



Severstal-Auto

Flash
Note

BUY

Upside: 16%
Target Price: 56\$

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Stock data

Ticker	svav	M.Cap, \$ mn	1,662
Shares Ords	34,270,159	Free float	35 %
Shares Prefs	-	Free float, \$ mn	582
Bid Ords, \$	48.00	Offer Ords, \$	49.00

Market performance

		1 month	6 months
Absolute	Ords	0.0%	50.4%
Relative to RTSI	Ords	-6.5%	36.4%
Price range, \$			
High	Ords	45.8	30.7
Low	Ords	49.5	49.5

Financials, 2007E

Revenue, \$ mn	1,741	P/S	0.95
EBITDA, \$ mn	253	EV/EBITDA	8.02
Net income, \$ mn	114	P/E	14.63
EBITDA margin, %	14.5%		
Net income, %	6.5%		

Severstal-Auto – Relative performance



Source: RTS, Sovlink

A handicap for Chinese auto producers!?

• On 10 November 2007, a government order will come into force, under which automobile manufacturers that have not launched an industrial assembly plant or have not signed at least a memorandum of understanding about the creation of an industrial assembly plant with the Ministry for Economic Development and Trade will not be entitled to benefit from lower import duties for importing auto-components. In accordance with the Russian government's resolution on industrial assembly plants, which came into force in March 2005, automobile producers that operate welding, painting and assembly units, producing at least 25,000 cars per annum, are entitled to import auto-components at a rate which does not exceed 3%.

• So far, 15 auto companies, including Toyota, Nissan, Ford, Renault, General Motors, Volkswagen, Suzuki, PSA Peugeot-Citroen, Severstal-Auto, IzhAuto and AutoVAZ, have entered into investment agreements with the Ministry for Economic Development and Trade, whilst Mitsubishi and Hyundai have signed memorandums of understanding. We note that the Ministry has not signed any agreements with any Chinese automobile manufacturers. The Chinese manufacturers decided to take a different route and have located their production facilities in free economic areas. Thus, Chery is willing to produce its cars jointly with the Kaliningrad manufacturer Autotor, and Great Wall has announced that it intends to set up an assembly production unit in the Tatarstan Republic.

• However, it is not clear whether the Russian government will allow the Chinese manufacturers to operate assembly plants in Tatarstan – as Russian government officials have been trying (for many years) to deprive companies in Kaliningrad of the benefits of reduced import duties on components used in the assembly of cars. We consider it likely that, at best, the government will drag out Great Wall's application for the establishment of car assembly production facilities (with the benefit of reduced import duties) in Tatarstan.

• We consider that Russian auto manufacturers will lobby the government to ensure that Chinese manufacturers in these free economic zones do not receive the opportunity of paying reduced duties on the components that they import. In accordance with the government's industrial assembly regime, companies benefiting from the regime must start reducing the components that they import tax free within 2.5 years, and reduce them by 30% within 4.5 years. This is particularly beneficial for Severstal-Auto, whose development strategy gives priority to the production of auto-components. We believe that delays in the deployment of Chinese automobile assembly facilities on Russian territory will allow Severstal-Auto to gain a strong foothold and enable it to launch its own auto-component production facilities, both for its own needs and for third party manufacturers.

• Such developments will undoubtedly result in a reduction of risks for Severstal-Auto and will have a positive impact on the company. As these factors were already included in our valuation model, we maintain a **BUY** recommendation on the company and reiterate our target price of \$56 per ordinary share, which implies potential upside of 16% from the current mid-price of \$48.5.



STOCK RATING POLICY

STRONG BUY:	Upside over 25%; confidence level – high / upside over 100%; confidence level - low
BUY:	Upside between 15 and 25%; confidence level – high / upside between 25% and 100%; confidence level – low
HOLD:	Upside of less than 15%; confidence level – high / upside of less than 25%; confidence level – low
SELL:	Target price at or below current price levels

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