

FINANCIAL MARKETS IN OCTOBER 2014

N.Andrievsky, E.Khudko

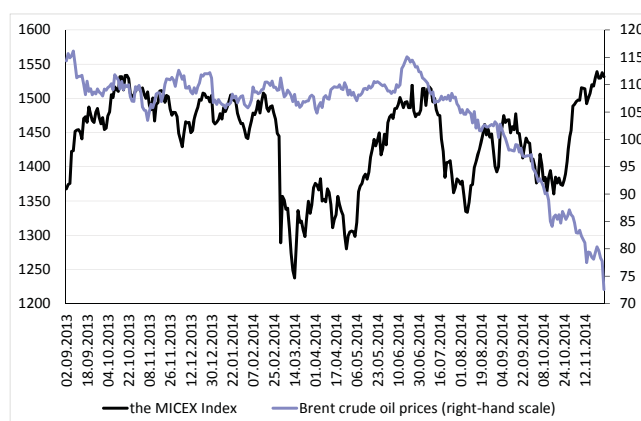
In November, the MICEX index was driven by the substantial devaluation of the ruble and reached another record-high-level of 1538.9 points during the year. It is the metalworking sector index that became a leader among the sector indices in November, up 12.1% since the beginning of the month. The stock market capitalization as of the 27th of November amounted to Rb 23,9 trillion (36.9% of GDP), an increase of Rb 218,5bn (0.9%) since the 3rd of November. The corporate bond market in November saw some adverse trends such as downward trend in the corporate bond index and investment, and the acceleration of the average weighted bond yield (especially in the production sector). Such indicators as the corporate bond market volume and investment activity of bond issuers showed positive dynamics. At the same time, deterioration in issuers' failure to discharge their obligations to bondholders was observed.

Dynamics of the Russian stock market basic structural indices

The MICEX rose substantially during the recent week in October: the index reached 115.55 points or 8.4% within a week from the 23rd thru 31st of October. The growth was basically driven by the weakening of the ruble against the US dollar. In November, the MICEX index reached 1538.9, breaking through the record-high-level on the 21st of November.

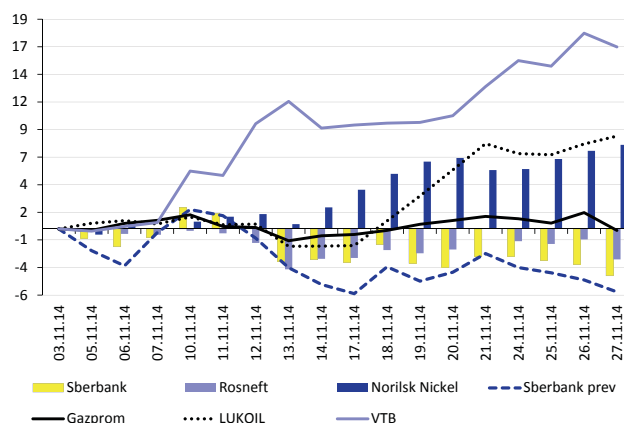
The MICEX index rose in November mostly in response to the appreciation of most liquid companies covered by the index. VTB's shares, a leader among highly liquid shares, were appreciated at a rate of 16.49% in the period of November 3–27, 2014. Lukoil's and Norilsk Nickel's shares appreciated 8.4% and 7.6% respectively during the same period. At the same time, Sberbank's shares depreciated during the month in the period of November 3 thru 27, 2014, its common shares depreciation reached 4.2% while preferred shares lost 5.7%. It's worth noting that no substantially positive news about companies whose shares appreciated in November was observed. At the same time, Sberbank¹ published on its official website on the 11th of November its financial performance results within the first 10 months of 2014 measured under the Russian Accounting Standards (RAS), showing that Sberbank's net profit dropped by 7.8% relative to the corresponding period of 2013.

Most of highly liquid shares showed a negative annual ROE in November. Sberbank's common shares depreciated 28.9%² during the year (in the period of



Source: RBK Quote.

Fig. 1. Dynamics of the MICEX Index and futures prices of Brent crude oil in the period between September 1, 2013 and November 27, 2014



Source: RBK Quote, author's estimates.

Fig. 2. Growth rates of most highly liquid Russian stocks in the Moscow Exchange in July (in the period between November 1–27)

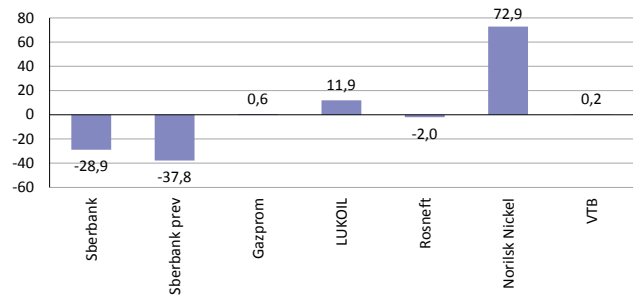
1 Company's official website, investor section. http://www.sberbank.ru/moscow/ru/press_center/all/index.php?id114=200005229

2 Annual yield on shares is calculated on the basis of shares price movement and doesn't include dividends paid to shareholders following the results of the annual general meeting of shareholder.

