



Best dividend ideas in the Russian equities

Russian equities are among best in terms of dividend yields. The average dividend yield of the Russian companies was 6.9% as of 2018, according to Bloomberg and 8% on our estimates. As of 2019, we expect it at 8%, on conservative basis, and at 9-10%, on a more optimistic stance. That is well above 3% average yield in emerging markets and 2.4% in developed markets, including 1.8% in the U.S. and 3.6% in Europe. That is also above than the average OFZ yield standing at 6% now.

We studied around 30 best local dividend stories and allocated them into three groups: (1) stocks with high yields and low risks and/or good fundamental stories, (2) stocks having good yields but exposed to high risks on global volatility and (3) stocks exposed to high risks not only on global volatility but also on internal corporate decisions.

Our top picks in terms of dividend plays are Veon and MTS, telecom operators with the most resilience to global markets volatility. Also, we favour Moscow Exchange, Globaltrans and Detsky Mir. In addition to attractive fundamentals of these companies, the shareholders of the latter two are seeking for good dividends.

In the second group we highlight banks and metallurgical companies. These names are more exposed to global risks vs the first group, that largely offsets high dividend yield factors.

We also highlight Etalon and LSR in the third group - the companies with high incentives to pay high dividends but lag due to real estate market vulnerabilities. In addition, some stocks may outperform against our conservative estimate, primarily Lukoil, Alrosa and Evraz.

We would also like to draw your attention to those issuers, which may adopt a new dividend policy through 2Q20, therefore bolstering their stocks: Novatek, Rosseti, PIK, Enel, TGC-1 and other Gazpromenergoholding subsidiaries.

Importantly, as a part of our analysis we have used average daily dividend yield for the period of February – August 2020 – parameter which incorporates particular dividend cut-off dates. Based on that, we prefer stocks of Veon and Globaltrans with cut-off dates in March-April (vs June-July for most others).

Company	Feb-Aug'20E dividend, rub/\$ per share	Period	Weighted average current daily dividend yield	Dividend cut-off dates (dd.mm.yy)	FY20E annual dividend, ITI Capital estimates	Annual dividend yield, FY19E
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Favorites: high yields/ low risks

Veon	\$0.16	2H19	0.1531%	20/03/20	\$0.29	11.0%
MTS excluding special div	19.32	2H19	0.0501%	09/07/20	28	8.6%
MTS including special div					41.3	12.6%
Globaltrans	\$0.74	2H19	0.1473%	18/04/20	\$1.5	17.1%
Moscow exchange	7.8	2019	0.0904%	14/05/20	7.8	7.1%
Detsky Mir	4	4Q19E	0.0401%	27/05/20	9.10	7.8%

High yields/ high global risks

MMK	3.2	4Q19E+1Q20	0.0706%	11.06.20/20.06.20	5.5	12.3%
NLMK	5.3	4Q19E+1Q20	0.0435%	06.05.20/19.06.20	16.9	11.8%
Severstal	48.2	4Q19E+1Q20	0.0607%	07.05.20/18.06.20	113.7	12.2%
Evrz	\$0				\$0.75	17.1%
Phosagro	106	4Q19E+1Q20	0.0409%	10.06.20/10.07.20	227	9.4%
Enel	0.12	2019	0.1179%	22/06/20	0.12	12.4%
Sberbank, pref	18.7	2019	0.0826%	13/06/20	18.7	8.2%
VTB, ord	0.004	2019	0.0767%	24/06/20	0.0038	8.2%
BSPB	3.01	2019	0.0556%	10/06/20	3.01	5.4%
Sberbank, ord	18.7	2019	0.0739%	13/06/20	18.7	7.3%

High yields/ high global risks + specific risks

Etalon	\$0.21	2019	0.0643%	30/08/20	\$0.21	9.9%
LSR	78	2019	0.0744%	10/07/20	78	8.8%
Alrosa	1.9	2П19	0.0180%	15/07/20	5.7	6.6%
TGK-1	0.0008	2019	0.0518%	26/06/20	0.0008	5.6%
Unipro	0.11	4Q19	0.0354%	25/06/20	0.22	7.6%
Rushydro	0.03	2019	0.0397%	09/07/20	0.03	4.7%
Gazprom	16	2019	0.0559%	18/07/20	16	6.9%
Gazprom neft	16	2H19	0.0323%	01/07/20	34.2	7.7%
Tatneft, ord	13.44	4Q19	0.0151%	05/07/20	77.9	10.0%
Tatneft, pref	13.44	4Q19	0.0154%	05/07/20	77.9	10.9%
Lukoil	193.9	2H19	0.0251%	09/07/20	397.4	6.1%

