



June 30, 2014

Eurasia | Agricultural Chemicals

Uralkali (URKA LI)



Tim Murray

+61 411 046 476

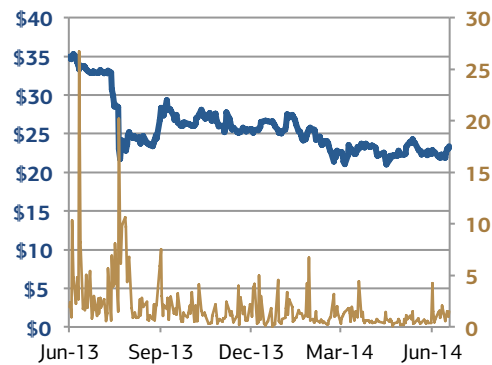
tim@jcapitalresearch.com

Susannah Kroeber

+61 413 128 212

suzhen@jcapitalresearch.com

Uralkali Group (URKA LI) one-year share price in USD (blue) and volume (gold, in mln shares)



Source: Bloomberg, June 30, 2014

Risk trumps reward

+ Not enough to stay positive

Uralkali's exports of potash in Asia, particularly China, so far in 2014 have been impressive, but the Russian takeover of Crimea has harmed the stock performance of most Russian companies this year. Given that more sanctions are threatened this month, we do not expect the overhang to clear.

+ Closing coverage

While we believe that the current share price for URKA undervalues its likely market-share increase in 2014-15, political risk could keep the price depressed until after the potash market potentially becomes oversupplied in 2015-16.

Uralkali Group (URKA LI)

Price	USD 23.35
Rating	BUY
Price Target	USD 32.02/GDR
Difference	37%
Market Cap	USD 13.71 bln
Simple Moving Avg.	1.35 mln
P/E	20.79x

Source: Bloomberg, June 30, 2014

Geographic risk trumps reward

In tracking exports of Russian potash to China so far this year, we've seen URKA take share from competitors and solidify its position as the majority supplier of potash to the Chinese market. Sanctions have had little impact on URKA's business that we can measure, and the company successfully secured a USD 500 mln loan from European banks in June¹ to help expand its low-cost capacity advantage. Despite these positives, URKA experienced a 13% decline in the price of its London-listed shares 2014 YTD, and, so far, all positive news have had little effect.

The stock is trading at a discount similar to its Russian-domiciled peers, due to geographic uncertainty relating to the 2014 Q1 crisis in Ukraine and Crimea. While some companies have recovered since the Crimean referendum resolved some of the uncertainty, most companies that have recovered have majority non-Russian shareholders (YNDX US, for example, has almost entirely recovered to its January 2014 price).

URKA's ownership and managerial changes now make it more aligned with Putin's interests ahead of its own financial interests.

URKA does not fit this description. After we initiated on URKA, an ownership change occurred that moved majority ownership of the company to Russian citizens, most of whom are strongly aligned with President Vladimir Putin, and earlier this year, management of the company shifted in the same direction.² This has made the company more likely to act in alignment with Putin's interests ahead of the company's own financial interests. We see two recent examples of this—first, increased discounted sales to Russian fertilizer companies, like related party Uralchem, and second, the appointment of members of Putin's inner circle to management and the executive board.

We therefore believe that the strong position of URKA in the global potash market as the low-cost, high-volume producer will likely be overshadowed long enough for these advantages to be effectively eliminated—the build-out of new capacity in 2015-2017 will likely lead to an oversupplied market, causing potash prices to fall, and bringing with them declines in major potash producers' margins.

¹ <http://www.tradefinancemagazine.com/Article/3351229/Regions/22998/Exclusive-Uralkali-loan-to-sign-in-two-weeks.html>

² <http://itar-tass.com/ekonomika/1035904>

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