

FINANCIAL MARKETS IN JANUARY 2015

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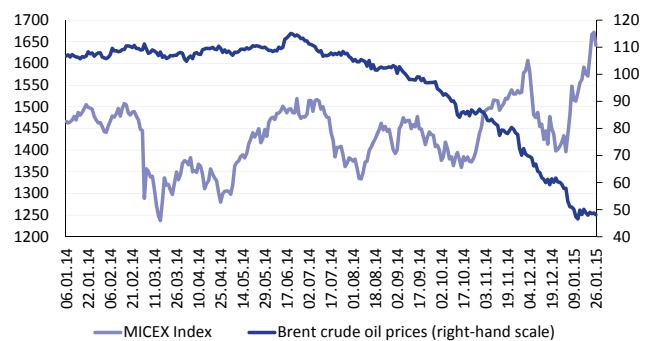
The MICEX Index skyrocketed in January 2015, gaining 16.44% in the period between the 5th and 26th of January. The Index hit its highest 1671.8 points on the 23th of January. At the same time, the crude oil Brent futures price dropped to 48,1 US dollars a barrel in the same month. The stock market capitalization by the 26th of January amounted to Rb 25,6 trillion (36.1% of GDP) (Rb 22,3 trillion as of the 19th of December last year). Both the accelerating dynamics of average weighted bond yield, tending towards deceleration though, and the deteriorated investment environment in the secondary market remained the key downtrend factors in the corporate bond market in January. The volume and the index of the corporate bond market saw positive dynamics while bond issuers and investors were highly active in the primary market. The situation with issuers' failure to discharge their obligations to bondholders saw some worsening early in the year.

Dynamics of the Russian stock market basic structural indices

The MICEX Index started to grow in January 2015, reaching 1547.4 points by the 8th of January from 1435.6 on the 5th of January. After two periods of correction, the first one began on the 8th and ended on 12th of January, and the second one began on the 16th and ended on 20th of January, the index gained 16.44% compared to the value seen early in the month, reaching 1671.8 points by the 23rd of January. At the same time, Brent crude oil futures prices kept declining from 53,1 US dollars a barrel early in January to 48,1 US dollars a barrel by the 26th of January.

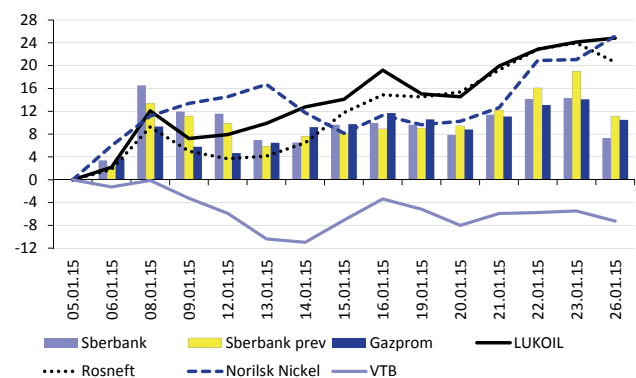
The MICEX Index grew in January basically in response to the growth in most liquid shares. Sberbank shares advanced in the period beginning on the 5th and ending on the 26th of January, its common shares were up 7.3% while preferred shares gained 11.1% during the same period. However, it is Lukoil shares and Norilsk Nickel shares that demonstrated a record high growth in January, having gained by the 26th of January 24.8% and 25.2% respectively since the beginning of the month. VTB shares slid down 7.2% in the period beginning on the 5th and ending on the 26th of January, and the bank reported that it expected its shares to drop further as a result of downgraded credit ranking.

The annual return on equity (highly liquid shares) during the period beginning on January 27, 2014 and ending on January 26, 2015, less the dividends paid in January, is shown in Fig. 3. Sberbank ROE went negative in the same period, facing a depreciation of 38.1% on common shares and more than 44.5% on preferred shares. On the contrary, Lukoil shares advanced by 46% during the year, most of the appreciation fell within the period between November and December 2014. Norilsk Nickel showed the highest



Source: RBK Quote.

