

## FINANCIAL MARKETS IN DECEMBER 2014

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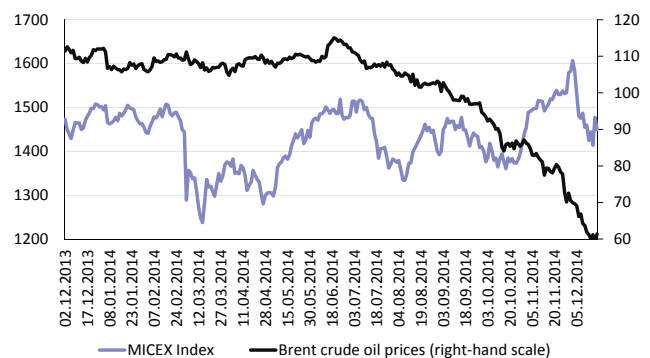
The MICEX index fell to 1413.8 points by the 17<sup>th</sup> of December, following the five-year highs early in December. It is only VTB's shares that demonstrated growth among highly liquid shares during the same month. The stock market capitalization as of the 19<sup>th</sup> of December amounted to Rb 22,3 trillion (34.4% of GDP). The domestic corporate bond market in December saw a downtrend induced by both external and internal trends. Rapid growth in the average weighted bond yield, as well as decrease in the market index and investing activities in the secondary market (especially in the production sector) became the key adverse factors in the market. The situation with bond issuers being able to fulfill their financial obligations before bondholders remained tense and made a certain contribution to the growth in bond yields.

### Dynamics of the Russian stock market basic structural indices

The beginning of December 2014 saw the MICEX Index reach its five-year highs, 1606.8 points, in response to the slump of the ruble exchange rate. The MICEX index plummeted after the ruble exchange rate stabilized and bounced back to Rb 55–60 per US dollar. The MICEX Index reached its lows on the 17<sup>th</sup> of December, falling to 1413.8 points. At the same time, the Brent crude price dropped to \$59,2 per barrel in December. It's worth noting that the last time the crude oil price reached the same level is May 2009.

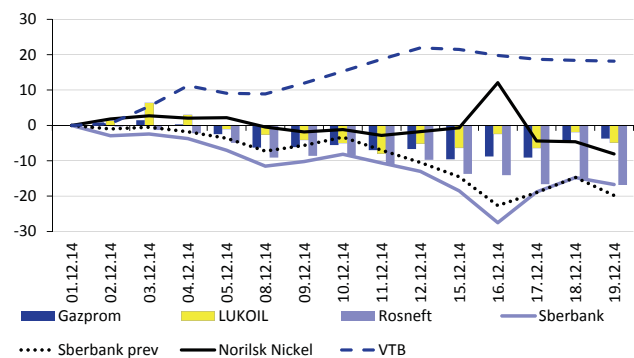
The dynamics of highly liquid shares saw a downtrend in December, except VTB's shares. Sberbank's common shares lost 16.7% since the beginning of the month until the 19<sup>th</sup> of December, while its preferred shares decreased 19.8% in the period under review. Rosneft's shares lost 16.85%, Norilsk Nickel's shares dropped 8.1%, while Gazprom' and Lukoil' shares lost 3.75% and 4.9% respectively during the same period.

Annual return on Sberbank's common stock equity dropped by 39.9%<sup>1</sup> in the period beginning on December 20, 2013 and ending on December 19, 2014, while the annual return on the preferred stock equity lost more than 48% during the year. Rosneft's shares were found to be loss making too, losing 20.3% during the year. The substantial growth in Norilsk Nickel's share early in 2014, as well as the growth in November in response to increasing nickel price in the global market resulted in a return on equity of 65.0%. Gazprom's shares lost 2.0% during the calendar year, which, taking into consideration a



Source: RBK Quote.

Fig. 1. The dynamics of MICEX Index and futures prices of Brent crude oil in the period between December 1, 2013 and December 19, 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 of December 1–19, 2014)

Rb 7 and 20 kopeks per share dividend payout, is indicative of a ROE of 3.11% p.a. By December 19, 2014, Lukoil's shares and VTB's shares demonstrated a ROE of 13.1% and 13.8% respectively.