November 28, 2013 thru November 27, 2014) while its preferred shares lost more than 37.8% during the same year. Rosneft's shares depreciated too, losing 2.0% during the calendar year. Norilsk Nickel's ROE boosted 72.9% in the period of November 28, 2013 thru November 27, 2014 due to the substantial growth in its shares earlier in 2014, as well as the growth in November in response to positive news on dividends.

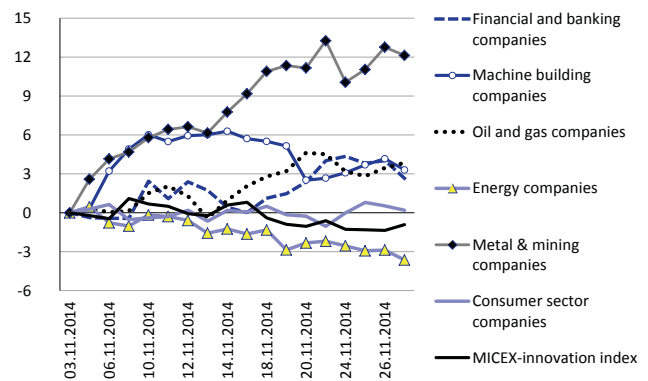
It is the metal production index that showed highest rise among sector indices in November: not only did Norilsk Nickel's shares appreciated, but also Polymetal International plc shares gained 22.0%, Russian Aluminum 53.8% and ALROSA 16.9% in the period of November 3–27, 2014. As a result, the index gained 12.1% in the period under review. The oil and gas sector index was gained a bit less in November, 3.8% in the period of November 3–27, 2014. The machine building sector index saw a substantial growth, up to 6.2% since the beginning of the month, within the first two decades of November. The index began to grow in response to an ongoing utilization program and the devaluation of the ruble, increasing the expectations of growth in durable goods consumption. There were two sectors in November – MICEX innovations and energy sector – that saw their index falling 0.9% and 3.6% respectively. Sector indices rose by an average of 2.5% in the period of November 1–27, 2014.

The Moscow Exchange trading turnover in November reached Rb 643,8bn while its average daily turnover was Rb 35,76bn. Sberbank's total turnover on common and preferred shares contributed 25.9% on average to the stock exchange trading turnover. It's worth noting that Sberbank contributed 5.6% less on the trading turnover on shares compared to October. Gazprom also contributed 1.3% less (down to 14.2%) to the turnover of the Moscow Exchange in November 2014. Therefore, the two most highly liquid shares accounted for 40.1% of the Moscow Exchange trading turnover. The other top-5 shares with the high-



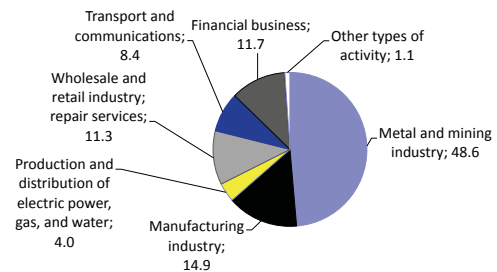
Source: RBK Quote, author's estimates.

Fig. 3. Growth rates of most highly liquid Russian stocks in the Moscow Exchange in the period between November 28, 2013 and November 27, 2014



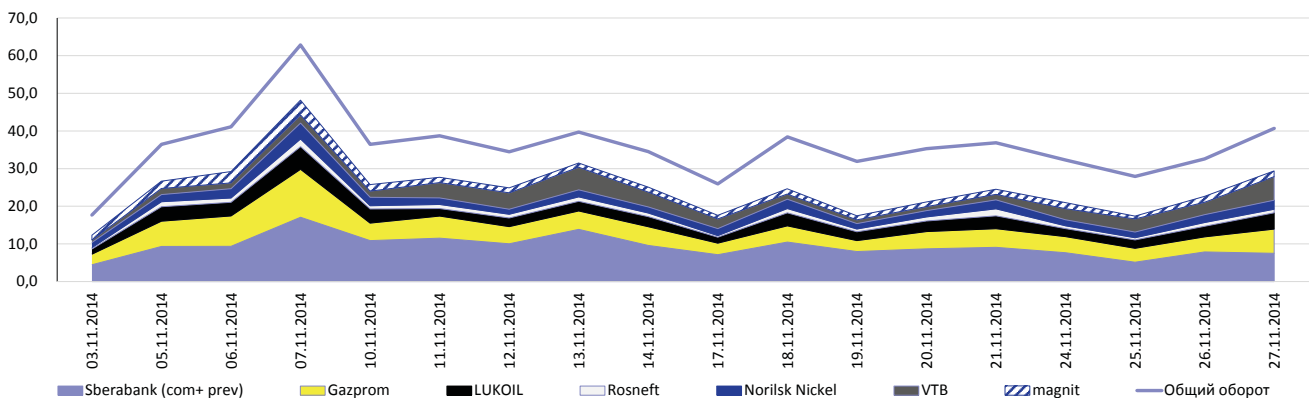
Source: RBK Quote, author's estimates.

