

MegaFon London IPO Finds Strength at Home

By [The Moscow Times](#)

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MegaFon is outpacing rivals in sales growth and upgrading infrastructure. **Y. Razumny**

MegaFon's initial public offering will give investors the chance to buy into a Russian telecom company that is outpacing its peers in a growing home market and, unlike them, shielded from tricky overseas operations and complex corporate disputes.

MegaFon, controlled by Russia's richest man, Alisher Usmanov, plans to float ordinary shares in Moscow and global depositary receipts in London within weeks.

Analysts estimate that the initial public offering of a stake of about 20 percent in the company could raise at least \$3 billion, making it the biggest in London since trader Glencore floated in May 2011.

Nordic co-owner TeliaSonera will offer a 10.5 percent stake, while MegaFon will sell 9.4 percent of treasury shares and is expected to repay debt it took on to buy a part of tycoon

Mikhail Fridman's holding.

Telecom companies are benefiting as Russia's middle class grows and disposable incomes rise, giving them the chance to boost profits by selling add-on services based on fast wireless access to the Internet.

Ownership of smartphones designed to surf the Web also remains low, promising growth in data, which should offset typically flat revenues from voice calls made by mobile-loving Russians, who own an average of 1.6 SIM cards per person, more than in most other countries.

Outpacing Rivals

MegaFon, which makes 99 percent of its revenues in Russia and is outpacing rivals in domestic sales growth, has invested aggressively in infrastructure to become a leader in 3G and is at the forefront of the rollout of fourth-generation technology.

It has also been strengthening its distribution by seeking to buy into Russia's No.1 cell phone retailer, Yevroset, half-owned by VimpelCom.

With its local focus, analysts say, MegaFon is likely to attract investors burned by exposure to VimpelCom and MTS, which have both hit trouble outside Russia.

"MegaFon does not have such risks. It gives investors a clear case. It is a well-focused story," said Konstantin Belov, a Moscow-based telecom analyst at UralSib.

Analysts at UralSib estimate that MegaFon's IPO will raise about \$3 billion based on an enterprise value, effectively the cost of taking over a company's equity and debt, of 4.8 times its forecast EBITDA for 2012. That works out to a slight discount versus rival MTS, which is valued at an EV/EBITDA ratio of five times.

London-based Nomura Securities analyst James Britton said Nomura expected a valuation of at least five times EBITDA. Other analysts were more optimistic, with some saying the market could value MegaFon 10 to 15 percent higher than MTS.

Alexander Vassiouk, a telecom specialist at Prosperity Capital Management, one of the biggest investors in Russian stocks, with about \$4 billion under management, also said he did not think there should be a discount to MTS.

"Geographically, MegaFon's business mix is less risky than MTS' because MTS has businesses in Uzbekistan, Turkmenistan and Ukraine, countries where political and currency risks are higher than in Russia," he said.

Analysts said risks attached to the lack of track record of MegaFon's new management and majority shareholder, its relatively weak position in the land-line market, and general struggles in financial markets explained why the expected premium was not greater.

"We think the business models are very comparable, and therefore the valuation of MegaFon versus MTS will boil down to the assessment of the corporate governance risk, or how the minority investor will be treated by the company and its controlling shareholder," said Tibor Bokor, a London-based analyst at ING.

MTS recently wrote off \$1.1 billion after a court in Uzbekistan revoked its license, resulting in a \$682 million quarterly net loss. It said Monday that a court had ordered the confiscation of its local unit's assets.

VimpelCom's moves to diversify away from Russia have exacerbated frictions between its two main owners, with Norway's Telenor saying the expansion distracted the group's focus from Russia, where VimpelCom lost market share to MegaFon. VimpelCom is also facing the nationalization of its Algerian business.

MegaFon's listing will follow this week's sale of a state stake in Sberbank and could compete with that of Spain's Telefonica, which wants to list between 10 and 20 percent of its German unit, O2, a financial source said last week.

Peaceful Investor

MegaFon's likely inclusion post-IPO in the MSCI Russia index, benchmarked by many emerging-market fund managers, will attract large institutional investors, said a Moscow-based trader with a Western bank.

Foreign investors often face difficulties in the oligarch-dominated Russian business world, with shareholder conflicts leading to gridlock on strategy and blockages of dividend payments, depressing stock prices.

While Usmanov owns 50 percent plus one share of MegaFon, the risk of a destructive shareholder dispute is significantly lower, said Stanislav Yudin, an analyst at Moscow brokerage Aton, as its shareholder has control, in contrast to VimpelCom.

A long-running corporate war at VimpelCom flared up in February when Telenor overtook Fridman's Altimo as the biggest shareholder. Following a court case, VimpelCom suspended dividend payments and a European listing.

"MegaFon has a controlling shareholder who is somewhat balanced by TeliaSonera, which is a very rational and quite peaceful investor. Besides, there appears to be no grounds for a conflict for now, so I would expect them to coexist peacefully and run the company in a constructive way," Vassiouk said.

High Expectations

After the \$1 billion London IPO of Internet group Mail.ru in 2010 and his early investment in Facebook, Usmanov "is not a dark horse for investors anymore but an example of a smart investor," Yudin said.

Expectations of healthy dividends, following a special payout in April, are another factor seen as spurring demand for the company's shares.

"It is a classic defensive-dividend story," Belov said. As major M&A and expansion opportunities are limited, "logic tells us MegaFon will be a strong dividend payer."

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