

Russian Oil&Gas sector Dividend plays for 2010

19 November 2010

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▲ The best Russian oil and gas dividend plays following the 3Q 10 reporting season

Almost all Russian oil and gas companies have reported their 9M 10 results, providing a pretty clear indication of financial results for the whole of 2010 and the outlook for 2010 dividends. As usual, the preferred shares of Tatneft and Surgutneftegas should be good dividend plays in 2010. However, we also recommend the ordinary and preferred shares of Nizhnekamskneftekhim and Kazanorgsintez, which should also provide attractive dividends in 2010.

▲ The interim dividend record dates for the best 9M 10 dividend payers have already passed

We note that the majority of the companies, which offer the most attractive dividend yields in Russian oil and gas industry, has already announced the record dates for EGMs, on which the 9M 10 interim dividends may be decided. We note 9M 10 high dividends for shareholders of Bashneft, TNK-BP and Udmurtneft. For all three companies we still note a possibility of good 4Q 10 dividends, and also expect all these three companies to deliver high dividends in 2011.

▲ Tatneft and Surgutneftegas preferred shares remain attractive, but we expect a decrease in yields

Among the most liquid Russian oil and gas names we note only two significant dividend plays for 2010, neither of which are surprising, Tatneft and Surgutneftegas. We expect dividends for both of these companies to decrease slightly. We expect the dividend yield for Surgutneftegas preferred shareholders to decrease by 0.7ppt to a 6.8% yield. Tatneft preferred shareholders may see a more significant decrease of 8ppt in dividend yield, from last year's 14% yield to a yield of around 6% for 2010.

▲ Among the 2nd tiers, petrochemical stocks offer the best yields

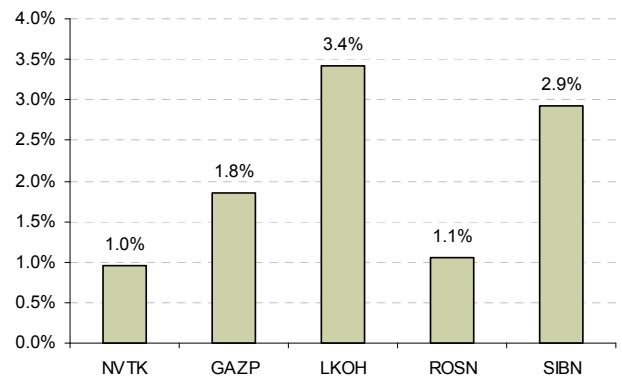
In 2nd tier shares we think two Tatarstan-based petrochemical companies are particularly interesting, Nizhnekamskneftekhim and Kazanorgsintez. Both companies reported excellent 9M 10 RAS results on the back of a rebound in the petrochemical market in 2010, and both companies may pay 30% of RAS net profit as dividends. We estimate Nizhnekamskneftekhim ordinary and preferred shares will yield 7.0% and 12.6%, respectively. We estimate Kazanorgsintez ordinary and preferred shares to yield 6.1% and 10.4%, respectively.

Top dividend plays in Russian oil and gas for 2010

	Ticker	Anticipated div. per share, RUB	Div. yield	Record date(E)
Tatneft(prefs)	TATNP RU	4.50	5.9%	May
Surgutneftegas (prefs)	SNGSP RU	1.03	6.8%	May
Nizhnekamskneftekhim	NKNC RU	1.20	7.0%	Feb
Nizhnekamskneftekhim (prefs)	NKNCP RU	1.20	12.6%	Feb
Kazanorgsintez	KZOS RU	0.33	6.1%	N/A
Kazanorgsintez (prefs)	KZOSP RU	0.25	10.4%	N/A

Source: IFC Metropol estimates

Estimated dividend yields for oil and gas majors in 2010



Source: Company data, IFC Metropol estimates

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First tier – usual dividend plays, but the yields got lower

