Profitability Ratios</b>											
Operating Profit Margin	1%	3%	6%	7%	7%	7%	6%	6%	5%	5%	5%
Net Margin	1%	1%	4%	4%	4%	4%	4%	4%	4%	4%	3%
ROE	7%	8%	20%	24%	24%	25%	25%	24%	21%	20%	18%
<b>Financial Risk Ratios</b>											
Debt-to-Equity Ratio	0.55	0.63	0.62	0.78	0.73	0.61	0.46	0.35	0.25	0.18	0.12
Total Debt-to-Assets Ratio	0.50	0.55	0.52	0.57	0.57	0.55	0.51	0.48	0.45	0.43	0.40
Interest Coverage	0.9	2.2	4.0	4.4	4.7	5.5	6.5	8.4	10.6	12.7	15.9
<b>Du Pont Analysis</b>											
Net Margin	1.2%	1.2%	3.7%	4.2%	4.1%	4.2%	4.2%	4.1%	3.8%	3.6%	3.4%
Total Asset Turnover	2.80	3.06	2.45	2.50	2.57	2.70	2.81	2.90	3.00	3.11	3.20
Fin Leverage Multiplier	2.00	2.13	2.15	2.22	2.31	2.25	2.13	1.98	1.87	1.78	1.71
ROE = NM x TAT x FLM	6.6%	7.9%	19.6%	23.5%	24.4%	25.3%	24.8%	23.5%	21.3%	20.0%	18.3%
<b>Per Share Data, USD</b>											
EPS	0.000	0.000	0.001	0.001	0.001	0.002	0.002	0.002	0.002	0.003	0.003
DPS	0.000	0.000	0.000	0.000	0.000	0.001	0.001	0.001	0.001	0.001	0.001
BPS	0.003	0.003	0.004	0.005	0.006	0.008	0.009	0.010	0.012	0.013	0.015

**Exchange Rates, UAH/USD**

	2003	2004E	2005F	2006F	2007F	2008F	2009F	2010F	2011F	2012F	2013F
Average exchange rate	5.33	5.32	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31
Year-end exchange rate	5.33	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31	5.31

**Concorde Capital**  
**72 Vel. Vasylkivska St,**  
**2nd entry, 6th floor**  
**Kiev 03150, UKRAINE**

Tel +380 44 206 8366  
Fax: +380 44 206 8367  
www.con-cap.com  
office@con-cap.com

**General Director**

Igor Mazepa

im@con-cap.com

**Managing Director**

John Suggitt

js@con-cap.com

**Equity Sales**

Marina Martyrosyan  
Olessia Kapustina

mm@con-cap.com  
ok@con-cap.com

**Head of Research, Strategy**

Konstantin Fisun, CFA

kf@con-cap.com

**Utilities (Telecommunications, Energy)**

Alexander Paraschiy

ap@con-cap.com

**Oil & Gas, Pipes, Non-Ferrous Metals**

Andriy Gostik

ag@con-cap.com

**Ferrous Metals**

Viktor Koval

vk@con-cap.com

**Chemicals**

Maxim Bougriy

mb@con-cap.com

---

**Disclaimer**

This report has been prepared by Concorde Capital investment bank for informational purposes only. Concorde Capital does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that Concorde Capital may have a conflict of interest that could affect the objectivity of this report.

Concorde Capital, its directors and employees or clients may have or have had interests or long or short positions in the securities referred to herein, and may at any time make purchases and/or sales in them as principal or agent. Concorde Capital may act or have acted as market-maker in the securities discussed in this report. The research analysts, and/or corporate banking associates principally responsible for the preparation of this report receive compensations based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors, firm revenues and investment banking revenues.

The information contained herein is based on sources which we believe to be reliable but is not guaranteed by us as being accurate and does not purport to be a complete statement or summary of the available data. Any opinions expressed herein are statements of our judgments as of the date of publication and are subject to change without notice. Reproduction without prior permission is prohibited. © 2005 Concorde Capital