

## **ALROSA reports robust 9M 2011 results; borrowings postponed but not shelved**

Yesterday, ALROSA (ALROSA, Ba3/BB-/BB-) published its Q3 and 9M 2011 consolidated accounts. All in all, it appears that the base scenario we communicated at the beginning of 2011, which envisaged that the company would avoid new borrowings this year, was broadly correct. Apart from the Euro Commercial Paper (ECP) worth USD 400 mn placed in Q2 2011, the company has stayed away from the market. However, the main reason behind that was **the postponement to 2012 of the buyback of around USD 1 bn of gas assets from VTB**, which we discuss below.

The company's revenues leapt by 19% yoy to RUB 107 bn in 9M 2011, which was only 5% lower than the figure reported for full-year 2010. In 9M 2011 ALROSA increased its output by 4.5% yoy and retained its leading position on the world diamond market. The company outpaced De Beers by almost 6% in terms of carats produced during the first nine months of the year. Although diamond production in Q3 was lower than in Q2, it was in line with the company's plans. ALROSA projects production of 34.5 mn carats in 2011 – virtually flat on 2010. We usually clear out the movements in inventories of diamonds, ore and concentrates in the cost of sales from our EBITDA and EBIT calculations. If excluded, the operating results look strong, with EBITDA up by 53% yoy in 9M 2011 and an EBITDA margin of about 50%.

A look at the PolishedPrices Overall Index shows that the pricing environment in the third quarter was favourable for the company and has remained fairly benign so far. Although the average diamond price is currently about 12% off its August 2011 highs, prices are still almost 45% higher than their local low in April 2009. Overall, the average diamond price in 2011 (year-to-date) has exceeded that of the same period in 2010 by almost 25%. In Q4 (year-to-date), average diamond prices slipped by some 5% compared to Q3 2011.

**ALROSA reported that its sales price per carat jumped by 19% in Q3 compared to Q2 2011**, whereas the average price in 9M 2011 was up by 44% on FY 2010. We calculate that the diamond price advanced by about 10% between Q2 and Q3, based on the PolishedPrices Overall Index. ALROSA's stronger result was achieved by a decrease in sales through auctions and short-term contracts (the share of long-term contracts increased from 62% in Q2 to 68% in Q3, and is set to continue rising), which helped the company to maintain its high sales prices. We estimate that **ALROSA's free cash flow in 9M 2011 was positive** by almost RUB 27 bn on the back of stronger cash flows from operating activities (OCF) of RUB 40 bn, and we believe the company will be able to easily cover its planned investments (ca. RUB 22 bn in 2012) from its operating cash flows as things stand.

**ALROSA's interim results show a stronger liquidity profile at end-9M 2011 as compared to end-H1 2011**, with some RUB 23 bn in cash and equivalents, while the diamond miner's short-term maturities totalled roughly RUB 33 bn (or 31% of total debt) at end-9M. While ALROSA attracted virtually no new debt in Q3, its total debt nudged up by 8% in rouble terms compared to the end of the first half of 2011, which is attributable to the devaluation of the rouble. In our view the debt currency structure remains well matched with that of revenues. We estimate that the company's total debt/EBITDA was 1.9x at end-9M 2011, slightly below our forecast figure for the total debt/EBITDA ratio of around 2.2x at the end of 2011. ALROSA's net debt/EBITDA ratio slumped to an impressive 1.5x in 9M 2011, which is in line with our projections that the company's net debt/EBITDA ratio will not exceed 2.0x by year-end (which, however, incorporated the purchase of assets from VTB).

On the M&A side, ALROSA is nearing the completion of its mooted deal with Evraz. To recap, the latter is set to purchase a 51% stake in the Timir iron ore project, which we discussed in greater detail earlier.

Also in line with our expectations, the company confirmed its plans to resell the gas assets that are supposed to be transferred from VTB in Q1 2012. That said, **ALROSA is likely to return to the markets prior to the purchase of the VTB assets with a shelved Euro Commercial Paper** issue reportedly worth at least USD 400 mn. Although this creates some concern about the future refinancing of these short-term debts in 2012, we believe the company will not face any problems on that front. As a backup, we presume ALROSA can use a portion of the available USD 2 bn credit line from VTB. Apart from that, the management does not expect any additional principal public borrowings, and **the company is set to follow through on its plan to cut total debt further**. As of yesterday, ALROSA estimated its total debt at about RUB 96 bn and the remaining maturities in Q4 at about RUB 7.5 bn.

In our note "ALROSA reports H1 2011 results. Borrowings are likely to take place this year after all" dated 19 October 2011, we elaborated on the potential outcomes of the privatisation of ALROSA. **The company announced that it had suspended any immediate plans to float an IPO**, which is not a surprise in the light of the ongoing volatility on the markets, as well as the need for a conclusive political decision. To recap, under our base scenario, we assumed that some part of the company would probably be privatised as early as 2013.

As things stand, we do not see any investment ideas in ALROSA's Eurobonds and are therefore retaining our neutral stance on the company's papers.

