

MERRY CHRISTMAS AND HAPPY NEW YEAR!
Market Wrap

There was very little action on the RTS last week as foreign investors quit for the Christmas Holiday. Trading volumes halved and the index level changed by just half a percent to close Friday at 567.4 points.

A Moscow court ruled early in the week that Yukos chief, Mikhail Khodorkovsky, will celebrate New Year in prison, but effect on the Yukos share price was minimal. The stock seems to have found a temporary equilibrium after its 13.4% rebound in mid-December. Trading in Yukos fell to just 5.5% of RTS turnover last week and the price slipped by 1.1%.

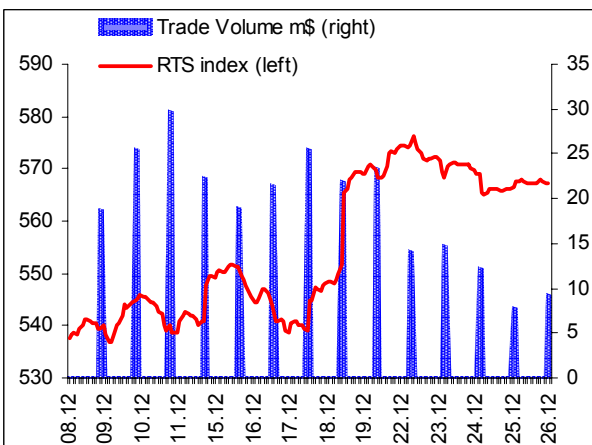
Surgut preferred shares were the only exciting stock last week as investors bought into expected high dividends. The shares rose by 4.8% on nearly \$6m turnover (nearly double the volumes of Surgut common share trading).

Oil companies were negatively affected by government threats last week to take away "excess" profits by new tax legislation. Lukoil was the biggest trader and showed a 1.7% price decline. The stock received surprisingly little benefit from good news on its Iraq contract. That may be due to the excessive Lukoil free float, which the company plans to reduce in 2004. Tatneft was the only oil sector winner, rising 3.7%.

UES lost support after it became clear that a final decision on wholesale generating companies would not be taken by the end of 2003. The stock fell by 1.7%.

Comments by Norilsk, committing to release of information on PMG reserves in 2004, contained little that was new for investors, and there was caution as international gold prices stabilized and a nickel price retreat was expected. However, the stock still managed to add 0.7%.

A 4% decline in the Rostelecom stock price reflects investor caution about sooner-than-expected ending of the company's long-distance monopoly, although the company CEO played down effects of the change in a press interview last week.

RTS Index & Volume

Key Figures

RTS Index	567.4	-0.38%
RTS Volume (\$m)	56.04	-48.8%
Ruble / Dollar	29.25	
Int'l Reserves (Dec 19)	\$74.5b	

Weekly data Fri-Fri.
Winners

Moscow City Telecom com	+9.6%
Saratovenergo com	+5.8%
Surgutneftegaz pref.	+4.8%
South Telecom com	+4.3%
Siberia Telecom com	+3.9%
Tatneft com	+3.7%

Top Volumes (\$m)

Lukoil com	17.1	30.5%
RAO UES com	12.2	21.7%
Surgutneftegaz pref.	5.9	10.6%
Surgutneftegaz com	3.6	6.4%
Norilsk Nickel com	3.3	5.8%
Yukos com	3.1	5.5%
KamAZ com	2.0	3.5%
Total (Top 7)	47.1	84.0%

Losers

Rostelecom com	-4.0%
Bashneft com	-1.9%
RAO UES com	-1.7%
Sberbank pref.	-1.7%
Avtovaz com	-1.2%
Yukos com	-1.1%

Sector Statistics

Sector Name	Volume \$	MC\$'000	% of MC	Change -week	Change -month	Change -year
Oil & Gas	31,390,656	95,239,180	60.79%	-0.91%	2.71%	50.65%
Power Utilities	13,699,019	19,717,796	12.59%	-0.98%	8.22%	119.08%
Metals	3,790,205	17,942,756	11.45%	0.65%	14.91%	210.59%
Telecom	3,313,902	10,442,918	6.67%	0.52%	8.32%	110.25%
Engineering	2,250,721	2,514,649	1.61%	0.30%	13.89%	57.61%
Banks	1,238,925	5,131,373	3.28%	-0.12%	4.46%	38.49%
Transportation	168,875	1,045,662	0.67%	0.21%	19.70%	101.67%
Chemicals	141,438	1,162,915	0.74%	5.66%	8.29%	234.35%
Others	36,110	3,318,388	2.12%	0.08%	-5.11%	27.50%
Retail	9,250	155,422	0.10%	-2.07%	-7.15%	-13.81%
Total	56,039,101	156,671,058	100.00%	-0.53%	5.19%	70.46%

VIEWPOINT: PUTIN AND GOVERNMENT GET TOUGH ON OIL TAXES

Weakness of oil stocks last week was mainly due to government threats to take away a bigger part of windfall profits due to high oil prices. The proposals came after Vladimir Putin objected to inadequate tax payment by oil companies and success of oil company lobbyists in blocking tougher taxation during the existence of the previous Duma (the role of Yukos in such lobbying is part of the explanation for the current attack on the company).

The most explosive proposal was leaked from the Ministry for Trade and Economic Development (MEDT), though it does not yet have official sanction of the minister, German Gref. The idea is to shift from a tax on oil production to a tax on “the right to produce oil”. Government officials said that such a change could be justified, since Russian companies let a very large percentage of their wells stand idle compared with international majors and license payments are “mere kopeks” (according to the head of the tax policy department at the Finance Ministry).

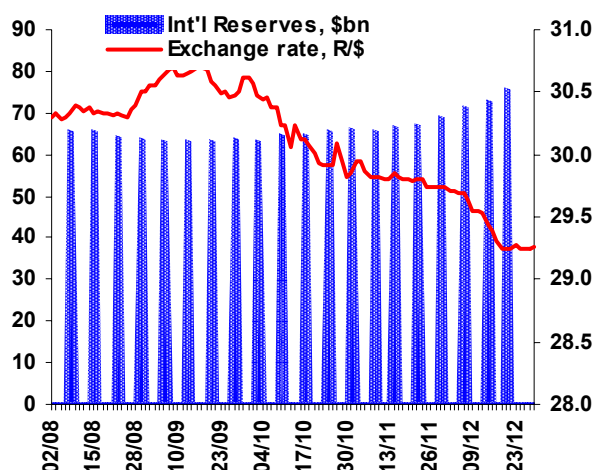
The proposal seems to revive an earlier MEDT draft, and the rates for the new tax, proposed in that draft, would be ruinous for Russian oil companies. But it is

not clear whether government officials would call for such rates to be imposed.

The MEDT is also proposing a relatively humane innovation, which is more subtle differentiation of production tax in view of oil production costs. But prime minister, Mikhail Kasyanov, said last week that he doubts the economic efficiency of such a measure, and spoke in favor of higher export duties as a way of taking away windfall profits. Kasyanov judged that windfall profits start at international oil price levels above \$25 per barrel.

It does look as if Russian oil companies are going to have to share more of their profit with the budget, and portfolio investors are potentially the main casualties of such a change, as dividend payouts will fall. However, potential takeover of some Russian oil companies by international majors is increasingly overshadowing dividend issues, and the remaining Russian companies (mainly Lukoil and Surgut) will have to maintain an investor friendly policy in order to stay competitive with the merged entities, as Russian government officials are bound to understand.

Economic Indicators



Source: CBR

Kasyanov predicts 6.5% GDP growth in FY2003

Prime minister Mikhail Kasyanov said that GDP growth in 2003 will be 6.5-7%, and inflation will be 12%. Kasyanov said that Russia experienced its sixth consecutive year of economic growth in 2003, and that the quality of growth in 2003 was the best since break-up of the USSR. The premier said that economic growth was based on increase of domestic demand, modernization of production and growth of labor productivity. Growth of real disposable income in 2003 was about 14%. Growth of total investments in the Russian economy was about 70% y-o-y.

The government plans to concentrate on reforms in the social sector in 2004, including reform of pensions, social and medical insurance, and also education.

Real effective ruble rate rose by 4.6% in 11M 2003

The real exchange rate of the ruble against a basket of currencies rose by 4.6% in 11M 2003, according to the CBR. The Russian currency rose by 1.7% in real terms in November. Strengthening of the effective rate of the ruble against a basket of currencies will be about 5-5.5% in 2003. Ruble strengthening in nominal terms against the dollar will be 8.5% in 2003.

