

**Postponement of VTB's merger with PSB****Analyst: Olga Belenkaya**

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On September 3, the Supervisory Council of Open joint-stock company VTB Bank (VTB) cancelled its EGM scheduled for September 27. The EGM had been convoked in order to decide issues related to the merger of VTB with OJSC VTB Bank North-West (formerly PSB).

As mentioned in the conference call by Nikolai Tsekhomsky, CFO and Member of the Board of VTB, the EGM was cancelled because of the risk that – in case of a reorganisation – due to the negative conditions prevalent on global credit markets, VTB's creditors might exercise their rights to demand the early redemption of its liabilities (including Eurobonds).

Nevertheless, VTB has not decided against the merger. The bank's press-release states that PSB plans to maintain valid the offer made to its shareholders to buy-back or swap its shares for VTB's shares. The final terms and conditions of the buy-back/swap will be announced separately. VTB is considering alternative ways of integrating the two banks, including conversion to a single share for both banks and plans to announce its decision within one month.

Initially the conversion terms provided a swap ratio of 361 VTB shares for 1 PSB share and a buy-out price of 0.136 roubles for 1 VTB share (the same price at which the IPO was held).

Until now PSB has not announced the cancellation of its EGM (scheduled for September 28). In August its Board approved a buy-out price of 41.72 roubles per share for those shareholders that were included in its shareholder register as of August 10 and who do not vote for the consolidation.

In our opinion, taking into account the unfavourable conditions prevalent on global financial markets, VTB's decision to cancel its EGM is quite reasonable. However, the news is negative for VTB minority shareholders (because they will lose the opportunity of selling their shares at the IPO price, which is significantly higher than the current price) and especially for minority PSB shareholders as it heightens the uncertainty about the terms and conditions of the consolidation.

In early morning trading today, PSB shares fell by 3.5%, whilst VTB shares rose by 0.34%. In our opinion, both VTB and PSB are significantly oversold. VTB is trading at a 2007E P/BV of 1.96 in comparison to an average P/BV of about 3 for Russian banks. At the same time, VTB's statement implies that the share swap and buy-back terms for PSB shareholders are likely to be maintained close to the conditions initially announced – whereas it is unlikely that the VTB share buy-out price announced earlier will be maintained.

04.09.2007	Market price, RUR.	Market price ratio	Swap ratio	Implied PSB price (assuming a swap ratio of 1:361), RUR	Implied PSB price (assuming a swap ratio of 1:361), \$	Upside	Buy-out price, RUR.
PSB	38.6	324.09	361 (?)	42.99	1.67	11.4%	41.72 (?)
VTB	0.119						0.136 (?)

If the buy-out price for PSB is maintained, its shareholders could earn a premium of about 11% in comparison to the current market price. Therefore, despite the increased risks, we recommend PSB shareholders not to be forced into panic sales but to **HOLD** and wait for the final terms and conditions of the buy-back/swap offer. We also advise VTB shareholders to **HOLD** their shares (as market multiple valuation implies a fair value of about 0.148 roubles).



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