Most blue chips do not offer attractive dividends

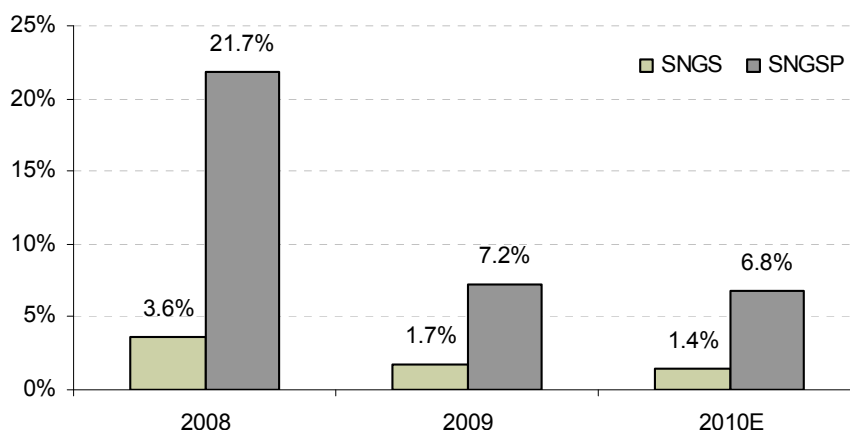
As was the case in previous years, we do not expect the major Russian oil and gas companies to pay out significant dividends for 2010. We believe only LUKOIL may offer a dividend yield of more than 3% for 2010, while the dividend yields for Gazprom and Rosneft shares could be less than 2%. Transneft could be the worst dividend play with an estimated 2010 dividend yield of just 0.7%.

Surgutneftegas: dividends should decrease on the back of lower net profit, but still offer an attractive yield

We consider Surgutneftegas preferred shares to be one of the best dividend plays among oil&gas blue chips in 2010. Surgutneftegas' 9M 10 RAS net profit was RUB 83.6bn, a 7.5% y-o-y decrease. With a 2009 payout ratio of 14.1% for common shares and 7.1% for preferred, this result may imply dividends of RUB 0.44 and RUB 1.03 per share respectively, yielding 1.4% per ordinary and 6.8% per preferred share.

On the back of lower deposit rates in 2010, Surgutneftegas' cash pile is bringing less interest income, which may be one of the reasons for the decrease in RAS net profit. However, although Surgutneftegas' dividend yield for preferred shares is expected to decrease from last year's 7.5%, it may still amount to 6.8%, higher than we expect any other blue chips to offer.

Figure 1:
Surgutneftegas dividend yield



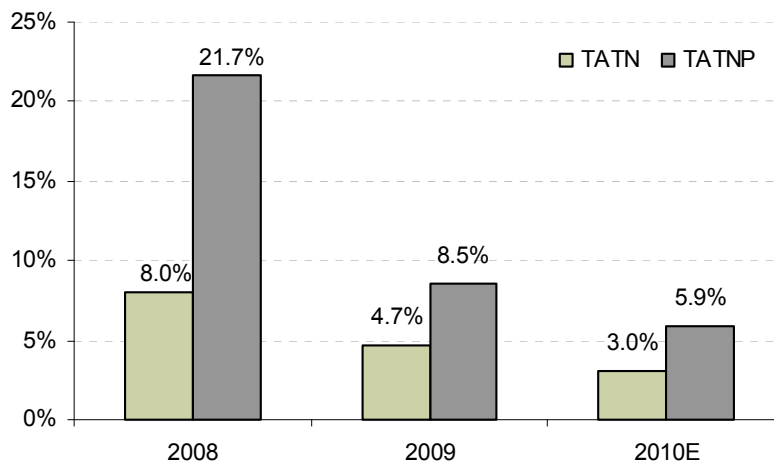
Source: Company data, IFC Metropol estimates

Tatneft: a significant decrease in RAS net profit may cause a sharp cut in dividends

Despite decrease in 2010 net profit, we think Tatneft can also be considered as a good dividend opportunity, as it should still provide a respectable dividend yield.