Ministry of Finance raised R132b from domestic debt market in 11 months

The Ministry of Finance raised R132b from issues of domestic debt against planned R169b in 11 months of 2003. Of the total, R17.4b was raised from GKO issue, R64b from issue of OFZ-FK securities, and R50.5b from OFZ-AD securities. Redemption of government securities totaled R106.4b and the total

Key Macro Figures

CBR refinancing rate, %	16	21/02/03
M2, Rbn	2740.1	1/11/03
M0, Rbn	975.9	1/11/03
CPI, %	1.0	11/03
Inter'l Reserves, \$bn	74.5	19/12/03
One-day MIACR, %	1.11	26/12/03
Exchange rate R/\$	29.45	30/12/03
Exchange rate R/euro	36.69	30/12/03
OFZ yields, % p.a.	5.10	26/12/03
GKO-OFZ duration, days	852.29	26/12/03
Eurobonds Russia 05 YTM	3.29%	26/12/03

volume of internal federal government debt in securities was R663.2b as of December 1, 2003.

Federal budget surplus could be R158b

The federal budget surplus for 2003 could be R10b higher than the planned level of R158b, due to unused resources on accounts of budget cash recipients. The size of the stabilization fund is expected to be R80-90b at the year-end.

Bankruptcy cases reduced by 40% in 9M 2003

According to the Federal Service for Financial Rehabilitation, the number of bankruptcy cases reduced by 40% y-o-y in 2003 from 104 000 to 65 224. A total 22 157 court cases were brought against debtors and bankruptcy proceedings were initiated against 17 000 companies.

Foreign trade surplus was \$49.6b in 10M 2003

The foreign trade surplus was \$49.6b in 10M 2003 against \$38.3b in 10M 2002. Foreign trade turnover was \$167.5b in 10M 2003, up by 23.5% y-o-y against \$135.7b in 10M 2002. Export was \$108.6b, up by 24.8% against \$86.9b in the same period of last year. Import in 10M 2003 rose by 21.1% from \$48.7b to \$58.9b.

Russian export to CIS was \$17.1b in 10M 2003, up by 30.5% y-o-y, and export to non-CIS countries was \$91.5b (growth by 23.8%). Import from CIS rose by 24.2% to \$12.1b, and import from non-CIS rose by 20.3% to \$46.8b.

Largest Russian companies increased sales by 27.8%

Largest Russian tax-payers and monopolies in Russian industry generated R4775.2b sales in 10M 2003, up by 27.8% y-o-y. Their sales in October were R562b, down by 3.5% m-o-m. The share of payments in cash rose from 85.1% to 85.6% m-o-m in October. The share of bills in payments was 4.4%, and the share of payments by barter was 0.7%.

GDP rose by 6.7% in 9M 2003

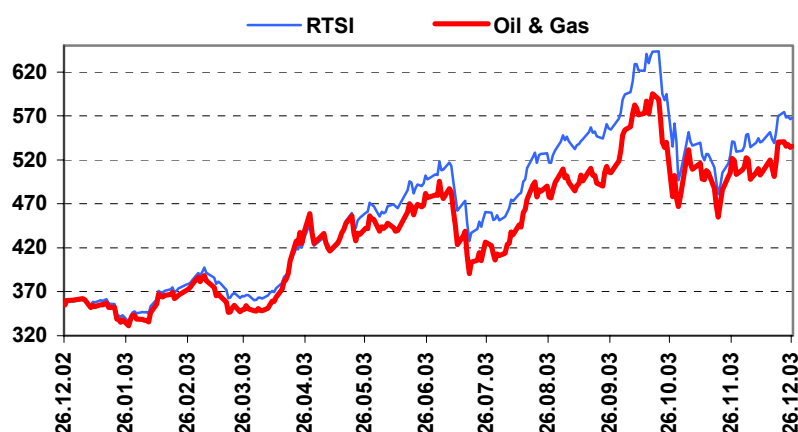
Russian GDP rose by 6.7% in January-September 2003, according to Goskomstat. GDP in current

prices was R9716.3b. The index-deflator of GDP was 115.8% y-o-y. GDP rose by 4% y-o-y in January-September 2002.

GDP in 3Q 2003 was R3688b, up by 6.2% y-o-y and by 16.9% q-o-q. The index-deflator of GDP in 3Q 2003 was 113% q-o-q. GDP growth in 2Q 2003 was 7.2% y-o-y, and 6.8% in 1Q 2003.

The share of goods in GDP structure was 34.7% in January-September 2003 (against 35.7% in 9M 2002), the share of services was 53.4% (52.9%), and the share of net taxes on goods was 11.9% (11.4%).

Oil & Gas Index vs. RTS Index



Oil & Gas Key Figures

Indicator	Value	Wk Change
Urals (\$/b)	27.6	-5.7%
Brent (\$/b)	29.1	-5.6%
OIX (CBOE oil index)	314.7	0.9%
Dow Jones Energy Index	242.9	1.0%
US crude inventory change (EIA data) m bbl	275	0.6%
US gasoline inventory change (EIA data) m bbl	203	0.3%
Tatneft ADR	22.58	2.4%
Lukoil ADR	91.74	1.4%
Surgutneftegaz ADR	29.05	-2.5%
Yukos ADR	43.25	-1.0%
Sibneft ADR	29.40	1.0%

Sector Wrap

- Lukoil said that it has purchased stakes in regional energos
- Capacity of the Baltic Pipeline System (BPS) will be increased to 62mt by the end of 2004.
- Surgutneftegaz in on track to build an export terminal in Batareynaya Bay next year.
- Tatneft will invest \$27m in Syria.
- The Gazprom BoD approved a date in February for its R10b (\$333m) bond placement.
- Rosneft, Gazprom and Surgutneftegaz created a consortium for oil and gas development in East Siberia and Sakha-Yakutia.

Sector Statistics

Issue	Issue RTS Code	Mid Market Price, \$	Weekly Change, %	Weekly Volume, \$mln	Market Cap, \$mln	52 week Low, \$	52 week High, \$	P/S 02	P/E 02
LUKoil com	LKOH	22.925	1.2	17.086	19 537.44	13.610	24.550	1.46	10.36
Megionneftegaz com	MFGS	12.225	-0.4		1 380.47	8.000	14.800		
Megionneftegaz pref	MFGSP	5.925	0.0			3.450	7.250		
Sakhalinmorneftegaz com	SKGZ	4.100	13.9		250.90	2.350	2.750		
Sakhalinmorneftegaz pref	SKGZP	2.521	-0.9	0.001		1.400	3.000		
Sibneft com	SIBN	2.915	-1.1	0.209	13 654.94	1.820	3.150	2.82	13.00
Surgutneftegaz com	SNGS	0.591	-0.8	3.577	23 929.32	0.287	0.607		
Surgutneftegaz pref	SNGSP	0.378	4.8	5.943		0.210	0.390		
Tatneft com	TATN	1.125	3.7	0.508	2 500.21	0.721	1.355	0.72	7.08
Tatneft pref	TATNP	0.568	0.9	0.029		0.435	0.740		
Udmurtneft com	UDMN	212.500	0.0		614.46	103.000	217.000		
Udmurtneft pref	UDMNP	145.000	11.5			79.000	127.000		
Yukos com	YUKO	10.775	-1.1	3.091	28 814.22	8.820	16.300	2.71	9.67

Lukoil (BUY) likely to keep Iraq contract

Lukoil (RTS: LKOH) CEO Vagit Alekperov discussed participation by the Company in development of the West Kurna-2 oilfield in Iraq with Abdel-Aziz al-Hakim, head of the Temporary Governing Council of Iraq, who was on a state visit to Russia last week. The Iraqi leader said that his country is not hostile to development of West Kurna-2 by Lukoil, but the issue will require negotiations. Abdel-Aziz al-Hakim also noted that Lukoil's work at the field had been broken off by deposed Iraqi leader, Saddam Hussein.

An agreement on development of the West Kurna-2 oil field on PSA terms was signed in March 1997 between the Iraqi Oil and Gas Ministry (25%), Lukoil (68.5%), and two Russian export organizations, which each took 3.25%. The PSA contract has a lifetime of 23 years and can be extended for 5 years.

The field has proven reserves of 6b bbl. Cumulative production during the lifetime of the project could be 4.8b bbl and 56.4bcm of associated gas. Planned capital expenditures for field development are about \$4b. The regime of sanctions with respect to Iraq after the Gulf War did not allow Russian companies to realize oil projects in Iraq.

We keep our long-term BUY recommendation for Lukoil shares.

Lukoil (BUY) to buy regional energos

A Lukoil official said that the company has bought stakes in regional energos and will buy more. The company is in talks on purchase of a stake in Komienergo (RTS: KOEN), while stakes in Nizhnovenergo (RTS: NNGE, NNGEP) and in Volgogradenergo (RTS: VGEN, VGENP) have already been bought in 2003 or earlier. Lukoil's stake in Nizhnovenergo is about 7-9% of voting shares.

