

RUSSIA'S FINANCIAL MARKETS IN JULY 2013

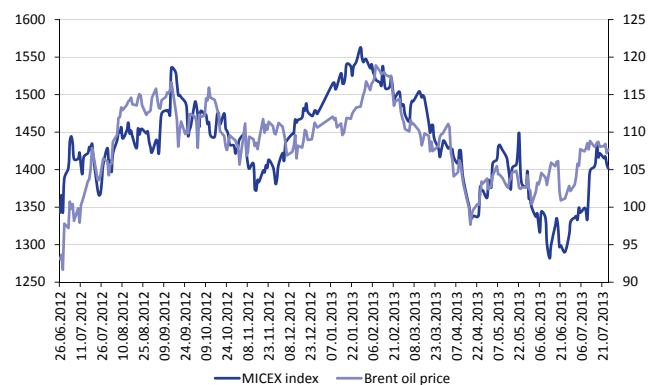
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The MICEX index grew up by 4.9% in the period between July 1 thru 25 basically in response to Gazprom stock price rise by 20.37%. Stock market capitalization in that period increased by 4% or Rb 941bn to account for 37.6% of GDP as of July 25. In July 2013, the domestic corporate bond market was also governed by optimistic expectations. Almost all key market indicators saw an uptrend: market volume, corporate bond market index, average weighted yield (especially in the industrial segment), issuers' activity. The situation with issuers' obligations to bondholders remains stable.

Dynamics of Russian stock market basic structural indices

In July 2013, unlike June 2013, when the Russian stock market was basically governed by a downtrend faced by international stock markets, the MICEX index was governed by an upward trend in crude oil prices. An increase in crude oil prices of up to \$108 per barrel by July 10 (106.2% of the price at the end of June) encouraged a growth of 4.9% in the MICEX index from 1330 points as of June 28 to 1400 points as of July 12. The MICEX index reached its ceiling up to 1431.8 points on July 17 (Fig. 1).

Apart from crude oil prices, the MICEX index was also pushed up by an uptrend for blue chips. For instance, Gazprom stock price increased by 20.3% in the period of July 1 thru 17 after the Russian Government announced in July that a few of the oil fields located in the Barents Sea and the Kara Sea would be handed over to Gazprom, whereas VTB and Norilsk Nickel stock prices saw a downtrend in response to a news about increased debt owed by these companies and their profit reduction forecasts for this year. VTB and Norilsk Nickel stock prices dropped by 1.6% and 2.9% respectively in the year to July 25. Other blue

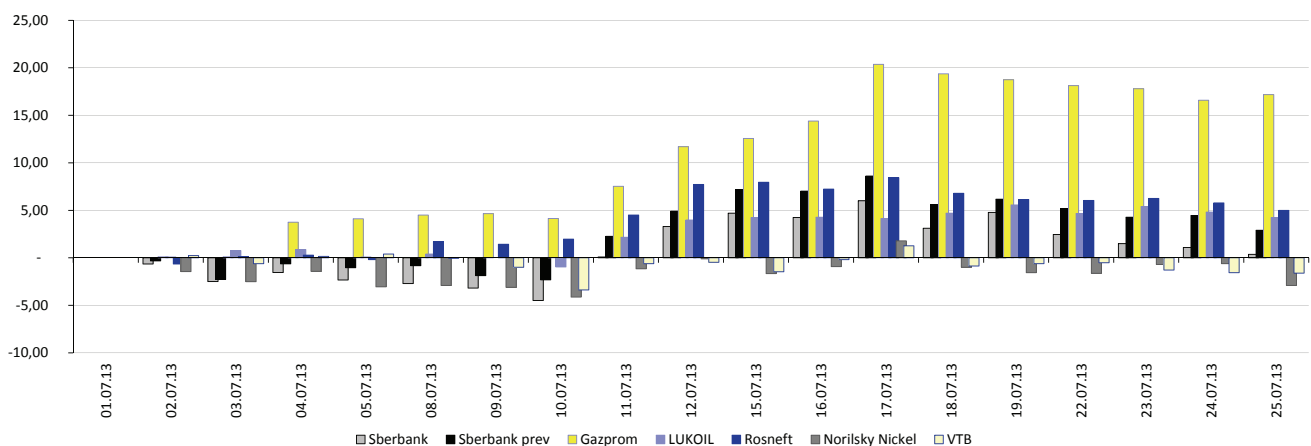


Source: RBC Quote.

