



ALOR INVEST CJSC

Syktyvkar Tissue Group



The Stock Belongs in Your Portfolio

**Research report
18/04/2011**



The Stock Belongs in Your Portfolio

Syktyvkar Tissue Group OJSC (STG), one of the largest tissue enterprises in Russia, plans to conduct its first initial public offering on the MICEX at the end of May this year. This will be the first IPO in the tissue segment. STG eyes to raise up to RUB700mn by offering up to 30% of its increased issue capital.

IPO is primarily targeted to investors who are willing to mitigate the risks via investments into the securities of the company, which sustains stable and predictable growth rates of its value.

From our standpoint, **the company's investment appeal** is shaped by the factors set out below:

- ✓ Stable sales market and ongoing growth of demand regardless of any economic shock;
- ✓ A high upside potential of the Russian tissue market due to a low level of per capita consumption of sanitary and hygiene products;
- ✓ Robust and stable growth of sanitary and hygiene products sales;
- ✓ The leadership on the base paper market (26% in 2010);
- ✓ A sizeable share of the toilet tissue market (8% in 2010);
- ✓ A potential sale of a large stake to a foreign tissue company;
- ✓ Transparent business structure and high corporate governance standards;
- ✓ Understandable for the investors business.

Goals of IPO:

STG plans to direct the proceedings raised from IPO to meet the increasing demand and to double its sales by 2014. The set of steps includes:

- ✓ Upgrade of existing production facilities;
- ✓ Capacity expansion in Syktyvkar;
- ✓ Construction of a new production site in the Central Federal District of Russia.

| IPO parameters | |
|---|--|
| Share of issue capital (additional share issue) | 30% (of the increased issue capital) |
| IPO capital raise | RUB550-700mn |
| Price range | RUB11.4-14.5/share |
| Placement date | May 2011 |
| Placement arranger | Veles Capital Investment Company LLC, ALOR INVEST CJSC |
| Trading floor | MICEX |

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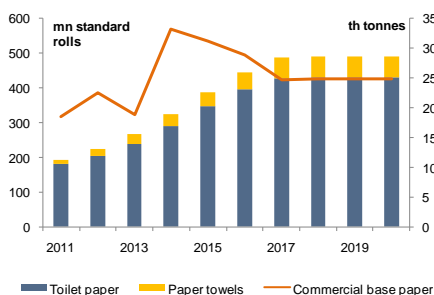
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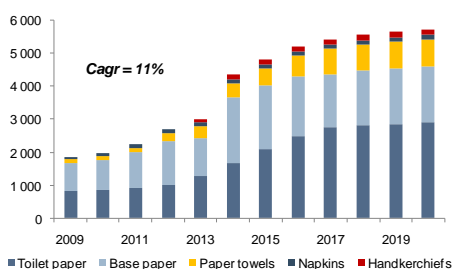
| Highlights | 2009 | 2010 | 2011 (F) | 2012 (F) |
|----------------------------|-------|-------|----------|----------|
| Sales, mn RUB | 1 235 | 1 743 | 2 023 | 2 386 |
| Growth, % | 97,5 | 41,2 | 16,0 | 17,9 |
| EBIT, mn RUB | 179 | 301 | 340 | 850 |
| EBITDA (OIBDA), mn RUB | 234 | 405 | 438 | 532 |
| EBITDA margin, % | 19,0 | 23,2 | 21,7 | 22,3 |
| EAT, mn RUB | 11 | 100 | 121 | 179 |
| net profit margin (EAT), % | 0,6 | 5,7 | 6,0 | 7,5 |
| Assets, mn RUB | 2 168 | 2 637 | 3 318 | 3 840 |
| BV, mn RUB | 677 | 1 087 | 1 808 | 1 988 |
| Net debt, mn RUB | 1 047 | 958 | 395 | 1 216 |

| Multiples | 2011 (F) | 2012 (F) | Industry 2011 |
|-------------|----------|----------|---------------|
| P/E | 16,54 | 11,15 | 14,09 |
| EV/S | 1,59 | 1,35 | 1,81 |
| $EV/EBITDA$ | 5,47 | 4,50 | 8,32 |

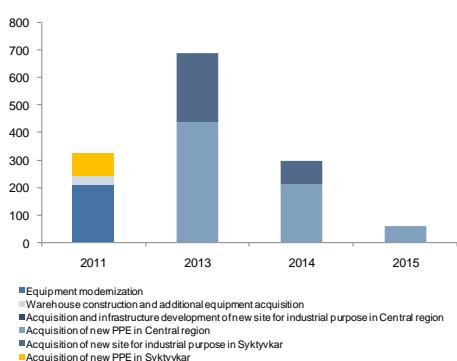
Production forecast



Sales forecast, mn RUB



Capex, mn RUB



Milestones

Syktyvkar Tissue Group JSC is one of the three Russia's large-scale tissue producers holding a 8% share of the toilet tissue market. The only companies with greater market shares of 26% and 18% are SCA (Zewa brand) and Naberezhnye Chelny Paper and Paperboard Mill CJSC, respectively. Syktyvkar Tissue Group (STG) occupies 26% of the local base paper market.

The group's product mix, which is represented by Syktyvkarskaya 56 and VEIRO brands, includes.

- High-quality base sanitary tissue
- Toilet tissue of budget, standard, and premium segments (from low grade to perfumed three-ply pulped toilet paper)
- Paper towels and handkerchiefs

The group has the vertically integrated manufacturing process, which incorporates raw materials processing and base paper production, as well as end tissue products fabrication, and ensures the competitive edge for STG (many manufacturers purchase base paper from the rivals). STG's production facilities are equipped by the state-of-the-art technologies (Metso Paper, Fabio Perini, SDF, Toscotec). The quality of base paper fully meets the strict international requirements enjoying popularity among foreign producers operating in Russia.

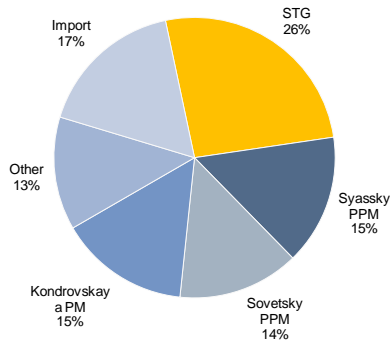
Russia's tissue industry demonstrates robust growth rates facing low market saturation. As such, Russia lags significantly behind the USA and Europe in terms of tissue consumption per capita (2.3 kg/person pa vs 22 kg/person pa and 13 kg/person pa, respectively, while the world average is 3.4 kg/person pa). However, the growth rates of the Russian market outpace the global ones – since 2006 the world tissue market increased less than 9%, while the Russian market soared more than 1.5 times. This indicates the per unit tissue consumption in Russia follows an upward path and is set for further growth. In addition, the commercial tissue production (sanitary base tissue for hotels, restaurants, etc.) should demonstrate strong performance in the long run, while in Russia this segment is relatively immature.

The company aims at ramping up the finished products facilities and strengthening its foothold in the Central Federal District of Russia. Within the development strategy STG plans to complete the last stage of PM-1 tissue machine upgrade (the acquisition of high-speed converting line) in November 2011. Thus, the highest technological requirements will be met by early 2012. Going forward the company intends to install the third paper making machine in Syktyvkar, as well as to launch the additional converting lines in Syktyvkar and in the central part of Russia.

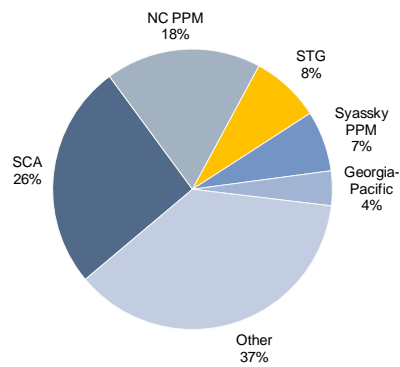
Based on the combination of income and comparative approaches, STG is valued at around RUB2.68bn, or RUB16.65/share (\$89.18mn, or \$0.55/share) as of the end of 2011 (post-money valuation).

Thus, the participation in STG's IPO at an offering price within the range of RUB11.4-14.5/share allows the investors to buy the stock which offers an upside potential of 15%-45% by the year-end (depending on an IPO price).

STG base paper market share in 2010



STG toilet paper market share in 2010



Company Snapshot

Syktyvkar Tissue Group owns one of the largest tissue factories in Russia, which produces mainly base paper, toilet tissue, paper towels, and napkins. In terms of production volume, STG comprised 7% of the Russian tissue market in 2009, while in 2010 it accounted for 8%. The company held 26% of the local base paper market in 2010.

STG manufactures the products by using pure pulp and scrap paper, thus satisfying the demand for high-quality, as well as for low-price goods in all population strata.

The most famous company's brands are high-quality Veiro sanitary tissue products, and Syktyvkarskaya 56, which is still in a great demand.

STG's base paper is a raw material of the best quality compared to the other Russia's producers, which is used for sanitary tissue products manufacturing and complies with all the European and American standards. STG's base paper is used in production of famous brand tissue products by foreign manufacturers, which operate in Russia.

STG is located in the Ezhvinsky District of Syktyvkar in a proximity to Kirov-Syktyvkar-Ukhta federal road. The location determines the sales market. That said the large consumers are Moscow and the Moscow region comprising one third of sanitary and hygiene tissue products in value terms.

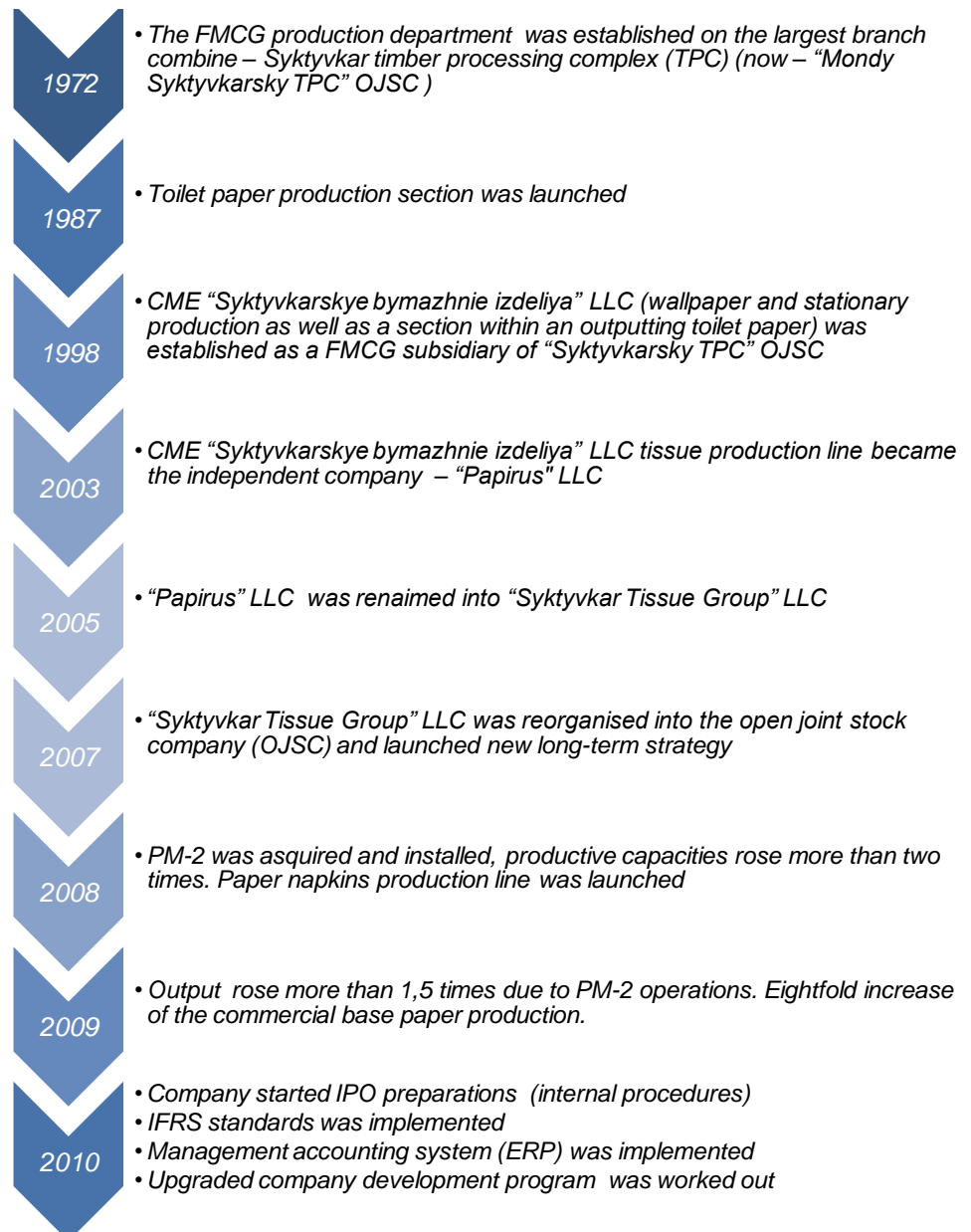


STG is equipped by the modern facilities supplied by the world leading producers, such as Metso Paper, Fabio Perini, and SDF. Currently, STG has two paper making machines and four automatically controlled processing lines. The total area of the company's facilities amounts to 35,000 sqm, while the headcount stands at 400 employees.

The annual capacities exceed 50,000 tonnes of base paper, 265mn of tissue rolls, and 14mn of napkin packs.

Company History

STG launched its production more than 40 years ago. The company succeeded in creating its brand awareness and gained the strong foothold on the Russian market. STG has ranked among TOP-3 Russia's tissue producers for several years.

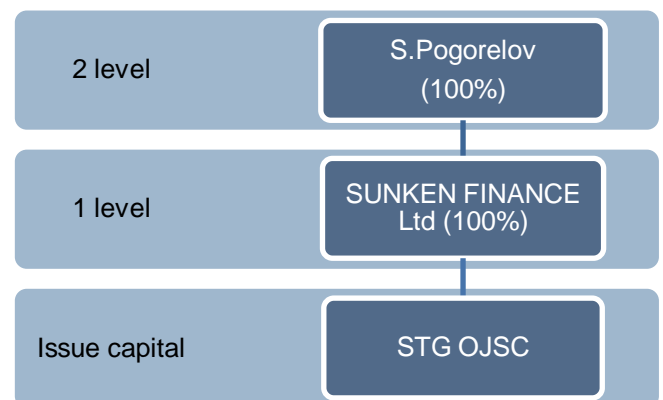


Ownership Structure

Currently, 100% of STG is owned by Cyprus-based Sunken Finance Ltd fund with Sergey Pogorelov being the end beneficiary.