Fig. 1. Dynamics of the MICEX Index and futures prices of Brent crude oil in the period between January 6, 2014 and January 26, 2015



Source: RBK Quote, author's estimates.

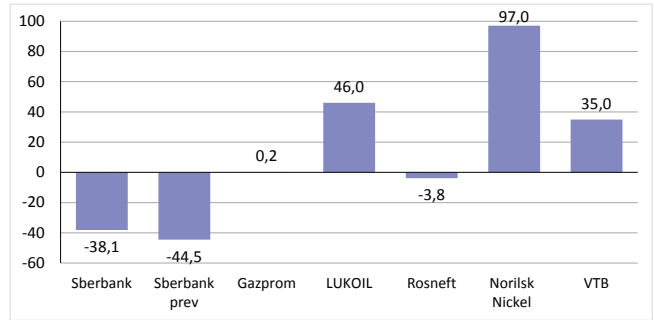
Fig. 2. Growth rates of most highly liquid Russian stocks in the Moscow Exchange in July (in the period beginning on the 5th and ending on the 26th of January, 2015)

annual ROE, facing almost double growth in value (a gain of 97.0%). VTB shares also advanced by 35% during the period beginning on January 27, 2014 and ending on January 26, 2015, being less than the ruble's devaluation during the same period, but higher

than interest rates on bank deposits. Gazprom's and Rosneft's annual ROE was 0.2% and -3.8% respectively. As a reminder, the data don't include the dividends paid, 7 rubles 20 kopeks (4.8% of the value seen as of the 26th of January 2015) on Gazprom shares and Rb 12,85 (5.4% of the value of shares as of the 26th of January, 2015) during 2014.

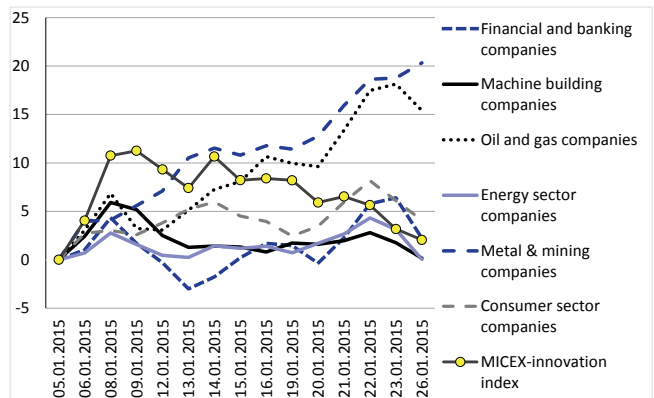
It is the metalworking index that showed highest rise among the sector indices in January 2015, up 20.3% in the period beginning on the 5th and ending on the 26th of January. The foregoing index was driven up by NMLK (Novolipetsk Iron & Steel Works) shares, Polymetal company shares and Norilsk Nickel shares. NMLK shares went up 25% in the period beginning on the 5th and ending on the 26th of January. Polymetal shares (the company contributed 15.14% to the metallurgical index as of the 26th of January) advanced by 18.6% by the 26th of January since the beginning of the month. The oil and gas index increased 15.4% in January. The index was driven up by basically Lukoil shares, however, it's worth noting that the following companies saw growth too: Novatec (up 10.6%), Gazprom (up 10.5%), Rosneft (up 20.6%) and Tatneft (up 20%). Other sector indices saw a growth less or equal to 4% by the 26th of January since the beginning of the month.

