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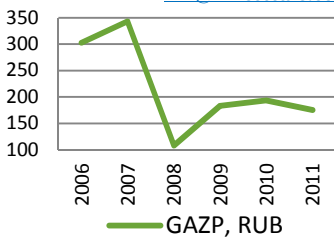
# GAZPROM

Analysts: oil and gas

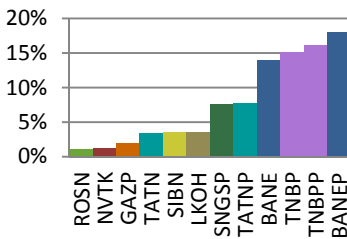
Grigory Birg, MiF, ACA  
+7 903 720 03 65  
[gb@investcafe.co.uk](mailto:gb@investcafe.co.uk)

Dmitry Adamidov, PhD  
[da@investcafe.co.uk](mailto:da@investcafe.co.uk)

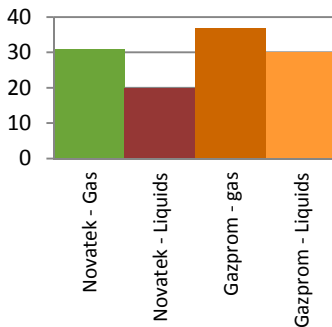
Vitaly Mikhailchuk  
[vm@investcafe.co.uk](mailto:vm@investcafe.co.uk)



Dividend Yield, 2010



Reserve Life, years



With this research we are initiating coverage of Gazprom. The current quotes for Gazprom shares reveal the company's low valuation by the market, and therefore Investcafe assigns a **BUY** rating to Gazprom common shares. Target price – **RUB 244**, implying **39%** upside potential.

Gazprom's monopolistic position in the Russian market is unshakeable in the near future and is firmly protected by the law. The law grants Gazprom exclusive ownership rights to Russian gas transit system. The company is endowed with the exclusive right to export natural gas from Russia at least until 2015 (gas exports by Novatek and Total from Yamal LNG are scheduled to begin in 2015). Concurrently, we expect the further deregulation of the Russian gas market, which, together with a continuous rise in prices, will mean a reduction in Gazprom's Russian market share from the current 71% to 68%. Meanwhile, the Russian gas market will grow by more than 30%, which means market share reduction will be compensated by much higher gas sales at higher prices.

The law 'On Subsoil Use' virtually makes Gazprom the sole beneficial owner of Russian strategic gas fields, at their nominal value and outside of competition. The Yamal-Nenets Autonomous Region in Western Siberia is presently the company's main production region and in the coming years. Gazprom extracts about 90% of its gas in this area. The regional oil & gas fields are depleted, but the existing resource base is to allow the company to almost double output by 2030. Fields in the Yamal Peninsula, Eastern Siberia and the Far East, as well as the Shtokman gas field, represent the most promising resource development projects by Gazprom. We expect natural gas production to reach 635 bcm by 2020.

Despite being strongly dependent on the market, Gazprom has been and remains the largest gas supplier to Europe, with a European gas market share of 25% and sales in 2010 of 148 billion cubic meters. The overwhelming majority of gas-importing markets in the CIS are likewise entirely reliant on Gazprom for gas shipments. Export sales by Gazprom are forecast to grow at a 4% CAGR over the next 10 years. The company is well placed to boost gas supplies to Asian markets by developing new oil fields and building gas pipelines and LNG plants. We expect gas exports to China via pipeline to commence in 2016 and average 30 bcm per year for the first 5 years.

From a financial viewpoint, Gazprom will continue to be pressured by its worsening position in Europe, its main export market. It is unlikely that Gazprom's market share will exceed 30%. However, the adopted course towards leveling off domestic gas prices with those in Europe in profitability terms eliminates this negative impact. By commissioning new pipeline capacity, and by bypassing transit countries, Gazprom will increase returns on future gas sales.

Having checked these assumptions with calculations, we assign Gazprom shares a **BUY** rating, with a target price of **RUB 244** per share.

## Gazprom ordinary shares

<b>Target price</b>	<b>RUB</b>	<b>244</b>
Current price (December 2011)	RUB	175
<b>Upside potential</b>	<b>%</b>	<b>39</b>
No. of shares	Mn	23,674
Free Float	%	40%
Market capitalisation	RUB bn	4,147
Enterprise Value	RUB bn	5,022

Sources: MICEX, Gazprom data, Investcafe estimates

## Financial and market indicators

	2010	2011E	2012E	2013E
Revenue (bn RUB)	3,597	4,171	5,100	5,648
EBITDA (bn RUB)	1,534	1,777	2,200	2,504
Net Income (bn RUB)	981	1,114	1,412	1,608
EBITDA margin (%)	43%	43%	43%	44%
Net margin (%)	27%	27%	28%	28%
EPS (RUB)	41.45	47.08	59.64	67.94
DPS (RUB)	3.85	5.55	8.52	11.41
P/E (x)	4.7	3.7	2.9	2.6
EV/S (x)	1.5	1.3	1.1	1.0
EV/EBITDA (x)	3.6	3.0	2.5	2.3
ROE (%)	16%	15%	16%	16%
Urals (\$/bbl)	90	96	105	110
Free Cash Flow (bn RUB)	(156)	175	260	178

Source: MICEX, company data, Investcafe estimates