S. Pogorelov has been involved in land properties business since 2003. He acquired Papirus LLC from Mondi Syktyvkarsk Forest Enterprise in 2005. Papirus LLC was Mondi's non-core asset and produced toilet issue. Thereafter, Papirus LLC was renamed to Syktyvkar Tissue Group LLC, which was subsequently reorganized into OJSC in 2007.

The asset is considered to be the financial investments of S. Pogorelov and has been managed by Mark Reznik, STG's CEO, since the very start.



The corporate structure is based on a linear-oriented principle of management and quite transparent. This is the result of a simple business idea, which underpins stability, flexibility and efficient in-house liaison.

Top Management



Mark Reznik – Chief Executive Officer

In 1991 Mr. Reznik graduated from the Moscow State University of Railway Engineering. He obtained Ph.D. in Economics, which was rewarded by the Institute of Economics of the Russian Academy of Science in 2007.

Mr. Reznik has been involved into pulp industry since 1992. In 1992-1996 he held the position of CCO at Bumaga Trade House LLC (Moscow). In 1996-2006 Mr. Reznik acted as Business Development and Investments Director and the BoD member at Polotnyano-Zavodskaya Paper Mill OJSC (Kaluga region) and in Drevplit LLC (Sukhonsky Paper Mill, Vologodsk region).

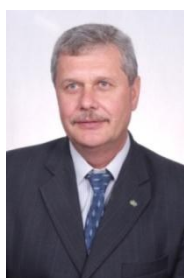
In 2004 he joined Syktyvkar Tissue Group OJSC as Project Manager, and in 2008 Mr. Reznik was appointed as CEO.



Alexander Kagan — Marketing Director, Production Logistics Specialist

In 1994 Mr. Kagan graduated from the Mendeleev University of Chemical Technology of Russia.

He has been engaged in pulp industry since 1999. In 2000-2004 Mr. Kagan occupied different positions at Plitprom Trade House (Moscow region), such as Head of Marketing Department, Head of Production Planning Department, and Head of Advertising and Promotion Department. Thereafter, till 2007 Mr. Kagan held the posts of Executive Director, Investment Project Deputy Director at Consolidated Paper Mills. During this period Mr. Kagan served as Executive Marketing Director at Mir Tissue LLC (Moscow). In 2007-2008 he acted as Head of Business Planning Department at Veles Capital Group (Moscow). Mr. Kagan has dealt with Syktyvkar project since 2004 and worked at Syktyvkar Tissue Group OJSC since 2008.



Anatoly Chernyatjev — Production Director

In 1976 Mr. Chernyatjev finished the Leningrad Pulp and Timber College.

He has over 30 years of industry expertise. In 1972-2005 Mr. Chernyatjev held the position of Base Paper Production Engineer. He joined Syktyvkar Tissue Group OJSC in 2005.



Alexey Zankin — Chief Technology Officer

In 1997 Mr. Zankin graduated from the Ural State Forest Engineering Academy.

In 1997-2001 he worked as Senior Supervisor and Foremaster at Repair and Mechanical Plant of Syktyvkar Forest Enterprise. For eight years since 2001 Mr. Zankin served as Head of Machine Assembly Department at Repair and Mechanical Plant of Mondi Forest Enterprise OJCS. In 2009 he joined Syktyvkar Tissue Group OJSC as Chief Technology Officer.

Board of Directors



Pavel Trigubov — Chairman of the Board

Pavel Trigubov — Chairman of the Board

In 1991 Mr. Trigubov graduated from the Lomonosov Moscow State University, Economics Department.

In 1992-2003 he occupied different positions within the financial departments of such companies, as Megaphros CSJC, NTC LLC, Ostrovnoy Rechnoy Port OJSC, etc. Mr. Trigubov has been CEO of AgroOblAktiv LLC since 2003.



Sergey Pogorelov — Shareholder

In 1983 Mr. Pogorelov finished the Lenin Polytechnic College, Chemical Plants and Refineries Department.

In 1992-2000 he held the position of Engineer at Soyuz Foreign and Economic Enterprise and Media UKVC, acted as Commercial Director at Yuzhnaya Fuel Company LLC. Mr. Pogorelov has served as Director at AgroOblAktiv LLC since 2004.



Stanislav Bulgakov

In 1996 Mr. Bulgakov graduated from the Lomonosov Moscow State University.

In 1996-2003 he occupied the position of Executive Director at Astra Telecom LLC.

Since 2003 Mr. Bulgakov has been Director at AgroOblAktiv LLC.



Mikhail Goncharov

In 1995 Mr. Goncharov graduated from the Lomonosov Moscow State University, Caustobiolith Geology and Geochemistry Department.

In 1996-2004 he worked as Engineer and Head of New Technologies Introduction Section in Medsantrud City Clinical hospital #23 and Energy Sales Service Center LLC. His expertise covers business planning and investment banking in such companies, as Vneshtorgbank LLC (currently VTB24), and Veles Capital Investment Company. Since 2008 Mr. Goncharov has held the post of Deputy Director of Design and Construction Department at UNIPARKS Development CJSC.



Fedor Shkunov

In 1990 Mr. Shkunov graduated from the Gorky State University, Mechanized Processing of Economic Data Department.

In 1992-1998 he was involved into auction trade within Nizhegorodskaya Chamber of Commerce and Nizhegorodskaya Stock Exchange LLC. In 1998-2003 Mr. Shkunov ran regional group "Support Fund for Agrarian Reform and Agricultural Development". Since 2003 he has acted as Director at AgroOblAktiv LLC.



Mikhail Zak

Mr. Zak graduated from the Lomonosov Moscow State University, Economics Department, and holds the Master's Degree in Economics.

In 2000-2002 he served as Analyst at NIKoil Brokerage Company. In 2002 Mr. Zak joined Veles Capital Investment Company as Senior Analyst and in 2003 he was appointed as Head of Research. Since 2010 Mr. Zak has been Managing Director at Veles Capital Investment Company.



Alexander Samozhenkov

In 1999 Mr. Samozhenkov graduated from the Ukhta State Technical University with a major in Finance, Credit and Money Turnover.

In 2000-2001 he worked as Financial Specialist at GAER LLC (Ukhta). In 2001-2005 Mr. Samozhenkov held the positions of Currency Workout Officer and Senior Loan Workout Officer at Sberbank's Ukhta office. In 2005 Mr. Samozhenkov acted as Chief Loan Inspector at Gazprombank OJSC, and in 2007 he was promoted to Project Manager.

Production

The entire production process can be divided into two lines:

1. Base paper production (from pulp and scrap paper);
2. Base paper processing into finished products.

Liquid pulp raw materials are supplied by Mondi Business Paper Syktyvkarsk Forest Enterprise via a trunk pipe that helps simplify and cheapen the raw materials treatment prior to transferring them to the paper making machines. In a case of stoppage of liquid pulp deliveries, STG secured dry pulp supplies from Arkhangelsk Paper Plant.

Scrap paper raw materials are supplied for the processing – defibering and decontaminating – and afterwards they are piped into the paper making machines.

1. Base paper is produced on two paper making machines (PM):
 - PM-1 (BP-82 trademark, Petrozavodskmash) was installed in 1987, and upgraded in 2005-2006. Metso Paper plans to implement a complete upgrade of PM-1 in 2011. The working speed is expected to reach 1,500 m/min, and productivity is forecast to increase up to 25,000 tonnes pa. PM-1 produces pulp base and scrap paper of higher quality weighing from 17 g/m² to 40 g/m²;
 - PM-2 (Advantage DCT 100 trademark, Metso Paper) was installed in 2008 with design capacities of 30,000 tonnes pa, design speed of 1,600 m/min, and a cutoff width of 2,700 mm. PM-2 is designed to output sanitary pulp base and scrap paper weighing from 13 g/m² to 36 g/m².
2. There are two divisions in the base paper processing:
 - Production of toilet issue, paper towels and napkins;
 - Production of base paper.

Toilet issue, paper towels and napkins are manufactured on automatically controlled converting lines:

- Synchro 4.0 line was launched in 2005, and modernized in 2008. It is designed to produce two-ply toilet paper (2, 4, and 8 rolls per pack) and poly printed paper towels (2 rolls per pack). The line has around 70mn rolls of annual capacities;
- X-5 line was installed in 2005 with annual capacities of 70mn rolls. It produces two-, and three-ply toilet tissue (4 rolls per pack) and poly color-printed paper towels (2 rolls per pack);
- 813 line was commissioned at the end of 1980s, and was upgraded in 2005-2006. It produces one-ply coreless non-printed paper rolls in a paper pack with annual capacities of 125mn rolls;
- Napkin line of SDF German trademark with working speed of 300 m/min and annual capacities of up to 14mn packs. The product mix includes one-, two-, and three-ply white and colorful napkins, as well as four-color napkins of 24 x 24 cm and 33 x 33 cm sizes. The napkin line of such a type is the first in Russia.

Base paper is produced on the lengthway sizing machines (PRS-1 and PRS-2) in the cut-size unit.

Manufacturing Scheme

Raw material

Scrap paper

Pulp

Scrap paper section

Grind Preparatory Department

Base paper production (Syktyvkar)

PM-1

Trademark BP-82 / Metso Paper (USSR / Sweden)
 Year of installation 1987
 Modernization 2005 - 2006, 2011
 Speed of work 1500 m/min
 Cropped width 2700 mm
 Capacity 25 kilo ton per year

PM-2

Trademark Advantage DCT100, (Metso Paper, Sweden)
 Year of installation 2008
 Speed of work 1600 m/min
 Cropped width 2700 mm
 Capacity 30 kilo ton per year

PM-3

Year of installation 2012 - 2013
 Capacity 30 kilo ton per year

Formatted cutting department (Syktyvkar)

PRS-1

Trademark Petrozavodskmash, USSR
 Year of installation 1987
 Модернизация 2010
 Max. speed 600 m/min

PRS-2

Trademark Toscotec, Italy
 Year of installation 2008
 Max. speed 1500 m/min

Toilet paper and paper towels (Syktyvkar, Centre)

Converting line 813

Trademark Fabio Perini, Italy
 Year of installation 1987
 Modernization 2005 - 2006
 Flow lines 2 pcs
 Capacity 125 mn stand. rolls/year

Converting line SINHRO 4.0

Trademark Fabio Perini, Imanua
 Year of installation 2005
 Modernization 2008
 Flow lines 1 pcs
 Capacity 70 mn stand. rolls/year

Converting line X-5

Trademark Fabio Perini
 Year of installation 2005
 Flow lines 1 pcs
 Capacity 70 mn stand. rolls/year

Converting line

Year of installation October 2011
 Flow lines 1 pcs
 Capacity 200 mn stand. rolls/year

Converting line (Centre)

Year of installation 2014
 Capacity 90 mn stand. rolls/year

Converting line (Centre)

Year of installation 2015
 Capacity 120 mn stand. rolls/year

Paper handkerchiefs (Syktyvkar)

Paper handkerchief converting line

Year of installation 2013
 Capacity 66 mn stand. packs/year

Economic, in the paper packing

«Syktyvkar'skaya 56» one-ply
 «Syktyvkar'skaya Comfort» one-ply

Standart embossing in the polymer pack

TP Veiro Classic 2 plies white (2 rolls)
 TP Veiro Classic 2 plies white (4 rolls)
 TP Veiro Classic 2 plies white (8 rolls.)
 TP Veiro Classic 2 plies pastel (4 rolls)
 TP Veiro Classic 2 plies pastel (8 rolls)
 TP private TM, 2 plies (4 rolls)
 PT Veiro (2 rolls)
 PT private TM2 plies (2 rolls)

Premium embossing in the polymer packing

TP Veiro Standart 2 plies white (4 rolls)
 TP private TM2 plies white (4 rolls)
 TP Veiro Floria 2 plies white arom. (4 rolls.)
 TP Veiro Luxoria 3 plies white (4 rolls)
 TP private TM3 plies white (4 rolls)
 PT Veiro (2 rolls)
 PT private TM2 plies (2 rolls)

TP2 layers economic (4 rolls, scrap paper)
 TP2 layers standart (4 rolls, scrap paper)
 TP2 layers premium (4 rolls, pulped)
 PT standart (2 rolls)

TP2 layers economic (4 rolls, scrap paper)
 TP2 layers standart (4 rolls, scrap paper)
 TP2 layers premium (4 rolls, pulped)
 PT standart (2 rolls)

TP2 layers economic (4 rolls, scrap paper)
 TP2 layers standart (4 rolls, scrap paper)
 TP2 layers premium (4 rolls, pulped)
 PT standart (2 rolls)

Paper handkerchiefs 3 plies, 20 x 20 (10 pcs)

Napkins (Syktyvkar)

Napkin line

Trademark SDF (Germany)
 Year of installation 2008
 Speed of work 300 m/min
 Capacity 14 mn stand. packs/year*

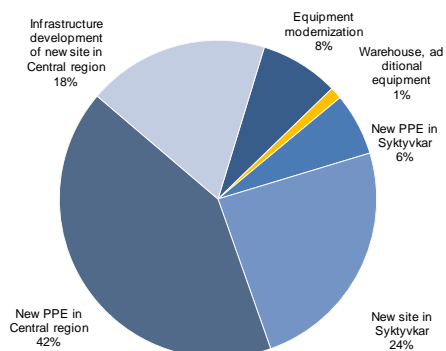
Paper napkins

Linia Veiro 24 x 24 1 ply white, col., with pic. (50 pcs)
 Linia Veiro 24 x 24 2 plies with pic. (25 pcs)
 Linia Veiro 33 x 33 2 plies white, coloured (25 pcs)
 Linia Veiro 33 x 33 3 plies with pic. (20 pcs)

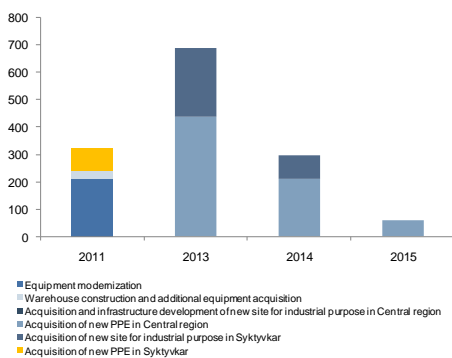
High quality commercial base paper

* In terms of 50-sheets packs of napkins without printing with format 24 x 24 sm.