The Moscow Exchange trading turnover amounted to Rb 493,6bn in the period beginning on the 5th and ending on the 26th of January, corresponding the a daily average turnover of Rb 39,2bn. The daily average turnover in January was 35.2% less than that seen in December. Sberbank's total turnover on common and preferred shares contributed 28.1% on average to the stock exchange trading turnover in January, up 2% compared to that in December, and confirms that the market has been rebounding to a market normal trading condition. Gazprom shares contributed 15.1% on average to the stock exchange trading turnover in January, which corresponds to a normal market condition too. Therefore, the two most highly liquid



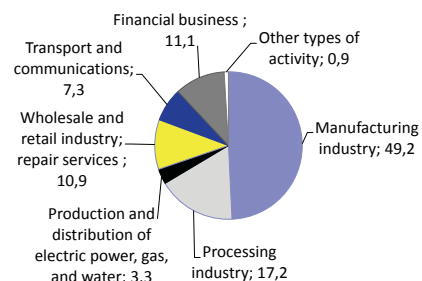
Source: RBK Quote, author's estimates.

Fig. 3. Growth rates of most highly liquid Russian stocks in the Moscow Exchange during the period beginning on January 27, 2014 and ending on January 26, 2015



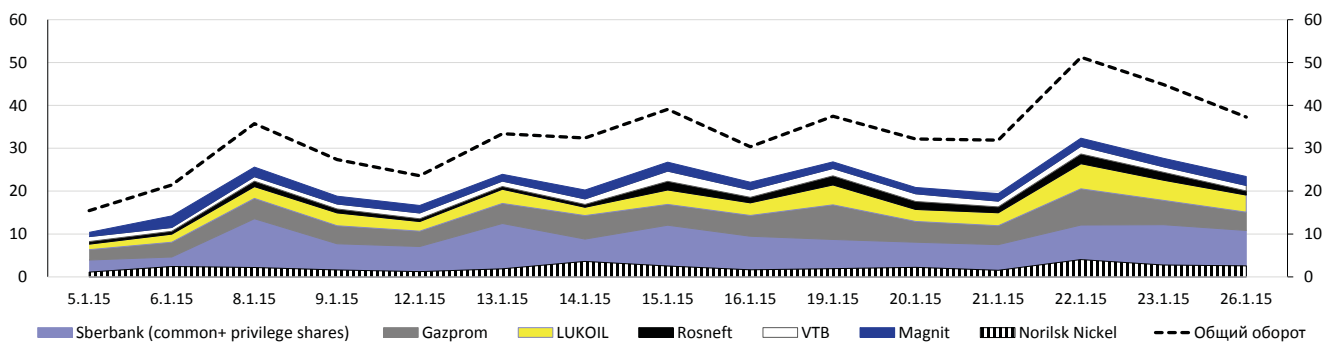
Source: RBK Quote, author's estimates.

Fig. 4. Growth rates in various sector stock indices in the Moscow Exchange (in the period beginning on the 5th and ending on the 26th of January, 2015)



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 beginning on the 5th and ending on the 26th of January, 2015)

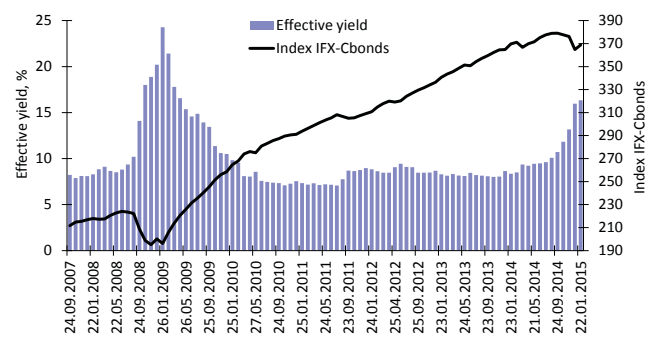
shares accounted for more than 43% of the Moscow Exchange trading turnover in January, up 4.5% over the value seen in December. The other top-5 shares with the highest trade volume accounted for an average of 30.6% of the Moscow Exchange trading turnover during the same month.

According to the Emerging Portfolio Fund Research (EPFR), foundations investing in Russian shares saw more than \$305,9m of capital inflow in the period beginning on the 1st and ending on the 21st of January. The Moscow Interbank Currency Exchange (MICEX) total capitalization amounted to Rb 25,6 trillion (36.1% of GDP) as of January 26, 2015, having increased by Rb 3 trillion and 166,8bn (14.1%) in the period since the 5th of January. In January, The share of extracting companies in the MICEX capitalization structure increased by 1.05 p.p. to 49.24%. The share of the manufacturing industry went up 0.97 p.p. to 17.2% as well. On the contrary, the share of transport and communication companies and the retail trade sector went down 0.15 p.p. to 7.3% and 10.9% respectively.

