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Severstal (SVST LI)

2Q10 IFRS strong financials

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2Q10 net income in line with our expectations. Severstal has announced strong 2Q10 and 1H10 financials. The company's revenue increased by 35% q-o-q to \$4,245 mn, EBITDA doubled q-o-q to \$955 mn. 2Q10 net income was \$192 mn vs. \$785 mn of net loss in 1Q10. It should be noted that revenue and EBITDA slightly exceeded our forecasts, but net income actually met our expectations.

Solid results in Russia. Severstal's Russian steel division showed traditionally good results due to seasonal increase in steel prices and demand in 2Q10. Thus, segment's EBITDA climbed by 31% q-o-q to \$528 mn. EBITDA margin climbed by 2 ppt to 22%. Severstal Recourse significantly improved its results thanks to coking coal and iron ore prices growth. EBITDA jumped by 2.3 times q-o-q to \$420 mn, and EBITDA margin added 18 ppt to 48%.

Gold mining segment: growth continues, on track to transparency increase. Along with coking coal and iron ore prices growth, one of the reasons behind Severstal Recourse's strong results was continuing improvement in the figures of gold mining segment. Particularly, EBITDA surged 33% q-o-q to \$89 mn and EBITDA margin rose 4 ppt to 54%. In the press release on 2Q10 financial statement, Severstal noted that in order to increase transparency of the gold segment the company should release selected operational data including gold resources and reserves. We positively regard Severstal's intentions to increase gold mining business transparency that will allow providing more accurate projections.

Severstal North America: 2Q10 positive EBITDA. As we expected, Severstal's North American (SNA) assets showed positive EBITDA in 2Q10. We think this is one of the key positive developments for the company. Thus, EBITDA of SNA amounted to \$59 mn vs. \$83 of EBITDA loss in 1Q10. SNA's revenue increased by 24% q-o-q to \$1,447 mn. The improvement is mainly explained by the revival of the USA steel market in 2Q10. Sales rose 24% q-o-q and selling prices grew by 8% q-o-q. At the same time, we assume that SNA could receive EBITDA loss in 3Q10 due to decline in steel prices and unstable situation on the steel market. We note that SNA received \$24 mn EBITDA loss over 1H10.

Comfortable debt load. Severstal's debt raises no concerns. Its short-term debt was \$989 mn, while cash and equivalents stood at \$1,840 mn. As of the end of 1H10, the company had \$4,081 mn net debt. We forecast Net debt-to-EBITDA ratio at 1.5 for the year-end that implies a comfort debt load.

Severstal remains our top-pick. We consider the company's 2Q10 financial statement as positive and confirm our BUY recommendation on the stock with a target price of \$15.5/share. However, 2H10 is likely to be weaker as compared to 1H10 due to lower steel prices and fragile demand on rolled steel products. Nevertheless, its gold mining segment, which is gaining momentum, and high vertical integration into the production of coking coal and iron ore to some extent offset negative market developments. As for North America assets, in our view, temporary improvement may help the company to sell them.

Severstal's 2Q10 key financials, \$ mn

	2Q10	1Q10	q-o-q	TKB Capital estimates	Diff.	Consensus	Diff.
Revenue	4,245	3,142	35%	4,144	2%	4,122	3%
EBITDA	955	492	94%	887	8%	857	11%
Net income	192	-785	-	190	1%	267	-28%
EBITDA margin	22%	16%		21%		21%	
Net margin	5%	-		5%		6%	

Source: Company data, TKB Capital estimates

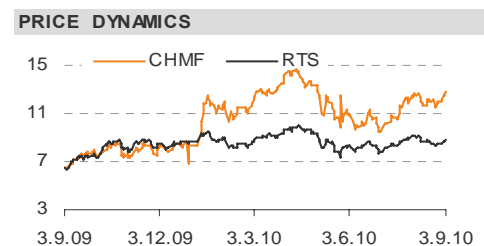
Severstal		
	Common	GDR
Ticker	CHMF	SVST
Recommendation	BUY	BUY
Price, \$	12.9	12.9
Target price, \$	15.5	15.5
Upside/downside, %	20%	20%

SHARE DATA	
Bloomberg	SVST LI
Reuters	CHMFq.L
	GDR
# of shares outstanding, mn	1,008
EV, \$ mn	17,370
MC, \$ mn	12,999
MIN 12 mnth., \$	6.27
MAX 12 mnth., \$	15.72
	GDR
Shares per GDR	1

SUMMARY FINANCIALS, \$ mn			
IFRS	2009	2010E	2011E
Revenue	13,054	15,566	18,350
EBITDA	812	2,643	3,560
Net income	-1,101	-216	1,373
EPS, \$	-1.09	-0.21	1.36
Rev. growth, %	-41.7	19.2	17.9
EPS growth, %	-154.1	-80.4	-735.8
EBITDA margin, %	6.2	17.0	19.4
Net margin, %	-8.4	-1.4	7.5

SUMMARY VALUATIONS			
	2009	2010E	2011E
P/E	-11.81	-60.18	9.47
EV/EBITDA	21.40	6.57	4.88

SHAREHOLDER STRUCTURE	
Alexey Mordashov	82.0%
Free-float	18.0%



Source: MICEX, RTS. TKB Capital estimates

CONFERENCE-CALL DETAILS:

DATE: 6 September, 2010

TIME:

5.30 pm (Moscow),
2.30 pm (London),
09.30 am (New-York)

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