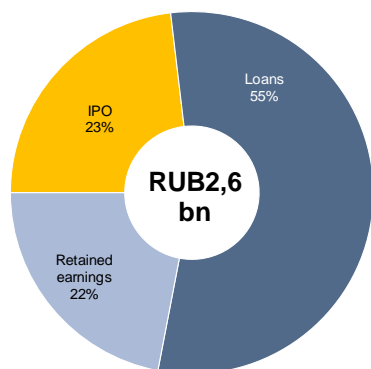
Capex breakdown



Capex breakdown (YoY), mn RUB



Source of capital



Investment Program

STG approved the long-term investment program aiming at further development and meeting the increasing market demands. The investment program envisages an upgrade of the existing capacities and the acquisition of new facilities.

It is designed till 2015 and stipulates several stages.

- 2011 — the modernization of 813 line and PM-1 is slated to improve the quality of pulp base paper and to enable the company to produce base paper of higher price segment, which is designed for multicolor printing, multilayer napkins and handkerchiefs production. The replacement of some PM-1 components is set to increase fault tolerance that, in turn, will reduce the risks associated with emergency shutdowns and idleness. Furthermore, the capacities upgrade will cut per unit chemicals and energy costs, as well as PM maintenance expenses. The capex, including the construction of storage facilities, is estimated at RUB241mn.
- October 2011 — the acquisition of a new converting line and a handkerchief production line to be installed on Syktyvkar production site. The total costs are estimated at RUB165mn.
- 2013-2014 — the acquisition of PM-3. The paper making machine is planned to be installed on a new Syktyvkar production site, which has developed infrastructure, and will be delivered by Metso Paper. PM-3 with annual capacities of 30,000 tonnes is expected to be commissioned at the end of 2013. The capex, including preparation equipment, is estimated at RUB1,470mn.
- 2015 — the installation of two converting lines on a new production site in the Central Federal District of Russia. The company targets the regions, which are in a proximity to sales market, such as the Moscow, the Kaluga, and the Leningrad regions, mainly located no more than 150 km away from Moscow. The capex, including the purchase of a new land plot for the converting lines installation, is estimated at RUB720mn.

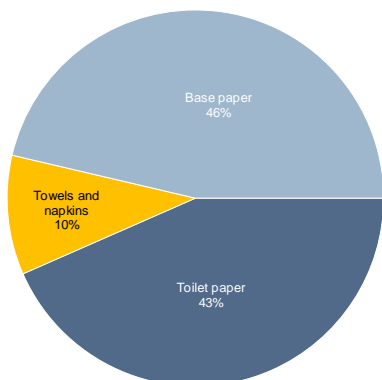
The investment program will be financed via funds raised during IPO, via generated profit, and obtained loans. The mix of financing sources is set out below:

- Investors' funds — 23%;
- Equity — 22%;
- Borrowings — 55%.

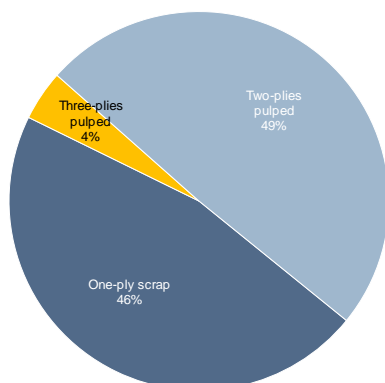
STG closely cooperates with Gazprombank, UniCredit Bank, and Sberbank. STG will borrow money at the maximum interest rate of 10% for a long-term period of 7-12 years.

| Stage | Deadline | Capex, mn RUB | Region |
|---|----------|---------------|----------------|
| PM-1 modernization, warehouse construction | 2011 | 232 | Syktyvkar |
| Converting line 813 modernization | 2011 | 9 | Syktyvkar |
| New converting line acquisition | 2011 | 165 | Syktyvkar |
| PM-3 and additional equipment acquisition | 2014 | 1 470 | Syktyvkar |
| New converting lines and infrastructure acquisition | 2015 | 720 | Central region |
| TOTAL | | 2 595 | |

Sales breakdown 2010



Toilet paper sales breakdown 2010



Product Mix

Paper base and sanitary tissue products are the key goods of STG. Toilet paper comprised around 43% of the company's total revenue in 2010, paper base accounted for 46% with paper towels and napkins standing at 10%.

STG produces toilet paper of various price segments and targets diverse residential groups:

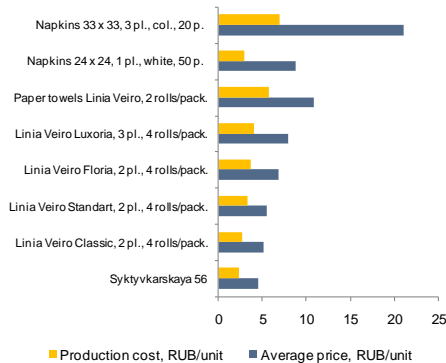
1. Budget segment — one-ply scrap toilet paper under Syktyvkarskaya 56 brand. It is the most famous and popular trademark, which accounted for 20% of the company's total revenue in 2010 (46% of revenue from total toilet paper sales). Syktyvkarskaya 56 is sold in the paper package. In addition, STG produces scrap toilet paper under Komfortnaya brand.
2. Standard segment — two-ply perfumed pulped paper in various packages (2, 4, and 8 rolls per pack). The company produces toilet paper of the following trademarks: Veiro Classic, Linia Veiro Classic, Veiro Standart, Veiro Floria, and Veiro Premium. Two-ply pulp paper comprised 21% of the company's total revenue and 49% of the company's revenue from toilet paper sales.
3. Premium segment — three-ply toilet paper under Veiro Luxoria brand.



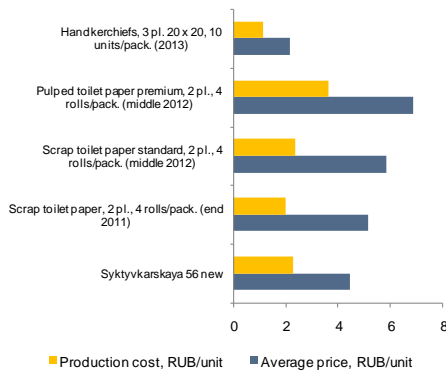
Base paper is produced on two PMs of total annual capacities of 20,000 tonnes (scrap and mixed paper) and of 30,000 tonnes (white pulped and colored paper). Around 24% of base paper is sold as commercial base paper, Being of high quality, STG's base paper is also supplied to foreign producers, e.g. to Metsä Tissue.

The sales of base paper enable the company to mitigate local hikes and decreases in demand. For example, if the company's finished products enjoy weak demand due to any reasons, the production capacities will be still fully utilized thanks to the strong demand for base paper.

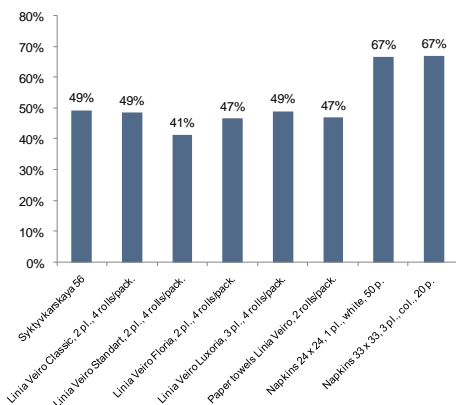
Price vs cost of products, RUB



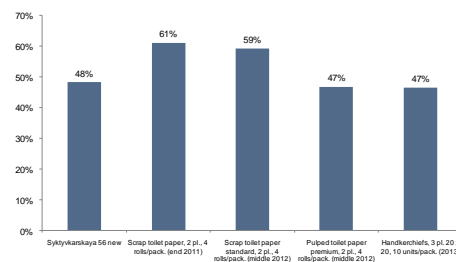
Price vs cost of new products, RUB



Products margin



New products margin



Brands Profitability

STG makes a balanced product mix of high profitability. Across the board, the cost of raw materials accounts for about 50% and 15%-40% of the selling price of finished products and base paper, respectively. This is due to the fact that base paper is a semi-finished product and needs to be processed.

The gross margin of toilet paper hovers in the range of 41%-50%, the most profitable STG's product is considered to be napkins with their production commissioned in 2008, which generated the gross margin at 67%.

In 2011-2013 STG plans to launch a new product line, which is envisaged by the company's investment program. In particular, STG intends to install new converting lines and to upgrade PM-1. As a result, two types of two-ply toilet paper – scrap paper and pulped paper (4 rolls per pack) – will be added to the product mix by 2012. In 2013, STG plans to start producing three-ply handkerchiefs. By the same token, the company is set to manufacture a renewed edition of Sytkyvkarskaya 56 toilet paper, as well as two-ply scrap toilet paper (4 rolls per pack) which is expected to post the gross margin above 60%.

The new products are slated to post profitability in line with the existing products that will balance the product mix.

Financials

In 2010 STG demonstrated robust financial growth following the previous-year trend. The positive financial performance was attributable to the launch of PM-2 in 2008, which helped the company significantly ramp up the production of paper base and napkins (by 8.5 times and 20.5 times YoY in 2009, accordingly).

The company's IFRS revenue surged 41.2% YoY to RUB1.74bn in 2010. The new efficient equipment favorably impacted STG's profitability with EBITDA margin soaring from 19% in 2009 to 23.2% in 2010.

On the back of net debt and debt servicing costs reduction, and higher financial income, the company's net income showed virtually a nine-fold YoY increase, and the net margin reached 5.7% in 2010.

STG's balance sheet looks burdensome (which is typical for any manufacturing enterprise) due to a large share of PPE and long-term sources of finance. The company's net debt stood at RUB958mn as of the end of 2010, while total assets amounted to RUB2.6bn. Nevertheless, the company witnesses its net debt declining on the back of the increased cash.

The financial leverage slipped to 1.0 in 2010 with net debt-to-EBITDA ratio reaching 2.26 and short-term obligations accounting for only 5% of gross loan portfolio.

| Profit and loss statement, mn RUB | 2009 | Change, % | 2010 |
|-----------------------------------|--------------|-------------|--------------|
| Sales | 1 235 | 41,2 | 1 743 |
| Cost of products sold | (899) | 41,1 | (1 269) |
| inc. amortization | (55) | 87,9 | (103) |
| Gross profit | 336 | 41,4 | 474 |
| Gross profit margin | 27,2 | | 27,2 |
| General expenses | (73) | 4,8 | (76) |
| Administrative expenses | (82) | 16,6 | (96) |
| Non-operational income (losses) | (2) | - | (1) |
| EBITDA | 234 | 72,8 | 405 |
| EBITDA margin, % | 19,0 | | 23,2 |
| EBIT | 179 | 68,1 | 301 |
| EBIT margin, % | 14,5 | | 17,3 |
| Financial income (expenses) | (164) | 3,1 | (169) |
| EBT | 16 | - | 132 |
| EBT margin, % | 0,0 | | 0,1 |
| Income tax | (5) | - | (29) |
| Minority interest | 0 | - | (3) |
| Net profit | 11 | - | 100 |
| Net profit margin, % | 0,9 | | 5,7 |

| Balance sheet, mn RUB | 2009 | Change, % | 2010 |
|---------------------------|--------------|--------------|--------------|
| PPE | 1 787 | 13,6 | 2 029 |
| Inventory | 186 | 16,6 | 216 |
| Accounts receivable | 113 | 63,3 | 185 |
| Cash and cash equivalents | 39 | 381,8 | 189 |
| Share capital | 677 | 60,7 | 1 087 |
| Long-term liabilities | 861 | 23,2 | 1 061 |
| Short-term liabilities | 225 | (62,0) | 86 |
| Net debt | 1 047 | (8,5) | 958 |
| Total assets | 2 168 | 21,6 | 2 637 |

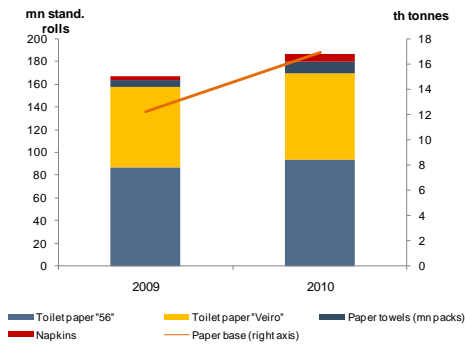
| Economic profitability analysis | 2009 | 2010 |
|---------------------------------|--------------|--------------|
| <u>ROIC analysis:</u> | | |
| EBITDA margin, % | 23,20 | 21,65 |
| amortization burden | 0,74 | 0,78 |
| effective tax rate, % | 21,88 | 20,41 |
| total assets turnover | 0,80 | 0,77 |
| invested capital multiplier | 1,29 | 1,30 |
| ROIC, % | 13,94 | 13,33 |
| <u>Du Pont ROE analysis:</u> | | |
| net profit margin, % | 0,91 | 5,71 |
| total assets turnover | 0,58 | 0,80 |
| equity multiplier | 3,22 | 3,21 |
| ROE, % | 1,69 | 14,71 |
| ROA, % | 1,66 | 17,12 |

| Financial leverage characteristics: | 2009 | 2010 |
|---------------------------------------|-------|------|
| Financial leverage | 1,52 | 1,02 |
| Net interest-bearing debt / EBITDA | 4,22 | 2,26 |
| Net interest-bearing debt / sales | 0,80 | 0,53 |
| Net interest-bearing debt / assets | 0,45 | 0,35 |
| Net interest-bearing SR debt / EAT | 14,06 | - |
| Net interest-bearing SR debt / assets | 0,07 | - |
| Interest payments / EBITDA | 0,58 | 0,31 |

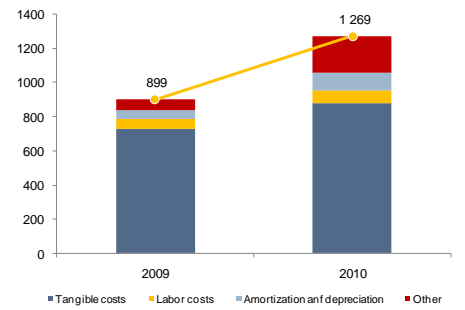
| Company's liquidity: | 2009 | 2010 |
|---------------------------------|------|------|
| current ratio (>2) | 0,76 | 1,93 |
| quick ratio (>1) | 0,34 | 1,21 |
| absolute liquidity ratio (>0,2) | 0,09 | 0,61 |

| Turnover estimates of (days): | 2009 | 2010 |
|-------------------------------|--------|-------|
| accounts receivable | 33,49 | 38,73 |
| interest free liabilities | 119,83 | 84,55 |
| inventories | 54,85 | 45,32 |

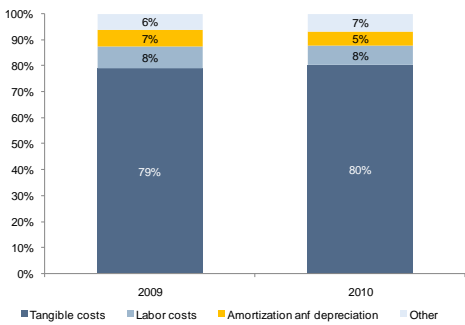
STG operational data in 2009-2010



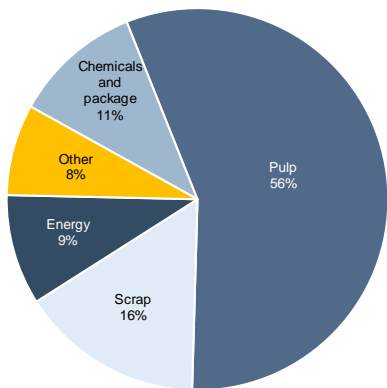
Costs changes, mn RUB



Costs breakdown



Tangible costs breakdown 2010



Sales Mix and Costs Breakdown in 2010

STG's 2010 IFRS revenue rose 41.2% YoY to RUB1.74bn in 2010 primarily due to the increased output of all types of products. The production of napkins, paper towels, and commercial base paper posted the fastest growth rates of 76%, 78%, and 38% YoY in 2010, respectively. Toilet paper output climbed 7-8% for the same period.