Lukoil subsidiaries have production and/or refining operations in the regions served by these energos and the stakes will permit to Lukoil to have a say in restructuring, aiming at better conditions for power supplies to its facilities.

Lukoil (BUY) wins award as best issuer

Lukoil was awarded the prize for "Best Issuer on the Russian Stock Market" in the competition "Best Russian Companies of 2003", organized by the Russian Union of Industrialists and Entrepreneurs together with the Chamber of Commerce and Industry of the Russian Federation. The "Best Issuer" category was established by the Moscow Interbank Currency Exchange (MICEX). Competition organizers said that the prize was awarded based on ownership structure, financial credibility, and stock market performance. Lukoil share trading on the MICEX rose by 124.3% to \$1.35b in October 2003 compared with

October 2002. Lukoil management said that the rise was due to publication of consolidated financial statements for 2Q 2003 and 6M 2003 under US GAAP, as well as upgrade of Lukoil's credit rating by S&P.

Lukoil (BUY) to organize lubricant production in Ukraine

Lukoil is considering alternative projects for production of lubricants in Ukraine, as the Ukrainian government has not yet responded to Lukoil's proposal for creation of a joint venture with Azmol. Azmol is a government-owned company, managed by Naftogaz Ukraine, and it produced 54 493 tons of lubricants in 2002.

Lukoil says that it will choose between three alternative Ukrainian lubricant projects in 1Q 2004, and plans to invest \$15m.

Gazprom (local share BUY) BoD approved bond issue term

A meeting of the Gazprom (SPBEX: GSPBEX) BoD approved the date for a R10b (\$333m) Eurobond issue. The placement will begin on February 3, 2004, and the bond will have a lifetime of three years.

The BoD called for rapid finalization of the company's financial plan, investment program and cost reduction program for 2004 (delay has been caused by debates on how to deal with a major financial deficit next year). The BoD also approved some current Gazprom deals, including purchase of the Lithuanian gas company, Lietuvos Dujos, for \$28m.

Gazprom says that it sold R6b (\$200m) of non-core assets in 2003 and plans to sell a further R3b (\$100m) next year. We keep our BUY recommendation for Gazprom local share market.

Gazprom (local share BUY) offers Belarus gas at higher prices

Gazprom has offered Belarus a contract for gas supplies in 2004 at prices higher than previous Belarus contracts. Some of the gas will be paid for by transit services, carrying Russian gas across Belarus to European markets, and the rest will be paid for in cash. Gazprom supplied 10.2bcm of gas to Belarus in 2003.

Total deliveries to Belarus, including transit to Europe (through the Yamal-Europe pipeline, which supplies Belarus, Poland and Germany), totaled 30.9bcm in 2003 and are expected to reach 31.3bcm in 2004. Transit of gas across Belarus to Europe is expected to be 21.6bcm in 2003 and 23bcm in 2004. Further development of the Yamal-Europe pipeline should increase its capacity to 33bcm per year.

The debt of Beltransgaz to Gazprom for gas supplied in 1999-2002 is \$79m (not including fines). The total debt of Belarus for gas as of November 1, 2003 is \$134.6m. The latest Russian-Belarus agreement envisages payment of this debt over three years.

Rosneft, Surgutneftegaz (HOLD) and Gazprom (BUY) create consortium

Rosneft, Gazprom and Surgutneftegaz (RTS: SNGS, SNGSP) are creating a consortium for oil and gas field development in East Siberia and in Sakha-Yakutia. Total estimated gas reserves in East Siberia are 6000bcm and reserves of oil are 1.7bt. The main fields are Chayandinskoye (1240bcm of gas reserves), Kovyktinskoye (2000bcm of gas reserves), Talakhan (124mt of oil and 47bcm of gas, temporary license owned by Surgutneftegaz), Yurubchensko-Tokhomskoye (1200bcm of gas and 780mt of oil, licenses owned by Yukos and Slavneft), Sobinsko-Payginskoye (170bcm of gas) and Sredne-Botuobinskoye (51.7mt of oil and 547bcm of gas, license owned by Taas-Yuryakh-neft). The consortium plans to set up a unified system of production and export to Western Europe.

Surgutneftegaz (HOLD) to build terminal in Batareynaya Bay

Surgutneftegaz (RTS: SNGS, SNGSP) is expected to commit to construction of a terminal at Batareynaya Bay in Leningrad region when its investment program for 2004 is approved by the BoD. Preparatory work has already been completed. Launch of the terminal will mesh with opening of a hydrocracking plant at Surgut's Kirishi Refinery, allowing export of light products from the facility. The new terminal should be operational before the end of 2004, and investments are expected to total \$320m. Capacity will be 7.5mt of light oil products per year. We keep our HOLD recommendation for Surgut shares.

Yukos (speculative BUY) to double oil exports bypassing Transneft

Yukos (RTS: YUKO) intends to almost double oil exports via non-Transneft routes, from 10.6mt to 19.9mt. Yukos export in 2003 will be 49.5mt, up by 37.5% y-o-y. The volume of export via Transneft will be 29.6mt, and 19.9mt bypassing Transneft. Transport bottlenecks are the main restrictive factor for Yukos production. Yukos intends to produce 88mt in 2004 against 81mt in 2003. We recommend speculative BUY for Yukos shares due to upside to our fair price.

BP to complete purchase of 25% stake in Slavneft

BP is pushing ahead with purchase of a 25% stake in Slavneft from TNK for \$1.35b. The European Commission gave approval for the deal last week. Division of Slavneft between TNK and Sibneft, which bought the company in a joint bid a year ago, should be completed by January 1, 2004. TNK is selling half of its stake to BP, but both halves will eventually be included in TNK-BP.

Alfa Group to buy stakes in refineries in West Europe

Alfa Group, one of the major shareholders of TNK-BP intends to buy stakes in four German refineries, which are owned by PdVSA (Venezuela). Alfa agreed to purchase a 50% stake in Ruhr Oel GmbH (ROG) from PdVSA. ROG is a 50-50 joint venture between BP and PdVSA. ROG controls stakes between 24% and 100% in four German refineries (Gelsenkirchen, Bayern-oil, Miro and Schwedt). Total capacity of these plants is 50mt per year (the ROG share is 23mt). The share of Alfa will be 12-13mt. The deal price will be announced after due diligence.

Financing of Shakh-Deniz to rise by 42% in 2004

The president of BP-Azerbaijan, David Woodward, said that financing of the Shakh-Deniz project will be increased by 42% to \$1081m in 2004 from \$762m in 2003. Expenditures on field development will be \$615m and expenditures on gas export to Turkey will be \$466m (\$550m and \$212m respectively in 2003). BP has a 25.5% stake in Shakh-Deniz and is the operator of the project. Other participants are Statoil (25.5%), the State Oil Company of Azerbaijan (10%), LUKAgip (10%), NICO (10%), TotalFinaElf (10%), and TPAO (9%). Reserves of Shakh-Deniz are 625bcm of gas and 101mt of gas condensate.

Baltic export projects move ahead

Annual capacity of the Baltic Pipeline System (BPS) will be increased to 42mt in March 2004 and to 62mt by the end of the year. The first 12mt of BPS capacity was launched in December 2001 and Transneft (RTS: TRNF) increased capacity to 30mt per year in 2003. Investment to build the initial capacity was \$500m and total cost including the enlargement in 2003 was \$765m. The BPS carries crude oil to export from Timano-Pechora, West Siberia and Kazakhstan. We recommend BUY Transneft preferred shares.

In separate news, Lukoil will increase capacity of its Vysotsk terminal on the Russian Baltic coast, to 12mt per year in 2004, of which 4.7mt should be launched

in March 2004. Investments of Lukoil to the first stage of terminal construction was \$200m.

Noyabrskneftegaz to increase production by 24% y-o-y in 2004

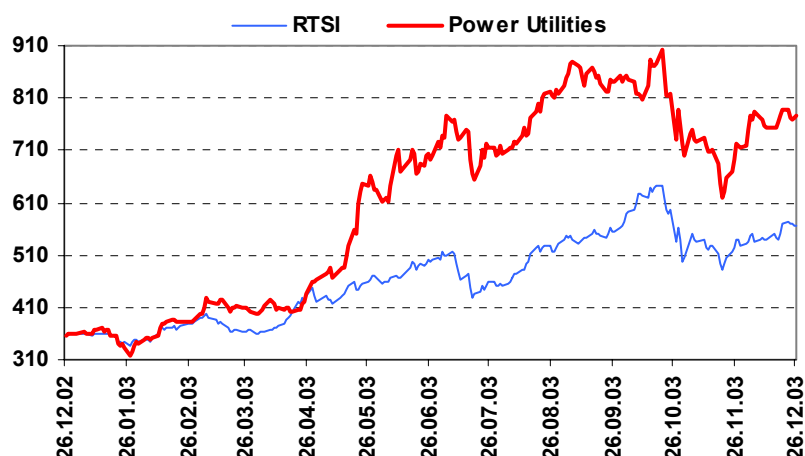
Sibneft (RTS: SIBN) subsidiary Noyabrskneftegaz plans to increase oil production by 24% y-o-y to 39.1mt of crude in 2004. In 2003 the company should produce 31.5mt of oil, up by 19.7% y-o-y. Oil production in 2002 was 26.3mt. The company is increasing production thanks to new technology, increase of well debit and intensive use of horizontal drilling. The company targeted opening of 244 new wells in 2003.