Fig. 1. Dynamics of the MICEX index and futures Brent oil prices in the period of May 28, 2012 thru June 26, 2013

chips went up by an average of 3% in the month to July 25 (Fig. 2).

The July uptrend in Gazprom stock price had no any drastic effect on company's annual yield: Gazprom investors lost 13.9% in the calendar year beginning with July 26, 2012. Norilsk Nickel and VTB stocks yielded losses too: 7.3% and 10.2% respectively in the calendar year. Unlike the foregoing companies, Rosneft



Source: RBC Quote, author's estimates.

Fig. 2. Blue chips growth rates in the Moscow Stock Exchange in July 2013 (month to date)

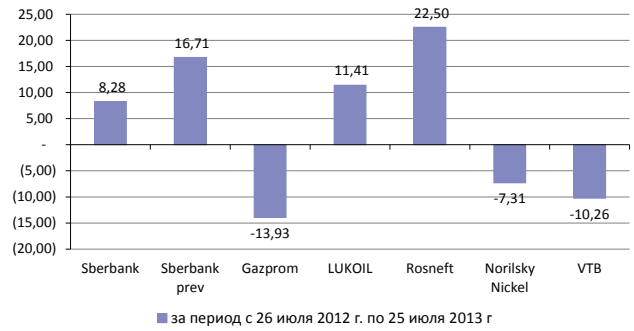
stock showed the highest yield among blue chips at 22.5% p.a. in the period beginning with July 26, 2012. Sberbank and LUKOIL privileged stocks gained 16.7% and 11.4% respectively in the period beginning with July 26, 2012.

A growth of 9.3% in the power industry index in the period of July 1 thru 23 was the most marked event concerning industrial indices. The growth was triggered by RusHydro stock price rise in response to information on higher dividends payout, and FGC UES (Federal Grid Company of Unified Energy System) stock price rise after it was announced that pension accruals accumulated in Vnesheconombank (VEB) would be invested in company's bonds. Therefore, the growth in the electric power industry index in the second half of July allowed it to regain a part of the losses incurred early in the year (it is to be recalled that the electric power industry index reached 1850 points on January 28, 2013, then it dropped to 1120 points by April 19). The metallurgic sector saw the same trend, i.e. a growth of 4.7% in the period between July 1 and July 25. The oil and gas industry index was governed by the same trend as Gazprom stock price, i.e. it gained up to 9.1% in the month to July 17. Indices in the consumer, innovation, and financial & banking sectors ranged around the values of the beginning of the month.

According to the Emerging Portfolio Fund Research (EPFR), a capital inflow of \$167m, or around Rb 5,5bn, to funds oriented toward the Russian market was registered in the period between July 1 and 24, of which 61% fell within the period between July 11 and 17. According to the same fund, capital outflow from such funds totaled \$660m in June. The Russian stock market (MICEX) capitalization totaled Rb 23,97 trillion or 37.6% of GDP as of July 25, 2013, having gained 4% or Rb 941bn against July 1. Furthermore, capitalization structure changed in response to different trends in industrial sector indices. In particular, the share of companies operating in the mineral extraction sector increased by 1.33% from the beginning of the month to 48% as of July 25. The share of companies operating in the transport and communications sectors increased by 0.37% in the same period. The share of companies operating in the mineral extraction and transport industries grew up in response to a decrease in the share of companies in the manufacturing and financial sectors from 13.4% to 12.6% and from 15.4% to 14.8% respectively in the period of July 1 thru 25.