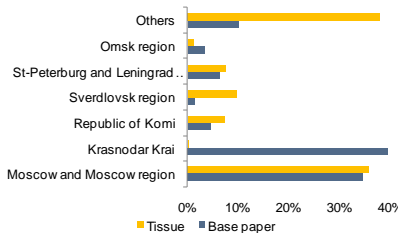
Toilet paper accounted for 43% of the total revenue, base paper comprised 46%, while paper towels and napkins constituted 10% of the company's total sale. Sales mix is represented below:

- One-ply scrap paper — 46%;
- Two-ply pulped paper — 49%;
- Three-ply pulped paper — 4%.

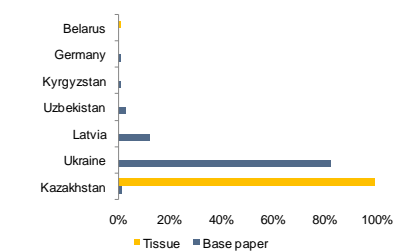
Over 93% of products were sold in Russia. Moscow and the Moscow region remain the main sales markets of STG accounting for 35% of total sales. The Krasnodar Territory, Moscow and the Moscow region totally comprise 70% of base paper sales on a proportional basis.

Ukraine and Kazakhstan are the key export markets with the former accounting for 82% of STG's base paper, and the latter comprising 99% of sanitary tissue products.

Regional sales breakdown in 2010



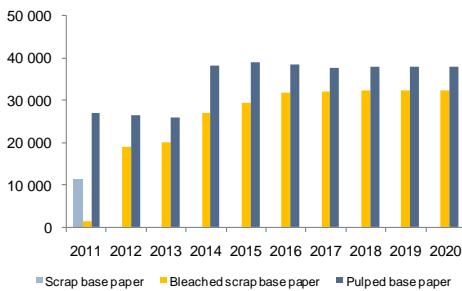
Export sales breakdown in 2010



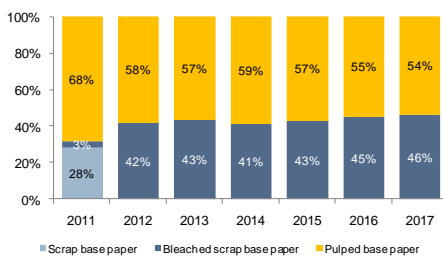
STG saw a 41% YoY increase in its cost of production in 2010. This is explained by a high share of tangible costs (of around 80% in 2010), which rose 50% YoY.

Pulp expenses comprise a sizeable share of 56% in the tangible costs breakdown having rose 74% YoY due the PM-2 installation and the increase in pulped paper output. Scrap paper, chemicals and package expenses of 16% and 11% of total tangible costs, respectively, are the smaller cost items.

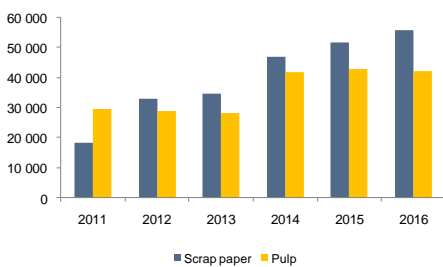
Base paper consumption, tonnes



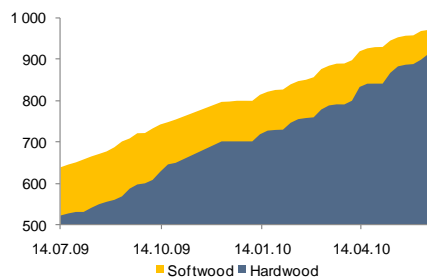
Base paper consumption breakdown



STG raw materials consumption, tonnes



Pulp price dynamics, USD/tonn



Raw Materials Market Overview

Two types of raw materials are used for the sanitary tissue products manufacturing:

- Bleached sulfate softwood and hardwood pulp;
- Scrap paper.

The pulp is mainly supplied by Mondi Business Paper Syktyvkar Forest Enterprise within the long-term agreements with the price being revised twice a year. The price calculation formula is a factor of pulp price on the global market and of Arkhangelsk Paper Plant.

STG also consumes pulp from Arkhangelsk Forest Enterprise, however the pulp is purchased on an irregular basis with the purchase price being set as of the date of a deal.

Scrap paper is supplied to STG from various sources, which count around 30 suppliers. Two large-scale plants account for about 35% of total scrap paper supplies. STG uses different kinds of scrap paper: office paper, newspaper, cardboard, etc. Paper sorting segment in Russia has been underdeveloped so far, therefore scrap paper is supplied unsorted.

The current STG's sales mix shows that scrap paper accounts for a half of the total amount. Depending on a form of scrap paper processing, base paper can also be over bleached. Meanwhile, prior to the start of the investment program the company has a relatively small share of over bleached scrap paper in its production. As such, in 2011 over bleached scrap paper output is estimated at an amount equaling 3% of total base paper needs.

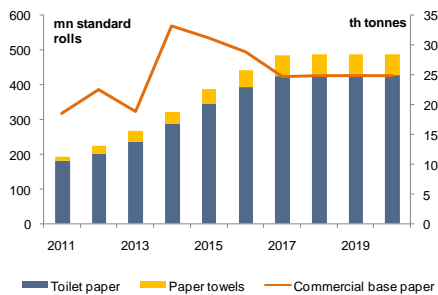
With implementing the first stage of the investment program – an upgrade of PM-1 – STG is expected to produce base paper of a better quality. As a result, scrap base paper should account for 42% starting from 2012, while pulped base paper – 58%. By 2010 a share of scrap base paper is estimated to advance 3 ppt to 45%. Thus, scrap raw materials needs are expected to triple already by 2016 compared to 2011, while pulp needs are forecast to surge 42%.

We consider STG's production mix and raw materials breakdown as optimal with regards to hedging against the risk of global pulp price increase.

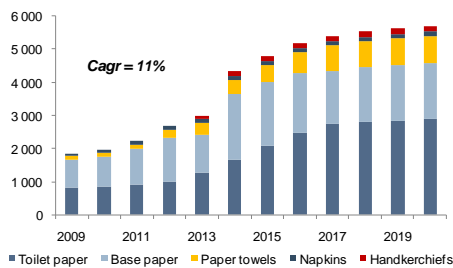
Amid crisis in 2H09, prices of softwood pulp soared 52% YoY, while of hardwood pulp jumped 75% YoY in 2H10. Abnormal price growth was attributable to the earthquake in Chili and the strikes in Finland. South America (in particular, Brazil and Chili), and Scandinavian countries as large pulp suppliers have a sizeable impact on raw materials pricing environment across the globe. Chili along with Finland account for 12% of total pulp suppliers. Amid environmental disaster and social unrest the major pulp manufacturers ceased their production that translated into vigorous price growth.

With recovery in pulp deliveries by Chili and Finland, raw materials supplies are expected to rebound that should lead to price stabilization and consequently improve tissue producers' profitability.

STG production forecast till 2020



STG sales forecast till 2020, mn RUB



Financial Forecasts till 2020

STG foresees an increase in its production numbers till 2020:

- by 2.2 times in toilet paper segment;
- by 5 times in paper towels segment;
- by 60% in commercial base paper segment.

Toilet paper production is estimated at 427 mn rolls in 2020 representing 9% of the Russian toilet paper market, which is up by 1 ppt compared to 2010. STG intends to reduce its share of the base paper market (excluding import) from 30% to 20% and to produce 25,000 tonnes annually by 2020.

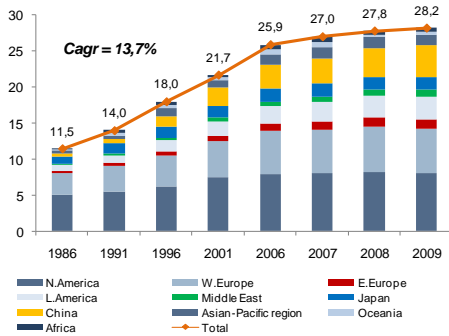
Provided the anticipated growth rates of production, STG forecasts its revenue CAGR of 11%. On the back of capacity expansion and gradual market saturation in 2014-2015, STG's revenues growth will be even more aggressive with revenue 2015E of around RUB4.3bn that is 2.4 times higher than the 2010 respective number.

Starting from 2014 toilet paper and paper towels are expected to be the main revenue contributors. The company forecasts the sales of toilet paper to increase 75% to RUB2.9bn, while those of paper towel to climb 92% to RUB816mn by 2020. It is worth mentioning that by 2014 STG intends to significantly expand its exposure to base paper compared to finished sanitary tissue products, according to the gradual implementation of its investment program. Going forward, the sales of base paper are set to decline.

STG views the central part of Russia (Moscow and the Moscow region, the Kaluga and the Ryazan regions, as well as the other regions neighboring to the Moscow region) as its major markets. The company plans to launch additional converting lines in these areas, which are expected to comprise around one third of the company's total sales.

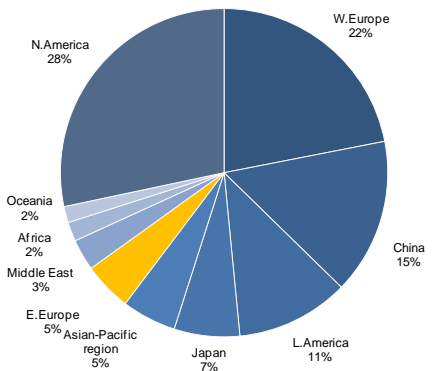
In addition, the introduction of new production capacities will increase STG's exposure to the Volga region market (Tatarstan, the Samar and the Saratov regions, etc.).

World tissue consumption, mn tonnes



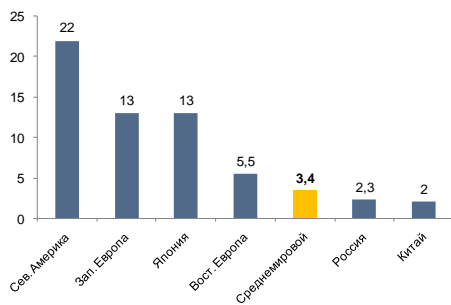
Source: RISI, <http://www.tissueworldmagazine.com>

Tissue consumption breakdown in 2009



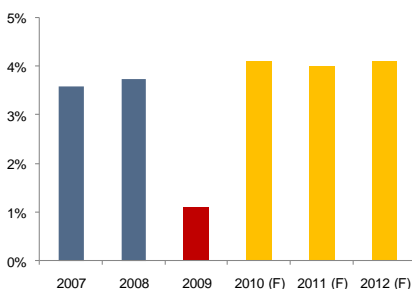
Source: RISI, <http://www.tissueworldmagazine.com>

Per capita tissue consumption in 2009, kg



Source: RISI

World tissue consumption growth



Source: RISI

Global Tissue Market

Sanitary tissue products market is one of a few which continues showing positive performance for several consequent years amid economic downturns. According to RISI and *Tissue World Magazine*, CAGR of global tissue consumption stood at 13.7% in 1986-2009. Global market of sanitary tissue products reached 28.2mn tonnes in 2009 and is expected to amount to 38mn tonnes by 2016. North America and Europe represent the most capacious markets accounting for 28% and 22% of global tissue consumption, respectively.

In value terms, North America also takes the lead in sanitary tissue products consumption of around \$16bn with the US and Canada comprising virtually 90% and about 10% of the total amount, respectfully.

Western Europe and the Asia Pacific region come second and third accordingly, accounting for the comparable shares in consumption mix. In 2009 the Asian tissue market totaled \$12.8bn.

The Asia Pacific region is viewed by the experts as the most promising tissue market being the only one which showed a 5% increase in the midst of 2009 financial crisis, while North America and Western Europe lost 3% and 5%, accordingly.

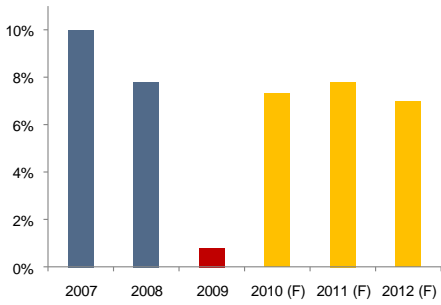
China is the most dominate in the Asia Pacific region. The Chinese tissue market grew 9% in 2009 to \$7.2bn, while it totaled \$3.3bn in 2000.