Tatneft (SELL) intends to invest \$27m in Syria

Tatneft (RTS: TATN, TATNP) plans to invest \$27m in Syria after winning a tender for oilfield development there. The company is negotiating to develop a reserve block on PSA basis over a period of 25 years.

Tatneft is also aiming to buy a 65.76% stake in Turkish refining and petrochemicals company, Turpas, in alliance with another foreign company. The results of this tender are due in 1Q 2004 and price of the stake is estimated at \$1.2b. Turpas includes four refineries with total capacity of over 27mt per year and a petrochemical complex. The company accounts for 90% of Turkish oil refining. Tatneft's rival for the stake is the Turkish company Anadolu Ortak Girişim Grubu. We keep our SELL recommendation for Tatneft shares.

Power Utilities Index vs. RTS Index



Power Utilities Key Figures

Sector indicators: median	Russia	Discount to emerging markets
MC / Net sales	0.66	52%
EV / EBITDA	4.01	26%
MC / Owned inst. capacity	86.20	68%
MC / Retail supplies of elec.	13.71	76%

ADRs of Russian power utilities	Last sale	Wk change
RAO UES	28.050	-2.2%
Mosenergo	6.550	-3.7%
Irkutskenergo	6.100	10.9%

Sector Wrap

- UES has tightened its information policy, limiting public statements to three top managers.
- FIGs are eager for more control of Boguchanskaya hydro station.
- The governments wants UES to sell Leader insurance company.
- The UES BoD may examine dividend-related questions on January 30.
- UES management approved the Mosenergo restructuring plan.
- Mosenergo reported preliminary full-year financials, showing overall positive growth.
- Several ministries oppose sale of the government stake in Irkutskenergo in 2004.
- An arbitration court rejected deprivatization of Sayano-Shushenskaya hydro station.
- Dalenergo plans no dividends for 2003.

Sector Statistics

Issue	Issue RTS Code	Mid Market Price, \$	Weekly Change, %	Weekly Volume, \$mln	Market Cap, \$mln	52 week Low, \$	52 week High, \$	P/S 02	P/E 02
Bashkirenergo com	BEGY	0.279	0.2	0.011	294.74	0.131	0.315	0.57	15.97
Irkutskenergo com	IRGZ	0.120	0.1		552.95	0.076	0.126	1.42	86.67
Lenenergo com	LSNG	0.725	-3.3	0.016	605.28	0.265	0.630	0.84	14.83
Lenenergo pref	LSNGP	0.481	0.8	0.012		0.180	0.480		
Mosenergo com	MSNG	0.068	-0.8	0.887	1 893.94	0.031	0.085	1.10	91.94
Permenergo com	PMNG	3.175	-0.8		140.99	2.000	4.250	0.31	16.36
Permenergo pref	PMNGP	3.075	1.7			1.720	3.000		
UES com	EESR	0.283	-1.7	12.151	12 119.70	0.104	0.346	0.80	11.45
UES pref	EESRP	0.255	-2.7			0.091	0.313		
Samaraenergo com	SAGO	0.067	2.3		247.82	0.033	0.074	0.53	66.09
Samaraenergo pref	SAGOP	0.056	0.0	0.012		0.019	0.053		
Sverdlovennergo com	SVER	0.482	4.2	0.023	286.80	0.170	0.300	0.36	35.02
Sverdlovennergo pref	SVERP	0.260	0.0			0.098	0.130		

UES (BUY) tightens information control

UES (RTS: EESR, EESRP) management issued a new ruling on company information policy, by which only the CEO, first deputy CEO and press-secretary can make public comments on company affairs, although other officials can offer comment when empowered to do so by the former three. The point of the initiative, which will require approval by the BoD in January, is to end information leakages and informal statements by company officials, which have been one reason for high price volatility of UES shares in recent months (the main reason for greater volatility has been free float reduction due to strategic purchases).

The ruling reinforces earlier moves by UES management censoring commentary on company affairs from within the company, and requiring top managers to report on any financial transactions with UES shares. The action should be appreciated by investors.

FIGs close in on Boguchanskaya GES

Vedomosti newspaper reported last week that Russian strategic investors are battling for stakes in the Boguchanskaya GES (hydro station). Boguchanskaya, has been under construction for the last 20 years and is still not completed. UES holds a 65% stake in Boguchanskaya GES and tried in 2002 to find investors who would supply \$1b needed for completion of the project. It reported negotiations with RusAL, which promised \$1m (sic) in exchange for a stake in the station and a seat on its board. This offer was treated seriously by UES, which had cordial relations with RusAl at the time, but any deal was blocked by resistance of UES minority shareholders. The incident speeded up adoption of a moratorium on asset deals by UES during company restructuring.

According to Vedomosti, RusAL and some other Russian financial-industrial groups (FIGs) have now revived talks with UES and the Krasnoyarsk regional administration on schemes for financing completion of the hydro station. The other interested FIGs are Interros, MDM and EvrazHolding, all of which (like RusAl) have or plan to have industrial facilities in the region with large energy needs, which could be largely and cheaply met by Boguchanskaya. Vedomosti suggested that RusAL may have accumulated a 26% stake in Boguchanskaya on the market, based on an earlier statement by RusAl CEO Oleg Deripaska.

However, it is hard to see how UES could cede major share stakes in Boguchanskaya to FIGs as a way of raising cash, since the GES is slated for merger in one of the hydro WGCs, all of which the government intends to control after completion of sector reform

and UES break-up. Some mechanism for increasing the government stake in Boguchanskaya GES prior to WGC transfer to a single share will be needed, and this should be different to sale of company shares to other investors.

UES likely to sell insurer

The UES BoD is due to discuss sale of the insurance company Leader, which the company fully controls, at a meeting in January 2004. Leader has insured all kinds of risks of UES and its subsidiaries since 2001, when UES bought it from another insurance company, ROSNO. Leader effectively acts as an intermediary between UES and other insurance companies, and has remained close to ROSNO: the UES deputy CEO Leonid Melamed is also the CEO of ROSNO, which remains the management company for Leader.

The plan to sell Leader was initiated by the government, which holds a 53% stake in UES, and which approved purchase of Leader in 2001. The decision to sell it may be due to efforts of UES minority shareholders, who favor disposal of non-core businesses. Complexity of integration of Leader into UES and doubts about ultimate efficiency of its integration make us believe that it will indeed be sold.

UES may propose dividend coefficient on January 30

The UES BoD may determine the coefficient for 2003 dividend calculation at a meeting on January 30, 2004. The coefficient will be used to calculate 2003 dividend payments, which the board will propose later and which must be approved at the spring AGM. A new dividend policy approved by UES in 2003 requires use of EBITDA as one of the multiples for dividend calculation, such that UES and its subsidiaries could pay up to 100% of RAS net profits as dividends. But the final decision is dependent on a specific coefficient, which must be set by UES BoD each year, making it harder to predict dividends. However, UES officials said earlier that 2003 dividends could be the same as for 2002, and we think that doubts over the coefficient will not have an effect on the UES share price.

Mosenergo (BUY) reports preliminary 2003 results

Mosenergo (RTS: MSNG) reported some preliminary financial results for 2003 at a conference last Thursday. Revenues are estimated at almost \$3b, up by 36% from 2002 mainly due to tariff rises, though growth of output also played a role. In 11M 2003 Mosenergo electricity production increased by 7% and heat output rose by 10%. Operating profit should be 56% higher y-o-y due to rapid tariff increases and cost cutting. Net profit under RAS may exceed \$50m,

which would be 150% higher than the previous year. However, company officials said that the picture could change in the last days of the year, as almost half of the net result depends on receipt of property rights to some grid facilities, and this transaction has not yet been completed.

Company officials also said that dividends will likely be unchanged from 2002, when they were R0.018 (0.06 cents). About \$30m of net profit will be used to finance capex.