### **ALROSA's key financial figures:**

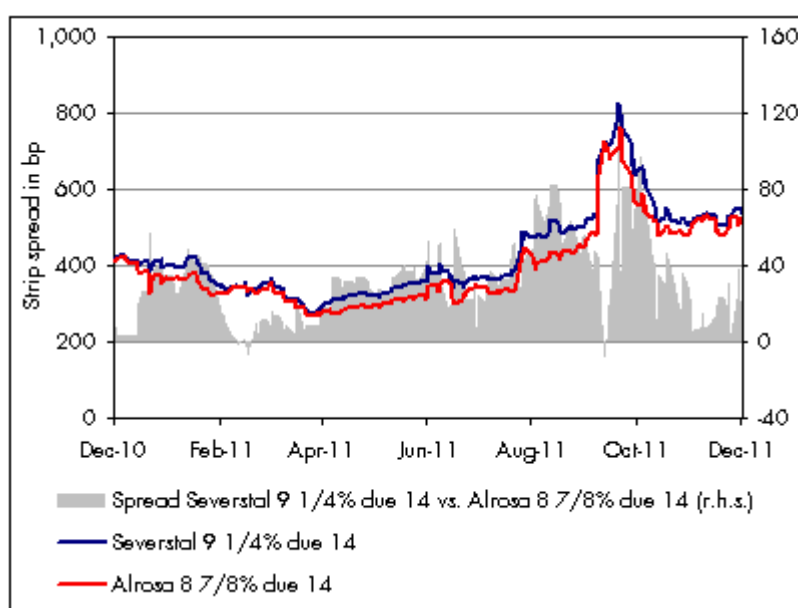
in RUB mn

<b>Income Statement</b>	<b>2010</b>	<b>9M 2011</b>
Revenues	113,394	107,315
Revenue growth (yoy)	45%	19%
EBITDA	37,497	52,602
EBIT	28,704	44,809
Interest expense	9,895	5,596
Net profit	11,690	34,845
<b>Cash Flow</b>	<b>2010</b>	<b>9M 2011</b>
Cash from operating activities	37,800	40,022
Cash from investing activities	-9,767	-13,313
Cash from financing activities	-29,134	-7,702
Operating cash flow margin	33%	37%
Free cash flow	26,591	26,538
<b>Balance Sheet</b>	<b>2010</b>	<b>9M 2011</b>
Total assets	222,427	256,785
LT interest bearing debt	89,021	74,381
Cash and equivalents	4,136	22,749
Net debt	97,829	84,734
LT debt	89,021	74,381
ST debt	12,944	33,102
Total debt	101,965	107,483

Ratios	2010	9M 2011
EBITDA margin	33%	49%
EBIT margin	25%	42%
Profit margin	10%	32%
Net debt/LTM EBITDA	2.6 x	1.5 x
Total debt/LTM EBITDA	2.7 x	1.9 x
Interest coverage ratio	2.9 x	8.0 x

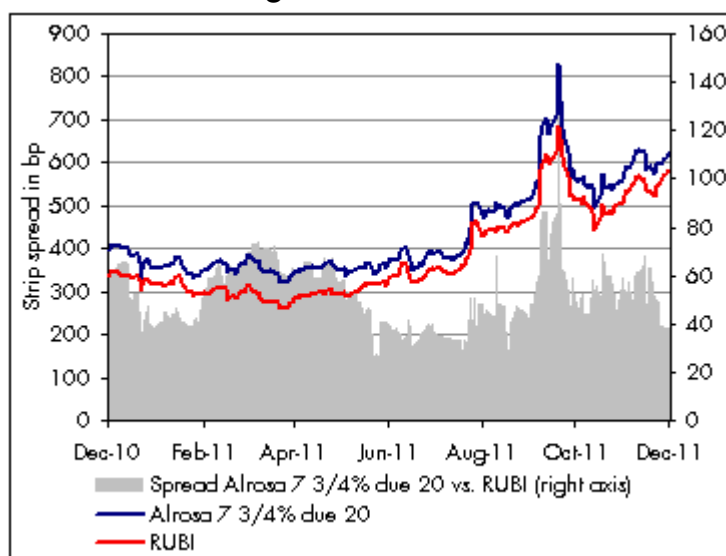
Source: Company data, Raiffeisen RESEARCH

### ALROSA vs. Severstal:

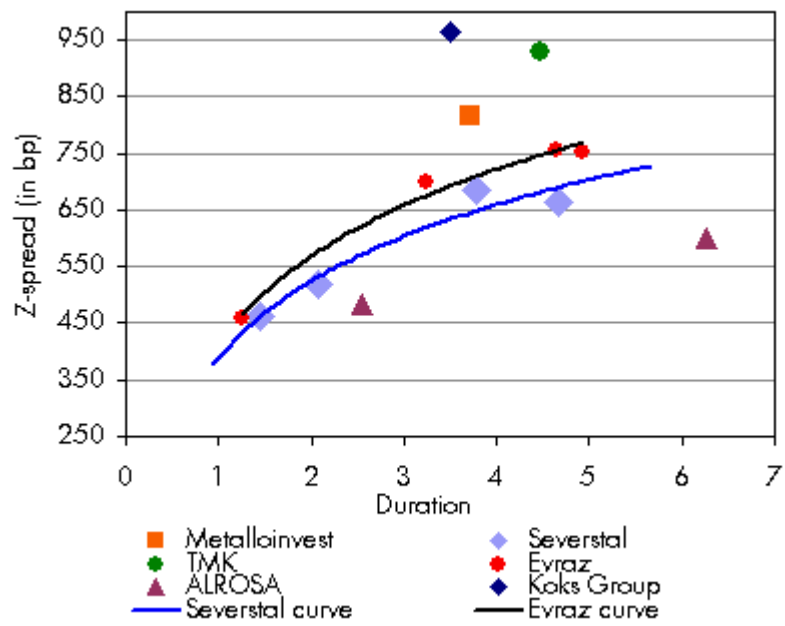


Source: JP Morgan, Raiffeisen RESEARCH

### ALROSA vs. JP Morgan RUBI Index:



Source: JP Morgan, Raiffeisen RESEARCH

**ALROSA vs. peers:**

Source: Bloomberg, Raiffeisen RESEARCH