

Ukrainian crops Farms over traders

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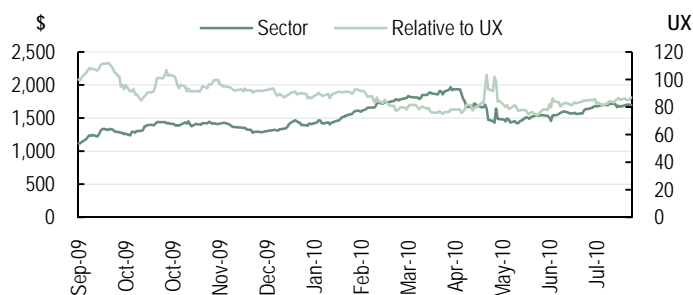
- We set Kernel's new TP at PLN60 and downgrade to HOLD.** On reviewing Kernel's business model, we are a little concerned with the company's future performance prospects. Specifically, we believe that the local crushing capacity will outgrow Ukraine's sunflower seed supply in 2011, which will put pressure on Kernel's oil margins and the weak 2010 grain harvest (we expect a 10-13% YoY decline) combined with a possible export quota may hamper the size of Kernel's trading operations. In the long term, we think Kernel may lose the bulk of its profitability as a trader because it will face more consolidated and thus stronger farmers in a more developed local market.
- We initiate coverage of three Ukrainian farming names:** Landkom International, MCB Agricole, and Sintal Agriculture. While Landkom is the most traded farming stock in Ukraine with a high level of corporate governance, we find that much like Sintal it has already eroded its upside during the recent wheat price rally. In our view, MCB is fundamentally the most undervalued, albeit rather illiquid. We initiate coverage of Landkom and Sintal with **HOLD** ratings (TPs at GBp9.6 and EUR3.4, respectively), and MCB Agricole with a **BUY** (TP at EUR3.8).
- Picking farmers over traders in the long term.** Our general sector view is that traders (and oil processors) are currently able to profit from the relatively weak and underfinanced farming operations that predominate in Ukraine. We think the situation will change in the long term, however, due to: 1) consolidation of Ukrainian farming; 2) improvement of agro debt financing; and 3) formation of a local commodities market. We thus expect trader margins to shrink and crop-growing margins to increase in the next five-to-ten years. Furthermore, comparing Ukrainian crop growers to that of Brazil and Russia indicates that Ukraine is the only place in the world with profitable large-scale farming.
- Risks.** Both traders and farmers are prone to the risk of a low harvest and export quotas. This year, we expect Ukraine to gather a total of 40-42mnt of grain and the government to set combined export quotas at 2.5mnt on wheat and barley until December. Oil processing companies may suffer from a local seed undersupply, due to recent processing capacity expansions, removal of the 12% sunflower seed export tariff, and long-term margin squeeze due to farming sector consolidation.

Summary sector ratings, as of 25 Aug 2010

Ticker	Company	Current price	Price target	Rating	Upside	MktCap, \$mn	EV, \$mn	Free float, \$mn	3M ADVT, \$'000
KER PW	Kernel	PLN61.5	PLN60.1	HOLD	-2.3%	1,425	1,681	841	2,424
LKI LN	Landkom International	GBp9.1	GBp9.6	HOLD	4%	62	54	63	141
4GW1 GR	MCB Agricole	EUR1.9	EUR3.8	BUY	93%	41	32	9	8
SNPS GR	Sintal Agriculture	EUR3.5	EUR3.4	HOLD	-1%	142	117	52	5

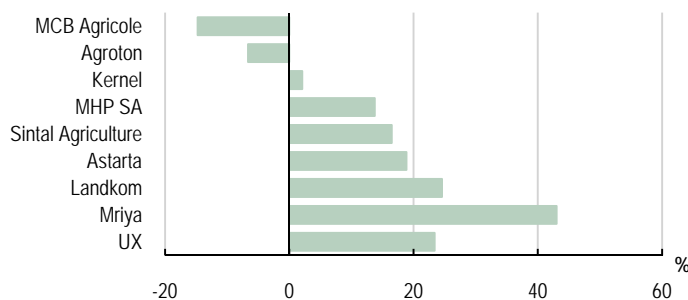
Source: Bloomberg, Renaissance Capital estimates

Figure 1: Price performance – 52 weeks



Source: Bloomberg

Figure 2: Sector stock performance – 3 months



Source: Bloomberg

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Executive summary

We review our outlook on Ukrainian agriculture by updating our forecasts on Kernel and initiating coverage of three Ukrainian farming names: Landkom, MCB Agricole, and Sintal. We downgrade our rating on Kernel to **HOLD** (from Buy) on the back of possible sunflower seed and grain shortages in 2011 as well as an expected drop in trading and oil processing margins over the long term. While overall we are bullish on Ukrainian farming, we give two of the farming stocks that we are initiating coverage on **HOLD** ratings: Landkom and Sintal, the stock price of which have both grown over 25% since the beginning of July on the world wheat price rally and already reached our target prices. We find MCB Agricole to be the most undervalued fundamentally: the company trades only at \$509/ha on 2010E EV per hectare of harvested land, which, in our view, already suggests a 50%-plus upside.

Our bullish view on Ukrainian farming is based on two principal observations: 1) the fact that current Ukrainian oil processing and trading margins are quite a bit above their peers; and 2) that large-scale Ukrainian farmers are actually profitable, which contrasts with their Russian and Brazilian counterparts. On comparing Kernel with Bunge and Archer Daniels Midland (ADM), we have found Kernel's agribusiness (we define agribusiness as a segment composed of grain trading, silo, and transshipping services) margins to be excessively large: 3x of Bunge and 7x that of ADM. We think such excessive profits are a temporary phenomenon largely resulting from distressed farming operations in Ukraine and an underdeveloped local commodities market; we believe that in the future, farmers will retain a larger share of the profit from growing crops. As for listed Ukrainian crop producers, we have found their business to yield a \$95/ha EBIT on average in 2009, which contrasts with loss-making farming in both Brazil and Russia.

On a more global scale, the recent wheat price rally is, in our view, largely ungrounded, as according to USDA's latest forecasts (12 Aug) low crop production in Eastern Europe will be compensated by ample harvests in Argentina and the US, leaving stock/use ratios only somewhat lower than last year and slightly above those of the year before (at 0.26). We forecast a 10-15% YoY increase in global wheat prices, and expect a similar dynamic to hold in Ukraine (although export quotas may put additional pressure on prices locally). We are somewhat more bullish on rapeseed prices, which are likely to have similar stock/use dynamics to wheat, but have rather low-ending stocks already (0.11 in 2009/10, 0.08 expected in 2010/11, according to USDA).

In addition, we hereby note that our coverage of the Ukrainian agriculture sector will from now on be conducted from our office in Kiev, with Konstantin Fastovets as the designated agriculture analyst.

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The recent wheat price rally is, in our view, largely ungrounded as 2010/11E stock/use ratios are only somewhat lower than last year and slightly above those of the year before (at 0.26). We forecast a 10-15% increase in global wheat prices

Ukraine's harvest in 2010

A harsh winter followed by an unusually dry summer has brought about concerns over the size of harvest that Ukraine will deliver this marketing year. We expect the grain harvest to total 40-41mnt (down 10-13% YoY), which is a consensus figure based on estimates from the Ukrainian Ministry of Agriculture, local consulting agencies, and market players (we give the most weight to local consulting agencies as they work in Ukraine and have no motivation to provide false data).

Figure 3: Ukraine 2010 harvest forecasts

	Grain, mnt	Date of forecast
AAA Agriagency	41.7	Aug 2010
Ministry of Agriculture	40-42	Aug 2010
USDA	38.6	Aug 2010
Kernel Group	40-45	July 2010
UAC	44.5	July 2010

Source: AAA Agriagency, Ministry of Agriculture, USDA, Kernel Group, UAC

Spring survival

Two main factors seem set to push the harvest down this year: winter kill (crops destroyed in the winter) due to low winter temperatures and moderate snow and a yield decline due to the recent drought.

Wheat and rapeseed are likely to take the largest hit, in our view, as 95% of these two crops are sown during the autumn (they need to survive the winter) and both crops are harvested in late June to early August, which coincides with the timing of the drought that hit Ukraine this year.

The poor grain harvest is likely to be compensated by an ample corn output brought about by larger corn planting areas (up 24% YoY)

On a positive note, the poor grain harvest is likely to be compensated by an ample corn output brought about by larger corn planting areas (up 24% YoY). We also expect oilseed to benefit from a 15% YoY increase in sunflower harvest and a 50% increase in soybean harvest, both of which will be on the back of increased sowing areas and comparable yields to last year. Sunflower and soy are both harvested between August and September, and we therefore do not expect them to be affected by the drought.

In addition, we note that the warmer weather seems to be positively affecting the quality of local grain. With roughly 85% of wheat already collected, 60-65% is of grade A (milling wheat), which is 10-15 ppts higher than last year.

Figure 4: Ukraine 2009 and 2010E harvested area, yield, and total harvest by crop

	2010E			2009			YoY change, %		
	Area, '000 ha	Yield, t/ha	Harvest, '000t	Area, '000 ha	Yield, t/ha	Harvest, '000t	Area, '000 ha	Yield	Harvest, '000t
Wheat	6,414	2.8	17,863	6,748	3.1	21,074	-4.9	-10.8	-15.2
Barley	4,417	2.2	9,576	4,987	2.4	11,999	-11.4	-9.9	-20.2
Corn	2,668	4.4	11,819	2,150	5.0	10,707	24.1	-11.0	10.4
Total grains	15,017	2.8	41,713	15,593	3.0	46,789	-3.8	-6.7	-10.8
Sunflower	4,580	1.6	7,443	4,098	1.6	6,458	11.8	3.1	15.2
Rapeseed	926	1.7	1,560	1,014	1.8	1,853	-8.7	-7.8	-15.8
Soybean	931	1.6	1,518	626	1.6	1,000	48.7	2.0	51.7

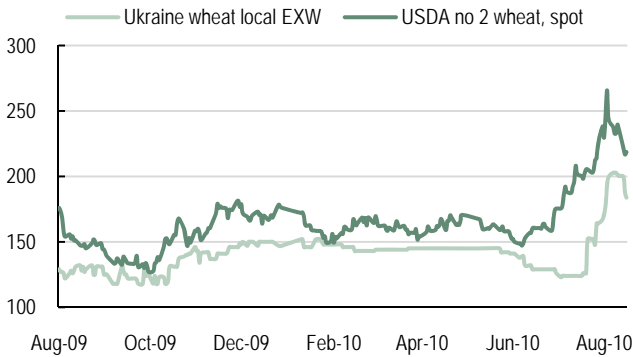
Source: AAA Agriagency, Ukrstat

The pricing rally

News of weaker-than-expected harvests in Russia and Ukraine has set wheat prices racing upwards. Although this trend seems to have already turned around to an extent, prices have still gained over 35% in the past two months. A similar albeit less extreme trend seems to be developing on the rapeseed market – both local and European prices have grown 10-15% in the past eight weeks.

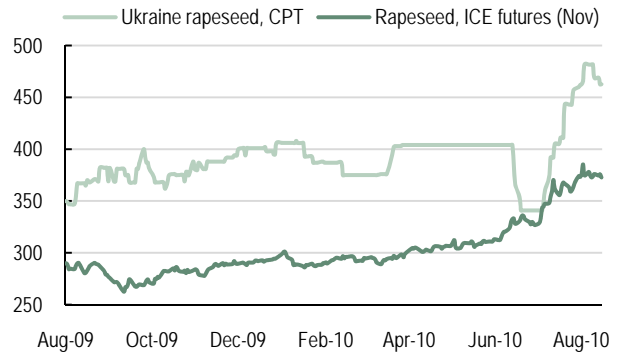
Crops that are harvested later in the year in the northern hemisphere (August-December) – namely corn, sunflower seed, and soybean seem to be less affected by the rush at the moment, but may start showing signs of moderate growth, as they can often be used as substitutes for wheat and rapeseed (corn for wheat in animal feed, and soybean for edible oil production).

Figure 5: World vs Ukraine wheat prices over the past 12 months, \$/t



Source: Bloomberg, AAA Agriagency

Figure 6: World vs Ukraine rapeseed prices over the past 12 months, \$/t



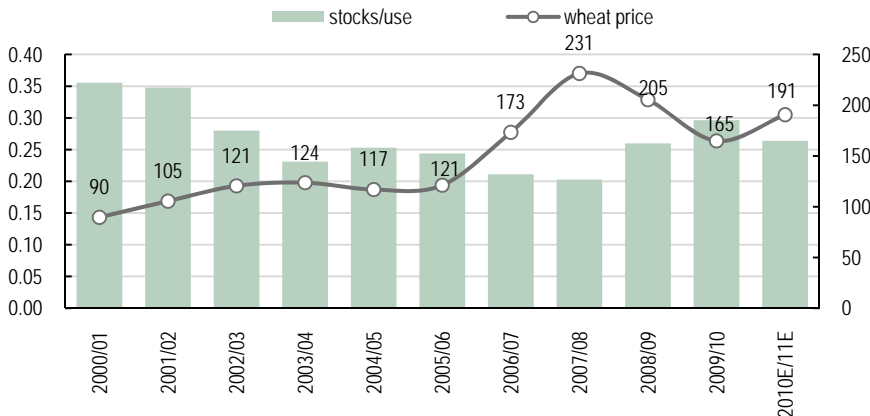
Source: Bloomberg, AAA Agriagency

Fundamentals: Wheat vs rapeseed

According to USDA's latest forecasts (made on 12 Aug), this year's wheat supply/demand balance points towards a slight increase in prices, though it forebodes nothing dramatic, in our view. The cumulative effect of the drought is estimated to cut the world wheat supply by roughly 34mnt (coming largely from Russia, Ukraine and Kazakhstan), which will easily be compensated by last year's ample 193mnt of ending stocks. Based on USDA's figures, we calculate the 2010/11 stock/use ratio to be at 0.264, which is somewhat below last year's 0.300 (an eight-year record) and just a bit higher than 0.260 of two years ago.

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Figure 7: World wheat stocks to use vs price dynamics



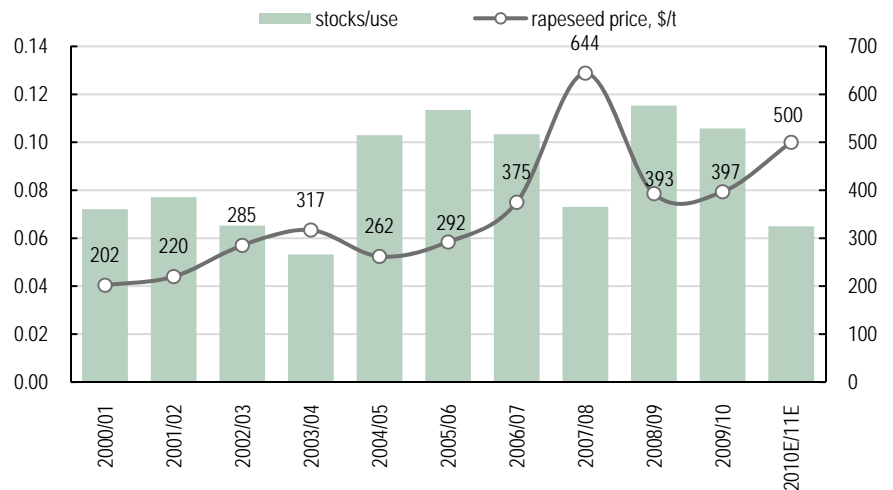
Source: Bloomberg, USDA, Renaissance Capital estimates

This year, partially due to an expected 16% YoY rapeseed harvest decrease in Ukraine, the world stock/use ratio may end up at 0.07-0.08

We therefore think that the recent wheat price rally has been driven largely by fear and speculation rather than fundamentals, and expect prices to keep dropping from their peak in early August. For our models, we assume a 16% YoY wheat price increase both locally and abroad (in dollar terms).

A similar rally on rapeseed markets has a more fundamental basis, in our view. Although Ukraine and Russia combined have a much smaller world production share in rapeseed than they do in wheat (roughly 4% combined share in rapeseed vs 12% in wheat, rapeseed ending stocks have historically been at low levels already (rapeseed 0.11 vs 0.30 wheat in 2009/10). This year, partially due to an expected 16% YoY rapeseed harvest decrease in Ukraine, the world stock/use ratio may end up at 0.07-0.08. For our forecasts, we model a 25% YoY local and international rapeseed price growth based on current price levels (we do not expect them to significantly drop back down).