Fig. 4. Growth rates in various sector stock indices in the Moscow Exchange (in the period between November 1 to 27, 2014)



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

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



Source: RBK Quote, author's estimates.

Fig. 6. Trading turnover structure in the Moscow Exchange (in the period between November 1 and 27)

est trade volume accounted for an average of 28.7% of the Moscow Exchange trading turnover.

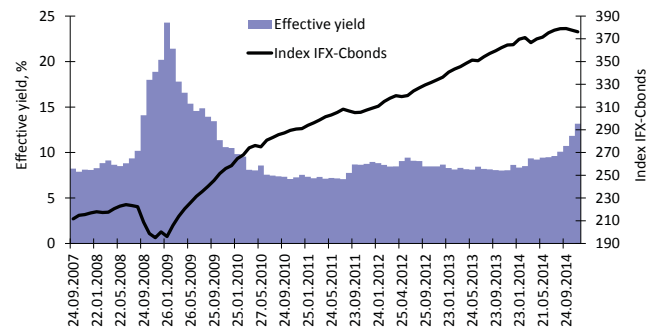
According to the Emerging Portfolio Fund Research (EPFR), foundations investing in Russian shares saw \$136,2m of capital inflow in the period between October 30 and November 26, 2014. Moscow Interbank Currency Exchange (MICEX) total capitalization amounted to Rb 23,9 trillion (36.9% of GDP) as of November 27, 2014, a gain of Rb 218,5bn (0.9%) since the 3rd of November. In November, the share of energy companies in the MICEX capitalization structure shrank by 0.2% to 0.4% and that of financial companies by 0.67% to 11.65%. The shrinking in the share of both sectors was set off by growth in the share of mineral extraction and manufacturing companies.

Corporate bond market

The Russian domestic corporate bond market volume (measured by the par value of outstanding securities denominated in the national currency, including those issued by non-residents) resumed to growth in November following a short period of stabilization. By the end of the month the market volume amounted to Rb 5.717,2bn, 1.5% higher than the volume observed as of the end of October¹ this year. At the same time, bond issues kept growing in number in the elapsed period (between October 25 and November 24, 2014) (1051 corporate bond issues registered in the national currency against 1041 issues as of the end of October), whereas the number of issuers in the debt segment remained unchanged (345 issuers like in the previous month). There were 17 outstanding issues of USD-denominated bond issues of Russian issuers (a total of more than \$2,7bn) and an outstanding JPY-denominated bond issue.

Investment activity in the secondary corporate bond market fell a bit in November after a moderate growth during the preceding several months, which, however, can largely be explained by fewer trading days in the period under review. Nonetheless, secondary market trading figures remained at the yearly average level. For instance, the Moscow Exchange total trading volume amounted to Rb 93,0bn in the period between October 25 and November 24, 2014 (to compare, the trading volume in the period between September 25 and October 24, 2014 was Rb 102,3bn). The number of transactions in the period under review also dropped a bit to 26,700 (27,700 in the previous period)².

The Russian corporate bond market index IFX-Cbonds kept falling in November as it did in October. By the end of November the index lost 1.4 points (or



Source: According to the data reported by Cbonds Information Agency.

Fig. 7. Dynamics of the Russian corporate bond market index and average weighted yield

0.4%) compared to the value observed as of the end of the preceding month. At the same time, the corporate bond average weighted yield reached a new record-high-level, up from 11.83% late in October to 13.17% by the end of November, the highest value since the end of the crisis-hit mid-2009 (Fig. 7)³. The corporate bond portfolio duration also declined: it was 397 days as of the month end, 31 days less than that observed as of the previous month end.

An important event took place in the money market late in October when the Central Bank lifted the key interest rate straight by 1.5 p.p., making the bond market yield skyrocket.

It should be noted that international rating service agencies didn't change their rating (due to steady budget and external indicators) after Moody's Ratings service downgraded the sovereign rating of Russia, which induced some optimism into investors, although it cannot alone have a serious effect on the existing downward trends. Regarding some issuers, many banks and mortgage agents saw their ratings (or projected ranking) downgrade, however the ratings of some major production and technology companies⁴ remained unchanged.