The company reported 9M 10 RAS net profit of RUB 26.3bn, a 42% decrease y-o-y. This matched our assumption that Tatneft would significantly decrease RAS net profit in 2010 and reduce the dividends accordingly. As Tatneft has historically paid out 30% of RAS net profit in dividends, we estimate that 9M 10 RAS net profit assumes 2010 dividends of just RUB 4.5 per share, yielding 3% and 5.9% per ordinary and preferred share, respectively.

Figure 2:
Tatneft dividend yield



Source: Company data, IFC Metropol estimates

Second tier petrochemical shares should provide the best dividends

This year we expect to find the best dividend yields in the 2nd tier, particularly in Tatar petrochemicals. We expect two Tatarstan-based petrochemical companies, Nizhnekamskneftekhim and Kazanorgsintez, will offer the best oil&gas dividends in 2010. Companies which are partially owned by the Tatarstan government, like Tatneft, Nizhnekamskneftekhim and Kazanorgsintez, historically pay out 30% of RAS net profit as dividends.

We estimate that both Kazanorgsintez and Nizhnekamskneftekhim will report excellent y-o-y performance in 2010 on the back of a strong rebound in petrochemical market, which should mean good dividends for 2010.

Nizhnekamskneftekhim: a good opportunity on the back of excellent performance

Nizhnekamskneftekhim (NKNC) reported excellent 9M 10 RAS net profit of RUB 6.3bn, 8.6x times higher than 9M 09 net profit. The excellent 9M 10 RAS report may lead to high dividend payments in 2010. If 4Q 10 brings the company another RUB 1bn in net profit, full-year 2010 net profit would be around RUB 7.3bn. In this case, dividends could be up to RUB 1.2 per share, yielding 7% for ordinary and 12.6% for preferred shares, respectively.

Figure 3:
Nizhnekamskneftekhim dividend yield



Source: Company data, IFC Metropol estimates

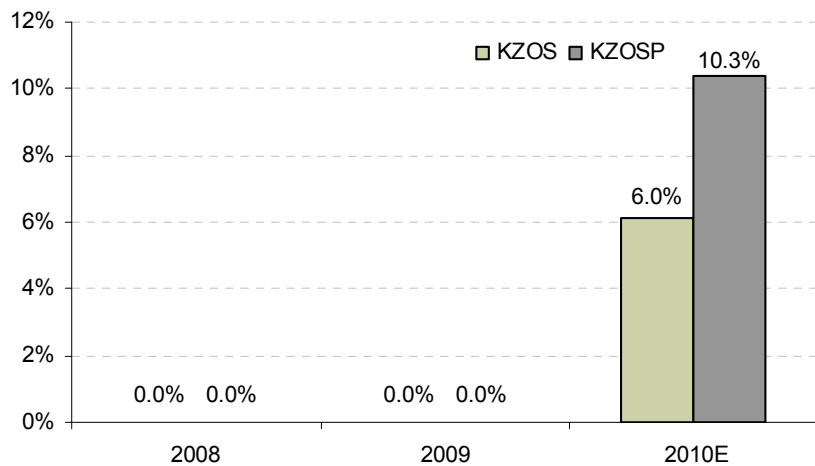
Kazanorgsintez: dividends should return for 2010

Kazanorgsintez has paid zero dividends for the last two years, and we believe the company could reward its shareholders following strong 9M 10 results.

Kazanorgsintez reported 9M 10 RAS net profit of RUB 1,54mn vs. net losses in 2008 and 2009. The result implies a possibility of dividend payments for 2010, because, as with the other large state-owned Tatar companies, the company has historically paid 30% of RAS net profit in dividends.

Assuming the same net profit dynamics for the fourth quarter as for 9M 10 and take into account the current conditions on the petrochemicals market, we estimate 2010 full-year net profit of RUB 2.06mn. This assumes the dividends of RUB 0.33 per ordinary share and RUB 0.25 per preferred share, yielding 6% and 10% for ordinary and preferred shares, respectively. Notable, there were no dividends from Kazanorgsintez in both 2008 and 2009.