Figure 8: World rapeseed (CIF Hamburg) vs stock / use ratio



Source: USDA, FAPRI, Renaissance Capital estimates

To further the distinction between wheat and rapeseed, we note that wheat has always been a strategic crop for Ukraine and the government is already considering installing temporary export quotas (at 2.5mnt for wheat and barley combined until December) in order to keep bread prices low and to fill government stocks. Quotas will undoubtedly constrain local price growth even if world prices do not drop as much as we expect.

The substitute story: Wheat for corn, rapeseed for soy

Although crops that are planted in the spring have been unaffected by winter kill and are damaged less by the drought, they too are likely to follow suit with price growth due to substitution. We expect local wheat, corn, and barley prices to all be priced roughly at UAH1,000/t (ex-VAT), as they can be substituted for each other in animal feed. A similar story holds for rapeseed substitutes – sunflower seed and soybean, which will also pull up to UAH2,400-2,800/t.

Figure 9: Ukraine 2009 and 2010E local principal crop prices, UAH/t (ex-VAT)

	2009	2010E	YoY change, %
Wheat	887	1,000	13
Barley	750	1,000	33
Corn	757	1,000	32
Rapeseed	2,300	2,800	22
Sunflower seed	1,964	2,400	22
Soybean	2,813	2,606	-7

Source: Company data, APK-Inform, Renaissance Capital estimates

Sunflower oil and seed sector

World sunflower oil production comprises a relatively small share (roughly 8% by volume) of the much larger edible oils market, which has been growing at a 5.0% CAGR over the past 10 years. In terms of consumption, edible oils are either used for food or industrial purposes (largely biodiesel, but also as engine lubricants and cosmetics). We note that the share of oil used for industrial purposes has increased to 44% in 2009/10 from 36% in 2001/02.

Figure 10: Historical edible oil shares, %

	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10E
Coconut oil	3.1	2.9	2.6	2.8	2.6	2.6
Cottonseed oil	4.6	4.1	4.2	4.1	3.6	3.4
Olive oil	2.7	2.2	2.4	2.2	2.2	2.1
Palm oil	30.0	30.1	30.6	31.9	32.9	32.9
Palm kernel oil	3.7	3.7	3.7	3.8	3.9	4.0
Peanut oil	4.5	4.2	3.7	3.8	3.7	3.4
Rapeseed oil	14.1	14.6	14.1	14.3	15.3	16.1
Soybean oil	29.2	29.2	29.9	29.3	26.8	27.4
Sunflower seed oil	8.2	8.9	8.7	7.7	8.9	8.2

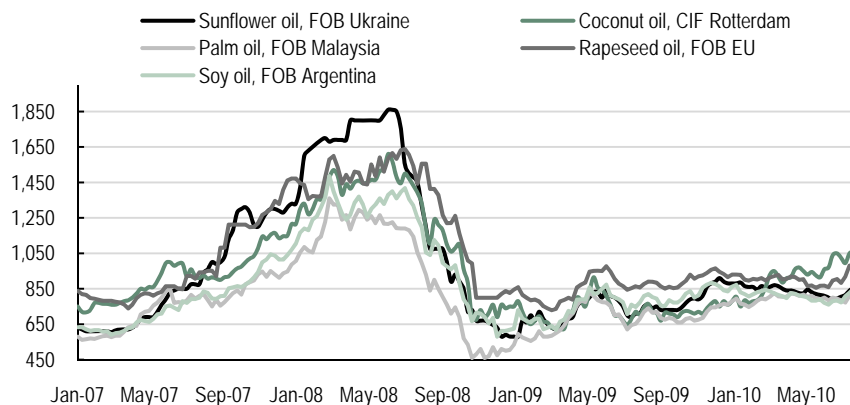
Source: USDA, Renaissance Capital estimates

From top to bottom: Oil defines seed

As edible oils can substitute one another in a number of uses (biodiesel, animal feed), we believe it is the supply/demand balance of the entire edible oils market that determines the price of sunflower oil

As edible oils can substitute one another in a number of uses (biodiesel, animal feed), we believe it is the supply/demand balance of the entire edible oils market that determines the price of sunflower oil (in other words sunflower oil producers are price takers, as sunflower oil has a less than 10% share in world edible oil production). The similarity in historical price movements is a good indicator that all edible oil prices are shaped by similar forces.

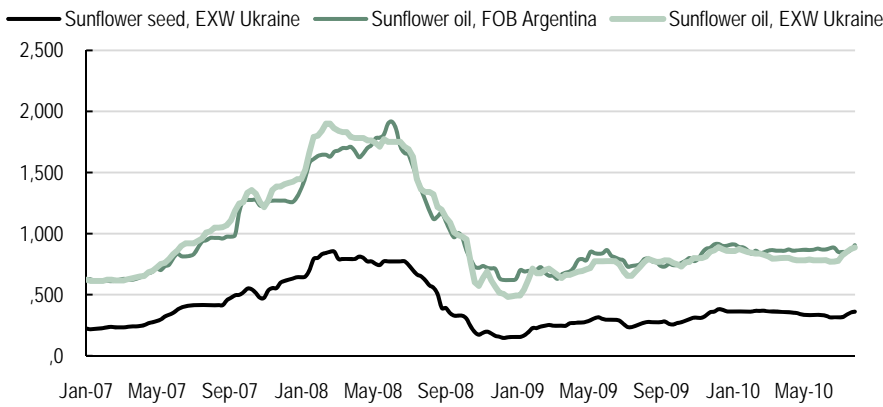
Figure 11: Edible oil price dynamics as of Jan 2007, \$/t



Source: Bloomberg, APK-Inform

International sunflower oil prices determine oil prices on the local market (the correlation between local prices and Argentina's export prices, for example, is 0.98), and local oil prices in turn determine the price of local sunflower seeds. We do note, however, that the Ukrainian seeds market is rather inefficient and the spread between local seed and oil prices can often spike up during times of harvest.

Figure 12: Historical sunflower oil and sunflower seed price dynamics as of Jan 2007, \$/t

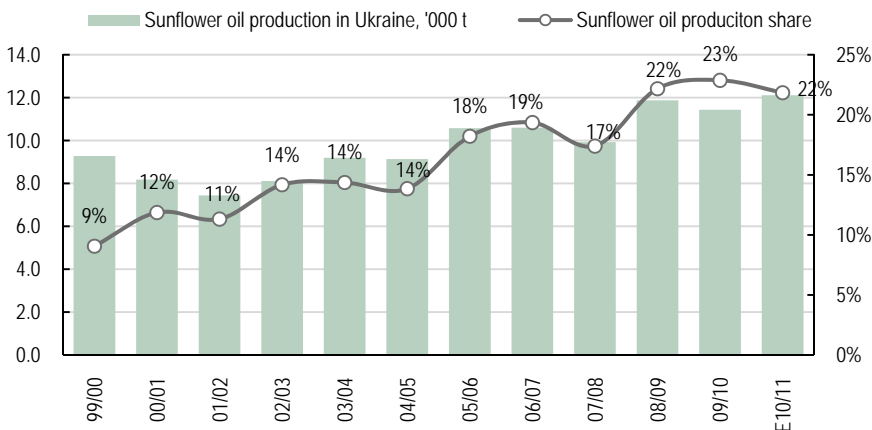


Source: APK-Inform

Ukraine – a player of global importance

Ukraine has been a large and growing sunflower oil producer in the past 10 years, having demonstrated a 12% CAGR over 1999/00-2009/10. We believe such growth to be a direct consequence of general recovery in the crop sector, a large arable land bank (32.4mn ha) and the fact that sunflower oil is much cheaper to transport than sunflower seed (it makes economic sense to crush sunflower seeds locally: less than 5% of seeds are exported).

Figure 13: Ukraine 1999/00-2010/11E sunflower oil production and world production share



Source: USDA, Renaissance Capital estimates

We note that this year Ukraine will harvest 4.6mn ha of sunflower, which, according to local agricultural practice, means that the country's arable land is nearly saturated by the crop (local practice dictates planting sunflower no more than once in seven-to-eight years on the same field). While we believe Ukraine's agricultural practice to be outdated (western farms plant sunflower once in three-to-four years), it will take some time for local farmers to adopt western practices, which means that sunflower seed planting areas will be capped at 4.6-4.7mn ha for at least a few years. We still see scope for production growth coming from consolidation in local agriculture, however, as large

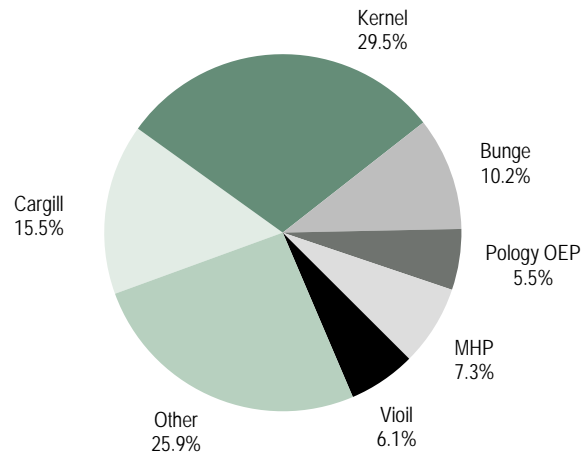
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commercial farms achieve over 50% higher sunflower seed yields than the country's average.

Oil production market already developed

We estimate that in 2010 the top three sunflower oil producers in Ukraine (Kernel, Cargill, and Bunge) will control over 55% of the country's crushing capacities, which means that the Ukrainian market is already consolidated. We think near-term growth will be limited by sunflower seed supply, which is already outstripped by production capacities (we estimate a 5-7% undersupply already in 2010).

Figure 14: Ukraine 2010E sunflower oil processing capacity distribution



Source: News reports, Ukrrolyaprom, Renaissance Capital estimates

Risks

We note the following main risks associated with the sunflower oil processing market:

Removal of the sunflower seed export tariff, which is currently set at 12% and will be reduced 1% pa until reaching a cap at 10%. There are already talks going on in the government concerning removal of the tariff completely in order for Ukraine to enter a free trading zone with the EU.

Consolidation of the farming sector, which means that stronger farmers will be able to retain a larger share of profit from growing sunflower seeds (sunflower seeds will become more expensive for processors).

Formation of a local soft commodities market and widespread use of futures and forwards contracts, which will mean farmers will be able to sell crops at higher prices and at any time (not just after harvest). Such a market will practically remove seasonal price fluctuations that allow processing companies to purchase seeds cheaply.

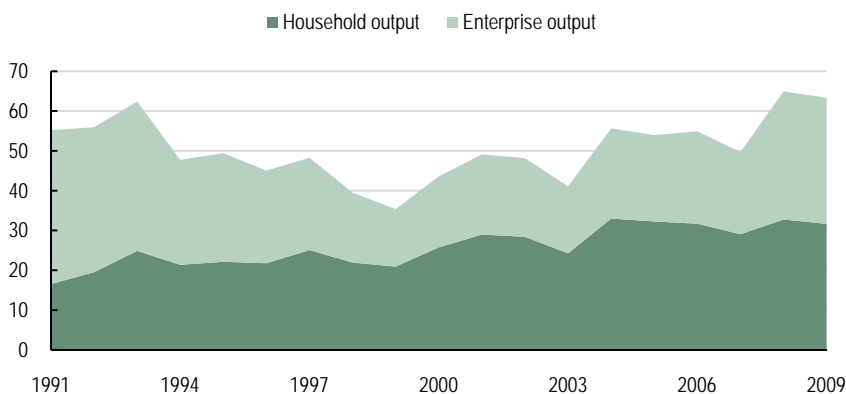
Sunflower seeds under-supply that is expected already this year; we estimate total 2010E processing capacities at 7.9mn tpa (13% above the expected seed harvest).

Crops: Driven by consolidators

Ukraine was a Soviet agricultural powerhouse prior to the collapse of collective farming in the early 1990s. The transition from central planning to a market economy has hit crop production hard – 1999 crop output dropped nearly 2x from 1985-1990 levels, mostly on the back of a 2.8x output drop in agricultural enterprises. As a result, household production became the backbone of Ukrainian agriculture, with a share in total crop output increasing to 59% in 1999 from 25% in 1990.

Private agricultural companies firmly entered the scene only in the early 2000s, and lifted industrial crop output by an estimated 5.9% CAGR over 2001-2009, compared with a 2.1% CAGR demonstrated by households. As a result, the country's grain production returned to its Soviet-era highs in 2008-2009.

Figure 15: Household vs enterprise crop output, UAHbn rebased to 2005 prices



Source: Ukrstat, Renaissance Capital estimates

We believe Ukrainian output of grain and oilseeds in the short-to-medium term will be driven by the continuing formation of new agricultural holdings, and the expansion of existing ones, as room for consolidation is large (we estimate that less than 10% of all arable land is currently under control of large holdings), and agro enterprises demonstrate 35-60% higher yields than farms run by the population at large with individual/small holdings.

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Figure 16: 2009 Enterprise vs Ukraine average yields, t/ha

	Corporate average ¹	Ukraine average	Difference, %
Wheat	4.2	3.1	37
Barley	3.0	2.4	25
Corn	7.2	5.0	44
Rapeseed	2.4	1.8	36
Sunflower seed	2.6	1.6	64

¹ We estimate the figure based on data from local agricultural companies that we cover

Source: Company data, Ukrstat, Renaissance Capital estimates

Ukrainian farming – the best performer

We believe Ukraine is the only place in the world offering exposure to profitable large-scale farming due to low land and labour costs combined with strong and easily accessible export markets. In our view, the only two countries with peer farmers are at a disadvantage when compared to Ukraine: Brazilian agriculture suffers too much from poor infrastructure and a geographical location that is far from European consumption markets; Russia has limited export opportunities and a less favourable climate for growing crops.

Farming that makes money

We found that Ukrainian names averaged a 16% EBIT margin and \$96/ha harvested of EBIT, compared with negative indicators for their peers from Ukraine and Brazil

In order to examine the profitability of Ukraine's agriculture sector, we pooled the latest land farming segment data from nine Ukrainian public agro names and compared them with their Russian and Brazilian counterparts. We found that Ukrainian names averaged a 16% EBIT margin and \$96/ha harvested of EBIT, compared with negative indicators for their peers from both countries.

Figure 17: Ukrainian farming vs Russian and Brazilian peers

Company	Country	Year financials	Farming EBIT ³ , \$mn	Farming sales, \$mn	Harvested, '000ha	EBIT margin, %	EBIT/ha
Agroton ¹	Ukraine	2009	1	43	121	2	9
Astarta ¹	Ukraine	2009	17	104	159	16	107
Kernel ¹	Ukraine	2009	-7	53	85	-13	-84
Landkom	Ukraine	2009	-27	15	29	-188	-941
MCB Agricole	Ukraine	2008	1	30	62	3	14
MHP ¹	Ukraine	2009	7	83	150	8	47
Sintal ¹	Ukraine	2008	10	27	64	38	123
Mriya ²	Ukraine	2009	83	148	150	56	553
Agrogeneration	Ukraine	2009	-4	3	20	-133	-197
Ukraine total			81	505	840	16%	96
Trigon ¹	Russia/Ukraine/Estonia	2009	-8	21	82	-37	-96
Razgulay ¹	Russia	2009	25	201	319	13	80
Russian Grain ¹	Russia	2009	-6	21	59	-29	-105
Black Earth Farming	Russia	2009	-36	75	183	-48	-199
Russia total			-25	320	644	-8	-39
SLC Agricola	Brazil	2009	9	298	176	3	52
Brasil Agro	Brazil	2008/2009	-24	35	20	-67	-1,200
Brazil total			-14	334	196	-4	-73
Total peers			-39	653	839	-6	-47

¹ From farming segment financials.

² Estimates exclude sugar beet sales and costs and land.

³ figures exclude biological revaluation everywhere except for Russian Grain and Kernel, where they are immaterial

Source: Company data, Renaissance Capital estimates

Transportation is the key

As Ukraine, Russia, and Brazil are all net agricultural exporters, we believe transportation costs to be a key variable that determines farming profitability. Ukrainian farmers benefit from lower export costs due to better logistics infrastructure. While Brazil is well known for its undeveloped railway and road network (only 30,000 km of rails to cover 8.5mn km² of area, which is 10x worse than in Ukraine), Russia only has 22-23mn tpa of port grain transshipment capacity, which is barely sufficient for its export potential (in 2008/09 Russia had trouble exporting its 23mnt of grains). Ukraine by contrast has a more extensive and better quality network – 98% of roads are paved, compared with 81% in Russia, and only 10% in Brazil.