The Chinese market offers a huge upside potential, as sanitary tissue products consumption per capita lags behind the world average (\$8 per capita) by 2.7 times and North America's average (\$46 per capita) by 15.3 times. In volume terms, per capita consumption in China is less than 2 kg pa vs. 22 kg in North America and 13 kg in Western Europe and Japan. The aggressive growth of the Chinese tissue market is underpinned by the economic boom, the improved quality of life, robust development of tourism and restaurant business.

Aside from China, in the Asia Pacific region India, Vietnam, Indonesia, and Thailand are set to uncover the upside potential. These countries have recently demonstrated growth rates outpacing the average.

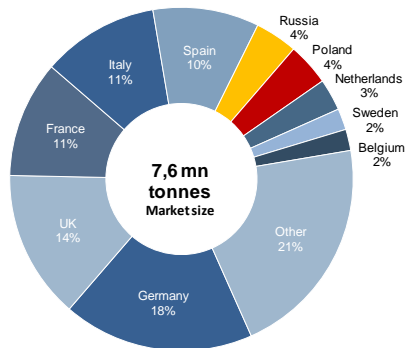
Eastern Europe is another emerging leader on the tissue market. Currently, Eastern Europe enjoys a relatively small share in global consumption standing at only 5%, or 1.4mn tonnes in 2009. However, in 2000-2008 growth rates of sanitary tissue products consumption varied from 6% to 13% that is several times higher than the global average, as well as Western Europe's average, which did not surpass 4%.

Eastern Europe tissue consumption growth



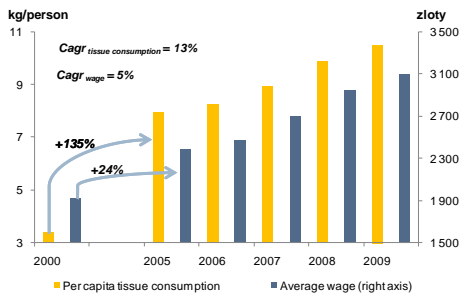
Source: RISI

Main European tissue markets in 2008



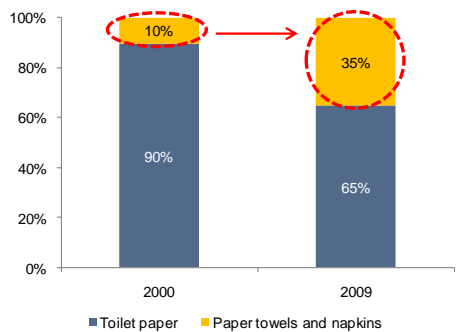
Source: RISI

Tissue consumption vs wages in Poland



Source: GUS

Tissue consumption breakdown in Poland



Source: GUS

Meanwhile, in 2009 Eastern Europe witnessed slowdown in growth rates. However, along the economic rebound, sanitary tissue products consumption growth is expected to outpace the average in a 10-year horizon. The tissue consumption is forecast to increase 7-8% CAGR in Eastern Europe, while maximum growth of tissue consumption in Western Europe is limited to 3% CAGR, and the global consumption will hardly grow 4% CAGR.

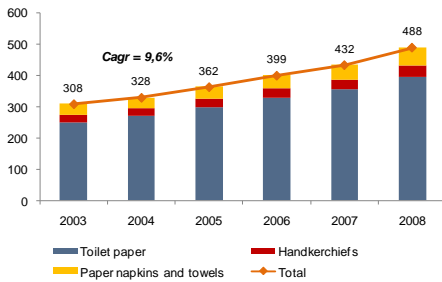
The largest consumer of sanitary tissue goods in Eastern Europe is Russia, which accounts for 25% of the total (4% of the Europe average) and represents the most roomy market of toilet paper and tissue napkins.

Poland with the similar to Russia mindset is the second largest consumer in Eastern Europe. According to RISI, Poland occupies the comparable share of the European tissue markets, while Russia has three-times less population. This implies that Poland demonstrates higher per unit sanitary tissue products consumption. According to Central Statistics Office of Poland (GUS), the average consumption of tissue topped 10 kg per capita in 2009, while in 2000 it slightly surpassed Russia's average of 3.4 kg per capita pa. Poland made breakthrough already by 2005 having increased its average consumption to 8 kg per capita. Thus, sanitary tissue products per capita consumption soared 13% CAGR that even outpaced the real income dynamic, which grew 5% CAGR for the same period.

In addition, consumption mix itself also changed. Toilet paper comprised 90% of total consumption in Poland, while paper towels and tissue napkins accounted for 10% in 2000. Over nine years the consumption breakdown dramatically changed with toilet paper comprising already 65%.

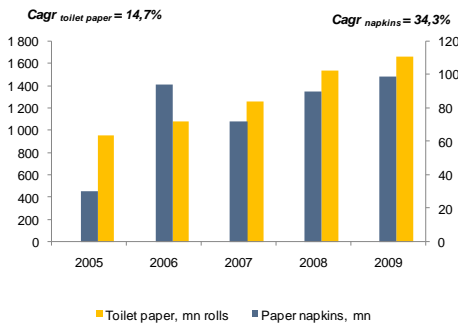
Based on the above-mentioned data, the other Slavic states of Eastern Europe, which lag behind Poland in terms of sanitary tissue goods consumption, will follow its upward path and post outpacing dynamic in a 5-7-year horizon with Russia, Ukraine, Belarus, Moldova, Serbia being among them.

Russian tissue consumption in 2003-2008, mn USD



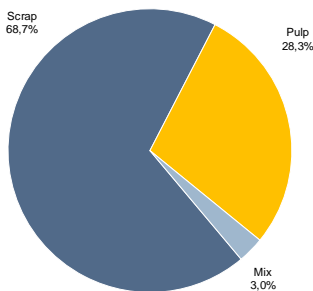
Source: Euromonitor, RISI

Russian tissue production size



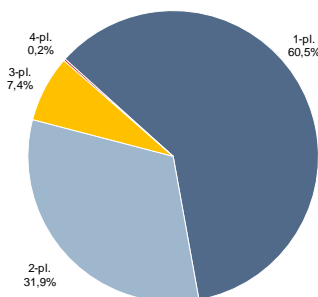
Source: Rosstat

Tissue consumption breakdown by base paper in 2009



Source: FCS RF, producers data

Tissue consumption breakdown by plies in 2009



Source: FCS RF, producers data

Russia's Tissue Market

The Russian market of sanitary tissue products is gaining momentum in the long term. According to Euromonitor, in 2003-2008 CAGR topped 9% in value terms. In 2008 the market volume exceeded \$480mn. Based on RISI data, Russia's tissue market amounted to 305,000 tonnes in volume terms in 2008, and 350,000 tonnes in 2009 (+14% YoY).

The tissue market mix implies that toilet paper comprises over 80%. Toilet paper suppliers accounted for a lion's share in total supply mix.

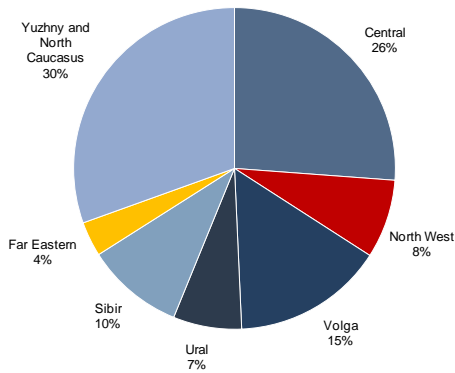
According to Rosstat, over 1.658bn of toilet paper rolls were produced in 2009 vs. 1.533bn of toilet paper rolls a year before. Toilet paper production grew at 14.7% CAGR in 2005-2009. Owing to the immaturity of paper towels and napkins market, their production increased more than 34% CAGR. As such, in 2009 about 100 mn napkin packs were manufactured.

Importantly, in the crisis year of 2009 Russia's toilet paper market remained generally intact with its growth rates declining 8% in volume terms, while in 2008 they stood at 22%. Despite some slowdown, toilet paper consumption rates continued exceeding the global average.

Three types of raw materials are used for toilet paper production. They are scrap paper, pure pulp and their mixture. For many years already toilet paper, made from processed scrap paper, has been the wide-spread type accounting for around 70%.

One-ply toilet paper, which comprised over 60% of the market in 2009, currently enjoys high demand in Russia. Meanwhile, there has been an increase in consumption of two-ply toilet paper, which accounted for 32% of the market in 2009. Furthermore, the demand for three-ply toilet paper, which comprised 7.4% of the market in 2009, is on the rise.

Regional tissue market breakdown



Source: FCS RF, producers data

In terms of regional breakdown of consumption, the region, which enjoys the largest share, is the Central Federal District of Russia. It occupies around 26% and 24% of tissue market in volume and value terms, accordingly. Yuzhny and North Caucasus Federal Districts are also large consumers with a total share of 30%. In addition, Volga, Sibir and North West Federal Districts offer capacious markets of sanitary tissue products, accounting for 15%, 10%, and 8%, respectively.

In Russia there are four toilet paper marketing channels:

- retail industry (small outlets, and stores, which are not included into the major retail chains);
- retail chains (retailers at federal and regional levels);
- wholesales companies;
- HoReCa (hotels, restaurants, etc.).

In 2006-2009 the focus of toilet paper market shifted away from small-scale retailers towards the centrally-managed segment. The sales of trade chains doubled, while those of small-scale retailers rose only 19%. The volume of sales sold out via trade chains expanded 5 ppt to reach 19%.

The sales of toilet paper across the HoReCa segment (so called commercial sanitary tissue goods) showed even faster growth rates (of 220%). HoReCa segment accounted for 15% in 2009 vs. 7% in 2006 in total sales volume.

Even the financial crisis failed to buck the trend. Therefore, the future development will be marked by the expansion of commercial sanitary tissue products, as well as by the sales via large retail chains.

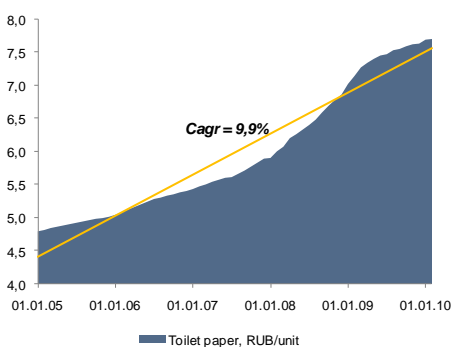
The current pricing environment on the toilet paper markets is quite favorable. Paper roll price has been on the rise for several years growing at 10% CAGR. Early in 2010 average price of a toilet paper roll slightly topped RUB7.5.

Main marketing channels

| Marketing channel | 2006 | | 2009 | | Change | |
|---------------------|------------------------|----------|------------------------|----------|-----------------|-------------|
| | Sales volume, th rolls | Share, % | Sales volume, th rolls | Share, % | sales volume, % | share, p.p. |
| Retail chains | 192 016 | 14% | 389 570 | 19% | 103% | 5 |
| Wholesales companit | 342 886 | 25% | 471 584 | 23% | 38% | -2 |
| HoReCa | 96 008 | 7% | 307 555 | 15% | 220% | 8 |
| Retail industry | 740 634 | 54% | 881 658 | 43% | 19% | -11 |

Source: producers data

Russian toilet paper market movement



Source: Rosstat

Amid high growth rates, Russia tissue market enjoys low saturation. The consumption of commercial sanitary tissue products in Russia of 2.3 kg per capita lags significantly behind the global average (3.4 kg per capita in 2009) and all the more as compared to developed countries. Moreover, Russia lags behind Europe and the USA by 5-10 times.

Consequently, Russia's tissue market offers a huge upside potential, which should uncover in a similar to Poland's way. Tissue consumption is estimated to grow at over 8% CAGR during the next 5-7 years with the real income increase driving the consumption of the high-margin products, such as paper towels and napkins, and Russia is likely to repeat Poland's scenario, where napkins consumption picked up more than 10 times in 2000-2009.

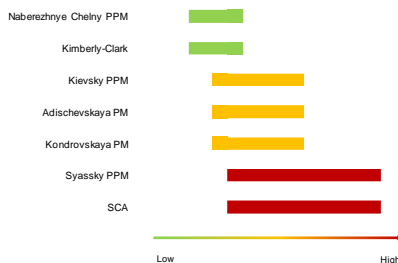
Main toilet paper producers in 2009

| Manufacturer | Market share, % | Trade marks |
|------------------------|-----------------|---|
| SCA | 22% | Zewa |
| Naberezhnye Chelny PPM | 14% | Toilet paper from Naberezhnye Chelny |
| STG | 7% | Veiro, 56 meters |
| Syassky PPM | 6% | Myagky znak |
| Kondrovskaya PM | 4% | Siren |
| Adischevskaya PM | 4% | Ostrovskaya standart 54, Azhur, Novinka, Myagky element, Chao |
| Kievsky PPM | 4% | Obukhov 65, Divo |
| Kimberly-Clark | 2% | Kleenex |
| Other | 36% | |
| Total | 100,0% | |

Main napkins producers in 2009

| Manufacturer | Market share, % | Trade marks |
|------------------------------|-----------------|-------------|
| Georgia-Pacific | 20% | Lotus |
| Syassky PPM | 8% | Myagky znak |
| Lily | 7% | Lily |
| Sansi | 6% | Papirus |
| Russian paper all production | 6% | Bouquet |
| Kondrovskaya PM | 4% | Siren |
| STG | 2% | Veiro |
| Other | 46% | |
| Total | 100,0% | |

Degree of competition with STG



Competitive Environment

Around 30 companies in Russia produce base paper from pulp, scrap paper or the mixture of pulp and scrape paper.

18 manufacturers, of which three are foreign enterprises, constitute about 80% of Russia's toilet paper market. In whole, the local tissue market, in particular paper toilet segment, is represented mainly by the domestic players. Yet, Swedish producer SCA occupied 22% of Russia's tissue market in 2009. Russia's three large-scale producers, STG being among them with a 7% market share, retained 28%.

The closest rivals of STG are Syassky Pulp and Paper Mill, and SCA. SCA is considered to be the strong competitor, however STG pursues the policy, which eliminates products overlapping. The major product of SCA is two-ply scrap toilet paper under Zewa brand, STG, in its turn, is represented in the scrap toilet paper segment by a cheaper product under Syktyvkarksaya 56 brand, which is targeted to the other consumer groups. SCA's products are not represented in the two-ply pulped toilet paper segment of the Russian market.