Figure 4:
Kazanorgsintez dividend yield



Source: Company data, IFC Metropol estimates

Opportunities to consider for 2011

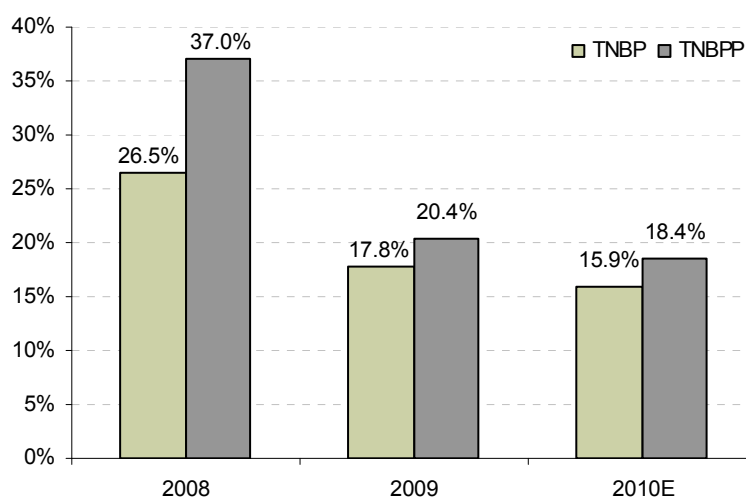
The three best dividend payers are TNK-BP, Bashneft and Udmurtneft, but these companies have already announced interim 9M 10 dividends, and are, therefore, excluded from our watch list for 2010. However, they should be back in the game in 2011. We also note that based on historical dividend payments, we may also expect some additional payments for 4Q 10.

TNK-BP: the best buy of 2010, shareholder structure suggests high dividends may continue

For 9M 2010 TNK-BP Holding paid dividends of RUB 8.04 for both common and preferred shares. This could yield 12% for common and 13.7% preferred shares respectively. In 2009, the company paid RUB 7.41 and RUB 2.18 per share for 9M and 4Q respectively, so we expect 4Q 10 dividends of approximately RUB 2.37 per share, resulting in a 7.8% payout ratio.

We, therefore, expect total 2010 dividends of up to RUB 10.41, yielding 15.9% per ordinary and 18.4% per preferred share. This means that TNK-BP Holding shares may show the highest dividend yield in the Russian oil&gas industry for 2010, and we currently consider the company to be the best dividend opportunity for 2011 as well. Supporting our view is the fact that TNK-BP's corporate structure sees dividends as the best way to transfer free cash flow generated by TNK-BP Holding to the parent company.

Figure 5:
TNK-BP dividend yield



Source: Company data, IFC Metropol estimates

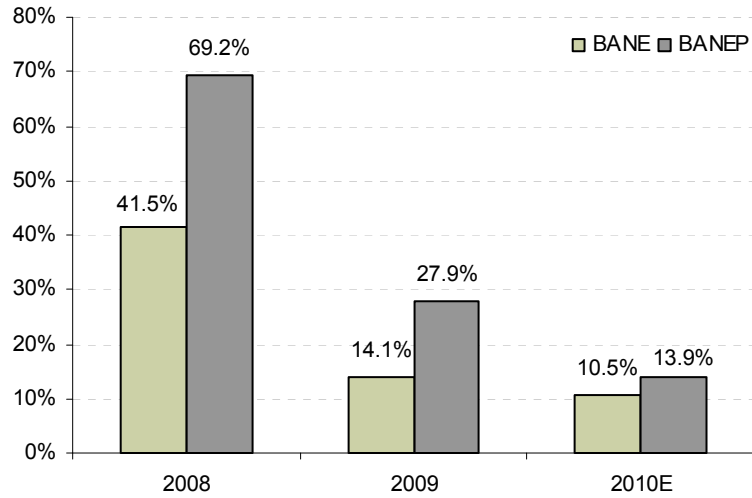
Bashneft: 100% payout in 2010, but what to expect in 2011?