Figure 18: Ukraine, Russia, and Brazil transportation infrastructure comparison

	Ukraine	Russia	Brazil
Rail lines, km ¹	21,676	84,158	29,817
Total area, mn km ²	0.60	17.10	8.51
Railway coverage ratio ²	36	5	4
Port capacity (grain), mn tpa	26	23	na
Paved roads (as % of total roads)	98%	81%	10% ³

¹ 2008 World Bank data,

² Calculated as the ratio of railway length (in km) and total country area (in '000 km²),

³ based on Brazilian Highway System data

Source: World Bank, Renaissance Capital estimates

Ukraine has a better climate than Russia

Ukraine has historically exceeded Russian yields on all principal crops, which, taking into account that the two countries have very similar agricultural practices (only 10 years ago they were both part of the same country), likely points to the fact that Ukraine is simply better suited for crop growing. The same is not necessarily true when comparing Ukraine with Brazil, as Ukraine usually has higher grain yields, but lower oilseed yields (Brazil 2008 soybean yield at 2.8 t/ha vs 1.5 t/ha in Ukraine).

Figure 19: Ukraine vs Russia yields on major grains in 2008 and 2009



Source: USDA, Rosstat

Risks

We see the following as the main risks associated with Ukrainian farming:

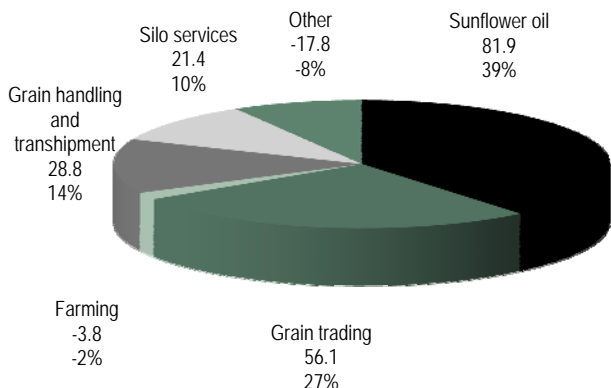
Harvest drops associated with winter kill and lower yields due to bad weather (either rain during harvesting seasons or drought, as this year).

Export quotas that can create unpredictability in farming company earnings, due a possible oversupply created in such a way on the local market. This year the government has announced plans to install a 2.5mnt combined export quota for wheat and barley until December.

Kernel: Company overview

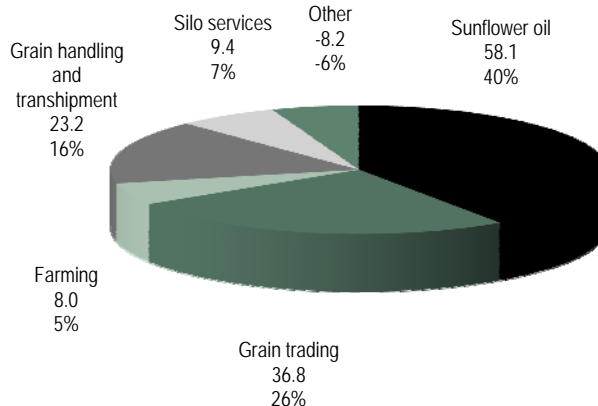
Kernel is one of the largest agricultural companies in Ukraine with an estimated EV of \$1.7bn as at 25 Aug 2010. Kernel engages primarily in grain trading, sunflower oil production and trading, farming, and silo and transshipment services.

Figure 20: Kernel FY09 EBIT breakdown by segment, \$mn



Source: Company data, Renaissance Capital estimates

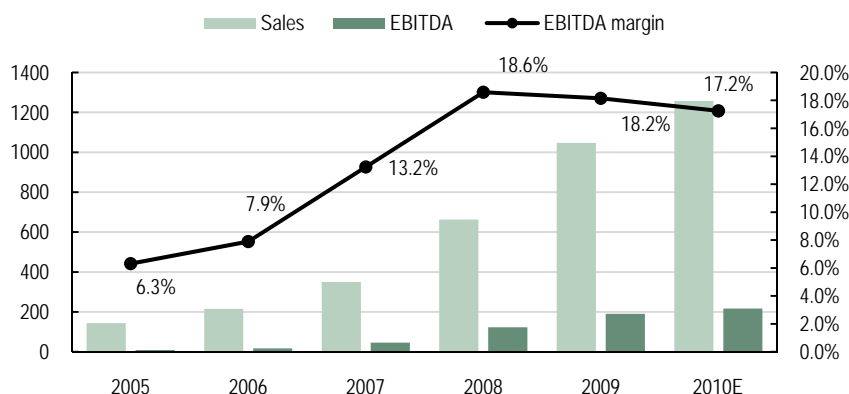
Figure 21: Kernel 9M10 EBIT breakdown by segment, \$mn



Source: Company data, Renaissance Capital estimates

Over the past four years Kernel has demonstrated an impressive 64% CAGR in sales and a 113% CAGR in EBITDA, and has grown to become the most liquid Ukrainian agro name (\$1.7mn/day 12-month average trades). We estimate that in 2011E Kernel will control roughly 28% of all of the country's crushing capacities, trade 10-12% of Ukraine's annual grain export, and provide 35% of all domestic bottled sunflower oil.

Figure 22: Kernel 2005-10E sales (\$mn), EBITDA (\$mn), EBITDA margin



Source:

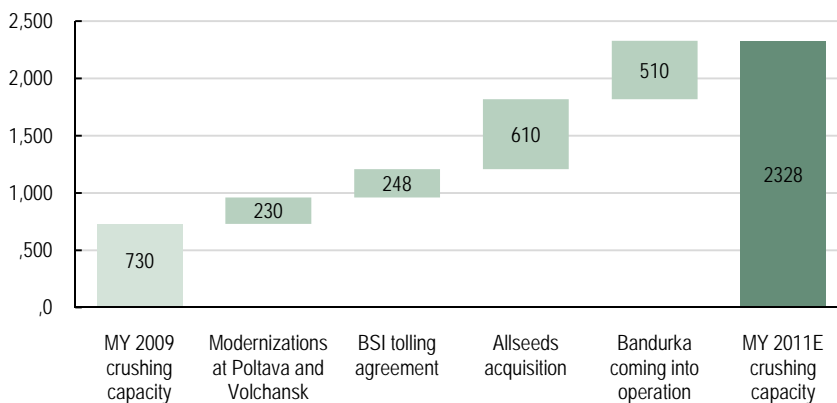
While we think this agricultural giant's progress is no doubt encouraging, we are somewhat concerned with the company's short- and long-term performance prospects. Specifically, we believe that the local crushing capacities will outgrow Ukraine's sunflower seed supply in 2011E, which will put pressure on Kernel's oil margins. The lower 2010 grain harvest (a 10-12% YoY decline is expected) and possible export quotas may hamper the size of Kernel's trading operations. In the long term, we think

Kernel may lose the bulk of its profitability as a trader that will face more consolidated and thus stronger farmers in a more developed local market.

Too much crushing and too little grain

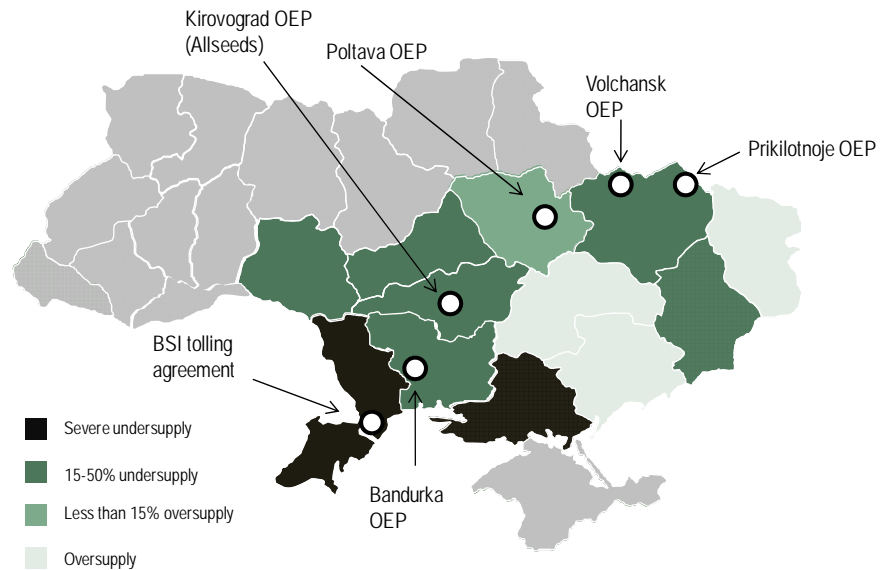
After Kernel's acquisition of Allseeds in Apr 2010, modernisations of Poltava and Volchansk crushing plants, and engagement into the BSI tolling agreement in Odessa, the company has been able to increase its total crushing capacity by 147% YoY to 1.8mn tpa, and become an undisputable leader of the Ukrainian sunflower oil market. With Kernel's 0.5mn tpa Bandurka OEP (oil extraction plant) coming into operation in the next few months, Kernel will raise capacity by a further 28%, consolidating just under a third of Ukraine's total crushing capacity under its roof.

Figure 23: Kernel 2009-2011 crushing capacities, mnt per year



Source: Company data

We estimate that Kernel's strong expansion combined with growth of other local oil producers (such as Creativ, which has upgraded its plant to crush roughly 0.4mn tpa of seeds) will bring Ukraine's total crushing capacity in 2010/11E to 7.9mn tpa, which is 13% above the expected sunflower seed harvest in Ukraine. A shortage persists even if we consider that Kernel may not launch the smaller of its Allseeds plants (the Mykolaiv OEP lacks an extractor, which means it can only achieve a 35% oil yield instead of the regular 45%) and the fact that Bandurka is a multiseed facility that can potentially substitute sunflower with rapeseed and soy.

Figure 24: Location of Kernel's OEP vs sunflower seed sufficiency¹

¹ We calculate sufficiency by examining the ratio between the 2009 sunflower seed harvest in a given region vs the capacities operating in the region. The Nikolaev plant is not included, as we believe that Kernel will not launch it this year, and will eventually sell the plant altogether
Source: Company data, Ukrstat, Renaissance Capital estimates

Examining how the supply of sunflower seeds is distributed geographically in relation to OEPs, shows that four of five of Kernel's plants are located in seed-deficient regions, which we believe aggravates the situation even more (we include BSI into this calculation, but exclude the Mykolaiv plant acquired from Allseeds, as it is likely not to be launched). We also note that considering that local agricultural practice dictates planting sunflower no more than once in seven-to-eight years on the same field, the projected shortage may last for a few seasons.

On the trading side, Kernel's export volumes may suffer due to the 2010 harvest being the lowest in three years (41.7mnt expected, down 11% and 26% to 2009 and 2008 harvests, respectively). We note, however, that although the company has been historically exporting about 10% of Ukraine's total exports, its farming penetration has increased via the additional 600kt of silos acquired in the 1Q10 Allseeds deal, which may mean that growth in export share may partially offset the effect of the poor harvest. We also consider the possibility of trading margins going down because of increased competition between traders, but historical data do not seem to support this view. For example, in 2007/2008 the country exported 14mnt, which is 30% below projections for the upcoming year, and Kernel's trading EBIT margin stayed strong at 8.0%.

A trader that makes more than its peers

Kernel's grain origination and trading segments have historically showed remarkably high margins when compared with the company's global peers. Over the past three years (2007-2009) the company averaged a 15% EBIT in agribusiness (comprising a 10% EBIT margin in trading and a 48% EBIT margin in silo and transshipment services combined), which is 3x that of Bunge and over 7x that of ADM.

Figure 25: Agribusiness (trading, silo, and transshipment combined) 2007-2009 EBIT margins summary

	2009	2008	2007
Kernel	16.5%	19.6%	8.1%
Bunge	4.5%	5.5%	5.2%
ADM	1.3%	1.0%	1.6%
Viterra ¹	5.5%	5.9%	6.5%
Graincorp ²	7.1%	0.7%	neg
Global trader average	4.6%	3.3%	4.4%

¹ EBITDA margin is taken, as no EBIT segment information is available.

² This is the company's consolidated margin, which is taken, as all of Graincorp's activity is linked to trading.

Source: Company data, Renaissance Capital estimates

While the profitability level is impressive, we believe that Kernel's margins are due to the relatively weak position most farmers currently have vs traders, which is bound to change in the mid and long term. Specifically, we believe the following factors will put pressure on Kernel's trading, silo, and transshipment margins:

Consolidation of the farming sector. Small farmers and households that still produce half of Ukraine's crop output (including sunflower) will in time unite to become larger players that will have the ability to negotiate better pricing contracts and store grain in their own elevators (we think consolidation is actively going on already, as privately owned land banks are quickly expanding and enterprise output is growing, according to Ukrstat). Large local players such MCB and Sintal are already able to negotiate prices (Sintal has even been successful in exporting by itself without using traders).

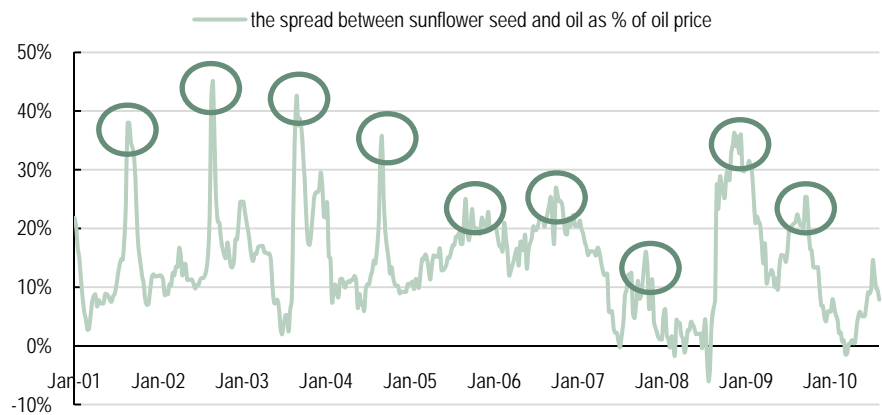
Improvement of debt financing. Farmers that have just harvested their crops tend to sell them immediately in order to fund the winter sowing campaign, which creates a temporary oversupply on the local market and puts downward pressure on prices. We believe that as the banking system in Ukraine improves and farmers gain access to more assets for collateral (such as machinery or land, once it becomes tradable), farmers will no longer be forced to sell directly from the fields.

Formation of a local commodities market (futures). One reason why farmers tend to sell crops at unfavourable seasonal prices is that there is no organised market and little access to financial instruments such as futures and forward contracts, which would help spread crop sales over the entire year (and thus allow farmers to receive financing when needed). The Ukrainian government has been planning on creating a market for some time, but nothing concrete has been decided to date. Nevertheless, we believe that the development of such a market (or proper access to an already developed market) is unavoidable in the future.

More trading than meets the eye

While Kernel's trading business may seem to be diversified by its sunflower oil production division, we feel that the bulk of Kernel's oil margin also comes from exploiting local market imperfections. As sunflower seed comprises 90-95% of sunflower oil costs, segment profits are made from timely seed purchases and timely oil sales (akin to trading). Examining the historical spread between the costs of sunflower seed required to make one tonne of oil (assuming a 45% oil yield) and the price of oil, shows clear signs of seasonality, which benefits Ukrainian oil producers immensely (peaks occur during sunflower harvest times in Aug-Sep).

Figure 26: Local historical spread between sunflower cost per ton of oil and oil price, as % of oil price



Source: APK-Inform, Renaissance Capital estimates

It is thus not surprising that Kernel's average oil EBIT over 2007-2009 has been at 18% compared with 5.5% for Bunge, 5.6% for ADM, and 4.5% for Elstar Oils (a Polish rapeseed processing company).

We believe the historical spikes in seasonality will flatten out in the long term and will bring Kernel's average oil segment EBIT down to 6-7% – due to the same factors that will bring down the company's agribusiness margins (consolidation of farming sector, improvement of debt financing, and development of a local commodities market). We note one additional factor specific to sunflower:

Liberalisation of sunflower exports. Currently there is a 12% export tariff on sunflower seeds in place that protects oil producers. Ukraine has negotiated this tariff with the WTO, and has agreed to reduce it to 10% in two years. Talks are ongoing, however, on removing the tariff completely in order to create a free trade zone with the EU. While the trade barrier may last for a few more years, we believe it is reasonable to assume it will not last indefinitely.