Syassky Pulp and Paper Mill retains the equal to STG market share of 6.4%, Syassky PPM's primary tissue brand is Myagky znak, which represents the same price segment as Veiro brand. Syassky PPM has similar to STG product mix including one-, two-, and three-ply pulped toilet paper and napkins of various perfume, color and package. STG undertakes steps aiming at establishing influence areas on the regional markets wherever it is possible. Expected growth rates of the Russian tissue market considerably outstrip the pace of new capacities introduction by the domestic pulp manufacturers. Therefore, full market saturation and the dramatic rise of competition are unlikely in the next 5-10 years.

Among the Russian pulp producers Naberezhnye Chelny Paper and Paperboard Mill occupies the bulk of market. It produces cardboard and sanitary tissue goods. The company gained 14.5% of market in 2009. The geographical scope and the market capacity eliminate competition with STG. On top of that, STG produces goods of a better quality (bleached scrap paper) that enables to differentiate the consumer segments of STG and Naberezhnye Chelny PPM.

Kimberly-Clark stands out among the foreign tissue producers, which run the business in Russia. It retains 2.2% of the local market and produces tissue goods under Kleenex brand. While Kimberly-Clark's products are of the same quality segments as those of STG, they are more expensive. In addition, Kimberly-Clark has neither its own production facilities in Russia, nor manufactures base paper that reduces the flexibility in setting the price policy.

STG has been engaged in napkins production only since 2008, when PM-2 was commissioned. However, already in 2009 STG accounted for 2% of the napkins market. This segment of the tissue market is notable for its high competition and represented by three local producers. However, three companies occupy over 35% of the market with Georgia-Pacific accounting for almost 20%.

SWOT-analysis

STG has quite a balanced SWOT-matrix that suggests the company is well-positioned in the sanitary and hygiene products market and can benefit from low saturation of the Russian tissue market.

| | Strengths | Weaknesses |
|----------------------|--|--|
| | <ul style="list-style-type: none"> • Transparent organizational structure, solid management. • Financials are stable and less sensitive to macroeconomic developments. • Strong brand. Balanced product mix in terms of profitability. • Streamlined distribution of finished products. • ISO 9001:2008 quality management system. • Advanced management accounting. • Upgraded, state-of-the art, high-quality facilities allowed the company to more than double its production. • Further modernization of equipment and new capacities introduction, in particular in the Central Federal District of Russia, will lead to higher production and lower logistic costs. • Long-term agreements with Mondi Business Paper on raw materials supply mitigate price risks. | <ul style="list-style-type: none"> • Currently restrained capacities prevent from meeting the increasing demand for sanitary and hygiene products in Russia. The company has to reject some orders. • High debt leverage undermines the company's financial stability. • Limited financial resources impede aggressive capacities build-up and slow down an increase in the company's production. • A lack of qualified personnel at the production facilities. |
| Opportunities | <ul style="list-style-type: none"> • High market capacity due to low per capita consumption of sanitary and hygiene products. Commercial tissue segment offers a huge upside potential. • Industry-specific technological risks: relatively simple production technology alleviates risks associated with the company's technological underdevelopment. • Resource base: extensive forest areas in the Komi Republic minimize risks of raw materials deficit. | <p>STG's development strategy aims at strengthening the foothold on the current markets and tapping new promising segments (e.g., commercial sanitary goods, foreign expansion). One of the development stages is the construction of a new production site in the Central Federal District of Russia.</p> <p>STG's development strategy envisages the growth rates, which encourage the company to generate higher cash flows. This, in turn, will reduce its dependency on external financial sources and enhance personnel qualification.</p> |
| Threats | <ul style="list-style-type: none"> • Foreign players may intensify the competition. • Changes to the monetary policy of Russia may adversely impact the company's business due to its high dependency on lending resources. • The underdeveloped business in commercial sanitary and hygiene products segment may result in losses of expected gain, as this segment is to unlock its high upside potential. | <p>STG's development strategy suggests that current competitive advantages and growth of market (sales) will lessen the dependency on external financial resources and will support the company's position on the existing markets.</p> <p>In a case of unfavorable market environment STG will be able to maintain the current capacity utilization and hedge against foreign rivals by increasing the production of base paper.</p> <p>In a case of urgent necessity, STG can successfully divest its assets to foreign players, as the company's business is vertically integrated, it has high-quality production facilities, and streamlined distribution.</p> |

Valuation

While performing STG's valuation, we employed the combination of the income and comparable approaches. The income approach is based on the detailed modeling of the manufacturing process and the company's financials including its planned capex and capacity expansion. For the purpose of the income approach, two DCF models, as well as the EVA and EBO valuation methods were used.

Our forecast of operating, investment, and financial activities development is built upon the monthly-based modeling, while our financial forecasts are calculated on a quarterly basis.

The forecast horizon is defined as the period of 2011-2020. By the end of the forecast period, STG's development program should be implemented, and the company will enter the cycle of sustainable growth.

Financials

Balance sheet, mn RUB

| | 2007 | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|---|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Current assets | 514 | 309 | 339 | 594 | 1 085 | 621 | 653 | 943 | 1 089 | 1 762 | 2 511 | 3 131 | 3 755 | 4 388 |
| Cash and cash equivalents | 401 | 18 | 39 | 189 | 666 | 95 | 120 | 155 | 229 | 828 | 1 542 | 2 137 | 2 744 | 3 365 |
| Accounts receivable | 43 | 107 | 113 | 185 | 176 | 207 | 228 | 334 | 368 | 399 | 415 | 425 | 432 | 438 |
| Inventories | 69 | 181 | 186 | 216 | 235 | 277 | 305 | 446 | 492 | 534 | 554 | 569 | 578 | 586 |
| VAT | 1 | 3 | 1 | 4 | 7 | 42 | - | 8 | - | - | - | - | - | - |
| Other operating assets | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Non-operating assets | 1 610 | 1 827 | 1 830 | 2 043 | 2 233 | 3 219 | 3 786 | 3 691 | 3 565 | 3 403 | 3 246 | 3 330 | 3 385 | 3 428 |
| PPE and intangible assets (exc. goodwill) | 1 589 | 1 789 | 1 787 | 2 029 | 2 219 | 3 202 | 3 767 | 3 663 | 3 534 | 3 369 | 3 212 | 3 294 | 3 348 | 3 391 |
| Goodwill | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Other assets | 21 | 38 | 43 | 14 | 15 | 17 | 19 | 28 | 31 | 34 | 35 | 36 | 36 | 37 |
| Total assets | 2 125 | 2 136 | 2 168 | 2 637 | 3 318 | 3 840 | 4 439 | 4 634 | 4 654 | 5 164 | 5 757 | 6 461 | 7 139 | 7 816 |
| Short-term liabilities | 568 | 431 | 448 | 308 | 248 | 601 | 1 151 | 991 | 597 | 656 | 642 | 669 | 688 | 708 |
| Short-term interest-bearing liabilities | 131 | 255 | 198 | 54 | - | 302 | 817 | 494 | 44 | 44 | - | - | - | - |
| Current portion of lease liabilities | 1 | 9 | 27 | 31 | - | - | - | - | - | - | - | - | - | - |
| Interest-free liabilities | 435 | 168 | 223 | 223 | 248 | 299 | 334 | 498 | 553 | 612 | 642 | 669 | 688 | 708 |
| Long-term liabilities | 958 | 1 039 | 1 044 | 1 242 | 1 258 | 1 241 | 1 020 | 899 | 737 | 595 | 560 | 572 | 579 | 586 |
| Long-term interest-bearing liabilities | 759 | 848 | 830 | 1 050 | 1 050 | 999 | 765 | 526 | 325 | 148 | 95 | 95 | 95 | 95 |
| Capital lease liabilities | 4 | 18 | 32 | 11 | 11 | 11 | - | - | - | - | - | - | - | - |
| Interest-free liabilities | 195 | 173 | 182 | 181 | 197 | 232 | 256 | 374 | 412 | 447 | 464 | 476 | 484 | 490 |
| Share capital | 599 | 666 | 677 | 1 087 | 1 808 | 1 988 | 2 248 | 2 709 | 3 266 | 3 837 | 4 455 | 5 094 | 5 720 | 6 346 |
| Shareholder's equity | 45 | 113 | 113 | 113 | 161 | 161 | 161 | 161 | 161 | 161 | 161 | 161 | 161 | 161 |
| Treasury stock | - | - | - | - | - | - | - | - | - | - | - | - | - | - |
| Additional paid-in capital | - | - | - | - | 552 | 552 | 552 | 552 | 552 | 552 | 552 | 552 | 552 | 552 |
| Retained earnings and reserves | 554 | 554 | 564 | 975 | 1 096 | 1 275 | 1 536 | 1 996 | 2 553 | 3 124 | 3 743 | 4 381 | 5 008 | 5 633 |
| Total liabilities | 2 125 | 2 143 | 2 175 | 2 637 | 3 318 | 3 840 | 4 439 | 4 634 | 4 654 | 5 164 | 5 757 | 6 461 | 7 139 | 7 816 |

Profit and loss statements, mn RUB

| | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|--------------------------------|-------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Sales | 625 | 1 235 | 1 743 | 2 023 | 2 386 | 2 645 | 3 866 | 4 259 | 4 625 | 4 802 | 4 926 | 5 007 | 5 072 |
| Cost of products sold | (541) | (899) | (1 269) | (1 484) | (1 742) | (1 879) | (2 744) | (2 991) | (3 200) | (3 293) | (3 367) | (3 451) | (3 504) |
| Gross profit | 84 | 336 | 474 | 539 | 644 | 766 | 1 122 | 1 269 | 1 425 | 1 509 | 1 559 | 1 557 | 1 567 |
| G&A and distribution costs | (101) | (155) | (172) | (199) | (235) | (261) | (381) | (420) | (456) | (473) | (485) | (493) | (500) |
| EBIT | (6) | 179 | 301 | 340 | 409 | 506 | 742 | 850 | 970 | 1 036 | 1 074 | 1 064 | 1 068 |
| EBITDA (OIBDA) | 47 | 234 | 405 | 438 | 532 | 634 | 917 | 1 019 | 1 135 | 1 194 | 1 232 | 1 224 | 1 231 |
| Net interest income (expense) | (33) | (164) | (169) | (181) | (175) | (152) | (143) | (125) | (111) | (98) | (98) | (100) | (101) |
| Non-operating gains and losses | (6) | 1 | 0 | (2) | (2) | (3) | (4) | (4) | (4) | (4) | (5) | (5) | (5) |
| EBT | (45) | 16 | 132 | 157 | 232 | 351 | 595 | 720 | 855 | 934 | 971 | 960 | 963 |
| Income tax payout | 37 | (5) | (29) | (32) | (47) | (70) | (119) | (144) | (171) | (187) | (194) | (192) | (193) |
| Minority interest | - | 0 | (3) | (4) | (6) | (9) | (16) | (19) | (23) | (25) | (26) | (25) | (25) |
| EAT | (8) | 11 | 100 | 121 | 179 | 272 | 460 | 557 | 661 | 723 | 752 | 742 | 745 |

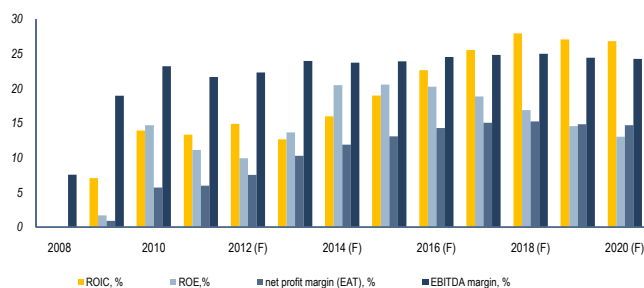
Source: company's data, Estimation: ALOR Invest

Financial position and efficiency ratios

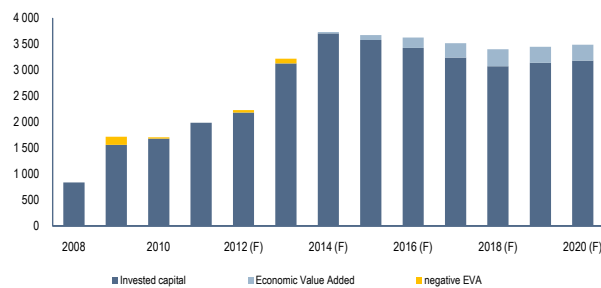
Economic profitability analysis

| | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|------------------------------|----------|------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| ROIC analysis: | | | | | | | | | | | | | |
| EBITDA margin, % | 7,6 | 19,0 | 23,2 | 21,7 | 22,3 | 24,0 | 23,7 | 23,9 | 24,5 | 24,9 | 25,0 | 24,4 | 24,3 |
| amortization burden | (0,14) | 0,77 | 0,74 | 0,78 | 0,77 | 0,80 | 0,81 | 0,83 | 0,85 | 0,87 | 0,87 | 0,87 | 0,87 |
| effective tax rate, % | - | 31,2 | 21,9 | 20,4 | 20,1 | 20,0 | 20,0 | 20,0 | 20,0 | 20,0 | 20,0 | 20,0 | 20,0 |
| total assets turnover | 0,29 | 0,58 | 0,80 | 0,77 | 0,72 | 0,69 | 0,87 | 0,92 | 0,99 | 0,93 | 0,86 | 0,77 | 0,71 |
| invested capital multiplier | 1,99 | 1,23 | 1,29 | 1,30 | 1,51 | 1,20 | 1,20 | 1,29 | 1,36 | 1,59 | 1,87 | 2,06 | 2,24 |
| ROIC, % | - | 7,1 | 13,9 | 13,3 | 14,9 | 12,7 | 16,0 | 19,0 | 22,6 | 25,6 | 28,0 | 27,1 | 26,8 |
| Du Pont ROE analysis: | | | | | | | | | | | | | |
| net profit margin (EAT), % | - | 0,9 | 5,7 | 6,0 | 7,5 | 10,3 | 11,9 | 13,1 | 14,3 | 15,1 | 15,3 | 14,8 | 14,7 |
| EBIT margin, % | - | 14,5 | 17,3 | 16,8 | 17,1 | 19,1 | 19,2 | 19,9 | 21,0 | 21,6 | 21,8 | 21,2 | 21,1 |
| Non-operating G&L multiplier | 1,93 | 1,00 | 1,00 | 0,99 | 0,99 | 0,99 | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 |
| financial (interest) burden | 3,62 | 0,09 | 0,44 | 0,46 | 0,57 | 0,70 | 0,81 | 0,85 | 0,89 | 0,91 | 0,91 | 0,91 | 0,91 |
| minority interest burden | 1,00 | 1,04 | 0,97 | 0,97 | 0,97 | 0,97 | 0,97 | 0,97 | 0,97 | 0,97 | 0,97 | 0,97 | 0,97 |
| tax burden | 0,17 | 0,71 | 0,75 | 0,77 | 0,77 | 0,77 | 0,77 | 0,77 | 0,77 | 0,77 | 0,77 | 0,77 | 0,77 |
| total assets turnover | 0,29 | 0,58 | 0,80 | 0,77 | 0,72 | 0,69 | 0,87 | 0,92 | 0,99 | 0,93 | 0,86 | 0,77 | 0,71 |
| equity multiplier | 3,55 | 3,22 | 3,21 | 2,43 | 1,83 | 1,93 | 1,97 | 1,71 | 1,43 | 1,35 | 1,29 | 1,27 | 1,25 |
| ROE, % | - | 1,7 | 14,7 | 11,1 | 9,9 | 13,7 | 20,5 | 20,6 | 20,3 | 18,8 | 16,9 | 14,6 | 13,0 |
| ROA, % | - | 0,5 | 4,6 | 4,6 | 5,4 | 7,1 | 10,4 | 12,0 | 14,2 | 14,0 | 13,1 | 11,5 | 10,4 |