Source: Company data, ITI Capital estimates, Bloomberg

An increasing number of Russian companies have been raising dividends and therefore boosting pay-outs, as their major shareholders seek to consolidate funds that can be diverted into other projects (including State companies; Sistema's subsidiaries - MTS, Etalon, Detsky Mir; Globaltrans). Another driver for increasing dividend payments is incentive to improve share price performance, as in the case of Phosagro or metal producers. In 2019, around 10 companies approved new dividend policy, including Lukoil, Gazprom, Alrosa, Veon, NLMK, Phosagro, MMK and Rushydro.

We have analysed some thirty Russian companies, selecting those which:

1. Approved new dividend policy in 2019;
2. Paid high dividends historically with an annual yield of above 7%;
3. Pay interim dividends, especially those that are paid in the first eight months of a calendar year (i.e. within the nearest timespan), since it results in significant increase of the weighted annual dividend yield.

We took conservative approach in our analysis to project 2H19 and 1Q20 profits and/or cash flows of the companies — the base for the dividend payments.

In our analysis we have not just used final annual dividend yields, but also total dividends of the companies paid for the period of February-August 2020, adjusted for the number of days till expected cut-offs — an approach taking into account potential cash flows of an investor. The latter approach resulted in Veon and Globaltrans being among the best with the nearest cut-offs days (March-April 2020). The list of best dividend plays includes 11 companies with a double-digit dividend yield and 14 — with a yield above 8%.

We allocated stocks into three groups. *FIRST*: fundamentally attractive high dividend-payers with limited exposure to global factors (such as Veon or MTS); and industry leaders with sustainable business model (like Globaltrans and Detsky Mir) and high dividends. *SECOND*: companies with high dividends, including interim dividends, but more exposed to global factors such as commodity prices (metals producers). *THIRD*: companies with potentially high dividend yield exposed both to global factors and the risk of management's dividend payments decisions. We've also highlighted those companies that may boost dividend pay-outs in the coming months.

Our favourites come from the first group (high yields and low risks). First of all, these are telecom operators Veon and MTS with 11% and 8.6% — final annual yields. Their fundamental profile is attractive and stable, and their financial performance is less volatile amid changing global climate as compared to companies from resource sectors. We also added Globaltrans, Moscow Exchange and Detsky Mir to this group with 17.1%, 7.1% and 7.8% — annual yields, respectively. Globaltrans is a dynamically developing cargo transportation operator, one of industry leaders, that has a safety margin to protect against negative external factors and one of the highest dividends yields among Russian issuers. Exposure to the Moscow Exchange provide investors with an opportunity to benefit from the Russian stock market growth and development. We have added Detsky Mir stocks to this group because we like the company's fundamentals, as it has established itself as a strong industry player and largely benefits from the growth of the Russian online-retail market.

The second-group companies are high dividend-payers, including interim dividends, highly exposed to global factors. If global environment deteriorates, the shareholders' losses from a decline in share prices would top gains from high dividends. These are primarily metal producers (MMK, NLMK, Severstal, Evraz). Metal producers, dividend policy leaders in the Russian market, make payments quarterly. The companies seek to pay 100% of free cash flow to shareholders.

The annual dividend yield of metal producers stands at about 12% (one of the highest in Russia). We assumed a zero residual dividend on Evraz shares for 2019 due to uncertainty of its dividend policy, but expect its final annual dividend yield is at 17%. Phosagro (about 9% yield), a leading Russian fertilizer producer, that boasts yield ratios similar to those of metal companies, was also added to the group. The list also includes bank stocks (Sberbank, VTB, Bank of St. Petersburg) with a high annual dividend paid in June 2020, but without interim dividends (5-8% annual yield). Finally, we also added Enel shares to this group (12%).