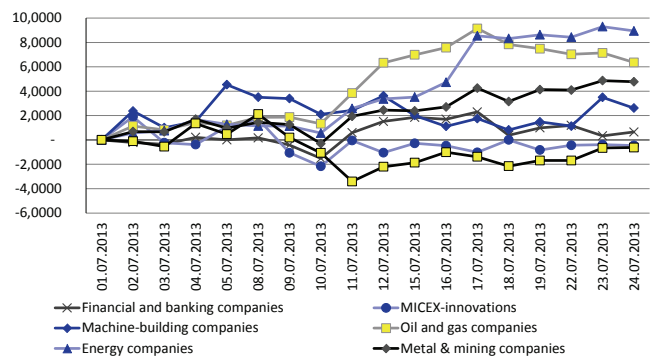
Corporate bond market

In July 2013, the domestic corporate bond market grew up to a much bigger size (measured by the par value of outstanding securities denominated in



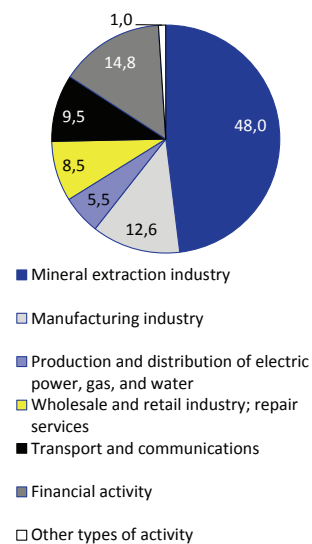
Source: RBC Quote, author's estimates.

Fig. 3. Blue chips growth rates in the Moscow Stock Exchange in the period of June 27, 2012 thru June 26, 2013



Source: RBC Quote, author's estimates.

Fig. 4. Different stock indices growth rates in the Moscow Stock Exchange (month to date)



Source: The Moscow Stock Exchange's official website, authors' estimates.

Fig. 5. Stock market capitalization structure by type of economic activity

the national currency, including those issued by non-residents), having exceeded the monthly average of H1 2013. By the end of July, this indicator reached Rb 4,621,0bn, having exceeded 2.4% the value registered late in May¹. Market capacity grew up with increase in the quantity of bond issues (983 corporate bond issues registered in the national currency against 971 issues by the end of the preceding month), whereas the quantity of bond issuers remained the same (348 issuers) by the end of the month. There are 12 USD-denominated bond issues and a JPY-denominated bond issue of Russian issuers outstanding.

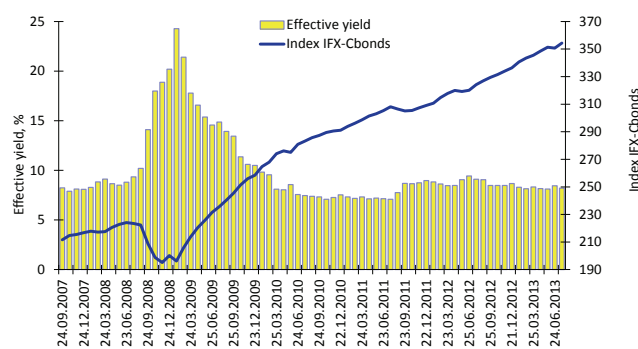
Investment activity in the secondary corporate bond market weakened in July against June, but maintained at the average level of the last few months. For example, the amount of contracts (transactions) in the Moscow stock exchange totaled Rb 115,5bn in the period between June 25 and July 19 (to compare, trading volume was Rb 128,9bn in the period between May 25 and June 24), and the quantity of transactions almost remained unchanged over the period under review, 23,800 (against 23,100 in the previous period)².

The Russia corporate bond market index (IFX-Cbonds) started to grow after a short decline. Its value increased by 3.6 points (or 1%) by the end of July against the preceding month. The corporate bond average weighted yield also saw a positive trend and dropped from 8.45% late in June to 8.20% by the end of July (Fig. 6)³.

Corporate bond portfolio duration decreased insignificantly. The duration was 740 days as of July end, being 23 days less than as of the previous month end. Relative stability of the duration value reflects insignificant duration of outstanding corporate bonds due to a decline in market interest rates.

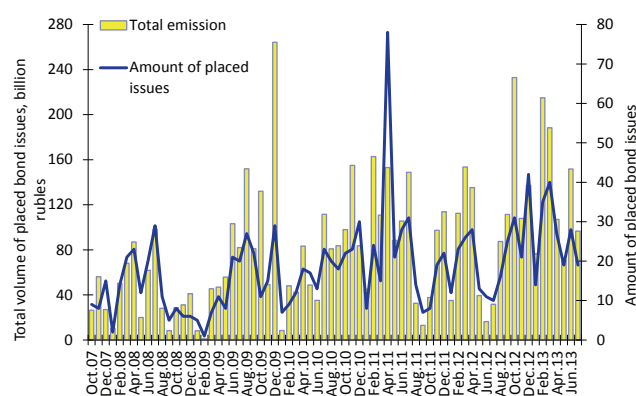
Most liquid segment of the corporate bond market saw a moderate decrease in issues' yield. Production and energy companies' bond yield saw most strongly pronounced downtrend by an average of 0.3 p.p., though investment activity in the energy segment was weak in July. Credit institutions' and telecom companies' most liquid bond yield saw a decrease of a bit more than 0.2 p.p.⁴. The general downtrend had no effect on OJSC VTB Bank whose 06-series bond yield increased more than 1 p.p.