Mosenergo FY 2003E results (RAS)

	FY03E, \$m	FY02, \$m	Change, %
Net sales	2 291.4	1 688.8	36%
Operating profit	228.2	146.5	56%
- Operating margin	10%	9%	15%
Net profit	52.2	20.6	153%
- Net margin	2%	1%	87%

Source: Company data, RMG estimates

It was reported that the Mosenergo BoD approved buyout of up to 10% of company stock on the market for sale to a strategic investor or cancellation. The move was announced earlier by company management and was supported by shareholders. Mosenergo plans to hold a tender in January for a share price appraiser, and is expected to choose a company with an international reputation. A final decision on the share buyout will be taken by the Mosenergo BoD after examination of the appraisal results. We estimate that Mosenergo stocks should soon achieve their fair level of \$0.087.

UES management supports Mosenergo restructuring plan

A meeting of UES management last Monday approved the restructuring plan for Mosenergo. UES stressed that the Mosenergo restructuring plan follows the general restructuring plan for energos, proposed by UES, and also takes account of earlier agreements between the power holding, as the major Mosenergo shareholder, and governments of Moscow city and Moscow region. The latter two will be allowed to take controlling stakes in two electricity distribution companies, which will be set up from distribution assets of Mosenergo when the company is broken into business units. Four Mosenergo power stations will be divested into wholesale generating companies while all other company generating assets will be united in a single territorial generating company (TGC), one of the largest by installed capacity in the future power system. Gazprom, which reportedly owns a 16% stake in Mosenergo, may well inherit the controlling stake in this TGC. The UES BoD plans examination of the Mosenergo restructuring project at a meeting in January 2004.

Ministries oppose sale of 40% in Irkutskenergo (Spec BUY)

According to the Russian Property Ministry, there has been a negative reaction by other ministries to proposed sale of the government stake in Irkutskenergo (RTS: ITGZ) next year. The government holds a 40% stake in Irkutskenergo while as much as 55% (a controlling stake) is owned by a consortium of Russia's two biggest aluminum holdings, RusAI-SUAL. Privatization of the government stake was mooted in 2002-2003 and is strongly supported by Irkutskenergo management, since it would increase the RusAI-SUAL stake to over 75%.

The Property Ministry put Irkutskenergo privatization on the agenda for 2004, despite failed privatization efforts in 2003. But other ministries and agencies, including the Ministry for Economic Development and Trade, the Energy Ministry, the Finance Ministry, the Russian Federal Property Fund and the Federal Energy Commission, are opposed. They believe that Irkutskenergo should first be restructured, taking account of national interests. This refers mainly to transfer of the energo's high-voltage transmission assets and dispatching units to state ownership.

Cancellation of 2004 privatization would be negative news for the Irkutskenergo share price, though the last word is still ahead. We change our recommendation on the stock from HOLD to Speculative BUY. Major undervaluation, based on fundamentals, is offset by risks associated with RusAI-SUAL control.

Deprivatization of Sayano-Shushenskaya GES (BUY) rejected

The arbitration court in the Republic of Khakassia rejected an application by regional government for cancellation of 1990s privatization of Sayano-Shushenskaya GES (hydro station) (RTS: SSHG, SSHGP). UES received over 80% of the company stock at privatization in 1993.

Deprivatization would have set a dangerous national precedent and its rejection was expected. The Khakassia government was clearly acting on behalf of RusAI, which wants continuation of cheap electricity supplies for its aluminum smelting plants in the region. The regional government has said that it will not seek deprivatization if UES agrees to keep low tariffs for Sayano-Shushenskaya power until 2020.

We continue to recommend shares of Sayano-Shushenskaya GES as good long-term investments in the power sector.

Dalenergo plans no dividends for 2003

Dalenergo CEO Viktor Myasnik said last week that the company BoD will recommend not to pay dividends for 2003 despite a positive net result in the P&L. The company estimates RAS net profit at R10-15m (\$300 000 - \$500 000) for 2003, which is double the figure in 2002, but still represents almost zero net margin. Dalenergo paid only preferred dividends for 2002. The company charter makes a payout on preferred stock obligatory.

Lukoil takes energo stakes

Lukoil said that it has accumulated stakes in Volgogradenergo (RTS: VGEN, VGENP) and Nizhnovenergo (RTS: NNGE, NNGEP) and plans to

increase them. The company also said that it will take a stake in Komienergo (RTS: KOEN, KOENP). The Lukoil stake in Nizhnovenergo was estimated last week by the energo CEO Alexei Sannikov at 7-8%, though it may be greater, since a stake of up to 25% was reportedly controlled by Prosperity Capital, which is the probable seller of shares to Lukoil. Lukoil's stake in Volgogradenergo is estimated at 25-30%, and this is confirmed by presence of four Lukoil representatives in the 11-seat BoD. The oil company seems to have no shares as yet in Komienergo. Negotiations are reportedly underway between Lukoil and a Komienergo strategic minority, probably SUAL, which has an estimated 30% stake.

Power utilities report 9M 2003 results (RAS)

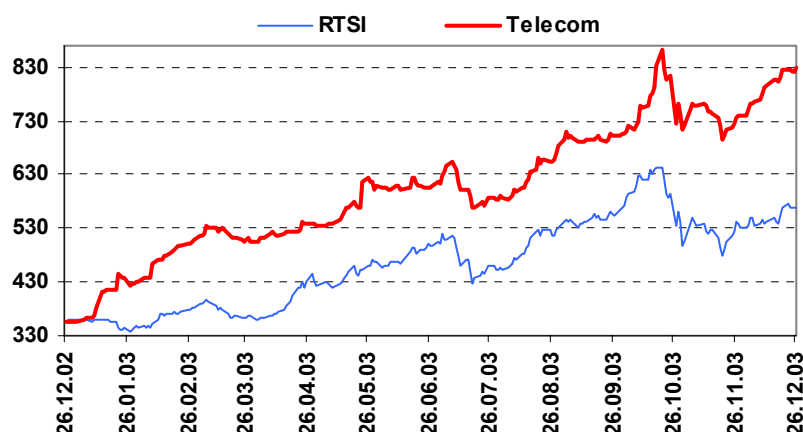
The following table shows key results reported by power sector companies for 9M 2003. We include our view of the **DYNAMICS** of these results, which may affect development of stocks in the short to medium terms.

Company	Dyna- mics	Net sales		Operating profit			Net profit			Receivables		Payables and debt	
		9M03, \$m	YOY, %	9M03, \$m	YOY, %	margin, %	9M03, \$m	YOY, %	margin, %	9M03, / FY02, \$m	/ FY02, %	9M03, / FY02, \$m	/ FY02, %
Altaienergo	pos	163	38%	6.3	n/a	4%	-10.3	n/a	neg	74	-4%	167	8%
Arkhenergo	neg	124	26%	-4.9	n/a	neg	-0.3	n/a	neg	76	-14%	103	-7%
Astrakhanenergo	neut	55	38%	-0.5	n/a	neg	-2.1	n/a	neg	35	4%	31	-4%
Bashkirenergo	neg	413	13%	28.3	-42%	7%	0.0	-100%	0%	224	0%	211	8%
Chelyabenergo	pos	413	22%	38.8	19%	9%	0.6	-73%	0%	138	-7%	186	-7%
Cherepetskaya GRES	neg	46	12%	5.2	-45%	11%	3.0	-42%	7%	7	-64%	10	-42%
Chitaenergo	neut	95	19%	5.5	-21%	6%	1.8	-3%	2%	9	-9%	12	-6%
Dalenergo	pos	223	44%	12.2	n/a	5%	0.3	n/a	0%	75	-12%	184	1%
Irkutskenergo	neg	337	21%	7.9	-45%	2%	-7.8	n/a	neg	163	-5%	126	-3%
Ivenergo	neut	85	27%	4.0	-28%	5%	2.7	36%	3%	17	-43%	13	-37%
Kalugaenergo	pos	67	39%	3.1	81%	5%	0.8	>1000%	1%	6	5%	6	39%
Khabarovskenergo	pos	269	33%	4.1	n/a	2%	6.4	n/a	2%	156	-2%	262	9%
Kirovenergo	neut	140	24%	7.3	-6%	5%	1.1	n/a	1%	72	23%	65	14%
Kolenergo	neut	167	23%	11.6	-30%	7%	1.5	-68%	1%	32	-21%	48	-3%
Komienergo	neut	177	18%	9.9	-1%	6%	-3.6	n/a	neg	58	-7%	75	0%
Konakovskaya GRES	pos	78	36%	13.5	406%	17%	5.3	124%	7%	20	-19%	33	-25%
Kostromskaya GRES	neut	114	50%	2.4	-55%	2%	-4.6	n/a	neg	44	23%	60	0%
Krasnoyarskenergo	neg	333	17%	13.3	-55%	4%	4.5	n/a	1%	74	12%	139	-4%
Kubanenergo	pos	259	39%	12.9	>1000%	5%	-0.2	n/a	neg	75	2%	123	-2%
Kurganenergo	pos	78	31%	12.6	n/a	16%	11.5	n/a	15%	85	5%	96	-12%
Kurskenergo	pos	110	37%	10.4	29%	9%	6.4	1%	6%	19	17%	11	-27%
Kuzbassenergo	neut	406	22%	35.9	-4%	9%	-1.1	n/a	neg	150	29%	272	36%
Lenenergo	neut	613	27%	39.9	-4%	6%	-6.6	n/a	neg	158	24%	230	43%
Magadanenergo	neut	38	22%	-7.8	n/a	neg	0.6	n/a	2%	31	5%	41	-9%
Mordovenergo	neut	56	29%	1.3	-52%	2%	0.0	n/a	neg	21	-8%	21	-2%
Mosenergo	pos	1 578	46%	81.4	n/a	5%	-34.5	n/a	neg	357	0%	549	25%
Nizhnovenergo	neut	309	26%	19.0	-30%	6%	4.3	n/a	1%	85	-17%	109	-18%
Novosibirskenergo	pos	232	35%	10.4	233%	4%	-5.6	n/a	neg	55	-2%	156	23%
Omskenergo	pos	196	45%	-2.5	n/a	neg	-6.1	n/a	neg	80	8%	129	12%
Orelenergo	pos	52	42%	2.5	n/a	5%	0.3	n/a	1%	25	-7%	46	-2%

