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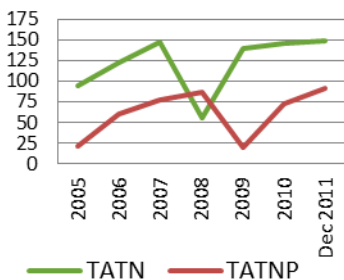
# TATNEFT

Analysts – Oil & Gas

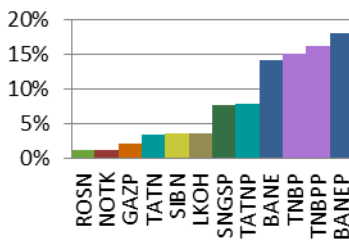
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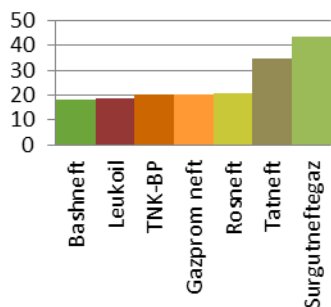
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Dividend Yield, 2010



Remaining Reserve life, years



## Company shares

Target Price - ord (TATN)	RUB	177,60
Upside - ord (TATN)		19%
No. of ord. shares	mln	2,179
Free Float - ord		31%
Target price - pref (TATNP)	руб.,	97,68
Upside - pref (TATNP)		6%
No. of pref. shares	млн	148
Free Float - pref		100%
Market cap	bln RUB	338,82
Enterprise Value	bln RUB	440,10

Source: MICEX, company data, Investcafe estimates

With this research note we are initiating coverage of Tatneft. The current prices of Tatneft shares reflect their fair valuation by the market and in light of this, Investcafe assigns a **HOLD** recommendation to Tatneft common and preferred shares.

**Tatneft - on the way to vertical integration.** After the construction of an oil refinery is complete, Tatneft will have the capacity to refine about 27% of its oil and thereby reduce its oil refining costs. This way, the company will be able to sell higher-margin oil products.

**Profitability growth.** We expect a significant increase in the company's net margin due to steadily rising oil prices, from 10% in 2010 to 13,6% in 2011 and 15,3% in 2012. Net profit margin in 2020 will be at 15%. The effect would have been even stronger if not for the rising unit extraction costs, which are forecast to outpace inflation, as our estimates show. This will happen as costs of maintaining production at its current level for the company continue to grow. The introduction of the 60-66-90 taxation system is to benefit the company. The EBITDA margin is forecast to increase by 6% in 2011 and by a further 3% in 2012.

**Dividend growth.** Tatneft pays its shareholders rather high dividends by Russian oil and gas sector standards. In 2010, the dividend yield on the preferred shares amounted to about 8% and that on common shares slightly exceeded 3%. We believe that as the company's CAPEX growth slows significantly and the company continues to generate consistently high cash flows, the size of dividends will increase. The payout ratio under US GAAP will reach 37% within five years, growing from 25% in 2010, as our estimates show.

**Debt reduction.** The company's debt leverage, which has exceeded a comfortable level due to the need to invest in oil refinery construction (the company closed 2010 with a net debt/EBITDA ratio of 1.32x), will gradually decrease, as the company repays the loans drawn for the construction of Taneco. By the end of the forecast period, the debt/equity ratio is forecast to more than halve to 11%, from 31% in 2010.

**Fair value.** To calculate a fair value for Tatneft shares, we built a discounted cash flow model, with a forecast period of ten years until 2020. Our estimates put the fair value for Tatneft shares at RUB 177.60 per **common share** and RUB 97.68 per **preferred share**. Taking into account the current prices, we assign a **HOLD** rating to Tatneft common and preferred shares.

## Financial and market indicators

	2010	2011П	2012П	2013П
Revenue (mln RUB)	468,032	596,753	568,929	592,903
EBITDA (mln RUB)	73,675	127,982	136,854	140,487
Net Income (mln RUB)	46,699	81,158	87,295	88,886
EBITDA margin (%)	16%	21.4%	24.1%	23.7%
Net margin (%)	10%	13.6%	15.3%	15.0%
EPS (RUB)	21	37	40	41
DPS (RUB)	5.02	9.42	10.89	11.85
P/E (x)	8.29	4.77	4.43	4.35
EV/S (x)	0.94	0.73	0.71	0.65
EV/EBITDA (x)	6.0	3.4	2.9	2.7
ROE (%)	13.32%	19.49%	18.06%	16.21%
Urals (\$/bbl)	78	110	105	110
Free Cash Flow (mln RUB)	(39,540)	53,275	54,879	47,688

Source: MICEX, company data, Investcafe estimates