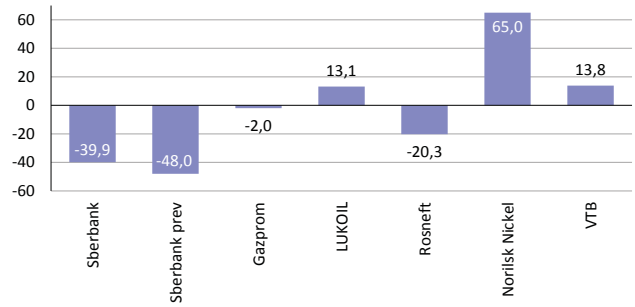
The industry indices showed a mixed dynamics in December. The metal production index and the fi-

<sup>1</sup> 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.

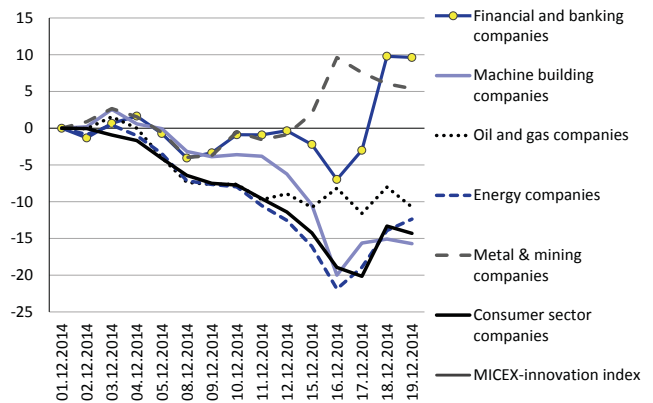
financial and banking index gained 5.4% and 9.6% respectively in the period of December 1–19. The metal production index increased in December basically in response to the dynamics of OJSC Polymetal’s shares. The company’s shares gained 35% since the beginning till the 17<sup>th</sup> of December. The financial and banking index increased basically in response to VTB’s, MICEX’s and AFC System’s shares. Other industry indices lost 10.7 – 15.7% in December.

The Moscow Exchange trading turnover in November reached Rb 889,5bn in the period of December 1–19, which corresponds to an average daily turnover of Rb 59,3bn. The growth in the Moscow Exchange trading turnover in the period under review was 19.7% higher than that throughout the entire month in November. Total turnover of Sberbank’s common and preferred shares accounted for an average of 26.1% of the Moscow Exchange trading turnover in December. Gazprom’s shares accounted for an average of 12.4% of the trading turnover in the period under review of December, 1.8% less than in November. Hence the shares of the two most liquid companies accounted for 38.5% in December, 1.6% less that in November. The other top-5 shares in the trade volume accounted for an average of 33.5% of the Moscow Exchange trading turnover.

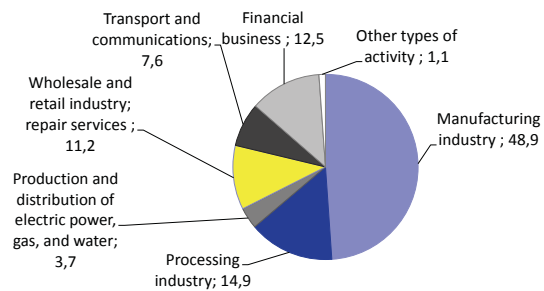
According to the data provided by the Emerging Portfolio Fund Research (EPFR), foundations investing in Russian shares saw \$185,7m of capital outflow during the period beginning on the 27<sup>th</sup> of November and ending on the 17<sup>th</sup> of December. The Moscow Interbank Currency Exchange (MICEX) total capitalization as of December 19, 2014 amounted to Rb 22,3 trillion (34.4% of GDP), the MICEX capitalization dropped by Rb 1 trillion 858,5 billion (7.7%) since the 1<sup>st</sup> of December. The share of manufacturing sector companies in the MICEX capitalization structure increased 0.85 p.p. to 14.92% in December, whereas the share of transport and communication companies dropped by 0.57 p.p. to 7.6%, while the share of retail trade sector companies slid by 0.27 p.p. to 11.2%.



Source: RBK Quote, author’s estimates.  
 Fig. 3. Growth rates of most highly liquid Russian shares in the Moscow Exchange in the period between December 20, 2013 and December 19, 2014