Company	Dynamics	Net sales		Operating profit			Net profit			Receivables		Payables and debt	
		9M03, \$m	YOY, %	9M03, \$m	YOY, %	margin, %	9M03, \$m	YOY, %	margin, %	9M03, \$m	/ FY02, %	9M03, \$m	/ FY02, %
Pechorskaya GRES	pos	33	71%	7.1	n/a	21%	1.9	n/a	6%	12	13%	21	-11%
Permenergo	pos	375	18%	45.0	99%	12%	7.5	>1000%	2%	104	-11%	111	-17%
Pskovenergo	pos	41	48%	1.1	n/a	3%	-0.6	n/a	neg	6	5%	7	16%
Rostovenergo	pos	229	29%	23.5	134%	10%	13.0	541%	6%	48	-46%	48	-51%
Samaraenergo	pos	457	45%	47.3	>1000%	10%	5.6	n/a	1%	76	18%	38	-50%
Stavropolskaya GRES	pos	96	37%	11.6	120%	12%	3.5	n/a	4%	57	-6%	73	-16%
Sverdlovenegero	neg	580	17%	27.5	-43%	5%	-6.3	n/a	neg	184	-2%	260	3%
Tambovenegero	pos	76	36%	5.8	22%	8%	0.1	>1000%	0%	30	-7%	38	-1%
Tulenergo	pos	165	30%	16.5	475%	10%	5.7	n/a	3%	34	-3%	28	-5%
Tverenergo	pos	120	43%	7.5	199%	6%	-4.1	n/a	neg	50	-12%	56	-3%
Udmurtenergo	pos	127	31%	7.3	82%	6%	1.6	n/a	1%	13	-7%	10	-1%
UES	pos	1 293	10%	730.7	3%	57%	633.5	-51%	49%	1 320	19%	669	-70%
Vladimirenergo	pos	112	42%	4.3	942%	4%	-0.4	n/a	neg	24	0%	32	-12%
Vologdaenergo	pos	198	22%	25.3	7%	13%	9.9	-2%	5%	17	12%	30	26%
Volzhskaya GES (Zhigulevsk)	pos	37	52%	11.9	602%	32%	7.7	n/a	21%	21	-3%	15	-44%
Voronezhenergo	neut	147	30%	2.7	-23%	2%	-17.7	n/a	neg	41	25%	55	53%
Votkinskaya GES	pos	12	77%	3.5	218%	29%	1.6	n/a	14%	3	25%	1	-24%
Yakutskenergo	neut	191	14%	8.5	-18%	4%	-7.2	n/a	neg	105	37%	167	43%
Yarenergo	pos	158	39%	6.4	26%	4%	5.8	165%	4%	24	1%	33	7%
Zeyskaya GES	pos	21	71%	4.9	858%	23%	1.3	n/a	6%	8	-18%	3	-44%

Source: Company reports, RMG estimates

Telecom Index vs. RTS Index



Telecoms Key Figures

Sector indicators: median	Russia	Discount to emerging markets
EV / EBITDA	4.2	9%
EV / Net sales	1.5	26%
EV / Access lines	136	86%
EBITDA / Access lines	32	87%

ADRs of Russian telecoms	Last sale	Wk change
Rostelecom	12.380	-2.9%
MTS	78.200	-0.6%
Vimpelcom	67.650	2.8%

Sector Wrap

- Monthly tariffs for households may be raised in line with inflation in 2004.
- Number of fixed-line and mobile users in Russia equalized in 2003.
- South Telecom announced last week that company capex in 2003 was \$277m versus expected \$163m.
- MGTS announced a network digitalization plan using own funds, borrowings (\$800m) and proceeds from sale or lease (\$800m) of real estate.
- Center Telecom bought alternative operator Rosnet for access to the promising corporate market.
- Sky Link bought MC-Direct (part of Accord-Tel holding), which owns controlling or smaller stakes in 39 NMT-450 regional cellular operators, for \$20-30m.
- Turkish cellular operator Turkcell is planning to enter the Ukrainian market, threatening MTS business in Ukraine. We downgrade MTS recommendation from BUY to HOLD due to this and other recent developments.

Sector Statistics

Issue	Issue RTS Code	Mid Market Price, \$	Weekly Change, %	Weekly Volume, \$mln	Market Cap, \$mln	52 week Low, \$	52 week High, \$	P/S 02	P/E 02
Center Telecom com	ESMO	0.344	0.7	0.048	668.55	0.235	0.357	1.28	19.33
Center Telecom pref	ESMOP	0.243	3.2			0.158	0.256		
Dalsvyaz com	ESPK	1.155	0.2	0.003	131.72	0.657	1.200	0.77	20.91
Dalsvyaz pref	ESPKP	0.755	0.0			0.460	0.770		
Moscow City Telephone com	MGTS	12.500	9.6	0.054	1 115.21	6.200	12.000	3.46	30.93
Moscow City Telephone pref	MGTSP	8.725	2.6	0.013		3.400	7.000		
North West Telecom com	SPTL	0.404	-1.0	0.172	345.59	0.345	0.450	1.04	31.42
North West Telecom pref	SPTLP	0.293	3.0	0.145		0.195	0.291		
Rostelecom com	RTKM	2.051	-4.0	1.497	1 822.38	1.122	2.235	2.25	1.86
Rostelecom pref	RTKMP	1.385	0.7	0.440		0.760	1.500		
Siberia Telecom com	ENCO	0.035	3.9	0.486	511.35	0.023	0.036	1.31	33.84
Siberia Telecom pref	ENCOP	0.025	6.0	0.025		0.016	0.024		
South Telecom com	KUBN	0.095	4.3	0.261	359.98	0.069	0.103	1.07	7.23
South Telecom pref	KUBNP	0.083	0.7			0.050	0.080		
Ural Svyazinform com	URSI	0.038	0.1	0.019	1 374.50	0.013	0.038	2.91	46.64
Ural Svyazinform pref	URSIP	0.023	-0.2	0.069		0.008	0.026		
Volga Telecom com	NNSI	2.535	3.0	0.056	755.12	1.203	2.540	2.16	15.91
Volga Telecom pref	NNSIP	1.670	2.1	0.026		0.800	1.700		

Tariff growth may be equal to inflation in 2004

Telecom minister Leonid Reiman said last week that Svyazinvest wants to raise monthly household tariffs for local services in line with inflation, although 2004 tariff increases have not yet been ratified by the Antimonopoly Ministry (MAP). The Russian government is targeting inflation under 12% in 2004, equal to the level in 2003. We incorporated 12% growth of local monthly tariffs, which are the main revenue source of regional telecoms, into our DCF model. The model also assumed that a small percentage of RTO customers would switch from fixed tariffs to a per-minute system in 2004, which should lead to slight reduction of overall monthly payments (the new telecom law, which comes into force on January 1, 2004, allows households to choose between fixed and per-minute systems, and results to date suggest that users pay less under a per minute system).

Number of fixed-line and mobile subscribers equalizes

Reiman also said last week that the number of fixed-line and mobile subscribers in Russia equalized in 2003 at 36-37 million each. Svyazinvest launched 3 million new fixed lines in 2003, spending \$1.5b, versus 1 million lines annually in previous years. The monopolist is planning to launch 4 million lines in 2004. The number of telephone lines in rural areas quadrupled in 2003, but some rural areas are still without any phone service.