Bashneft continues to pay out high dividends. After reporting good 9M 10 RAS results, with net profit growing by 143% y-o-y to RUB 21.4bn, all of this was distributed back to the shareholders as dividends. This equals RUB 104.5 per share for both ordinary and preferred shares, yielding 7.75% and 10.3% per ordinary and preferred share, respectively. We estimate 4Q 10 will bring in an additional RUB 7.5-8.5bn, and expect additional dividends for 4Q 10 of RUB 36.6 per share, with the total 2010 yield of 10.5% and 13.9% for ordinary and preferred shares respectively.

At the same time, Bashneft remains the main profit center for all Bashkirian oil holdings. Although the Ufa refineries reported good RAS net profit dynamics, we still don't expect large dividends for the minorities. According to our preliminary estimates, Ufa refinery shareholders may get RUB 0.15-0.2 per share, which should yield no more than 1.5% for 2010.

However, we are cautious regarding the dividends from Bashneft beyond 2010. The company may need significant cash to pay for the license and to develop the Trebs-Titov deposits.

Figure 6:
Bashneft dividend yield



Source: Company data, IFC Metropol estimates

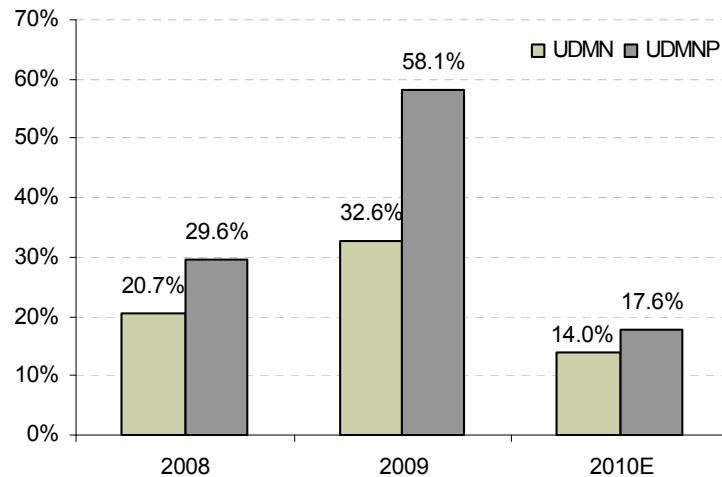
Udmurtneft: high stable yield on shareholder parity

Udmurtneft historically pays high dividends. In 2010, the company reported RAS net profit of RUB 3.9bn for 9M 10, a 15% y-o-y decrease. However, we forecast that Udmurtneft may be one of the best dividend plays in Russian oil&gas second tier in 2010 and 2011. We believe the company will pay RUB 2,437 per share for 9M 10, yielding 10.5% and 13.2% per common and preferred share respectively.

We expect total 2010 dividends could be up to RUB 3,249 on the back of 3Q net profit dynamics, yielding 14% and 17.6% per common and preferred share, respectively.

The reason for the high dividend payout ratio lies in the company's shareholder structure. Udmurtneft is held jointly by Rosneft and Sinopec, and pays out almost all of RAS net profit as dividends.

Figure 7:
Udmurtneft dividend yield



Source: Company data, IFC Metropol estimates

Oil and gas majors: limited dividend opportunities

Compared to the second tier names, the dividend yields offered by Russian oil and gas majors do not look impressive.

We expect LUKOIL to offer the largest yield among oil majors of 3.4%, paying a dividend of about RUB 60.32 per share.