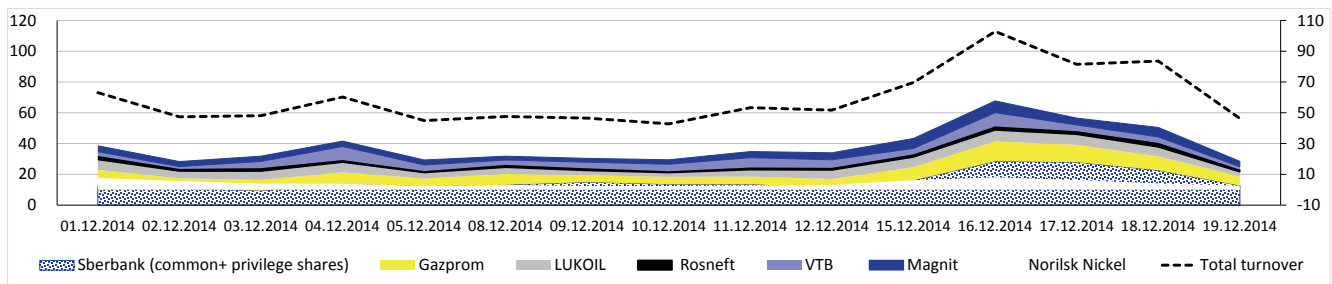


Source: RBK Quote, author’s estimates.  
 Fig. 4. Growth rates in various sector stock indices in the Moscow Exchange (in the period of December 1–19, 2014)



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 of December 1–19, 2014)

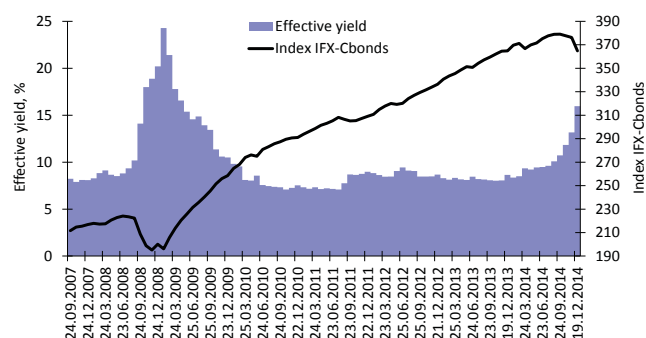
### Corporate bond market

The domestic corporate bond market saw an increase in volume in December. By the end of December, 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) amounted to Rb 6383,8bn, a record gain of 11.5% over the highest value recorded as of the end of November<sup>1</sup>. Bond issues kept growing in number in the elapsed period (1057 corporate bond issues registered in the national currency against 1051 issues as of the end of November), whereas the number of issuers in the debt segment remained unchanged (345 issuers like in November). 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.

Investing activities in the secondary corporate bond market kept decreasing, despite the fact that trading indicators normally tend to be subject to year-end seasonal uptrend. For instance, the Moscow Exchange total trading volume amounted to Rb 71,0bn during the period beginning on the 25th of November and ending on the 19th of December (to compare, the trading volume was Rb 93,0bn during the period beginning on the 25th of October and ending on the 24th of November). At the same time, the number of transactions, on the contrary, increased to maximum values and totaled 30,500 in the period under review (26,700 in the previous period)<sup>2</sup>, which among other things means that the securities were attractive to retail investors.

The Russian corporate bond market index IFX-Cbonds kept falling since October. By the end of December, the index saw a record loss of 11.3 points (or 3.0%) compared to the value observed as of the end of the preceding month. At the same time, the corporate bond average weighted yield made a new record gain from 13.17% as of the end November to 15.97% by the end of December, the highest value of this indicator since the beginning of the crisis-hit 2009 (Fig. 7)<sup>3</sup>. The corporate bond portfolio duration also declined: it was 348 days as of the end of December, 49 less than that observed as of the previous month end. It is rapid growth in interests rates in the bond market that was responsible for such a negative dynamics of duration.

Even the most liquid segment of the corporate bond market saw a skyrocketing growth in bond issues yield in December. It is some issues of financial companies



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

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

and production companies (and the affiliate persons therewith) that saw the highest growth in yield rates (more than 8 p.p.), which also was followed by selling these securities, namely OJSC RUSAL Bratsk Aluminum Smelter, OJSC Metalloinvest Holding Company, OJSC VTB Bank, OJSC Russian Agricultural Bank. However, a special emphasis should be paid to a very significant fall, in terms of these market trends (more than 1 p.p.), in the yield of the bonds issued by Alfa-Bank and Moscow United Power Grid Company. Overall, the production segment saw, as in the recent months, the heaviest pressure on bond yield rates, 5.0 p.p on average. Bond yield rates in the tech sector and financial sector saw a smaller than average increase of 4.7 p.p. and 3.8 p.p. respectively. The energy segment appeared to be less attractive for investors, especially with regards to loans to regional energy companies. Additionally, investors paid a small interest to iron and steel companies, which is not case with the financial sector which saw a rather high trading turnover<sup>4</sup>.