South Telecom (BUY) announces high capex for 2003

South Telecom (RTS: KUBN, KUBNP) announced last week that it estimates capex spending of \$277m (R8.3b) for the whole of 2003, which is almost 70% higher than previously announced capex guidance (used in our DCF model). The company also said that operating costs will be R9.8b (\$320m), which is less than we expected. We will incorporate the new figures in our model, but we keep our BUY recommendation on company stocks (\$0.113 target price per common share) for the present. We do not expect much difference between the company's IAS and RAS results due to small exposure of South Telecom to the cellular market and other value-added services.

In other negative news, company revenues from international long-distance traffic are expected to decrease by 4% due to loss of market share to alternative operators and insufficient traffic growth. Payments to Rostelecom dropped to 14% from 15% of total expenses, but salary expenses grew from 32% to 33% of total expenses despite 7% y-o-y staff reductions in 2003.

Pre-tax profit will decline by 7% y-o-y in 2003 as sale of Kuban GSM brought about \$40m in non-operating gains in 2002.

The company is targeting net profit of \$55m, representing 7% y-o-y growth, thanks to tax savings that are little higher than our prediction of \$50m. Revenues are expected to be \$445m, which is in line with our estimates.

South Telecom FY03 financial forecast (RAS)

	FY03E, \$m	FY02, \$m	y-o-y change, %
Revenues	445	336	27%
- local	104	132	46%
- domestic LD	169	142	19%
- international LD	32	32	-4%
Operating expenses	328	250	26%
Operating profit	117	86	36%
-operating margin	26%	26%	
EBITDA	152	116	32%
- EBITDA margin	34%	33%	
Pre-tax profit	71	77	-7%
Net profit	56	52	7%
- net margin	13%	15%	

Source: Company data; RMG estimates

In other South Telecom news, the company appointed Ivan Ignatenko, the former head of one of the company's branches, as South Telecom CEO. Vladimir Gorbachev quit as company CEO after his election as a deputy in the State Duma, where he is expected to lobby interests of Svyazinvest. We view the management reshuffle as neutral, since the company's strategy is determined by Svyazinvest anyway.

MGTS (HOLD) announces investment plan

MGTS (RTS: MGTS, MGTSP) announced plans to invest \$1.6b in network digitalization over the next few years, using own funds, borrowings (\$800m) and proceeds from sale or lease of redundant real estate (\$800m). The company said earlier that network modernization could be carried out in 3-5- years if an IPO is goes ahead in 2004, but will take 10 years if Sistema Telecom and Svyazinvest (the biggest shareholders of MGTS) cannot agree on an IPO.

The MGTS digitalization level of 17% is the lowest among Russian telecoms and network modernization is a priority for company's new CEO Andrei Smirnov. The MGTS modernization plan includes reconstruction of 350 automatic telephone exchanges, with changeover from analog to digital. The plan will require investment of about \$300 per line, while average cost of creating a new line is only \$200 at other RTOs. Planned capex as a percentage of revenues (more than 30%) also look excessive.

Lease or sale of redundant real estate seems a good way to finance a part of investments in modernization

and makes the company's investment plan more realistic. But huge scale of the modernization task suggests that \$1.6b financing may be insufficient. We currently reiterate our HOLD recommendation for MGTS stock with fair price at \$12 pending the outcome of IPO negotiations between Sistema Telecom and Svyazinvest.

MGTS said last week that it is planning to start switching analog lines to digital lines in January 2004, and that the process will be accompanied by changing of some telephone numbers.

MGTS installs internet coin-box telephones in Moscow

In other MGTS news, the company started installation of internet coin-box telephones, which allow internet access and sending of text and multimedia (MMS) messages in addition to usual telephone services. The tariff for internet use is \$0.4 per minute for the first 5 minutes and less than \$0.4 thereafter, which exceeds rates offered by Moscow internet cafes. The company is planning to install the first 12 internet coin phones in test mode this January, and plans to install a total 1000 sets in Moscow.

Center Telecom (HOLD) begins acquiring alternative operators

Center Telecom (RTS: ESMO, ESMOP) BoD approved a plan to acquire full control of the alternative operator, Rosnet. The acquisition will be a key step in the company's strategic plan to enter the promising alternative market. Rosnet serves corporate clients in Moscow, St. Petersburg and other regions in central European Russia.

Rosnet turnover was \$11m in 2002, and Vedomosti newspaper reported that Center Telecom will pay \$30-35m for the company.

Rosnet provides services to the Central Bank of Russia, Detsky Mir (retail company), the State Pension Fund, Sberbank and others. Comincom-Combella and Telenor were involved in acquisition talks with Rosnet a few years ago, but agreement was not reached.

Center Telecom managers said recently that the company's capex for 2004 envisages purchase of some alternative operators, although they did not name an amount. We see Center Telecom's debut on the alternative market as very positive.

In other Center Telecom news, the company said that it spent more than \$17m to launch 8 million lines with a new area code (498) in Moscow region.

CEO of Rostelecom (HOLD) comments on development

Dmitry Yerokhin, the CEO of Rostelecom (RTS: RTKM, RTKMP), said in an interview with Vedomosti newspaper that EBITDA margin is expected to be 40% in 2003 and 2004, exceeding market expectations.

Yerokhin also said that Rostelecom is discussing increase of its stake in internet provider RTComm.ru (Rostelecom lost control of the provider when it sold RTK-Leasing). He said that agreement on such increase has almost been reached.

According to Yerokhin, Rostelecom's main problem is excessive spending on analog networking, which constitutes 70% of total networking and generates only 30% of revenues.

Yerokhin also commented on termination fees of CIS operators, which are expected to decline in the future.

We keep our HOLD recommendation on Rostelecom with target price of \$2.12 for common shares.

Sky Link acquires MC-direct

Sky Link, recently created by RTDC to run a project for development of the CDMA (IMT-MC-450) cellular standard in Russia based on the NMT-450 standard, is speeding up its expansion. The company purchased MC-Direct (part of Accord-Tel holding), which owns controlling or smaller stakes in 39 regional NMT-450 cellular operators. The company did not comment of the deal amount. The company is also not commenting on creation of a nationwide cellular system based on CDMA operators.

Vedomosti newspaper said that Sky Link paid \$20-30m for MC-Direct and that Accord-Tel preliminarily transferred all its assets into MC-Direct. Sky Link also has the right to demand all debts (\$50m) owed to Accord-Tel by its subsidiaries. Vedomosti's source said that MC-Direct was acquired taking debts into account.

Sistema AFK acquired 50% of Sky Link in November. We do not expect that the project will be a serious rival to the Big Three GSM operators, although mobile data transmission services may find a small niche. Currently 40 000 cellular subscribers use CDMA-450 standard in Russia, most of them in St-Petersburg.

Vimpelcom (BUY) redeems notes in advance

Vimpelcom (NYSE: VIP) redeemed its 2005 convertible notes at \$67.2 ahead of schedule. The company said that 98% of the notes were converted by holders into shares: the notes were converted into 2 449 011 ADS, as a result of which the total

outstanding amount of ADS increased by 4.6%. Vimpelcom placed a five-year \$75m note issue on the NYSE in 2000. We reiterate our BUY recommendation for Vimpelcom shares.

MegaFon to place bonds

The BoD of MegaFon, the only non-traded Big Three operator, decided to place \$50m of three-year local bonds on the MICEX. MegaFon plans capex at \$365m in 2003 and \$590m in 2004.

The company announced borrowing plans earlier, but we expected that MegaFon's current shareholder troubles would complicate the plans. Approving of the \$50m borrowing plans by shareholders may indicate that the shareholder battle will be resolved sooner than expected. We believe that Alfa Group, which recently acquired a blocking stake in MegaFon and also owns Vimpelcom, will be able to influence future development of MegaFon.

MTS (HOLD) under pressure in Ukraine and at home

Vedomosti newspaper reported last week that the Turkish cellular operator Turkcell (owned by a Ukrainian businessman), has agreed with the Ukrainian government on investment of \$400m in development of cellular networking in Ukraine through creation of a joint venture with the local operator Digital Cellular Communication (\$100m) and acquisition of a controlling stake in Ukrtelecom, a monopolist in fixed telephony, owned by the government.

There are currently four GSM operators active on the Ukrainian market: UMC (owned by MTS), Kiev Star, Golden Telecom and WellCom. These four have total 5.8 million subscriber base. Turkcell is targeting a subscriber base of 3 million.

Meanwhile MTS reported last week that the subscriber base of its Ukrainian subsidiary UMC soared by 76% to 3 million subscribers in 2003 (mostly on the back of the recently launched pre-paid Jeans tariff, which is used by 30% of UMC subscribers). UMC thus holds 48% of the Ukrainian mobile market. MTS plans to invest \$150m in developing UMC in 2004. Ukraine accounted for 17% of both revenues and net income of MTS in the third quarter of 2003.