Kernel FY10 results preview

Overall we expect Kernel to beat management guidance of \$1,050mn revenues and \$195mn EBITDA reiterated in the 3Q10 earning release on the back of the Allseeds acquisition, the effect of which is planned to be included in FY10 financials. The addition of the 443 tpa Kirovogradoliya plant (began operating for Kernel on 1 Apr) combined with the BSI tolling agreement will help boost Kernel's bulk oil sales by 69% YoY (crude and refined combined), on our estimates. We will also see a significant increase in grain export (trading) volumes (up 10% YoY) despite the recent VAT refund problems, as Kernel has already exported 2.1mnt in the first nine months of the financial year.

Of note is the expected 55% increase in net debt due to Kernel taking on an approximate \$152mn of debt from the Allseeds balance sheet, which will increase the company's net debt/EBITDA ratio to 1.2x. We find such leverage to be very manageable for the company, particularly taking into consideration the growth in 2011E EBITDA (we expect \$261mn, up 20% YoY).

Figure 27: Kernel 9M and FY results comparison for 2009 and 2010E

	9M09	9M10	YoY	2009	2010E	YoY
Revenue	866	782	-10%	1047	1257	20%
CoGS	-598	-538	-10%	-707	-875	24%
Gross profit	268	244	-9%	340	382	12%
SG&A expenses	-139	-124	-10%	-167	-186	12%
Other operating income, net	13	8	-40%	18	21	16%
EBITDA	160	142	-11%	191	217	13%
D&A	-18	-15	-19%	-23	-26	12%
EBIT	142	127	-11%	168	191	13%
Financial expenses	-29	-14	-52%	-32	-24	-26%
Other non-operating income/expenses	-8	9	-205%	-4	0	-100%
PBT	105	122	17%	128	167	30%
Income (tax)/benefit	6	0	-93%	5	-8	-263%
Net income	105	123	17%	133	158	19%
Margins						
Gross	31%	31%	0.2ppt	32%	30%	-2.1ppt
EBITDA	19%	18%	-0.4ppt	18%	17%	-1ppt
Net income	12%	16%	3.6ppt	13%	13%	-0.1ppt
Main operating data						
Bulk oil sales, '000t	144	227	57%	224	379	69%
Bottled oil sales, mn litres	79	92	16%	98	109	12%
Export volume, mnt	1.8	2.1	14%	2.3	2.5	10%
Net debt, \$mn	158	282	79%	165	256	55%
Other ratios						
Net debt/EBITDA	1.0	2.0	102%	0.9	1.2	37%
ROIC	21%	17%	-3.7ppt	19%	20%	1.3ppt
ROE	43%	37%	-5.9ppt	33%	36%	2.8ppt
SG&A as % of revenue	16%	16%	-0.1ppt	16%	15%	-1.1ppt

Source: Company data, Renaissance Capital estimates

Kernel: Valuation

We value Kernel based on a 10-year DCF model and peer trading multiples. Our DCF approach gives a TP of PLN60/share, and we believe this is the most dependable figure, as our DCF is rather resilient to a number of factors that are difficult to predict, such as oil and grain prices. Our peer comparison approach generally indicates that Kernel trades at a premium to peers, but we feel this does not suggest the stock to be overvalued, as the company does show high EBITDA growth rate in the next 3 years (18.7% CAGR). We therefore set our TP for Kernel at PLN60/share (down 19% from PLN74 previously) and downgrade our rating to **HOLD** from Buy.

DCF valuation

Our 10-year DCF approach yields a fair equity value of \$1.46bn, which is equivalent to PLN60/share at the current exchange rate.

Our model assumes a constant WACC of 12.4% based on a 15% cost of equity and 7% after-tax cost of debt. We believe Kernel will be successful in keeping the cost of debt low in the future, as the company has grown to be an extremely large institution with assets that can be used as collateral (OEP plants, elevators, and the transshipping terminal).

Figure 28: Kernel DCF valuation, \$mn

	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
EBIT	232	269	284	273	270	254	247	225	219
Less taxation	-10	-15	-16	-19	-19	-20	-25	-23	-22
Tax adjusted EBIT	222	254	267	254	251	234	222	203	197
Tax shield on interests	-1	-1	-1	0	0	0	0	0	0
Depreciation	29	29	28	28	27	27	26	25	25
Less: Capex	-112	-34	-29	-28	-28	-27	-27	-26	-25
Change in working capital	-134	-23	-34	-26	-21	-22	-20	-22	-23
Unleveraged free cash flow	3	225	232	227	230	211	202	180	174
WACC	12.5%	12.5%	12.5%	12.5%	12.5%	12.5%	12.5%	11.5%	11.5%
Discounted cash flow	2	178	163	142	128	104	89	71	61
Future cash flow growth rate	3.0%								
Terminal value	2,238								
Discounted terminal value	791								
Net debt	266								
Fair equity value	1,463								
Implied TP (in PLN)	60								
Implied multiples									
P/E	7.4	6.2	5.7	5.9	5.9	6.3	6.6	7.2	7.4
EV/EBITDA	6.6	5.8	5.5	5.8	5.8	6.2	6.3	6.9	7.1

Source: Renaissance Capital estimates

We set our WACC in perpetuity at 11% in order to reflect Kernel's below-average risk and the growth rate at 3%.

Figure 29: Sensitivity of share price to WACC and growth rate, PLN/share

		Perpetuity growth rate				
		1%	2%	3%	4%	5%
WACC in perp.	9%	59	64	71	80	94
	10%	56	60	65	71	81
	11%	53	56	60	65	72
	12%	51	53	56	60	65
	13%	49	51	54	57	61

Source: Renaissance Capital estimates

We note that Kernel's shares are actually relatively insensitive to the price of oil, as the company makes its profits on the spreads between seed and oil prices (we basically employ a fixed margins assumption here), and the same applies to the price of grain.

Main model assumptions

We see Kernel's operating profit growth mainly coming from the expansion of seed crushing capacities in operation and grain trading volumes (although 2010-2015E CAGR is negative due to an assumed 20% export volume decline in 2011E). The silo segment receives the largest boost in 2011 due to the acquisition of 600kt of storage facilities from Allseeds in April, while the transshipment division volumes grow at 3-4% every year until they are capped at 3.1mnt in 2014. We assume that Kernel's farming segment stays fixed at 84,000 ha, as the company has not announced any plans to expand and/or cut it.

Figure 30: Kernel's operating volumes and capacities

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2010-15E CAGR
Seed crushing capacity in operation, mnt	675	730	1,137	2,036	2,041	2,046	2,051	2,056	12.6%
Grain trading volumes, '000t	335	2,260	2,485	1,998	2,158	2,330	2,440	2,440	-0.4%
Silo service volumes, '000t	1099	1925	1247	1840	1928	1952	1952	1952	9.4%
Transshipment volumes, '000t	3,381	3,125	3,225	3,325	3,425	3,525	3,525	3,525	1.8%
Total harvest volumes, '000t	69	223	223	238	250	250	250	250	2.4%
Harvested area, '000 ha	26	84	84	84	84	84	84	84	0.0%

Source: Renaissance Capital estimates

Kernel's valuation is, in our view, almost entirely dependent on prospective margins both in oil and grain trading. We think the company's profitability will suffer as Ukraine's farmers become more consolidated and the local market becomes more developed, as currently both oil and trading profits are based on purchasing commodities in the fields at low prices. We therefore gear Kernel's margins towards peer companies (Bunge and ADM), ending up with a 7% combined EBIT margin in oil, and a 6% margin in trading. In order to refrain from being overly conservative, we leave our gross margin estimates at both silo and transshipping terminal at roughly 50% (vs 60-70% in 2009).

Figure 31: Kernel key margin forecasts¹, %

	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Combined oil margin, EBIT	21	16	14	16	16	14	13	11	10	8	7
Trading margin, EBIT	8	9	8	8	8	7	7	7	7	6	6
Silo segment margin, gross	74	74	69	66	64	62	59	57	54	51	49
Transshipping margins, gross	58	58	58	57	56	56	55	54	53	52	51
Farming margins, gross	14	21	25	25	25	26	26	26	26	26	26

(1) We look at EBIT margins for oil and trading divisions because these segments include freight costs, which means that the gross margin figure is meaningless. In contrast, for silo and transshipping service segments gross and EBIT margins are close

Source: Company data, Renaissance Capital estimates

Financial history and projections

We note that our forecasts and historical financials are net of biological revaluation (according to IAS 41, biological assets need to be at fair value on the balance sheet, which affects the income statement). For historical financials, we group biological assets together with inventories on the balance sheet.

Figure 32: Kernel IFRS income statement and operating data, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Revenue	663	1,047	1,257	1,569	1,751	1,906	2,018	2,102	2,187	2,266	2,346	2,440
CoGS	-495	-707	-875	-1,129	-1,248	-1,366	-1,470	-1,545	-1,633	-1,707	-1,795	-1,880
Gross profit	168	340	382	440	503	540	548	557	553	559	551	560
SG&A expenses	-70	-167	-186	-206	-234	-260	-281	-295	-309	-324	-340	-357
Other operating income, net	7	18	21	26	29	32	34	35	36	38	39	41
EBITDA	105	191	217	261	298	312	300	297	281	273	251	244
D&A	-12	-23	-26	-29	-29	-28	-28	-27	-27	-26	-25	-25
EBIT	93	168	191	232	269	284	273	270	254	247	225	219
Financial expenses	-28	-32	-24	-25	-17	-11	-7	-2	0	0	0	0
Other non-operating income/expenses	5	-4	0	0	0	0	0	0	0	0	0	0
PBT	73	128	167	207	252	272	266	268	254	247	225	219
Income (tax)/benefit	-9	5	-8	-10	-15	-16	-19	-19	-20	-25	-23	-22
Net income	64	133	158	197	237	256	247	249	234	222	203	197
Margins												
Gross	25.3%	32.4%	30.4%	28.1%	28.7%	28.4%	27.1%	26.5%	25.3%	24.7%	23.5%	23.0%
EBITDA	15.8%	18.3%	17.2%	16.6%	17.0%	16.4%	14.9%	14.1%	12.8%	12.0%	10.7%	10.0%
Net income	9.7%	12.7%	12.6%	12.5%	13.5%	13.4%	12.2%	11.9%	10.7%	9.8%	8.6%	8.1%
Main operating data												
Bulk oil sales, '000t	167	224	379	727	802	798	798	792	795	796	799	805
Bottled oil sales, mn litres	101	98	109	117	127	132	135	143	144	144	144	144
Land under cultivation, '000ha	26	84	84	84	84	84	84	84	84	84	84	84
Export volume, '000t	317	2,260	2,485	1,998	2,158	2,330	2,440	2,440	2,440	2,440	2,440	2,440
Net debt, \$mn	167	165	256	272	61	-163	-385	-614	-826	-1,029	-1,210	-1,384
Other ratios												
Net debt/EBITDA	1.6	0.9	1.2	1.0	0.2	neg	neg	neg	neg	neg	neg	neg
ROIC	16%	19%	20%	20%	23%	21%	18%	17%	14%	12%	10%	0%
ROE	25%	33%	36%	32%	29%	24%	19%	16%	13%	11%	9%	0%
SG&A as % of revenue	11%	16%	15%	13%	13%	14%	14%	14%	14%	14%	14%	15%

Source: Company data, Renaissance Capital estimates

Figure 33: Kernel IFRS balance sheet, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
PP&E, net	232	222	404	488	493	493	494	495	495	496	496	497
Construction in progress	0	0	0	0	0	0	0	0	0	0	0	0
Deferred tax assets	0	0	0	0	0	0	0	0	0	0	0	0
Other non-current assets	147	100	100	100	100	100	100	100	100	100	100	100
Non-current assets	378	321	504	588	592	593	594	594	595	595	596	597
Cash & equivalents	89	129	218	78	166	337	458	614	826	1,029	1,210	1,384
Trade receivables & prepayments	30	26	41	52	58	63	66	69	72	75	77	80
Inventories	187	118	166	272	277	297	314	328	344	357	374	389
Other current assets	72	105	126	157	175	191	202	210	219	227	235	244
Current assets	377	378	551	559	676	887	1,041	1,221	1,460	1,687	1,895	2,097
Total assets	756	700	1,055	1,147	1,268	1,480	1,634	1,815	2,055	2,282	2,491	2,694
Share capital	2	2	2	2	2	2	2	2	2	2	2	2
Retained earnings	104	240	398	595	832	1,088	1,335	1,584	1,818	2,040	2,243	2,440
Reserves and other	335	116	116	116	116	116	116	116	116	116	116	116
Shareholder equity	440	357	516	713	950	1,205	1,452	1,702	1,936	2,158	2,360	2,558
LT interest bearing debt	98	133	274	224	174	124	74	0	0	0	0	0
Deferred tax liabilities	32	14	17	21	24	26	27	29	30	31	32	33
Other non-current liabilities	0	0	0	0	0	0	0	0	0	0	0	0
Non-current liabilities	130	147	291	245	198	150	101	29	30	31	32	33
ST loans	151	150	150	77	3	0	0	0	0	0	0	0
Current portion of LT debt	7	11	50	50	50	50	0	0	0	0	0	0
Trade payables & prepayments	27	33	48	62	68	75	81	85	89	94	98	103
Taxes payable	0	0	0	0	0	0	0	0	0	0	0	0
Other current liabilities	0	0	0	0	0	0	0	0	0	0	0	0
Current liabilities	185	195	248	189	121	125	81	85	89	94	98	103
Total liabilities & equity	756	700	1,055	1,147	1,268	1,480	1,634	1,815	2,055	2,282	2,491	2,694
Net debt	167	165	256	272	61	-163	-385	-614	-826	-1,029	-1,210	-1,384
Net debt/Equity	0.4	0.5	0.5	0.4	0.1	-0.1	-0.3	-0.4	-0.4	-0.5	-0.5	-0.5

Source: Company data, Renaissance Capital estimates

We forecast that Kernel will accumulate a relatively large amount of cash on its balance sheet by 2014E, and believe that the company is likely to make an acquisition or expand

its land bank at that time. However, we do not have any guidance on such developments at the moment, and therefore in our estimates, we let the cash sit on Kernel's balance sheet (in terms of fair equity value this scenario is equivalent to one where dividends are paid).

Figure 34: Kernel IFRS cash flow statement, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Profit before tax	64.1	133.4	166.7	207.1	252.1	272.3	265.5	268.0	254.2	247.0	225.2	219.2
Depreciation	-11.6	-23.4	26.2	28.6	29.0	28.5	27.9	27.3	26.7	26.1	25.4	24.8
Income tax paid	-3.4	-1.7	-8.3	-10.4	-15.1	-16.3	-18.6	-18.8	-20.3	-24.7	-22.5	-21.9
Increase in working capital	-185.4	45.6	-68.8	-133.9	-23.1	-33.9	-26.0	-21.0	-22.2	-19.6	-22.5	-23.5
Less non-oper. income/cost	10.7	-24.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating cash flow	-125.6	129.3	115.8	91.4	242.9	250.5	248.8	255.5	238.3	228.7	205.7	198.6
Capital expenditures, net	-24.4	-88.6	-208.9	-112.4	-33.6	-29.0	-28.5	-27.9	-27.3	-26.7	-26.1	-25.4
Other investments, net	-145.7	-6.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Investing cash flow	-170.1	-95.3	-208.9	-112.4	-33.6	-29.0	-28.5	-27.9	-27.3	-26.7	-26.1	-25.4
Net borrowings/(repayments)	61.7	80.8	179.1	-122.8	-124.6	-52.5	-100.1	-73.6	0.0	0.0	0.0	0.0
Other	253.7	-45.3	2.8	4.2	2.5	2.1	1.5	1.1	1.2	1.1	1.1	1.3
Financing cash flow	315.4	35.6	181.9	-118.5	-122.2	-50.4	-98.6	-72.5	1.2	1.1	1.1	1.3
Net change in cash and translation difference	34.1	39.3	120.0	-139.6	87.1	171.0	121.8	155.2	212.1	203.1	180.7	174.4
Cash, bop	24.8	58.8	98.1	218.0	78.4	165.6	336.6	458.4	613.6	825.7	1,028.8	1,209.5
Cash, eop	58.8	98.1	218.0	78.4	165.6	336.6	458.4	613.6	825.7	1,028.8	1,209.5	1,383.9

Source: Company data, Renaissance Capital estimates

Peer valuation

As we see it, the best peers for Kernel are Bunge and ADM. While being roughly 7x and 13x larger, respectively, they derive most of their operating profit from grain trading and oil processing (note that as with Kernel, both Bunge and ADM purchase most of their oilseeds externally). We believe Bunge offers the closest comparison to Kernel, as it has two OEPs as well as silos in Ukraine and is a direct competitor to Kernel.