Profitability dynamics, %



Business value dynamics, mn USD



Financial standing analysis

| | 2007 | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|--|------|-------|-------|------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| Financial leverage characteristics: | | | | | | | | | | | | | | |
| Financial leverage | 1,49 | 1,65 | 1,52 | 1,02 | 0,58 | 0,65 | 0,70 | 0,38 | 0,11 | 0,05 | 0,02 | 0,02 | 0,02 | 0,02 |
| Net interest-bearing debt / EBITDA | - | - | 4,22 | 2,26 | 0,88 | 2,27 | 2,31 | 0,94 | 0,14 | - | - | - | - | - |
| Net interest-bearing debt / sales | - | - | 0,80 | 0,53 | 0,19 | 0,51 | 0,55 | 0,22 | 0,03 | - | - | - | - | - |
| Net interest-bearing debt / assets | 0,23 | 0,51 | 0,45 | 0,35 | 0,12 | 0,31 | 0,33 | 0,19 | 0,03 | - | - | - | - | - |
| Net interest-bearing SR debt / EAT | - | - | 14,06 | - | - | 1,15 | 2,57 | 0,74 | - | - | - | - | - | - |
| Net interest-bearing SR debt / assets | - | 0,11 | 0,07 | - | - | 0,05 | 0,16 | 0,07 | - | - | - | - | - | - |
| Interest payments / EBITDA | - | 0,39 | 0,58 | 0,31 | 0,28 | 0,23 | 0,17 | 0,09 | 0,06 | 0,03 | 0,02 | 0,02 | 0,02 | 0,02 |
| Company's liquidity: | | | | | | | | | | | | | | |
| current ratio (>2) | 0,91 | 0,72 | 0,76 | 1,93 | 4,38 | 1,03 | 0,57 | 0,95 | 1,82 | 2,69 | 3,91 | 4,68 | 5,46 | 6,20 |
| quick ratio (>1) | 0,78 | 0,29 | 0,34 | 1,21 | 3,40 | 0,50 | 0,30 | 0,49 | 1,00 | 1,87 | 3,05 | 3,83 | 4,62 | 5,37 |
| absolute liquidity ratio (>0,2) | 0,71 | 0,04 | 0,09 | 0,61 | 2,69 | 0,16 | 0,10 | 0,16 | 0,38 | 1,26 | 2,40 | 3,19 | 3,99 | 4,75 |
| Turnover estimates of (days): | | | | | | | | | | | | | | |
| accounts receivable | - | 63 | 33 | 39 | 32 | 32 | 32 | 32 | 32 | 32 | 32 | 32 | 32 | 32 |
| interest free liabilities | - | 199 | 120 | 85 | 80 | 81 | 81 | 82 | 83 | 84 | 84 | 85 | 85 | 86 |
| inventories | - | 106 | 55 | 45 | 42 | 42 | 42 | 42 | 42 | 42 | 42 | 42 | 42 | 42 |
| non-operating assets | - | 1 067 | 541 | 428 | 403 | 493 | 522 | 348 | 306 | 269 | 247 | 247 | 247 | 247 |
| net current assets | - | 83 | 34 | 78 | 151 | 49 | 44 | 42 | 46 | 91 | 142 | 182 | 224 | 265 |

Balance sheet structure analysis, %

| | 2007 | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|---|-------|-------|-------|-------|----------|----------|----------|----------|----------|----------|----------|----------|----------|----------|
| Current assets | | | | | | | | | | | | | | |
| Cash and cash equivalents | 24,2 | 14,5 | 15,6 | 22,5 | 32,7 | 16,2 | 14,7 | 20,4 | 23,4 | 34,1 | 43,6 | 48,5 | 52,6 | 56,1 |
| Accounts receivable | 18,9 | 0,8 | 1,8 | 7,2 | 20,1 | 2,5 | 2,7 | 3,3 | 4,9 | 16,0 | 26,8 | 33,1 | 38,4 | 43,0 |
| Inventories | 2,0 | 5,0 | 5,2 | 7,0 | 5,3 | 5,4 | 5,1 | 7,2 | 7,9 | 7,7 | 7,2 | 6,6 | 6,1 | 5,6 |
| Other operating assets | 3,3 | 8,5 | 8,6 | 8,2 | 7,1 | 7,2 | 6,9 | 9,6 | 10,6 | 10,3 | 9,6 | 8,8 | 8,1 | 7,5 |
| Non-operating assets | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 |
| PPE and intangible assets (exc. goodwill) | 75,8 | 85,5 | 84,4 | 77,5 | 67,3 | 83,8 | 85,3 | 79,6 | 76,6 | 65,9 | 56,4 | 51,5 | 47,4 | 43,9 |
| Other assets | 74,8 | 83,8 | 82,4 | 76,9 | 66,9 | 83,4 | 84,9 | 79,0 | 75,9 | 65,2 | 55,8 | 51,0 | 46,9 | 43,4 |
| Total assets | 1,0 | 1,8 | 2,0 | 0,5 | 0,4 | 0,5 | 0,4 | 0,6 | 0,7 | 0,6 | 0,6 | 0,6 | 0,5 | 0,5 |
| Total liabilities | | | | | | | | | | | | | | |
| Short-term interest-bearing liabilities | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 |
| Long-term interest-bearing liabilities | 6,2 | 11,9 | 9,1 | 2,1 | 0,0 | 7,9 | 18,4 | 10,7 | 1,0 | 0,9 | 0,0 | 0,0 | 0,0 | 0,0 |
| Interest-free liabilities | 35,7 | 39,5 | 38,1 | 39,8 | 31,6 | 26,0 | 17,2 | 11,3 | 7,0 | 2,9 | 1,7 | 1,5 | 1,3 | 1,2 |
| Minority interest | 29,6 | 15,9 | 18,6 | 15,3 | 13,4 | 13,8 | 13,3 | 18,8 | 20,7 | 20,5 | 19,2 | 17,7 | 16,4 | 15,3 |
| Share capital | 0,0 | 0,3 | 0,3 | (0,0) | 0,1 | 0,3 | 0,4 | 0,7 | 1,2 | 1,5 | 1,7 | 2,0 | 2,1 | 2,3 |
| Total liabilities | 28,2 | 31,1 | 31,1 | 41,2 | 54,5 | 51,8 | 50,6 | 58,5 | 70,2 | 74,3 | 77,4 | 78,8 | 80,1 | 81,2 |

Source: company's data, Estimation: ALOR Invest

Calculation of share capital fair value, mn RUB

| | EV '11 | TV | Cagr, % | Net debt' 11 | SV '11 | Target price ord. | Target price pref. | weight |
|---|--------|-------|---------|--------------|--------------|-------------------|--------------------|-------------|
| Income approach | | | | | | | | |
| 1. Unified object estimation concept (SV calculation through EV) | | | | | | | | |
| Classical DCF (through FCFE calculation) | 3 194 | 1 303 | 3,0 | 395 | 2 799 | 17,42 | - | 0,20 |
| EVA method (through calculation of economic profit) | 3 194 | 480 | 3,0 | 395 | 2 799 | 17,42 | - | 0,20 |
| 2. Direct calculation of share capital value (SV) | | | | | | | | |
| DCF (through FCFE calculation) | - | 1 022 | 3,0 | - | 2 495 | 15,53 | - | 0,20 |
| EBO method (through calculation of economic profit to shareholders) | - | 324 | 3,0 | - | 2 495 | 15,53 | - | 0,20 |
| Comparables approach | | | | | | | | |
| Valuation through multipliers | - | - | - | - | 2 789 | 17,35 | - | 0,20 |
| Weighted valuation | | | | | 2 675 | 16,65 | - | 1,00 |

Free cash flows calculation, mn RUB

| | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|---|--------------|------------|--------------|------------|--------------|--------------|------------|------------|------------|------------|------------|------------|------------|
| 1. Unified object estimation concept (EV): DCF method (FCFF) | | | | | | | | | | | | | |
| NOPAT | (6) | 123 | 235 | 271 | 327 | 405 | 593 | 680 | 776 | 829 | 860 | 851 | 855 |
| Gross operational CFF | 47 | 178 | 339 | 369 | 450 | 533 | 769 | 849 | 941 | 986 | 1 017 | 1 011 | 1 017 |
| Gross CapEx needs: | (721) | 3 | (453) | (258) | (1 128) | (642) | (45) | (19) | 20 | 11 | (225) | (204) | (192) |
| inc. PPE CapEx | (254) | (53) | (346) | (287) | (1 107) | (693) | (71) | (41) | 0 | 0 | (240) | (214) | (205) |
| net current assets change | (467) | 56 | (108) | 28 | (21) | 51 | 27 | 22 | 20 | 11 | 15 | 10 | 13 |
| Free Cash Flow to Firm | (673) | 181 | (115) | 110 | (678) | (109) | 724 | 831 | 961 | 998 | 792 | 807 | 825 |
| 2. Direct calculation of share capital value (SV): DCF method (FCFE) | | | | | | | | | | | | | |
| Operational EAT | (7) | 10 | 103 | 127 | 187 | 283 | 479 | 579 | 687 | 751 | 781 | 771 | 774 |
| Financial flows | 306 | (43) | 61 | 514 | 251 | 270 | (563) | (649) | (177) | (97) | 0 | 0 | 0 |
| Gross operational CFE | 353 | 22 | 267 | 739 | 561 | 681 | 91 | 99 | 675 | 811 | 938 | 932 | 937 |
| Gross CapEx needs: | (721) | 3 | (453) | (258) | (1 128) | (642) | (45) | (19) | 20 | 11 | (225) | (204) | (192) |
| inc. PPE CapEx | (254) | (53) | (346) | (287) | (1 107) | (693) | (71) | (41) | 0 | 0 | (240) | (214) | (205) |
| net current assets change | (467) | 56 | (108) | 28 | (21) | 51 | 27 | 22 | 20 | 11 | 15 | 10 | 13 |
| Free Cash Flow to Equity | (367) | 25 | (187) | 480 | (567) | 39 | 47 | 81 | 695 | 822 | 713 | 728 | 744 |

Economic value added calculation, mn RUB

| | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|--|--------------|--------------|-------------|-------------|-------------|-------------|-----------|------------|------------|------------|------------|------------|------------|
| 1. Unified object estimation concept (EV): EVA method | | | | | | | | | | | | | |
| EVA spread (ROIC-WACC), % | (21,7) | (10,6) | (0,4) | (2,2) | (0,4) | (2,0) | 0,6 | 2,7 | 5,9 | 8,5 | 10,7 | 9,8 | 9,5 |
| Invested capital | 1 746 | 1 688 | 2 031 | 2 192 | 3 196 | 3 710 | 3 580 | 3 429 | 3 243 | 3 075 | 3 143 | 3 186 | 3 216 |
| Economic Value Added | (231) | (185) | (7) | (44) | (9) | (65) | 24 | 97 | 201 | 277 | 329 | 308 | 304 |
| 2. Direct calculation of share capital value (SV): EBO method | | | | | | | | | | | | | |
| SVA spread (ROE-ks), % | 12,1 | (25,6) | (4,4) | 61,5 | (4,1) | (4,7) | 4,0 | 5,3 | 5,2 | 7,4 | 8,8 | 7,9 | 7,6 |
| Invested capital attributable to shareholders | 617 | 602 | 885 | 1 131 | 1 885 | 2 129 | 2 561 | 3 059 | 3 051 | 2 979 | 3 047 | 3 091 | 3 121 |
| Shareholders Value Added | 21 | (158) | (26) | 544 | (47) | (89) | 85 | 136 | 160 | 225 | 261 | 240 | 235 |

Weighted average cost of capital estimation (WACC)