We think that future subscriber base growth of UMC may be more modest due to increasing competition on the local market and government support for Turkcell. There was also some concern about \$600m investment spending in the third quarter, announced by MTS, which brings overall company investments to \$1.6 for 2003. The figure is higher than expected. MTS said that it will spend 30% of revenues on capex in 2004. MTS saw decline of its total market share from 38% in October to 37% in November, due to fall of its Moscow subscriber base by 2%.

Following recent developments, we decided to downgrade our recommendation for MTS from BUY to HOLD. Company ADRs are traded with 7% premium to our fair price of \$83. However, financials remain strong and we believe that overall prospects for the company are good.

Severstal (HOLD) buys Rouge, misses Dunafer, considers further acquisitions

Severstal (RTS: CHMF) outbid US Steel to buy the US steelmaker, Rouge Industries, for \$285.5m. The purchase should be completed before January 31. Severstal is expected to deliver slabs for processing by Rouge Industries, helping Severstal to avoid antidumping restrictions on Russian steel exports to the US. Severstal also has plans to either modernize or close current blast-furnace and converter production by Rouge, shifting to electric arc steel production. The company plans to invest about \$40-45m annually for this purpose. Total investment needs of Rouge for the next few years are \$200-300m.

Acquisition of Rouge represents a successful start to Severstal's foreign acquisition strategy. It also gives the Russian company a new market with established customers taking high-value added products (automobile sheet), and not only hot- and cold-rolled steel.

However, Severstal lost a tender to buy Dunafer, the biggest Hungarian steelmaker. The Severstal bid was beaten by alliance of Ukrainian companies, which also overcame the international steel giant, LNM Group. Dunafer was bought for \$472m.

In separate news, a Severstal source said that the company may bid for control of Krivorozhstal, the largest Ukrainian steel producer, which has about 20% of the local market in Ukraine. The Ukrainian government currently owns 100% of Krivorozhstal. According to Vedomosti, the price may be as high as \$1b.

Krivorozhstal produced about 6.9mt of crude steel in 2002, compared with 9.6mt produced by Severstal. Their combined output of 16.5mt would be equal to that of Thyssen Krupp, the German steel giant, which took seventh position worldwide in 2002 (Severstal was 19th and Krivorozstal was 26th).

Nizhnekamskneftehim (BUY) borrows \$150m

Citibank and Nizhnekamskneftehim (RTS: NKNC, NKNCN) are to sign a \$150m credit agreement. The Russian company will use the money to build a new facility to make polypropylene (PPL), which is used in the automobile and construction industries. The company plans to launch the plant in 2006 and to produce about 120 000 tons of PPL annually.

Nizhnekamskneftehim also reached agreement in principle with the Korean company LG on collaboration to produce polystyrene foam in Russia. Project cost is estimated at \$40-50m and final agreement is expected in February 2004.

Power Machines borrows \$35m

Power Machines (RTS: SILM) took a \$35m long-term credit from the EBRD. The borrowing is the first tranche of an overall \$81.5m facility. The \$35m will be used by Power Machines to finance export contracts. The other \$46.5m is expected to be invested in modernization of equipment.

EvrazHolding buys GOK

EvrazHolding, the largest Russian steel holding, acquired 87.4% stake of Vysokogorsk GOK (ore mine and concentrator). The acquisition was paid for using a part of funds, which were raised from a \$175m Eurobond placement. Vysokogorsk is the main supplier of ore for the Nizhny Tagil steel plant (RTS: NTMK), which is controlled by EvrazHolding.

Irkut in talks with EADS

The aerospace manufacturer Irkut is in talks with EADS (European Aeronautic Defence and Space Company) on sale of a minority stake. Gregor von Kursell, an EADS official with responsibility for investor relations, confirmed his company's interest in the Russian aircraft maker, but added that serious negotiations will not start until next year.

Sergei Tsilev, vice-president of Irkut, said that his company will carry out a road-show in Europe and Asia before going ahead with planned IPO of a 20% stake.

Aeroflot (HOLD) to improve restructuring

The Aeroflot BoD will revise its fleet restructuring plan in order to address rapid increase of passenger numbers. The company has decided to purchase three A-321 airliners instead of two A-319s and A-320s. since the A-321 has 170-180 seats compared with only 150 seats on the other two planes. The BoD will be able to make the change to its restructuring plan without calling an EGM.

Norilsk Nickel (HOLD) commits to publishing reserves

Anton Berlin, an official of Norilsk Nickel (RTS: GMKN), confirmed plans to publish data on reserves of precious metals at company fields. The law, which declassifies this information (previously a state secret), comes into force on February 19, 2004. Previously information regarding production, realization, cost of production of platinum-group metals, and also reserves in fields and inventories of platinum-group metals were a state secret. Berlin said further steps will be needed after February 19 before reserve figures can be published. He also said that the company will not publish cost of production of platinum-group metals since it is difficult to calculate accurately for technical reasons. Norilsk Nickel accounts for 50% of worldwide palladium production and 15% of platinum production.

Detsky Mir enters St. Petersburg market

Detsky Mir (RTS: !DTMR), the Moscow-based retailer of children goods, plans to start trading operations in St. Petersburg in March 2004 using leased space. Detsky Mir has also said that it will open 15 sites in Kazan, Volgograd, Novosibirsk and Nizhny Novgorod. The company plans to spend \$10m on a retail site in Nizhny Novgorod.

Detsky Mir is owned by AFK Sistema (70.5%), the corporation with close links to the Moscow city government, and Moscow Municipal Bank (20%). Detsky Mir consists of a main retail site in downtown Moscow, as well as the Moscow shops Toy House and Bauland (decorating and building materials), and warehouse and retail subsidiaries in the cities of Orel and Tambov. Consolidated company turnover was \$52m in 2002. The main site alone is expected to show \$18m revenues for 2003 versus \$20m in 2002 under RAS, though net profit is expected to increase from \$2m in 2002 to \$4m in 2003. The Russian market of children's goods is estimated at \$1b annually.

We view regional expansion by Detsky Mir as positive, since (1) Detsky Mir is a strong brand name, with recognition in Russian regions, (2) the company has strong financial support from AFK Sistema, and (3) there is low competition on regional markets for children's goods. It is difficult to estimate the company's free float and capitalization due to illiquidity of its stock. We do not offer any recommendation.

Planeta considers \$100m bond placement in 2004

Planeta group, one of the largest Russian food market operators, may carry out a \$100m domestic bond issue in mid-2004 if the market situation is favorable. The group, which was established by Millhouse, the offshore company used by Roman Abramovich and Sibneft owners, originally planned a bond placement in August 2003, but has postponed it repeatedly. The group has also postponed a seven-year 32m euro credit line from ING due to revision of its investment program. Planeta hopes to revive the ING borrowing plan in the first quarter of 2004.

The only traded subsidiary of Planeta is the dairy company, Petmol (PMOL, PMOLP). In November

Planeta Group said that it may sell off its main assets, including dairy business, Unimilk, which consolidates Petmol, Danone, Wimm-Bill-Dann and Planeta's own management might be interested in purchasing Unimilk.

ICN and Chudo-Doktor creates third largest drugstore chain

The drugstore chain ICN, Russian subsidiary of ICN international, and Russian company Chudo-Doktor ("Miracle-Doctor") decided to merge, creating the third largest drugstore chain in Russia under the ICN brand. ICN and Chudo-Doktor are both owned by the Russian investment company, Profit House.

Roman Abramovich, following his policy of disposal of major Russian assets, sold Russian assets of ICN International to the Russian investment company Profit House in mid-2003 for \$55m. ICN in Russia includes five pharmaceutical plants, a retail chain of 98 drugstores, and an office center. Turnover of ICN drugstores in 2002 was \$27m, compared with \$12m for Chudo-Doktor.

Profit House already owned the pharmaceutical plant Ufavit and Chudo Doktor drugstores before purchase of ICN. Profit House and Millhouse, the Abramovich offshore vehicle, which previously owned Chudo-Doktor, have worked together in several deals.

The cosmetics chain, L'Etoile, which has 101 stores in Moscow with \$90m annual turnover also plans to be involved in the ICN-Chudo-Doktor project.

Estimates by the industry consultancy, Pharmexpert, suggest that the united chain will have 134 drug stores. The biggest Russian drugstore chain, Natur Product (based in St Petersburg), runs 141 drug stores, while the second largest, Implosii (based in Samara) has 140 stores.

The only traded Russian drugstore chain, 36.6 (MICEX: RU14APTK1007) currently owns 60 stores, and will face stronger competition on the market after unification of ICN and Chudo Doktor. 36.6 showed weak interim financials in 2003, partly due to rapid expansion, and we expect a net loss for the full year.

We reiterate our HOLD recommendation for 36.6, whose stocks are traded with only 2% premium to \$10 fair price.

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