For comparison purposes, we also include a 'pure trader' group (Graincorp and Viterra), as well as a 'pure processor' (all oilseeds acquired externally) located in Poland (Elstar Oils).

Figure 35: Peer valuation, as of 25 Aug 2010

	Ticker	Country	Price, \$	MktCap, \$mn	P/E			EV/EBITDA			EV/Sales		
					2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E
Kernel	KER PW	UA	19.5	1425	9.0	7.2	6.0	7.8	6.5	5.0	1.5	1.1	0.9
Bunge	BG US	US	52.1	7302	14.1	8.9	8.1	6.0	4.6	4.3	0.2	0.2	0.2
ADM	ADM US	US	30.1	19362	10.5	10.4	9.5	7.0	6.7	5.6	0.4	0.4	0.3
Closest peer average					12.3	9.7	8.8	6.5	5.6	5.0	0.3	0.3	0.2
Premium to closest peers					-27%	-25%	-32%	19%	15%	0%	437%	343%	303%
Graincorp	GNC AU	AU	6.0	1187	15.0	10.4	9.8	7.6	5.6	5.2	0.8	0.6	0.6
Viterra	VT CN	CA	8.1	3028	19.5	13.4	11.3	7.8	6.3	5.2	0.4	0.4	0.4
Pure trader average					17.2	11.9	10.6	7.7	5.9	5.2	0.6	0.5	0.5
Premium to pure traders					-48%	-39%	-43%	1%	10%	-5%	144%	120%	99%
Elstar Oils	ELS PW	PL	2.0	98	10.4	7.8	na	9.4	7.9	na	0.8	0.7	na
Premium to oil processor					-14%	-7%	na	-18%	-17%	na	83%	55%	na

Source: Bloomberg, Renaissance Capital estimates

Our closest peer average shows that on an EV/EBITDA basis Kernel trades at a 19% premium for 2010E, on 15% premium for 2011E, and at the same level for 2012E, which makes sense in our view, given Kernel's capacity expansion and utilisation rate growth over these three years. That said, we do not think the multiples suggest any upside to Kernel's price either.

Comparing Kernel to 'pure traders' average multiples suggests a similar story – premiums of 1% and 10% respectively on EV/EBITDA 2010E and 2011E, followed by a discount on 2011E. We think this again makes sense given Kernel's EBITDA growth in the next 3 years (18.7% CAGR over 2010-2013). We are somewhat surprised by Elstar Oils, which seems to be trading at a premium compared to Kernel, but think that this may have to do with stock specifics, as Elstar trades over 50% above oil producers (companies that grow their own oilseeds, as are therefore more vertically integrated) such as Sipef and TH Plantations.

We note that that comparing Kernel with Bunge alone (the best match, in our view) actually suggests to us that Kernel may be overvalued.

The farming universe

We begin coverage of the Ukrainian farming universe with three small-cap stocks: Landkom, MCB Agricole, and Sintal Agriculture. We are very positive on Landkom because of its liquidity, which is roughly 10x that of both MCB and Sintal (\$140k/day 12-month average trading volumes), but along with Sintal find it already trading close to our TP, having been driven over 25% upwards since the beginning of July on the wheat price rally. Our top-pick agro name is MCB; it is relatively illiquid, but is very cheap, in our view (we calculate close to 90% implied upside potential).

Overall, we are very bullish on Ukrainian farming, which we think will benefit from consolidation and the formation of a more organised domestic market for agricultural commodities. Furthermore, we believe it offers the only opportunity to invest in profitable large-scale crop growing.

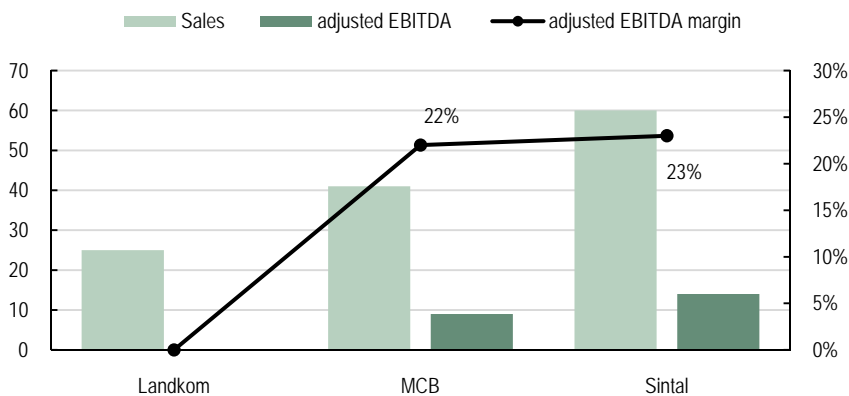
Figure 36: Farming companies comparison

	Landkom	MCB Agricole	Sintal Agriculture
MCAP, \$mn	62	41	142
Value traded per day (12m average), \$ '000	140	9	14
2010 harvested land, '000ha	40	80	88
2009 winter wheat yield, t/ha	4.5	3.6	3.0

Source: Company data, Renaissance Capital estimates

The most profitable of the three agro companies is Sintal, which we conservatively expect to attain an EBITDA margin of 23% in 2010. We think MCB will be able to reach Sintal's level in 2010E (such a profitability level is unusually low for Sintal, but unusually high for MCB, as we expect Sintal to lose a large share of crops this year in contrast to MCB).

Figure 37: 2010E Sintal, MCB, Landkom sales (\$mn), adjusted EBITDA⁽¹⁾(\$mn), and adjusted EBITDA margin



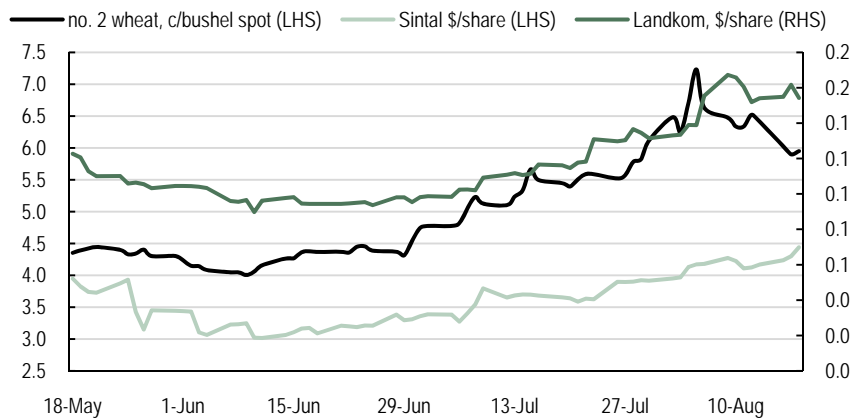
(1) EBITDA excluding biological revaluation

Source: Renaissance Capital estimates

Eroding the farming Buy

The recent wheat rally has led us to put **HOLD** ratings on both Sintal and Landkom, as both stocks' prices have grown over 25% since the beginning of July as a result of the wheat-price appreciation. We advise watching both of these names closely, as we believe that wheat prices are going to drop in the next few months, and both Landkom and Sintal may go below their targets on such news (this is especially true of Landkom, which is much more liquid than Sintal; the stock has already stopped growing, resembling what is happening to wheat with a lag).

Figure 38: World wheat price vs Sintal and Landkom share performance over the last three months



Source: Bloomberg

Valuation principles

We value companies in our farming universe using a 10-year DCF model and peer valuation. Our DCF approach implies significant upside potential for MCB (93%), but suggests that both Sintal and Landkom may already be trading near their fair valuations (we found a 4% upside potential for Sintal and a 1% upside for Landkom).

For peer comparison we look mostly at 2010E and 2011E EV/EBITDA multiples and EV/ha of harvested land corrected for land ownership (the value of owned land is subtracted from the EV in order to arrive at this multiple) as P/E ratios can be distorted easily by different levels of leverage, which is often found in start-ups (Ukrainian farming companies are mostly debt-free, but this is not true of their Russian and Brazilian peers). We once again confirmed MCB to be quite cheap, while we found Sintal and Landkom to be trading fairly

DCF model principal assumptions

The following are the most important assumptions that we used in all of our farming models:

No biological revaluation. According to IFRS accounting standards (IAS 41) biological assets have to be kept at fair value on the balance sheet, which means that income statements of agricultural companies are flooded with revaluation effects. We find revaluation to be misleading and easy to manipulate, and therefore provide forecasts on a historical accounting basis only (we also provide revaluation-free historical financials; on the balance sheet we group together inventories and biological assets). An additional bonus to providing revaluation-free financials is that it makes agricultural companies that use US GAAP (such as those located in Brazil) comparable with Ukrainian peers.

Capped profitability in perpetuity. While we are bullish on Ukrainian farming, we believe it is unreasonable to assume very high perpetual profitability, as competition in the sector will increase and government subsidies will go down, both of which will squeeze margins. We cap the EBITDA margin for all of our Ukrainian farmers at just

above 20%, which we think is a reasonable level that can be sustained over the long term.

Organic land bank growth ends in 2017. We think that Ukrainian farming will near consolidation in nine years, and that it will become extremely difficult to grow harvested land banks without large-scale acquisitions. On this basis, we favour companies that already harvest large land banks, as we believe they will end up generating larger amounts of cash in perpetuity.

Land-sale moratorium still active. As there are a multitude of scenarios that can come from the land moratorium being lifted, we assume the current situation to hold indefinitely. As perpetual leasing should theoretically be equivalent to acquiring land, we find the assumption to be reasonable for modelling purposes even if the ban is lifted in reality.

In all of our models we assumed the same soft commodity prices in the forecasting period, as given below:

Figure 39: 2010E-19E Ukrainian domestic crop price assumptions, UAH/t

	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Winter wheat	1,000	1,057	1,017	1,125	1,194	1,265	1,341	1,408	1,479	1,552
Spring wheat	1,000	1,057	1,017	1,125	1,194	1,265	1,341	1,408	1,479	1,552
Winter barely	1,000	995	909	919	931	957	954	963	969	994
Spring barley	1,000	995	909	919	931	957	954	963	969	994
Rye	900	849	8,24	839	833	841	858	856	862	868
Corn	1,000	1,082	1,004	1,034	1,034	1,034	1,034	1,034	1,034	1,034
Buckwheat	2,999	2,752	2,657	2,657	2,657	2,657	2,657	2,657	2,657	2,657
Winter rapeseed	2,800	2,860	3,015	3,242	3,439	3,646	3,864	4,058	4,261	4,474
Spring rapeseed	2,800	2,860	3,015	3,242	3,439	3,646	3,864	4,058	4,261	4,474
Sunflower seed	2,400	2,193	2,162	2,156	2,169	2,215	2,234	2,260	2,273	2,274
Soybean	2,606	2,426	2,384	2,352	2,352	2,352	2,352	2,352	2,352	2,352

Source: FAPRI, Bloomberg, Renaissance Capital estimates

Landkom: Company overview

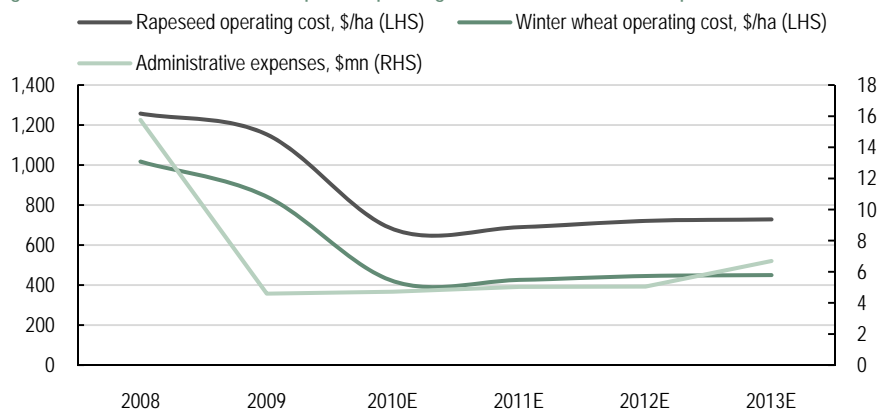
Landkom is an agricultural producer located in western Ukraine (near Lviv) that manages a 74,000 ha land bank (40,000 ha to be harvested in 2010) and specialises in the production of wheat, corn, rapeseed, and soybeans. The company was incorporated in early 2007 and raised \$111mn via an IPO in November of the same year (AIM listing) and an additional \$43mn through three SPOs in 2008-2009. Today Landkom is the most liquid Ukrainian farming name, with an estimated 12-month daily traded volume of \$0.14mn and a market cap of \$45mn.

A difficult history

Landkom's farming operation has been losing money since it began operating in 2007. In its first year the company's EBIT was at -\$1.9mn and in 2008 the loss increased to \$57.1mn. As a result of such a poor performance, Landkom's management has been reshuffled and Richard Spinks, the company's former CEO, was asked to step down (May 2009).

With a new team on board (Vitaliy Skotsyk as the new CEO) the company started a reformation. While the FY09 results were still unimpressive (-\$27.4mn operating profit loss posted), the new management was able to cut production costs by 19% YoY on comparable crops, and slashed administrative expenses by some 70% compared with 2008 levels. With this year's harvest nearing completion, we are looking at an additional 40-50% YoY operating cost cut per hectare practically without a yield loss, which we think means that company will nearly break even on EBITDA (we expect a slight loss at -\$2.2mn).

Figure 40: Landkom historical and expected operating costs and administrative expenses



Source: Company data, Renaissance Capital estimates

Still running on injected cash

While we have been impressed with Landkom's ability to cut costs, we expect the company to still post a \$3.3mn operating cash-flow loss in FY10, which means it will still have to depend on previously injected cash (namely the \$16mn SPO fund raising in Nov 2009) in order to fund the upcoming season's sowing and harvesting campaigns. Due to Landkom's loss-making history, we think it will be difficult for the company to raise any additional funds via debt or equity (except trade credit), which in our view means that expansion in the near term will have to be done with great care. During a conference call

in August, management said it was looking to plant 50,000 ha, which in our view is an achievable target.

The last chance

Overall, we find Landkom’s new management efforts to revitalise the company to be very positive and are particularly encouraged by the level of transparency and high end corporate governance so rarely found in Ukraine. That said, we believe Landkom still has to be treated as a high risk operation – it only just avoided a total shut-down back in early 2009. Considering that investors have already invested a total of \$168mn from 2007 to 2009, we are doubtful that the company will be able to raise more funding if the road to recovery turns out to be overly bumpy.

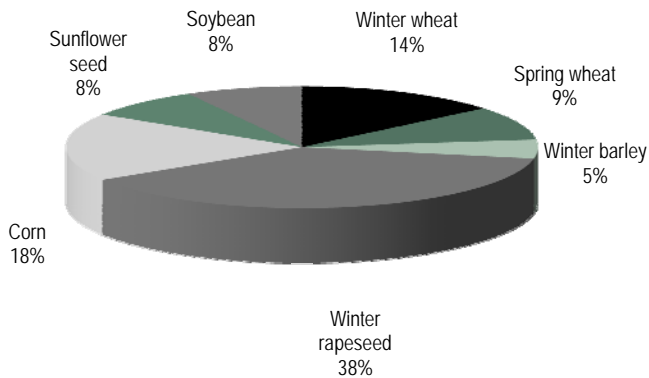
Figure 41: Landkom fund raising history, \$mn

	2007	2008	2009
Pre-IPO, April	14		
IPO, November	111		
SPO, March		22	
SPO, March			5
SPO, November			16
Subtotal	125	22	21

Source: Company data, Renaissance Capital estimates

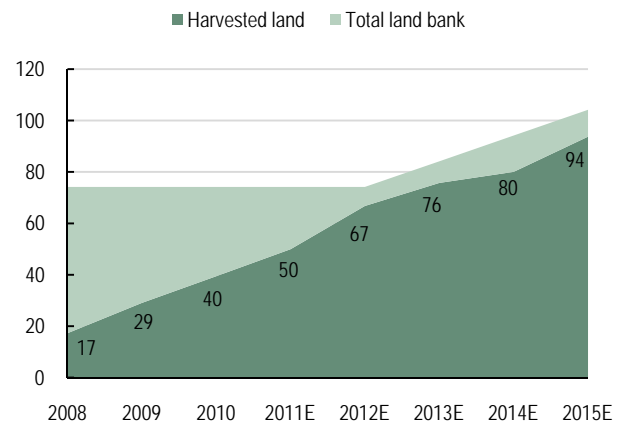
Land bank summary

Figure 42: Landkom 2010E harvested area breakdown



Source: Company data

Figure 43: Landkom 2008-15E land bank dynamics, '000ha



Source: Company data, Renaissance Capital estimates

Landkom: Valuation

Our approach to Landkom's valuation is based on a 10-year operating model and peer trading multiples. Our DCF valuation suggests that Landkom is already trading close to its fair value. From relative valuation we can only conclude that the company does not look undervalued and that its premium to peers on 2010E EV/EBITDA and EV/ha harvested multiples is justified by rapid profitability growth. We thus set Landkom's target price at GBp9.6/share, and initiate coverage of the stock with a **HOLD** rating.