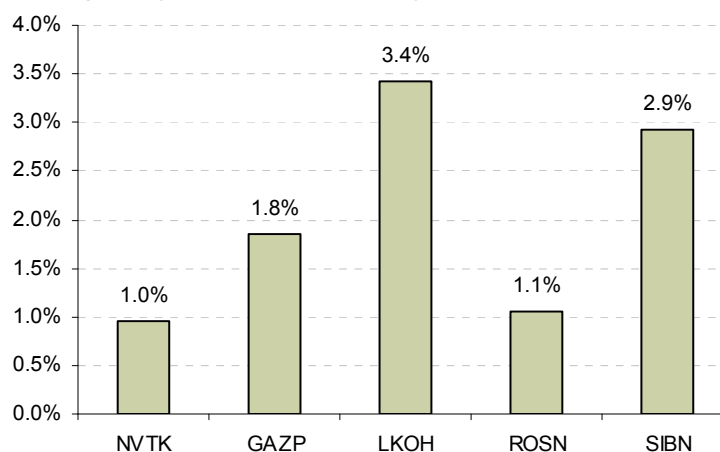
For 1H 10 Novatek paid out 33% of net profit or RUB 0.15 per share, and in 2H 10 we expect about RUB 1.64 per share, with the total 2010 yield of 1%.

Although Gazprom has increased the maximum dividend payout up to 35%, we do not expect the company to pay more than 17.5% of 2010 net profit, or RUB 3.18 per share, yielding 1.8%, on the back of a decrease in gas sales and large CAPEX during 2010.

We also expect Rosneft to pay RUB 2.29 per share, with a yield of 1.1%, while we estimate Gazprom Neft will pay RUB 3.7 per share with 2.9% yield.

Figure 8:

Oil and gas majors estimated dividend yields for 2010



Source: Company data, IFC Metropol estimates

Figure 9:
Selected dividend stock

	Ticker	Div yield 2010E	Div per share(E),	Cut of date(E)	Rating	Fair value, USD	Upside/ Downside
Blue chips							
Novatek*	NVTK LI	0.5%	1.64	April	Hold	107.50	3%
Gazprom	OGZD LI	1.8%	3.18	May	Hold	21.20	-8%
LUKOIL	LKOH RU	3.4%	60.32	April	Buy	95.60	66%
Rosneft	ROSN LI	1.1%	2.29	May	Buy	9.07	29%
Gazprom neft	SIBN RU	2.9%	3.70	May	Hold	4.55	10%
Tatneft	TATN RU	3.0%	4.50	May	Sell	4.18	-13%
Tatneft(pref)	TATNP RU	5.9%	4.50	May	N/A	N/A	N/A
Surgutneftegas	SNGS RU	1.4%	0.44	May	Hold	0.90	-10%
Surgutneftegas(pref)	SNGSP RU	6.8%	1.03	May	Buy	0.57	19%
2nd Tier							
TNK BP**	TNBP RU	3.6%	2.37	May	U/R	U/R	U/R
TNK BP(pref)**	TNBPP RU	4.2%	2.37	May	N/A	N/A	N/A
Transneft (pref)	TRNFP RU	0.7%	287.10	May	Sell	360	72%
Eurasia Drilling(in USD)	EDCL LI	1.3%	0.35	Dec	Buy	U/R	U/R
CAToil(EUR)	O2C GR	1.2%	0.07	Jun	U/R	U/R	U/R
Nizhnekamskneftekhim	NKNC RU	7.0%	1.20	Feb	Buy	0.59	5%
Nizhnekamskneftekhim (pref)	NKNCP RU	12.6%	1.20	Feb	Buy	0.32	3%
Bashneft**	BANE RU	2.7%	36.59	May	Hold	41.50	-2%
Bashneft(pref)**	BANEP RU	3.6%	36.59	May	Sell	25.10	-24%
Kazanorgsintez	KZOS RU	6.1%	0.33	N/A	Sell	0.11	-48%
Kazanorgsintez(pref)	KZOSP RU	10.4%	0.25	N/A	N/A	N/A	N/A
Udmurtneft**	UDMN RU	3.5%	811.62	May	N/A	N/A	N/A
Udmurtneft(pref)**	UDMNP RU	4.4%	811.62	May	N/A	N/A	N/A

*2H 10 dividends (1H 10 dividends already paid)

** 4Q 10 dividends (9M 10 dividends already paid)

Source: Company data, IFC Metropol estimates

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