Despite the prevailing high yield rates, bond issues showed an extremely high activity in new fundraising late in November–December. For instance, during the period beginning on the 25<sup>th</sup> of November and ending on the 19<sup>th</sup> of December 16 issuers registered 50 bond issues at an aggregate par value Rb 994,3bn (to compare, 57 bond series at Rb 228,3bn were registered during the period beginning on the 25<sup>th</sup> of October and ending on the 24<sup>th</sup> of November, which is high value of an indicator). However, it is OJSC NK Rosneft who is the only issuer who registered 12 series of listed bonds at Rb 800bn, thus making a major contribution to such a high value. Additionally, major bond issues were registered by LLC Gazprom Capital, PJSC KHMB Otkrytiye, OJSC Bank of Moscow<sup>5</sup>. Listed bonds accounted for

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 Finam Investment Company.

5 According to the data reported by Rusbonds Information Agency.

more than 50 percent of the registered bond issues, and a few debut bond issues were registered too.

The situation in the primary market was similar to the registration figures. For instance, during the period beginning on the 25th of November and ending on the 19th of December 25 issuers placed 54 bond issues at an aggregate par value of Rb 751,1bn, an absolute record in the corporate segment of the Russian bond market (to compare, only 9 series of bonds at a par value of Rb 42,3bn were placed during the period beginning on the 25th of October and ending on the 24th of November) (Fig. 8). NK Rosneft was again the key market player in the period under review, borrowing Rb 625bn through 14 listed series of bonds in the market. Additionally, major bond issues were placed by Vnesheconombank (at Rb 20bn), LLC Agent SB-2014 (a total of Rb 11,1bn), ZAO Mortgage Agent KHMB-2 (at Rb 7,3bn)<sup>1</sup>. Listed bonds at that time accounted for a bit less than a half of all bond issues placed in the period under review, because a big number of debut issues were placed at that time (mostly from among mortgage securities). Furthermore, despite a complex situation in the financial markets, half of the issuers managed to obtain long-term borrowings: 10 mortgage agencies managed to borrow for a period of 28 to 33 years, one for a period of 15 years, three for a period of 10 years.

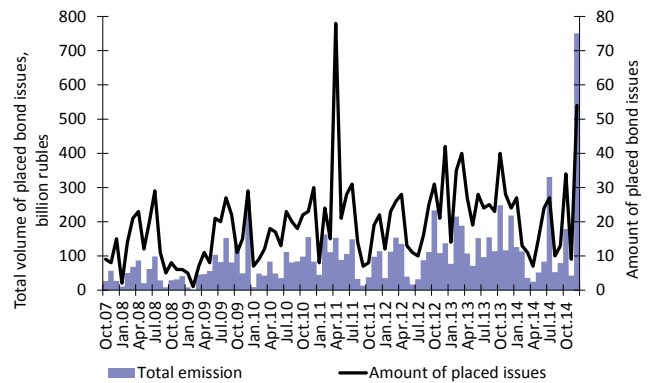
A special emphasis should be placed on the fact that late in November – December all of the bond issues offered in primary market were placed with success, and the Bank of Russia declared void none of the corporate bond issues for non-placement of a single bond (one corporate bond issue was declared void for the same reason in the preceding period)<sup>2</sup>.

In the period beginning with the 25th of November and ending on the 19th of December, all of the 16 issuers redeemed their 37 bond issues at an aggregate value of Rb 86,6bn (all issuers honored their obligation in due time in the preceding period). Four corporate bond issues at a total of Rb 12,0bn<sup>3</sup> are to be redeemed in January 2015.

1 According to the data reported by Rusbonds Information Agency.

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

3 According to the data reported by Rusbonds Information Agency.



Source: According to the data reported by Rusbonds company.

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

The situation with issuers being able to fulfill their financial obligations before bondholders remained tense late in November – December. One issuer declared a technical and real default on paying the coupon yield accrued for some of its bond issues; another issuer declared a technical default on repurchase of the securities from the holders on the put date<sup>4</sup>. The default cases by rather major issuers added no optimism for investors in the market and also played a certain role in pushing yields up. No actual defaults<sup>5</sup> on coupon yield payment and early redemption(s) of securities on the put date and full repayment were reported in the market in the preceding period.

Certain transformations are expected to take place soon in the domestic corporate bond market as a result of planned update of the rules for entering corporate bonds into the top listing, because top-listing bonds may be purchased by pension funds (provision is made for shortening the list of credit rating agencies whose ratings will be sufficient for listing, raising collateral requirements for loans).

4 According to the data reported by Rusbonds Information Agency.

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