Russian bonds issuers were highly active in terms of bond issues, having approached most nearly towards the record of the past two months. For instance, 17 issuers registered 55 bond issues at an aggregate par value of Rb 466,2bn in the period of June 25 thru July 19 (to compare, 79 bond issues at a total of Rb 590,7bn



Source: According to Cbonds Information Agency.

Fig. 6. Dynamics of the Russian corporate bond market index and average weighted yield



Source: According to Rusbonds information agency.

Fig. 7. Dynamics of initial public offerings of corporate bonds denominated in foreign currencies

were registered in the period between May 25 and June 24). More than a half of the registered bond issues included listed bonds.

However, irrespective of positive market dynamics and high issuers' activity, there were much less IPOs against the previous period and figures concerning registration of bond issues. For instance, 19 issuers placed 24 bond issues at an aggregate par value of Rb 96,6bn (to compare, 28 bond issues were placed at Rb 151,8bn in the period between May 25 and June 24) in the period of June 25 thru July 19 (Fig. 7). Major bond issues were placed by OJSC Russian Railways (Rb 25bn) and, Bank of Development and Foreign Economic Affairs (Vnesheconombank) state-owned company (Rb 20bn)⁵. It should be noted that all of the above issues included listed bonds, whereby suggesting that investors gave preference to reliable issuers which have long been present in the market. However, the placed bond issues included four debut issues of mortgage bonds with a maturity of 27 to 32 years. The maturity of the rest of bond issues was 10 years or less.

1 According to Rusbonds information agency.

2 According to Finam Information Company.

3 According to Cbonds Information Agency.

4 According to Finmarket Information Agency.

5 According to Rusbonds information agency.

In June, as little as one debut bond issue was declared void by the Federal Commission for Securities Market of Russia (FCSM) for non-placement of a single bond, whereas none of the corporate bond issues was cancelled for the same reason in the period between May 25 and June 24 (although 10–15 issues were cancelled monthly in the first quarter). It is quite a positive signal indicative of the demand for corporate debt securities¹.

Thirteen issuers were to redeem their debt at an aggregate par value of Rb 59,9bn in the period of June 25 thru July 19. However, three of the issues failed to redeem their debt on the date of maturity (a single issuer declared a technical default in the preceding period), being an adverse event in the market. Twelve corporate bond issues at a total of Rb 33,9bn² are expected to take place in August 2013.

Though there were a few cases of technical default on debt redemption, the situation with issuers' obligations to bondholders still remains stable. In the period between June 25 and July 19, like in the previous period, (i.e. a situation when the issuer is unable to pay to security holders even shortly after a scheduled due date) concerning coupon yield payment, redemption

at par value of bond issues and early redemption of securities through offer³.

Quite a number of regulatory and administrative market innovations have been proposed over the last few weeks. First, early in July, the State Duma of Russia adopted a federal law on financial mega-regulator which empowers the Bank of Russia to conduct prudential regulation and supervision over financial market participants and macroeconomic policy. Second, the Russian Government stated about the need to balance taxation on personal interest income generated from bank deposits and stocks and bonds. In particular, the same concept is set forth in a road map on the "Creation of International Financial Center and Enhancement of Investment Climate in the Russian Federation". Finally, the Moscow Stock Exchange announced that by the end of the year it would be possible to trade in outstanding classic bonds on the date of placement (such a possibility already appeared for listed bonds early in the year). It became possible, because of replacement of the securities placement report with a placement notice filing for classic bonds⁴.

1 According to the Federal Financial Markets Service of Russia (FFMS).

2 According to Rusbonds company.

3 According to Rusbonds company.

4 According to the materials of Rusbonds Information Agency.