DCF

We assume a somewhat high WACC for Landkom in order to reflect the company's above average risk: 20% in 2011 that slowly decreases to 15% and stays that way in perpetuity. We assume the terminal growth rate to be at the usual 3%.

Our valuation suggests a fair equity value at \$64mn (an EV of \$54mn), which is equivalent to GBp9.6/share.

Figure 44: Landkom DCF model, \$mn

	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
EBIT	-7	0	3	8	14	18	20	22	21	19
Less taxation	0	0	0	0	0	0	-1	-1	-1	-1
Tax adjusted EBIT	-7	0	3	8	14	18	20	21	20	19
Tax shield on interests	0	0	0	0	0	0	0	0	0	0
Depreciation	4	4	4	5	5	5	5	6	6	6
Less: Capex	-3	-2	-14	-13	-10	-17	-14	-5	-6	-6
Change in working capital	-1	-1	-5	-1	-1	-3	-2	-1	-1	-1
Unleveraged free cash flow	-7	1	-11	-1	7	3	9	21	19	18
WACC		20.0%	20.0%	19.0%	18.0%	17.0%	16.0%	15.0%	15.0%	15.0%
Discounted cash flow		1	-8	0	3	1	3	7	5	4
Future cash flow growth rate		3%								
Terminal value		155								
Discounted terminal value		37								
Net debt		-10								
Fair equity value		64								
Implied TP (in GBp)		9.6								
Implied multiples										
P/E (adjusted)	neg	neg	20.1	8.6	4.8	3.6	3.2	3.0	3.1	3.4
EV/adjusted EBITDA	neg	12.5	6.8	4.3	2.9	2.4	2.1	2.0	2.0	2.2

Source: Company data, Renaissance Capital estimates

Figure 45: Sensitivity of share price to WACC and growth rate, GBp/share

		Perpetuity growth rate				
		1%	2%	3%	4%	5%
WACC in perp.	13%	9.4	10.0	10.7	11.5	12.5
	14%	9.0	9.5	10.1	10.7	11.5
	15%	8.7	9.1	9.6	10.1	10.8
	16%	8.4	8.7	9.1	9.6	10.2
	17%	8.1	8.4	8.8	9.2	9.7

Source: Renaissance Capital estimates

Figure 46: Landkom IFRS income statement and operating data, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Revenue	11	15	25	34	43	59	69	82	96	106	112	117
CoGS	-38	-30	-23	-26	-32	-42	-46	-54	-65	-72	-79	-84
Gross profit	-27	-16	2	8	11	18	23	28	32	34	34	33
SG&A expenses	-16	-4	-5	-5	-5	-8	-8	-10	-11	-12	-12	-13
Other operating income, net	-5	-1	0	1	2	3	3	4	5	5	5	5
Adjusted EBITDA	-47	-21	-2	4	8	13	18	23	26	27	27	25
D&A	-5	-6	-4	-4	-4	-5	-5	-5	-5	-6	-6	-6
EBIT	-52	-27	-7	0	3	8	14	18	20	22	21	19
Financial expenses	2	0	0	0	0	0	0	0	0	0	0	0
Other non-operating income/expenses	0	-15	0	0	0	0	0	0	0	0	0	0
PBT	-51	-42	-7	0	3	7	13	18	20	22	21	19
Income (tax)/benefit	0	-15	0	0	0	0	0	0	0	0	0	0
Net income	-56	-40	-7	0	3	7	13	18	20	21	20	19
Margins												
Gross	-254%	-108%	8%	23%	25%	30%	34%	35%	33%	32%	30%	28%
EBITDA	-443%	-144%	-9%	13%	18%	21%	27%	28%	27%	26%	24%	21%
Adjusted net income	-522%	-277%	-27%	0%	7%	12%	19%	21%	21%	20%	18%	16%
Main operating data												
Harvested land bank, '000ha	17	29	40	50	67	76	80	94	103	103	103	103
Grain harvest, '000t	26	52	78	123	161	189	211	243	270	281	285	285
Total harvest, '000t	46	91	130	178	235	273	306	354	395	413	421	421
Net debt, \$mn	-4	0	-10	-10	1	2	-4	-7	-16	-37	-56	-75
Other ratios												
Net debt/adjusted EBITDA	0.1	0.0	4.4	neg	0.1	0.2	neg	neg	neg	neg	neg	neg
ROIC	-133%	-71%	-14%	0%	6%	12%	18%	21%	20%	17%	15%	0%
ROE	-146%	-68%	-14%	0%	6%	13%	19%	21%	19%	17%	14%	0%
SG&A as % of revenue	146%	30%	18%	14%	11%	13%	12%	12%	11%	11%	11%	11%

Source: Company data, Renaissance Capital estimates

Figure 47: Landkom IFRS balance sheet, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
PP&E, net	48	41	39	37	47	55	60	72	80	80	80	79
Construction in progress	0	0	0	0	0	0	0	0	0	0	0	0
Deferred tax assets	0	0	0	0	0	0	0	0	0	1	1	1
Other non-current assets	0	0	0	0	0	0	0	0	0	0	0	0
Non-current assets	49	41	39	37	47	55	60	72	81	80	80	79
Cash & equivalents	4	0	10	10	2	3	4	7	16	37	56	75
Trade receivables & prepayments	11	1	2	3	4	6	9	11	13	15	15	16
Inventories	21	9	8	10	16	17	18	21	25	27	29	30
Other current assets	0	0	0	0	0	0	0	0	0	0	0	0
Current assets	36	10	20	23	22	27	31	40	54	78	100	121
Total assets	85	51	59	61	69	82	92	112	135	158	181	201
Share capital	0	0	0	0	0	0	0	0	0	0	0	0
Retained earnings	-54	-98	-104	-104	-101	-94	-81	-63	-43	-22	-2	17
Reserves and other	130	140	156	156	156	156	156	156	156	156	156	156
Shareholder equity	76	43	52	52	55	63	76	94	113	134	155	174
LT interest bearing debt	0	0	0	0	0	0	0	0	0	0	0	0
Deferred tax liabilities	0	0	0	0	0	0	0	0	0	0	0	0
Other non-current liabilities	0	0	0	0	0	0	0	0	0	0	0	0
Non-current liabilities	0	0	0	0	0	0	0	0	0	0	0	0
ST loans	0	0	0	0	3	5	0	0	0	0	0	0
Current portion of LT debt	0	0	0	0	0	0	0	0	0	0	0	0
Trade payables & prepayments	8	7	5	5	7	9	9	11	13	15	16	17
Taxes payable	0	0	0	0	0	0	0	0	0	0	0	0
Other current liabilities	1	1	2	3	3	5	6	7	8	8	9	9
Current liabilities	9	8	7	8	13	19	15	18	21	23	25	27
Total liabilities & equity	• 85	• 51	• 59	• 61	• 69	• 82	• 92	• 112	• 135	• 158	• 181	• 201
Net debt	-4	0	-10	-10	1	2	-4	-7	-16	-37	-56	-75
Net debt/Equity	neg	neg	neg	neg	0	0	neg	neg	neg	neg	neg	neg

Source: Company data, Renaissance Capital estimates

We forecast that Landkom will accumulate a relatively large amount of cash on its balance sheet starting in 2017E, but do not assume any more land bank growth, as it would counter our general assumption of land being consolidated by that time. We think Landkom may either start paying dividends or expand its business in other directions, such as into production of biofuels.

Figure 48: Landkom IFRS cash flow statement, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Profit before tax	-55.6	-40.3	-6.7	0.0	3.2	7.4	13.2	17.7	20.4	21.7	21.0	19.2
Depreciation	-4.9	-6.4	4.5	4.3	4.5	4.7	4.9	5.1	5.4	5.6	5.6	5.5
Income tax paid	-0.2	0.0	-0.1	0.0	0.0	-0.1	0.0	-0.1	-0.7	-0.7	-0.7	-0.6
Increase in working capital	-23.0	1.9	-1.2	-1.3	-4.9	-0.8	-1.5	-3.0	-1.9	-0.8	-1.0	-0.6
Less non-oper. Income/cost	19.3	35.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating cash flow	-64.5	-9.1	-3.3	3.0	3.0	11.8	16.9	19.9	23.3	25.8	24.9	23.6
Capital expenditures, net	-37.6	-0.4	-3.2	-2.2	-14.2	-12.6	-10.2	-16.7	-14.1	-5.1	-5.6	-4.3
Other investments, net	-0.6	-0.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Investing cash flow	-38.2	-0.7	-3.2	-2.2	-14.2	-12.6	-10.2	-16.7	-14.1	-5.1	-5.6	-4.3
Net borrowings/(repayments)	20.7	5.7	0.0	0.0	3.3	2.1	-5.1	-0.3	0.0	0.0	0.0	0.0
Other	0.1	0.3	15.9	0.0	0.0	-0.1	0.0	-0.1	-0.1	0.0	0.0	0.0
Financing cash flow	20.8	6.0	15.9	0.0	3.2	2.1	-5.2	-0.3	-0.1	0.0	0.0	0.0
Net change in cash and translation difference	-83.4	-4.0	9.4	0.8	-8.2	0.8	1.2	2.8	9.1	20.7	19.3	19.3
Cash, bop	87.6	4.2	0.2	9.6	10.4	2.2	3.0	4.2	7.0	16.1	36.8	56.1
Cash, eop	4.2	0.2	9.6	10.4	2.2	3.0	4.2	7.0	16.1	36.8	56.1	75.4

Source: Company data, Renaissance Capital estimates

Peer valuation

Overall, we think that it is difficult to value Landkom by multiples, as the company will be close to breaking even this year and will then show a rapid earnings growth in the next two years (80% CAGR in EBITDA over 2011-2013), which relative valuation does not account for.

In our opinion, the best peers for Landkom are Sintal and MCB – companies that both run farming operations in Ukraine and do not own any land (although MCB is undervalued, in our opinion). We also include Black Earth Farming, SLC Agricola, and Brasil Agro, however, to increase our peer group and to populate it with companies that we do not value in this report.

Figure 49: Landkom peer valuation, as of 25 Aug 2010

Ticker	Country	Price, \$	MktCap, \$mn	P/E			EV/EBITDA ⁽⁴⁾			EV/Sales			EV/ha harvested	EV/ha harvested (less ownership) ³	
				2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2010E	
Landkom	LKI LN	UA	0.1	62	neg	neg	19.5	neg	12.0	8.0	2.1	1.5	1.5	1331	1331
MCB Agricole	4GW1 GR	UA	2.4	41	5.5	6.0	6.6	4.6	4.9	5.5	1.0	0.7	0.6	509	509
Sintal	SNPS GR	UA	4.3	142	11.5	10.0	7.2	9.9	8.9	6.4	2.3	2.1	1.7	1512	1512
Black Earth Farming ²	BEFSDB SS	RU	2.9	363	162.7	12.4	8.4	34.0	8.9	6.4	3.1	2.5	2.1	1721	1110
SLC Agricola ¹	SLCE3 BZ	BZ	9.1	897	55.6	32.9	21.4	15.6	10.8	9.3	3.0	2.6	2.5	4863	771
Brasil Agro	AGRO3 BZ	BZ	5.6	325	neg	neg	neg	neg	neg	neg	8.8	5.3	4.2		
Peer median					11.5	10.0	7.2	9.9	8.9	6.4	3.0	2.5	2.1	1617	941
Premium to peers					n/a	n/a	171%	n/a	35%	26%	-30%	-39%	-29%	-18%	41%

1 Expected 2010E harvested land based on company 2Q10 report. SLC Agricola owns 247,886 ha of land, 217,865 ha of which was valued by Deloitte Touche Tohmatsu at an average \$3,688/ha at the current exchange rate:

2 Black Earth Farming owns 222,000 ha of land, which we estimate to be valued at \$600/ha;

3 The multiple is arrived at by subtracting the value of owned land from the EV.

4 The multiple is based on adjusted EBITDA (equal to EBITDA less biological revaluation).

Source: Bloomberg, Renaissance Capital estimates

On 2011E EV/EBITDA, Landkom trades at a 35% premium to peers (74% premium to the average multiples of Sintal and MCB), which only occurs because earnings growth is

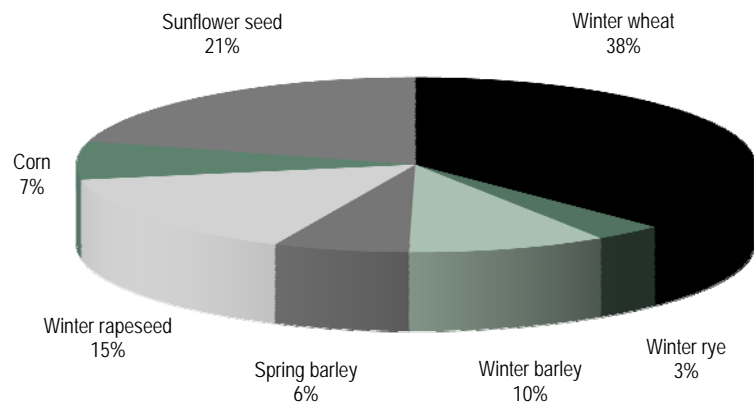
not taken into account. A good way to see this is by looking at the 2011E EV/EBITDA multiple, where the premium goes down to 26%.

If we compare Landkom with its peers based on 2010E EV/ha harvested correct for land ownership, we see that the company trades at a 41% premium to peers. If we take out MCB (a company that we find to be undervalued), the premium drops to 20%. We believe such a premium to be reasonable given that once again Landkom's EBITDA growth is not accounted for by peer valuation.

MCB Agricole: Company overview

MCB Agricole (Ukrzernoprom Agro) began operations in 2006 as an independent crop growing division of a much larger agricultural enterprise named Ukrzernoprom, which has operated on the Ukrainian bread market since 1999. Today the company runs a completely independent operation (although it has the same shareholders as Ukrzernoprom) with 98,000 ha under management, of which it cultivates 82% (a total of 80,000 ha will be harvested this autumn). MCB engages primarily in cultivation of grains (winter wheat) and oilseed crops (winter rapeseed and sunflower seed).

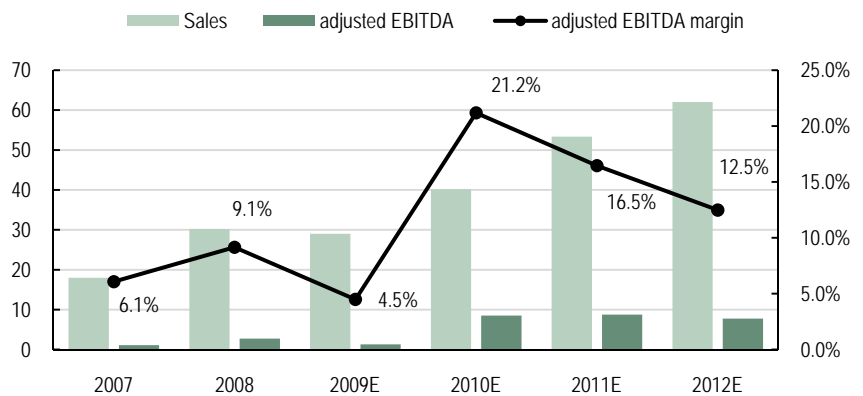
Figure 50: MCB Agricole 2010E harvested land distribution



Source: Company data, Renaissance Capital estimates

Historically, the company has showed reasonable financial results, although profitability margins were notably lower than those of its agricultural peers such as Sintal. We are a little discouraged by the fact that MCB has yet to announce its 2009 financials (expected in September), but the company did provide harvest results last autumn, which, along with management guidance suggest 2009 performance to be weak. Despite relatively poor figures to-date, we think in 2010 MCB may outperform expectations for the first time.