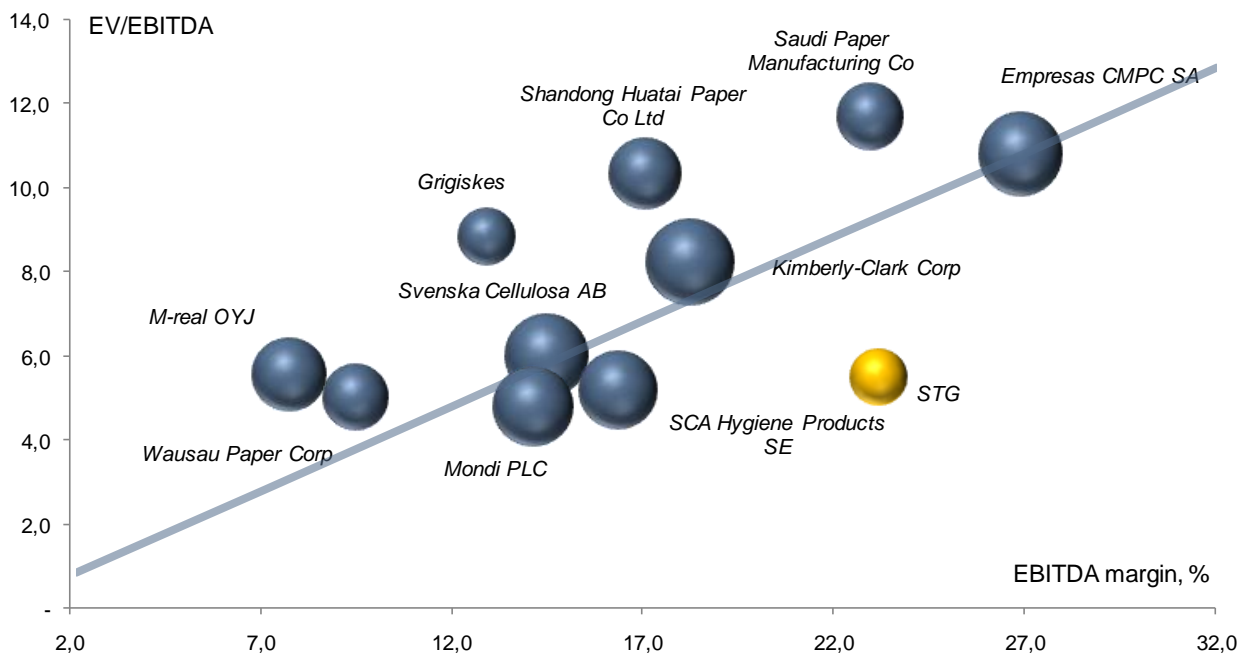
| | 2007 | 2008 | 2009 | 2010 | 2011 (F) | 2012 (F) | 2013 (F) | 2014 (F) | 2015 (F) | 2016 (F) | 2017 (F) | 2018 (F) | 2019 (F) | 2020 (F) |
|--|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Risk-free yield rate for RF | 5,54 | 7,41 | 8,26 | 5,60 | 5,09 | 5,06 | 5,09 | 5,13 | 5,20 | 5,20 | 5,21 | 5,42 | 5,42 | 5,42 |
| Average yield for developed markets in 5 years, % | 4,39 | 4,32 | 4,12 | 3,90 | 3,86 | 3,96 | 4,09 | 4,13 | 4,20 | 4,20 | 4,21 | 4,42 | 4,42 | 4,42 |
| RF default spread, % | 1,15 | 3,08 | 4,14 | 1,69 | 1,23 | 1,10 | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 | 1,00 |
| Shareholders' required yield rate | 21,49 | 23,36 | 27,21 | 21,52 | 20,64 | 20,67 | 19,74 | 18,49 | 17,31 | 17,25 | 17,24 | 17,44 | 17,44 | 17,44 |
| Expected market return, % | 5,00 | 5,00 | 7,00 | 5,00 | 5,00 | 5,00 | 5,00 | 5,00 | 5,00 | 5,00 | 5,00 | 5,00 | 5,00 | 5,00 |
| βL coefficient (according to financial leverage) | 1,50 | 1,50 | 1,50 | 1,50 | 1,42 | 1,43 | 1,44 | 1,38 | 1,33 | 1,32 | 1,32 | 1,31 | 1,31 | 1,31 |
| Premium for the quality of corporate governance, % | 8,45 | 8,45 | 8,45 | 8,45 | 8,45 | 8,45 | 7,45 | 6,45 | 5,45 | 5,45 | 5,45 | 5,45 | 5,45 | 5,45 |
| Creditors' required yield rate | 8,99 | 19,71 | 16,88 | 9,68 | 8,43 | 8,95 | 9,33 | 8,64 | 8,52 | 8,44 | 8,41 | 8,60 | 8,58 | 8,57 |
| Premium for credit risk, % | 3,45 | 12,30 | 8,62 | 4,08 | 3,33 | 3,89 | 4,24 | 3,51 | 3,32 | 3,24 | 3,19 | 3,17 | 3,16 | 3,15 |
| Capital's structure: | | | | | | | | | | | | | | |
| Share of source «shareholders capital» | 40,1 | 37,4 | 38,6 | 48,7 | 63,1 | 60,4 | 58,9 | 72,9 | 90,0 | 95,3 | 98,0 | 98,2 | 98,4 | 98,6 |
| Share of source «debt finance» | 59,9 | 62,6 | 61,4 | 51,3 | 36,9 | 39,6 | 41,1 | 27,1 | 10,0 | 4,7 | 2,0 | 1,8 | 1,6 | 1,4 |
| WACC, % | 14,00 | 21,07 | 17,64 | 14,36 | 15,50 | 15,31 | 14,70 | 15,36 | 16,26 | 16,76 | 17,02 | 17,26 | 17,27 | 17,29 |

Source: company's data, Estimation: ALOR Invest

Peers' multiples

| | Country (registration) | Current capitalization, mn USD | Enterprise value, mn USD | Market multiples | | | | | | | | | | Financial coefficients | | | | | |
|---|------------------------|--------------------------------|--------------------------|------------------|------|-----------|------|-------|-------|------|------|-------|------|------------------------|---------|------------------|---------------------|------------------|-----------------|
| | | | | EV/IS | | EV/EBITDA | | P/E | | P/BV | | EV/IC | | ROE, % | ROIC, % | EBITDA margin, % | Fin. leverage (D/S) | Net Debt/ EBITDA | Net Debt/ Sales |
| | | | | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 | | | | | | |
| Developed markets | | | | | | | | | | | | | | | | | | | |
| Mercer International Inc | CANADA | 645 | 1627 | 1,36 | 1,58 | 5,48 | 5,53 | 5,63 | 10,41 | 2,26 | - | 1,28 | - | 48,03 | 17,04 | 24,87 | 3,44 | 3,31 | 0,82 |
| M-real OYJ | FINLAND | 1 452 | 2 711 | 0,8 | 0,7 | 10,1 | 5,5 | 39,1 | 9,0 | 1,1 | 0,9 | 1,0 | 1,0 | 2,9 | 1,1 | 7,8 | 0,9 | 4,7 | 0,4 |
| SCA Hygiene Products SE | GERMANY | 3 548 | 4 278 | 0,8 | - | 5,2 | - | 14,6 | - | 1,6 | - | 1,5 | - | 13,3 | 8,1 | 16,3 | 0,3 | 0,9 | 0,1 |
| Svenska Cellulosa AB | SWEDEN | 11 578 | 16 729 | 1,1 | 0,9 | 7,6 | 6,0 | 15,0 | 10,0 | 1,1 | 1,0 | 1,1 | 1,0 | 8,3 | 6,4 | 14,5 | 0,5 | 2,3 | 0,3 |
| Mondi PLC | BRITAIN | 5 000 | 6 823 | 0,8 | 0,7 | 5,8 | 4,8 | 16,8 | 11,2 | 1,2 | 1,1 | 1,1 | 1,1 | 8,7 | 6,6 | 14,2 | 0,4 | 1,6 | 0,2 |
| Kimberly-Clark Corp | UNITED STATES | 26 632 | 31 726 | 1,6 | 1,5 | 8,8 | 8,2 | 14,5 | 13,4 | 3,9 | 5,5 | 2,7 | 2,9 | 32,6 | 15,9 | 18,3 | 0,8 | 1,4 | 0,3 |
| Orchids Paper Products Co | UNITED STATES | 90 | 108 | 1,2 | 1,1 | 7,2 | 6,3 | 15,2 | 14,8 | 1,3 | - | 1,2 | - | 8,9 | 7,5 | 16,1 | 0,3 | 1,2 | 0,2 |
| Wausau Paper Corp | UNITED STATES | 389 | 514 | 0,5 | 0,5 | 5,1 | 5,0 | 10,5 | 15,0 | 1,5 | 1,3 | 1,3 | 1,5 | 15,2 | 11,2 | 9,5 | 0,5 | 1,2 | 0,1 |
| Developed markets weighted average | | | | 1,2 | 1,1 | 7,6 | 6,7 | 14,8 | 12,1 | 1,7 | 2,0 | 1,5 | 1,6 | 12,2 | 7,7 | 15,6 | 0,6 | 1,7 | 0,3 |
| Developed markets median | | | | 1,1 | 0,9 | 7,2 | 5,5 | 15,0 | 12,3 | 1,3 | 1,1 | 1,2 | 1,1 | 8,9 | 7,5 | 14,5 | 0,5 | 1,6 | 0,3 |
| Developing markets | | | | | | | | | | | | | | | | | | | |
| Empresas CMPC SA | CHILE | 11 181 | 13 434 | 3,2 | 2,8 | 11,8 | 10,8 | 17,5 | 17,3 | 1,4 | 1,4 | 1,3 | 1,3 | 8,6 | 7,2 | 26,9 | 0,3 | 2,0 | 0,5 |
| China Paper Holdings Ltd | CHINA | 89 | 29 | 0,2 | - | 0,8 | - | 4,6 | - | 0,4 | - | 0,2 | - | 11,1 | 12,7 | 22,3 | - | - | - |
| Shandong Huatai Paper Co Ltd | CHINA | 973 | 1 499 | 1,8 | - | 10,3 | - | 6,1 | - | 1,0 | - | 1,0 | - | 22,4 | 3,8 | 17,1 | 0,6 | 3,6 | 0,6 |
| African Champion Industries Ltd | GHANA | 2 | 2 | 0,7 | - | - | - | - | - | 0,4 | - | 0,5 | - | - | - | - | 0,1 | - | 0,1 |
| Grigiskes | LITHUANIA | 72 | 109 | 1,1 | - | 8,8 | - | 24,3 | - | 2,3 | - | 1,6 | - | 10,4 | 5,3 | 12,9 | 1,2 | 3,0 | 0,4 |
| Saudi Paper Manufacturing Co | SAUDI ARABIA | 365 | 574 | 2,7 | - | 11,7 | - | 11,2 | - | 2,3 | - | 1,6 | - | 22,2 | - | 23,0 | 1,3 | 4,3 | 1,0 |
| Manufacturas de Papel CA | VENEZUELA | 103 | 111 | 0,3 | - | 1,0 | - | 1,4 | - | 0,5 | - | 0,5 | - | 40,8 | 39,6 | 27,1 | 0,0 | 0,1 | 0,0 |
| Vien Dong Investment Development Tradit | VIETNAM | 11 | 32 | 0,68 | - | - | - | 13,88 | - | 0,71 | - | 0,88 | - | 5,14 | 8,29 | - | 1,45 | - | 0,45 |
| Emerging markets weighted average | | | | 2,6 | 2,8 | 10,6 | 10,8 | 13,7 | 17,1 | 1,4 | 1,4 | 1,3 | 1,3 | 9,4 | 6,8 | 25,5 | 0,3 | 1,7 | 0,4 |
| Emerging markets median | | | | 1,5 | 2,8 | 10,3 | 10,8 | 11,2 | 13,8 | 1,0 | 1,4 | 1,2 | 1,3 | 15,6 | 5,3 | 19,7 | 0,9 | 3,6 | 0,6 |
| Russia | | | | | | | | | | | | | | | | | | | |
| STG | RF | 2 000 | 2 395 | 1,4 | 1,2 | 5,9 | 5,5 | 20,1 | 16,5 | 1,8 | 1,1 | 1,6 | 1,1 | - | 15,34 | 23,20 | 0,36 | - | - |
| Russia weithed average | | | | 1,4 | 1,2 | 5,9 | 5,5 | 20,1 | 16,5 | 1,8 | 1,1 | 1,6 | 1,1 | - | 15,3 | 23,2 | 0,4 | - | - |
| Russia median | | | | 1,4 | 1,2 | 5,9 | 5,5 | 20,1 | 16,5 | 1,8 | 1,1 | 1,6 | 1,1 | - | 15,3 | 23,2 | 0,4 | - | - |

STG demonstrates the highest growth rates of the profitability (specifically, on the EBITDA margin side) relative to its peer group. On the contrary, based on the average of the IPO range, STG's multiples are lower than those of the comparable companies. Our results directly indicate that the stock offers an upside to the IPO price level, which should be unlocked by the end of 2011.



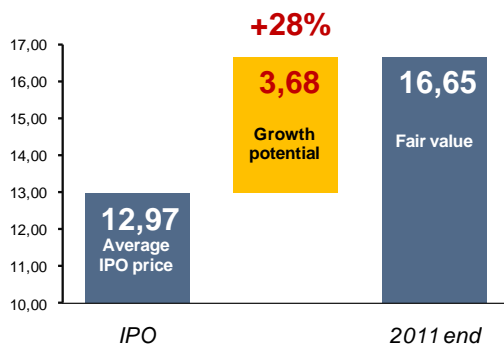
Fair value calculation: comparable approach, RUB mn

| | Capitalization, mn USD | | | EV/S | | EV/EBITDA | | P/E | | P/BV | | EV/IC | |
|----------------------------|-------------------------|----------------|-----------------|------|------------|------------|------------|------------|-------------|-------------|------------|------------|------------|
| | Current | Fair (current) | Fair (forecast) | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 | 2010 | 2011 |
| | Target multiples | | | | 1,8 | 1,8 | 8,8 | 8,3 | 14,4 | 14,1 | 1,6 | 1,8 | 1,4 |
| Weight (current multiples) | | | | 20% | | 50% | | 30% | | - | | - | |
| Weight (forward multiples) | | | | | 20% | 50% | | 30% | | - | | - | |
| STG | 2 000 | 2549 | 2789 | 2675 | 3260 | 3170 | 3251 | 1431 | 1704 | 1721 | 3185 | 1662 | 2874 |

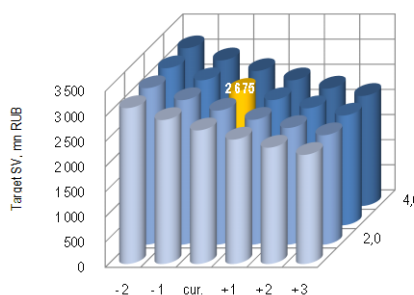
Based on the valuation methods, we derived STG’s fair value at RUB2.68bn (\$89.18mn), or RUB16.65 (\$0.55)/share, as of the end of 2011E (post-money valuation). This value is weighted average. The weight of the income approach of the total valuation is 80%, while the weight of the comparative approach is 20%.

Consequently, the participation in STG’s IPO at an offering price within the range of RUB11.4-14.5/share allows the investors to buy the stock which offers an upside potential of 15%-45% by the year-end (depending on an IPO price).

Fair value breakdown, RUB



Sensitivity analysis, mn RUB



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