The third group includes companies with potentially high dividend yield facing heightened risks specific for companies and global. These include Etalon and LSR due to the risks of the real estate sector as a whole, or Alrosa, and energy companies and Gazprom. The final annual yield of Etalon should be 10%, based on just adopted new dividend pay-out approach: least ₴12 per share per year, which is widely understood given that Sistema is seeking to cover its financial needs. Etalon financial performance is highly exposed to global and domestic factors, and the company has not fully recovered after consolidation of Leader-Invest. LSR management has also said that dividend per share will be not lower than ₴78, which implies a 9% yield. The important thing is that most companies in the group may raise dividends to an unexpected level as compared to our rather conservative forecast, including Alrosa, TGC-1, Lukoil, Gazprom and Gazprom neft.

Some Russian issuers mull changes to dividend policy in the near future. These include Enel Russia (as part of the strategy update in early 2020), Novatek (raising dividend pay-out ratio in 2Q20), Rosseti (starting from 2020 it may raise pay-out ratio to 75% of net profit under RAS), PIK (may switch to payments of dividends based on net profit and EBITDA), NorNickel (is considering linking dividends to free cash flow instead of EBITDA after 2022), TGC-1 and other Gazpromenergoholding subsidiaries (weigh switching to dividend ratio of 35% of IFRS profit).

We would also like to mention Sistema and Mechel preferred shares. Under the current dividend policy, Sistema should pay a minimum of ₺1.19 per share for the year, but recently the company hasn't been complying due to limited financial resources required to develop its projects and repay its debt. Under our baseline scenario, the dividend for 2019 rolled over from 2018 (₺0.11 per share) imply only a 0.6% current yield on Sistema shares. Thus, the return to previous dividend policy (assuming a minimum payment of ₺1.19 per share) translates into a 6.6% potential dividend yield. The management said it will get back to dividend payments deliberations by 2Q20, but our expectations are conservative given the group's limited financial resources. Mechel's preferred dividends wholly depends on 4Q19 earnings. Our estimate of Mechel's 2019 profit at 9M19 translates into a potential 17% yield, which may prove to be optimistic scenario.

Company	Ticker	Current share price (as of close 27.01.20) rub/\$ per share/GDR	Final annual dividend, rub/\$ per share/GDR, 2019E	Final annual dividend yield as of 2019E
Globaltrans	GLTR LI	\$8.6	\$1.5	17.1%
Evraz	EVR LN	\$5.7	\$0.75	13.1%
Enel	ENRU RX	1.0	0.12	12.4%
MMK	MAGN RX	44.3	5.5	12.3%
Severstal	CHMF RX	930	114	12.2%
NLMK	NLMK RX	143	16.89	11.8%
Norilsk Nickel	GMKN RX	21.1	2.402	11.4%
VEON	VEON US	\$2.6	\$0.29	11.0%
Tatneft, pref	TATNP RX	715	78	10.9%
Tatneft, ord	TATN RX	780	78	10.0%
Etalon	ETLN LI	\$2.12	\$0.21	9.9%
Phosagro	PHOR RX	2.426	227	9.4%
LSR	LSRG RX	888	78	8.8%
MTS excl special dividend	MTSS RX	327	28	8.6%
VTB, ord	VTBR RX	0.047	0.004	8.2%
Sberbank, pref	SBERP RX	229	18.7	8.2%
Detsky Mir	DSKY RX	116	9.1	7.8%
Gazpromneft	SIBN RX	444	34.2	7.7%
UNIPRO	UPRO RX	2.9	0.22	7.6%
Sberbank, ord	SBER RX	255.3	18.7	7.3%
Moscow Exchange	MOEX RX	111	7.8	7.1%
Gazprom	GAZP RX	231	16	6.9%
Alrosa	ALRS RX	87	5.75	6.6%
Lukoil	LKOH RX	6.545	397	6.1%
TGK-1	TGKA RX	0.013	0.0008	5.6%
BSPB	BSPB RX	56	3	5.4%
Rushydro	HYDR RX	0.7	0.03	4.7%

Source: Company data, ITI Capital estimates, Bloomberg

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