In the highly liquid segment of the corporate bond market saw a new round of growth in bond yields. Certain bond issues of financial and production companies (and their affiliates) showed highest growth (beyond 2 p.p.), although these securities saw no large sales. Only a few bond issues of major financial issuers experienced a downtrend (AK Bars Bank, Zenit Bank, Federal Grid Company of Unified Energy System). The strongest growth in bond yields was observed in the production sector, by an average of 1.6 p.p. among highly liquid securities, and about 1 p.p. in the financial and technology sectors. Securities in the energy segment showed the slowest

¹ According to the data reported by Rusbonds Information Agency.

² According to the data reported by Finam Investment Company.

³ According to the data reported by Cbonds Information Agency.

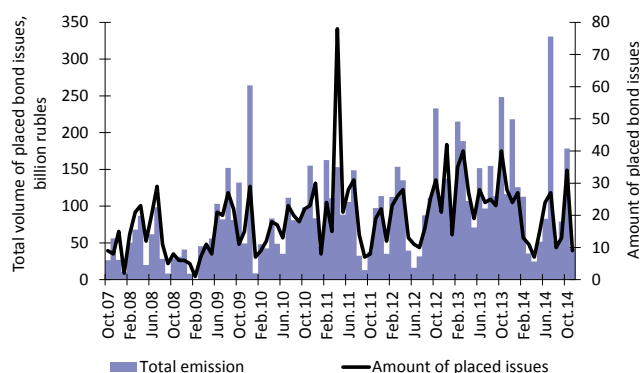
⁴ According to the data reported by Cbonds Information Agency.

growth (0.7 p.p. or less). Active sales were observed in the financial sector¹.

Despite high yields, issuers were active in fundraising in November. For instance, in the period between October 25 and November 24, 2014 17 issuers registered 57 bond issues at an aggregate par value of Rb 228,3bn (to compare, 27 series of bonds at a par value of Rb 88,6bn were registered in the period between September 25 and October 24, 2014). Major bond issues were registered by OJSC Gazprombank (10 series of exchange traded bonds and two series of mortgage bonds at a total of Rb 77bn), Ing Bank (Eurasia) ZAO (six series of exchange traded bonds at Rb 40bn), OAO TransFin-M (nine series of exchange traded bonds at Rb 27bn), OJSC New Forwarding Company (three series of exchange traded bonds at Rb 15bn)². Exchange traded bonds accounted for more than two thirds of the registered issues, and there were also a few debut issues among the registered bond issues. Additionally, OJSC Gazprombank registered seven bond issues denominated in US dollars, a total value of \$2,5bn.

However, investment activity in the primary market appeared to be far below the annual average level. For instance, in the period between October 25 and November 24, 2014 only seven issuers placed nine bond issues at an aggregate par value of Rb 42,3bn (to compare, 34 series of bonds at a par value of Rb 178,4bn were placed in the period between September 25 and October 24, 2014) (see Fig. 8). Major bond issues were placed by OJSC Gazprombank (a series of exchange traded bonds at Rb 15bn) and OAO TransFin-M (three series of exchange traded bonds at Rb 12bn)³. Exchange traded bonds accounted for more than 50% of the registered issues. Only two issuers managed to borrow for a long term, namely Gazprombank for 30 years and TransFin-M for 10 years.

Late in October, earlier in November, the Bank of Russia declared void a corporate bond issue for non-



Source: According to the data reported by Rusbonds information agency.

Fig. 8. Dynamics of initial public offerings of corporate bonds denominated in the national currency

placement of a single bond (three corporate bond issues of a single issuer were declared void for the same reason in the preceding period)⁴.

In the period between October 25 and November 24, 2014 all of the 13 issuers redeemed 14 issues at an aggregate par value of Rb 60,7bn (all issuers honored their obligation in due time in the preceding period). Eighteen corporate bond issues at a total of Rb 71,3bn are to be redeemed in December 2014⁵.

A certain deterioration in corporate bond issuers' failure to discharge their obligations to bondholders was observed late in October, earlier in November due to a technical default on some bond issues. At the same time, no actual defaults on coupon yield payment and early redemption(s) of securities on the put date and full repayment were reported in the market in the period under review⁶ (no real defaults were reported in the previous period)⁷.

1 According to the data reported by Finam Investment Co.

2 According to the data reported by Rusbonds Information Agency.

3 According to the data reported by Rusbonds Information Agency.

4 According to the data reported by the Bank of Russia.

5 According to the data reported by Rusbonds Information Agency.

6 In other words, when a bond issuer is unable to repay to bondholders even during the grace period.

7 According to the data reported by Rusbonds Information Agency.