Figure 51: MCB Agricole sales (\$mn), adjusted EBITDA⁽¹⁾ (\$mn), and adjusted EBITDA margin, %



(1) EBITDA excluding biological revaluation

Source: Company data, Renaissance Capital estimates

Misfortunes left behind

In terms of operating performance, we find MCB to be a fundamentally strong player that has been adversely affected by a number of unfortunate circumstances. Specifically, the company has been affected by the following shocks:

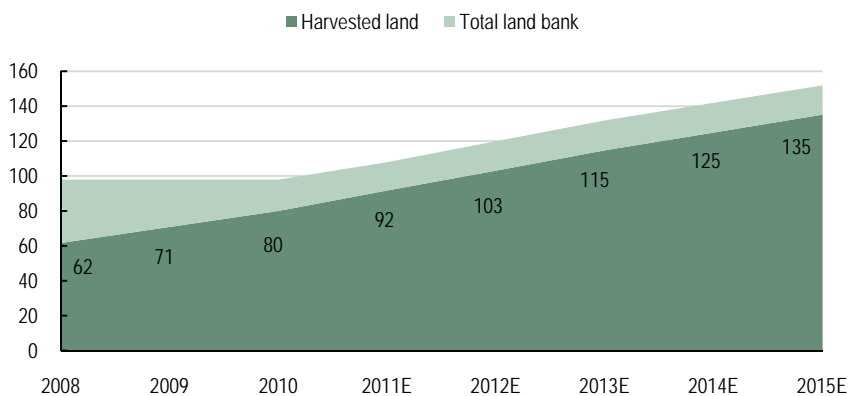
In 2007 MCB expanded its land bank by 85% and had to farm land that was previously subject to improper agricultural practice. The new land produced low yields, which affected the company's average performance.

In 2008 MCB's harvest coincided with the bursting of the worldwide commodity bubble (wheat prices fell 54% in Aug-Dec 2008), which effectively meant that inputs were expensive (fertilisers and plant protectors were purchased prior to the price drop), but output was cheap.

In 2009 the liquidity crisis hit Ukraine, which, combined with low cash reserves on the company's balance sheet from 2008 led to insufficient funding (it was practically impossible for agricultural producers to get a loan at the time). MCB was thus forced to cut back on fertiliser and plant protector use, which once again negatively impacted yields.

This season, however, MCB's situation looks to be the best in four years. The company has lost a relatively small portion of its crops despite harsh weather conditions (a cold winter with little snow in Ukraine and the Eastern European drought) and prices have recently increased over 20% from last year's levels. We expect MCB to show EBITDA profitability above 20% for the first time since founding.

Figure 52: MCB Agricole harvested land bank vs total land bank, '000 ha



Source: Company data, Renaissance Capital estimates

MCB Agricole: Valuation

We value MCB Agricole based on a 10-year operating model and peer trading multiples. Both approaches suggest that MCB could offer close to 90% upside potential. We set MCB's target price at EUR3.8/share and initiate coverage with a **BUY** rating.

DCF

We assume a 19% WACC for MCB in 2010 and reduce it to 13% in perpetuity in order to reflect the company's somewhat low liquidity and the risk associated with not being fully covered by own machinery (MCB can only cover 70,000 ha with its machinery and needs third party services for the rest). MCB's terminal growth rate is set at the usual 3%.

Our valuation suggests a fair equity value of \$92mn (an EV of \$85mn), which is equivalent to EUR3.8/share (93% upside to the current price).

Figure 53: MCB Agricole DCF model, \$mn

	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
EBIT	8	7	6	10	12	19	22	24	25
Less taxation	0	0	0	-1	-1	-1	-1	-1	-1
Tax adjusted EBIT	7	7	6	10	11	18	21	22	24
Tax shield on interests	0	0	0	0	0	0	0	0	0
Depreciation	1	1	1	1	1	2	2	2	3
Less: Capex	-1	-8	-5	-5	-22	-16	-9	-6	-3
Change in working capital	-2	-1	-2	-3	-2	-3	-3	-2	-2
Unleveraged free cash flow	6	0	0	3	-12	0	11	17	22
WACC		19.0%	18.0%	17.0%	16.0%	15.0%	14.0%	13.0%	13.0%
Discounted cash flow		0	0	2	-6	0	5	6	7
Future cash flow growth rate		3.0%							
Terminal value		230							
Discounted terminal value		72							
Net debt		-7							
Fair equity value		92							
Implied TP (in EUR)		3.8							
Implied multiples									
P/E	9.6	10.4	11.5	7.8	6.5	4.1	3.5	3.3	3.1
EV/adjusted EBITDA	12.4	13.5	14.9	9.6	8.3	5.3	4.4	4.1	3.8

Source: Company data, Renaissance Capital estimates

Figure 54: Sensitivity of share price to WACC and growth rate, EUR/share

		Perpetuity growth rate				
		1%	2%	3%	4%	5%
WACC in perp.	11%	3.7	4.1	4.5	5.1	5.8
	12%	3.4	3.7	4.1	4.5	5.1
	13%	3.2	3.5	3.8	4.1	4.6
	14%	3.0	3.2	3.5	3.8	4.2
	15%	2.9	3.1	3.3	3.5	3.8

Source: Renaissance Capital estimates

Figure 55: MCB Agricole IFRS income statement and operating data, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Revenue	30	29	41	58	67	81	94	107	122	132	140
CoGS	-21	-23	-26	-41	-50	-58	-68	-72	-82	-89	-94
Gross profit	8	6	15	17	18	23	26	36	40	43	46
SG&A expenses	-5	-5	-7	-10	-11	-14	-15	-17	-18	-20	-21
Other operating income, net	0	1	1	1	1	2	2	2	2	3	3
Adjusted EBITDA	3	1	9	8	7	11	13	21	24	26	28
D&A	-2	-1	-1	-1	-1	-1	-1	-2	-2	-2	-3
EBIT	1	0	8	7	6	10	12	19	22	24	25
Financial expenses	-1	0	0	0	0	0	0	0	0	0	0
Other non-operating income/expenses	0	0	0	0	0	0	0	0	0	0	0
PBT	0	0	8	7	6	10	12	18	22	24	25
Income (tax)/benefit	0	0	0	0	0	0	0	0	0	0	0
Net income	0	0	7	7	6	10	11	17	21	22	24
Margins											
Gross	28%	19%	37%	29%	26%	28%	28%	33%	33%	33%	33%
EBITDA	9%	4%	22%	14%	11%	13%	14%	19%	20%	20%	20%
Adjusted net income	0%	1%	18%	12%	9%	12%	12%	16%	17%	17%	17%
Main operating data											
Harvested land bank, '000ha	62	71	80	100	112	123	134	144	155	159	161
Grain harvest, '000t	195	149	173	242	279	319	354	389	425	443	453
Total harvest, '000t	240	191	232	308	354	403	445	488	532	554	566
Net debt, \$mn	-2	-2	-1	-7	-7	-7	-10	2	2	-9	-26
Other ratios											
Net debt/adjusted EBITDA	neg	neg	neg	neg	neg	neg	neg	0.1	0.1	neg	neg
ROIC	0%	0%	0%	19%	14%	11%	15%	15%	19%	20%	18%
ROE	0%	0%	0%	18%	13%	11%	14%	14%	19%	19%	17%
SG&A as % of revenue	18%	17%	17%	17%	17%	17%	16%	16%	15%	15%	15%

Source: Company data, Renaissance Capital estimates

Figure 56: MCB Agricole IFRS balance sheet, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
PP&E, net	11	10	11	18	22	26	46	61	68	72	71
Construction in progress	0	0	0	0	0	0	0	0	0	0	0
Deferred tax assets	0	0	0	0	0	0	0	0	0	0	0
Other non-current assets	1	1	1	1	1	1	1	1	1	1	1
Non-current assets	12	10	12	18	22	26	47	62	69	72	71
Cash & equivalents	3	1	7	7	7	10	2	3	9	26	49
Trade receivables & prepayments	2	3	4	6	6	8	9	10	12	13	13
Inventories	19	18	21	21	22	22	22	23	23	23	23
Other current assets	6	9	11	12	13	16	19	21	24	26	28
Current assets	30	30	43	45	49	56	52	57	68	88	114
Total assets	42	40	55	63	71	82	100	119	137	160	185
Share capital	29	27	32	32	32	32	32	32	32	32	32
Retained earnings	-1	-1	7	14	20	29	41	58	79	101	125
Reserves and other	9	9	10	10	10	10	10	10	10	10	10
Shareholder equity	37	36	49	56	62	71	82	100	121	143	167
LT interest bearing debt	0	0	0	0	0	0	0	0	0	0	0
Deferred tax liabilities	0	0	0	0	0	0	0	0	0	0	0
Other non-current liabilities	0	0	0	0	0	0	0	0	0	0	0
Non-current liabilities	0	0	0	0	0	0	0	0	0	0	0
ST loans	1	0	0	0	0	0	5	5	0	0	0
Current portion of LT debt	0	0	0	0	0	0	0	0	0	0	0
Trade payables & prepayments	2	3	3	3	4	5	6	6	7	7	8
Taxes payable	0	0	0	0	0	0	0	0	0	0	0
Other current liabilities	1	2	3	4	5	6	7	8	9	9	10
Current liabilities	4	5	6	7	9	10	17	19	15	17	18
Total liabilities & equity	42	40	55	63	71	82	100	119	137	160	185
Net debt	-2	-1	-7	-7	-7	-10	2	2	-9	-26	-49
Net debt/Equity	-0.1	0.0	-0.1	-0.1	-0.1	-0.1	0.0	0.0	-0.1	-0.2	-0.3

Source: Company data, Renaissance Capital estimates

We note that our model for MCB also indicates high cash reserves starting in 2017, at which point the company will either pay dividends or diversify its business, as we assume land consolidation by 2017.

Figure 57: MCB Agricole IFRS cash flow statement, \$mn

	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Profit before tax	0.0	0.2	7.8	7.2	6.5	10.0	11.7	18.3	22.1	23.6	25.3
Depreciation	-1.7	1.1	1.1	1.0	0.9	0.8	1.2	1.8	2.2	2.4	2.6
Income tax paid	0.0	0.1	-0.4	-0.4	-0.3	-0.5	-0.6	-0.9	-1.1	-1.2	-1.3
Increase in working capital	-15.2	-0.9	-5.6	-0.8	-1.8	-2.9	-2.2	-3.1	-2.8	-1.9	-1.6
Less non-oper. Income/cost	-0.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating cash flow	-12.6	0.4	2.9	7.0	5.3	7.5	10.1	16.1	20.4	22.9	25.0
Capital expenditures, net	-5.9	0.0	-1.2	-7.5	-4.8	-4.9	-22.1	-16.2	-9.2	-6.2	-1.7
Other investments, net	-1.8	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Investing cash flow	-7.7	0.0	-1.1	-7.5	-4.8	-4.9	-22.1	-16.2	-9.2	-6.2	-1.7
Net borrowings/(repayments)	-4.7	-0.9	0.0	0.0	0.0	0.0	4.7	0.5	-4.9	-0.2	0.0
Other	25.1	-1.8	5.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing cash flow	20.4	-2.7	5.7	0.0	0.0	0.0	4.7	0.5	-4.9	-0.2	0.0
Net change in cash and translation difference	0.2	0.0	0.8	6.1	-0.5	0.5	2.7	-7.4	0.3	6.3	16.6
Cash, bop	0.2	0.3	1.0	7.1	6.6	7.1	9.7	2.3	2.7	9.0	25.5
Cash, eop	0.3	1.0	7.1	6.6	7.1	9.7	2.3	2.7	9.0	25.5	48.8

Source: Company data, Renaissance Capital estimates

Peer valuation

We think that the closest peer for MCB is Sintal, as the company also farms in Ukraine and is not loss-making like Landkom. We also include Black Earth Farming, SLC Agricola, and Brasil Agro, however, to make our peer group larger and to populate it with companies that we do not value in this report.

Figure 58: MCB peer valuation, as of 25 August

Ticker	Country	Price, \$	MktCap, \$mn	P/E			EV/EBITDA ⁽⁴⁾			EV/Sales			EV/ha harvested	EV/ha harvested (less ownership) ³	
				2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E	2010E	2010E	
MCB Agricole	4GW1 GR	UA	2.4	41	5.5	6.0	6.6	4.6	4.9	5.5	1.0	0.7	0.6	509	509
Landkom	LKI LN	UA	0.1	62	-9.3	-3477.7	19.5	-23.9	12.0	8.0	2.1	1.5	1.5	1331	1331
Sintal	SNPS GR	UA	4.3	142	11.5	10.0	7.2	9.9	8.9	6.4	2.3	2.1	1.7	1512	1512
Black Earth Farming ²	BEFSDB SS	RU	2.9	363	162.7	12.4	8.4	34.0	8.9	6.4	3.1	2.5	2.1	1721	1110
SLC Agricola ¹	SLCE3 BZ	BZ	9.1	897	55.6	32.9	21.4	15.6	10.8	9.3	3.0	2.6	2.5	4863	771
Brasil Agro	AGRO3 BZ	BZ	5.6	325	neg	neg	neg	neg	neg	neg	8.8	5.3	4.2		
Peer median					11.5	10.0	8.4	9.9	8.9	6.4	3.0	2.5	2.1	1616.6	1220
Premium to peers					-52%	-40%	-22%	-54%	-44%	-15%	-67%	-71%	-71%	-69%	-58%

¹ Expected 2010E harvested land based on company 2010 report. SLC Agricola owns 247,886 ha of land, 217,865 ha of which was valued by Deloitte Touche Tohmatsu at an average \$3,688/ha at the current exchange rate:

² Black Earth Farming owns 222,000 ha of land, which we estimate to be valued at \$600/ha:

³ The multiple is arrived at by subtracting the value of owned land from the EV.

⁴ The multiple is based on adjusted EBITDA (equal to EBITDA less biological revaluation).

Source: Bloomberg, Renaissance Capital estimates

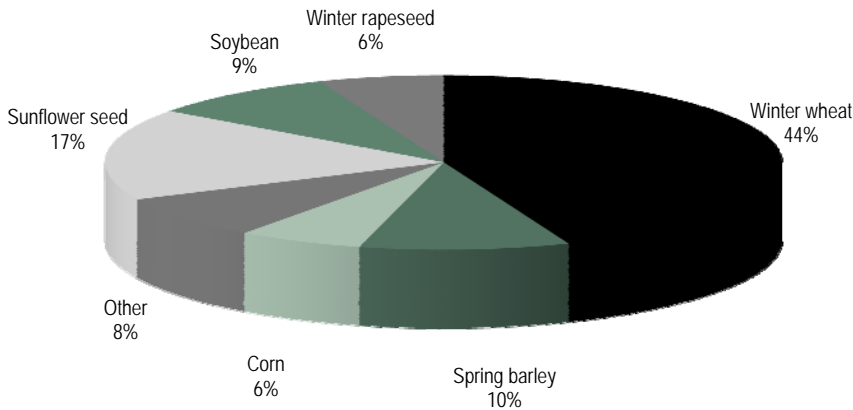
Comparing MCB on a 2010E EV/EBITDA basis to Sintal suggests that MCB is trading at a 45% discount, which we find to be unjustified. Similarly, comparing MCB to the peer median shows that the stock trades at a 67% discount on 2010E EV/EBITDA and an 71% discount on 2011E EV/EBITDA.

We also think that the \$509/ha EV/ha harvested at which MCB currently trades is another good indicator that the company is undervalued, considering that the land entry ticket (a one-off price for leasing land) plus machinery capex are at least at \$450-550/ha. The company trades at a 58% discount to the peer median on EV/ha correct for land ownership.

Sintal: Company overview

Sintal Agriculture effectively started up in 2002 with an acquisition of two small sugar production facilities (30,000 tpa total capacity) and grew to become a 90,000 ha farming operation (total land under management at 100,400 ha as of Aug 2010). Roughly 75% of Sintal's land is located in Kherson (southern Ukraine) and the rest is in Kharkiv. The company plants just under half of its land with wheat, and uses the rest mostly for sunflower seed, soybean, and winter rapeseed.

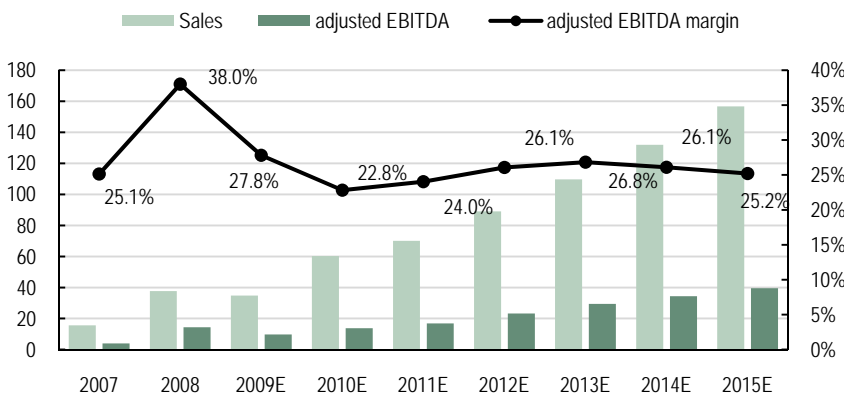
Figure 59: Sintal 2010E harvested land distribution



Source: Company data, Renaissance Capital estimates

Sintal is among the most profitable farming companies we have come across in Ukraine. The enterprise was able to attain a 25% adjusted EBITDA margin (net of biological revaluation) in 2007 and a 38% margin in 2008. We expect Sintal's profitability to stay high at an EBITDA of 23-27% (we think the 38% seen in 2008 was a one-off due to high yields in that year and a successful crop sale that occurred just before prices bottomed), despite a possible yield drop caused by the expectedly rapid harvested land expansion. We believe 2010E will be one of the worst performing years for the company, as Sintal's harvest was badly hit by the weather (over a 35% YoY winter wheat yield decrease) and while prices will help to offset the damage, we think a decline in profitability is unavoidable.

Figure 60: Sintal 2007-15E sales (\$mn), adjusted EBITDA⁽¹⁾(\$mn), and adjusted EBITDA margin



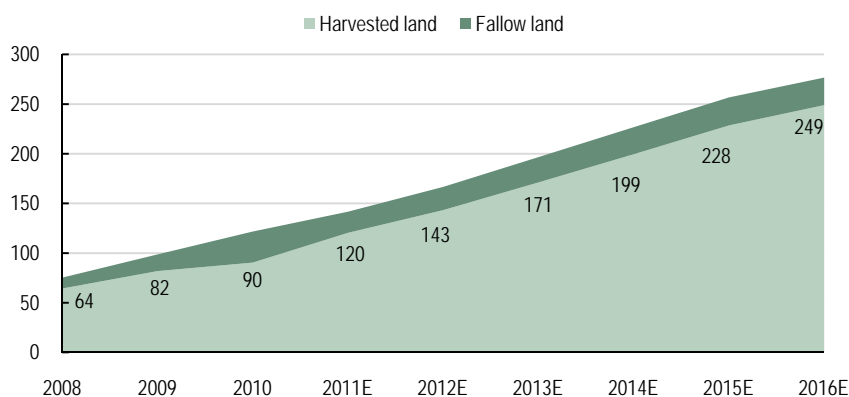
(1) EBITDA excluding biological revaluation

Source: Company data, Renaissance Capital estimates

Sufficient cash to expand quickly

As Sintal runs one of the most efficient farming operations in Ukraine, the company generates high levels of operating cash flow (we estimate a total of over \$50mn in the next three years), which combined with a \$12.5mn SPO raising in Oct 2009 leaves sufficient funds to fuel a rapid expansion. We think the company may increase harvested land by as much as 30% YoY in 2011E, and could potentially grow to harvest around a quarter million hectares in 2016E.

Figure 61: Sintal 2008-16E land bank expansion, '000ha



Source: Company data, Renaissance Capital estimates

Packaged with machinery and infrastructure

Unlike many of its peers, Sintal uses mostly its own machinery (machinery coverage is almost at 100%) and expects to become completely self sufficient in storage by YE10. At the moment the company owns 50% of a 100,000 tonne silo in Kranoperekopsk (the rest is expected to be acquired by the end of the year) and is in the process of constructing an additional 115,000 tonne silo in Kharkiv (50% to be completed by September). Additionally, the company owns 40,000 tonne of warehouse storage, which means that its storage capacity is large enough to be used to provide third-party services to other Ukrainian farmers.

Sintal: Valuation

Sintal Agriculture's valuation is based on a 10-year DCF model and peer trading multiples. Both approaches suggest that Sintal currently trades close to its fair value. We set Sintal's target price at EUR3.4/share (1% downside to current price) and initiate coverage with a **HOLD** rating.

DCF

We assume a regular 19% WACC for Sintal in 2010, and reduce it to 12% in perpetuity, which is associated with average level of risk. We set terminal growth rate at the usual 3%.

Our valuation suggests a fair equity value at \$161mn (an EV of \$164mn), which is equivalent to EUR3.4/share.

Figure 62: Sintal DCF model, \$mn

	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
EBIT	9	13	16	22	28	32	37	41	43	43
Less taxation	0	-1	-1	-1	-1	-2	-2	-2	-2	-2
Tax adjusted EBIT	9	12	15	21	26	31	35	39	41	41
Tax shield on interests	0	0	0	0	0	0	0	0	0	0
Depreciation	1	1	1	2	2	2	2	3	3	3
Less: Capex	-12	-16	-23	-15	-19	-20	-21	-16	-9	-3
Change in working capital	17	4	-5	-5	-5	-6	-8	-8	-7	-4
Unleveraged free cash flow	14	0	-12	2	4	7	9	19	28	37
WACC			19.0%	18.0%	17.0%	16.0%	15.0%	14.0%	13.0%	12.0%
Discounted cash flow			-10	1	2	4	4	7	10	12
Future cash flow growth rate		3%								
Terminal value		422								
Discounted terminal value		134								
Net debt		3								
Fair equity value		161								
Implied TP (in EUR)		3.4								
Implied multiples										
P/E (adjusted)	20.0	13.1	11.3	8.2	6.3	5.3	4.6	4.1	3.9	4.0
EV/adjusted EBITDA	16.9	11.9	9.7	7.1	5.6	4.8	4.1	3.7	3.6	3.6

Source: Company data, Renaissance Capital estimates

Figure 63: Sensitivity of share price to WACC and growth rate, EUR/share

WACC in perp.	Perpetuity growth rate				
	1%	2%	3%	4%	5%
10%	3.4	3.8	4.3	4.9	5.8
11%	3.1	3.4	3.8	4.3	4.9
12%	2.9	3.1	3.4	3.8	4.3
13%	2.7	2.9	3.2	3.5	3.9
14%	2.5	2.7	2.9	3.2	3.5

Source: Renaissance Capital estimates

Figure 64: Sintal IFRS income statement and operating data, \$mn

	2007	2008	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Revenue	16	38	35	60	70	89	110	132	157	180	199	212
CoGS	-9	-24	-22	-41	-47	-58	-70	-86	-103	-120	-135	-147
Gross profit	6	14	13	19	23	31	39	46	54	60	64	65
SG&A expenses	-1	-3	-3	-5	-6	-8	-10	-12	-14	-16	-18	-19
Other operating income, net	-1	4	0	0	0	0	0	0	0	0	0	0
Adjusted EBITDA	4	14	10	14	17	23	29	34	39	44	46	46
D&A	0	-1	-1	-1	-1	-2	-2	-2	-2	-3	-3	-3
EBIT	3	13	9	13	16	22	28	32	37	41	43	43
Financial expenses	-1	-6	-1	0	-1	-1	-1	0	0	0	0	0
Other non-operating income/expenses	0	0	0	0	0	0	0	0	0	0	0	0
PBT	2	7	8	13	15	21	27	32	37	41	43	43
Income (tax)/benefit	0	0	0	0	0	0	0	0	0	0	0	0
Net income	1	6	8	12	14	20	26	30	35	39	41	41
Margins												
Gross	39.8%	36.7%	36.8%	31.8%	33.0%	35.1%	35.8%	35.1%	34.2%	33.4%	32.1%	30.6%
EBITDA	25.1%	38.0%	27.8%	22.8%	24.0%	26.1%	26.8%	26.1%	25.2%	24.4%	23.1%	21.6%
Adjusted net income	8.6%	16.5%	23.1%	20.4%	20.3%	22.1%	23.3%	23.1%	22.5%	21.7%	20.5%	19.1%
Main operating data												
Harvested land bank, '000ha	64	82	90	120	143	171	199	228	249	261	264	264
Grain harvest, '000t	210	295	164	340	406	489	572	658	725	768	784	789
Total harvest, '000t	281	338	237	457	547	657	769	885	975	1,033	1,055	1,061
Net debt, \$mn	7	9	-5	-5	8	7	4	-3	-12	-31	-58	-95
Other ratios												
Net debt/adjusted EBITDA	1.1	0.5	1.9	2.5	3.3	3.0	2.9	3.0	3.1	3.1	3.1	3.1
ROIC	29%	18%	14%	20%	18%	20%	21%	22%	21%	19%	17%	0%
ROE	28%	21%	15%	19%	18%	21%	22%	21%	20%	18%	16%	0%
SG&A as % of revenue	7%	9%	9%	9%	9%	9%	9%	9%	9%	9%	9%	9%

Source: Company data, Renaissance Capital estimates

Figure 65: Sintal IFRS balance sheet, \$mn

	2007	2008	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
PP&E, net	4	7	19	34	56	69	86	104	122	135	142	142
Construction in progress	0	0	0	0	0	0	0	0	0	0	0	0
Deferred tax assets	1	0	0	0	0	0	0	0	0	0	0	0
Other non-current assets	2	5	5	5	5	5	5	5	5	5	5	5
Non-current assets	8	12	23	39	60	74	91	109	127	140	146	146
Cash & equivalents	0	0	5	5	2	2	3	3	12	31	58	95
Trade receivables & prepayments	2	2	4	6	7	9	11	13	15	17	19	20
Inventories	18	29	31	28	33	37	41	46	52	58	62	66
Other current assets	9	32	7	11	13	16	20	24	28	32	36	38
Current assets	28	62	47	50	54	64	75	86	108	138	175	219
Total assets	36	74	70	89	115	138	166	195	235	278	322	366
Share capital	13	47	47	47	47	47	47	47	47	47	47	47
Retained earnings	-3	11	19	31	45	65	91	121	156	195	236	277
Reserves and other	0	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7	-7
Shareholder equity	9	51	59	71	85	105	130	161	196	235	276	316
LT interest bearing debt	0	1	0	0	0	0	0	0	0	0	0	0
Deferred tax liabilities	0	0	0	0	0	0	0	0	0	0	0	0
Other non-current liabilities	0	0	0	0	0	0	0	0	0	0	0	0
Non-current liabilities	0	1	0	0	0	0	0	0	0	0	0	0
ST loans	6	7	0	0	9	9	6	0	0	0	0	0
Current portion of LT debt	0	1	0	0	0	0	0	0	0	0	0	0
Trade payables & prepayments	7	5	4	8	9	11	13	16	20	23	26	28
Taxes payable	0	0	0	0	0	0	0	0	0	0	0	0
Other current liabilities	12	10	7	10	11	13	15	17	19	20	20	21
Current liabilities	26	23	11	18	30	33	35	34	39	43	46	49
Total liabilities & equity	36	74	70	89	115	138	166	195	235	278	322	366
Net debt	7	9	-5	-5	8	7	4	-3	-12	-31	-58	-95
Net debt/Equity	0	0	0	0	1	1	1	1	1	1	1	0

Source: Company data, Renaissance Capital estimates

As with our models for the other two companies, Sintal's cash begins to accumulate in 2016, which we leave assuming either a DCF payout or a business diversification via acquisitions.

Figure 66: Sintal IFRS cash flow statement, \$mn

	2007	2008	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Profit before tax	1.3	6.2	8.5	12.9	15.0	20.7	26.9	32.1	37.1	41.2	42.8	42.6
Depreciation	-0.4	-0.9	0.6	0.8	1.2	1.5	1.7	2.0	2.4	2.7	3.0	3.2
Income tax paid	0.0	0.0	-0.4	-0.6	-0.7	-1.0	-1.3	-1.6	-1.9	-2.1	-2.1	-2.1
Increase in working capital	-6.2	-11.3	17.2	3.5	-5.3	-5.3	-5.5	-6.3	-7.7	-7.5	-6.8	-3.6
Less non-oper. Income/cost	2.2	-9.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating cash flow	-3.1	-10.0	25.8	16.6	10.2	15.9	21.8	26.2	30.0	34.4	37.0	40.1
Capital expenditures, net	-1.7	-4.4	-12.2	-16.5	-22.8	-15.1	-18.7	-19.7	-20.7	-15.6	-9.4	-3.3
Other investments, net	-0.2	-1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Investing cash flow	-1.9	-5.9	-12.2	-16.5	-22.8	-15.1	-18.7	-19.7	-20.7	-15.6	-9.4	-3.3
Net borrowings/(repayments)	-0.4	-3.7	-8.8	0.0	9.3	-0.3	-2.6	-6.0	-0.4	0.0	0.0	0.0
Other	5.4	20.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing cash flow	5.1	16.4	-8.8	0.0	9.3	-0.3	-2.6	-6.0	-0.4	0.0	0.0	0.0
Net change in cash and translation difference	0.0	0.0	4.8	0.2	-3.2	0.5	0.5	0.6	8.8	18.7	27.5	36.8
Cash, bop	0.0	0.1	0.0	4.8	5.0	1.8	2.2	2.7	3.3	12.1	30.8	58.4
Cash, eop	0.1	0.0	4.8	5.0	1.8	2.2	2.7	3.3	12.1	30.8	58.4	95.2

Source: Company data, Renaissance Capital estimates

Peer valuation

We find that both of our Ukrainian peers are not particularly close comparisons for Sintal, as Landkom is loss-making and MCB is, in our view, undervalued. We find the best multiple to be EV/ha harvested corrected for land ownership.

Figure 67: Sintal peer valuation, as of 25 August

	Ticker	Country	Price, \$	MktCap, \$mn	P/E			EV/EBITDA ⁽⁴⁾			EV/Sales			EV/ha harvested 2010E	EV/ha harv (less ownership) ³ 2010E
					2010E	2011E	2012E	2010E	2011E	2012E	2010E	2011E	2012E		
Sintal	SNPS GR	UA	4.3	142	11.5	10.0	7.2	9.9	8.9	6.4	2.3	2.1	1.7	1512	1512
Landkom	LKI LN	UA	2.4	41	5.5	6.0	6.6	4.6	4.9	5.5	1.0	0.7	0.6	509	509
MCB Agricole	4GW1 GR	UA	0.1	62	neg	neg	19.5	neg	12.0	8.0	2.1	1.5	1.5	1331	1331
Black Earth Farming ²	BEFSDB SS	RU	2.9	363	162.7	12.4	8.4	34.0	8.9	6.4	3.1	2.5	2.1	1721	1110
SLC Agricola ¹	SLCE3 BZ	BZ	9.1	897	55.6	32.9	21.4	15.6	10.8	9.3	3.0	2.6	2.5	4863	771
Brasil Agro	AGRO3 BZ	BZ	5.6	325	neg	neg	neg	neg	neg	neg	8.8	5.3	4.2		
Peer median					5.5	6.0	8.4	4.6	8.9	6.4	3.0	2.5	2.1	1526.0	941
Premium to peers					110%	67%	-14%	117%	0%	-1%	-25%	-14%	-19%	-1%	61%

¹ Expected 2010E harvested land based on company 2010 report. SLC Agricola owns 247,886 ha of land, 217,865 ha of which was valued by Deloitte Touche Tohmatsu at an average \$3,688/ha at the current exchange rate;

² Black Earth Farming owns 222,000 ha of land, which we estimate to be valued at \$600/ha;

³ The multiple is arrived at by subtracting the value of owned land from the EV.

⁴ The multiple is based on adjusted EBITDA (equal to EBITDA less biological revaluation).

Source: Bloomberg, Renaissance Capital estimates

Sintal's EV/ha harvested (less land ownership) comparison to peers suggests that the company trades at a 60% premium to peers. We find such a premium to be justified, however, given the company's higher profitability.

Overall we feel that multiples do not indicate a clear upside or downside for the stock.

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	7	

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