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) kept growing fast early in 2015, although the growth rate wasn't as record-high as it was in December. The value reached Rb 6604,2bn by the end of the month, up 3.5% over the value seen as of the end of December¹. At the same time, bond issues kept growing in number during the elapsed period (1074 corporate bond issues registered in the national currency against issues as of the end of December), while the number of issuers in the debt segment increased too, whose number remained almost unchanged throughout the entire fourth quarter last year (355 issuers against 345 companies). 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 kept declining driven by seasonal factors. For instance, the Moscow Exchange total trading volume amounted to Rb 58,8bn in the period beginning on December 20, 2014 and ending on January 22, 2015 (to compare, the trading volume amounted to Rb 71,0bn in the period between November 25 and December 19 last year). On the contrary, the number of transactions in the period under review remained at its maximum, 30,100 (30,500 stock-exchange transactions were



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

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

closed during the previous period)², implying that the securities were appealing to retail investors.

The Russian corporate bond market index IFX-Cbonds attempted to rebound following the 2-month downtrend. By the end of January, the index went up 3.9 points (or 1.1%) over the last year-end value. However, the corporate bond average weighted yield saw negative dynamics amid a hard-line monetary policy, making a new record of 16.34% by the end of January up from 15.97% late in December 2014, showing the highest value since the onset of 2009 crisis (see Fig. 7)³. The corporate bond portfolio duration also kept declining: it was 318 days as of the end of January, 30 less than that seen as of the previous month end. The fall in duration is driven by the growth in interest rates in the bond market.

Late last year – early this year, Russia's domestic corporate bond market was driven by adverse developments and downtrends. During the same period the market was "overwhelmed" by the wave of downgraded sovereign and sub-sovereign and corporate credit ratings/forecasts. Fitch Ratings was first to downgrade the rating for Russia to BBB-, the rating outlook is negative, then Moody's downgraded its rating for Russia at Baa3. The sovereign rating was followed by downgrades of ratings/forecasts on Russia's large issuers such as Sberbank of Russia, Vnesheconombank, Russian Agricultural Bank, Gazprom, Lukoil, Rosneft, Novatec, Russian Railways, Federal Grid Company of the United Energy System of Russia (RGC UES), Norilsk Nickel, Rostelecom and others. Later, Russian rating agencies began to downgrade credit ratings (basically on issuers in the banking sector).

Even the most liquid segment of the corporate bond market saw high, both upward and downward, volatility in yields in the period under review. The yield of bonds issued by OJSC VTB Bank, OJSC

1 According to the data provided by Rusbonds Information Agency.

2 According to the data provided by Finam Investment Company.

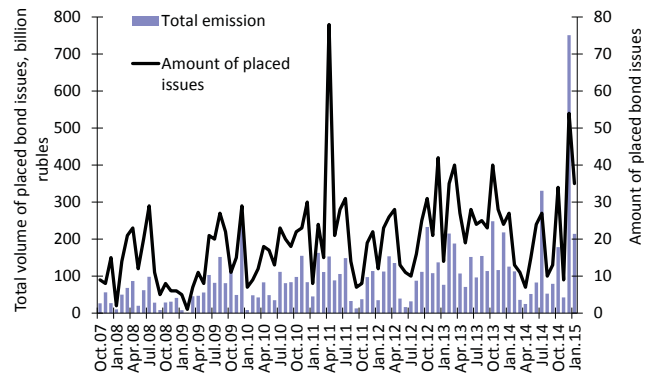
3 According to the data provided by Cbonds Information Agency.

MOSCOW CREDIT BANK, CJSC Raiffeisen Bank, OJSC Norilsk Nickel kept skyrocketing (more than 4 p.p.). Certain bond issues of financial and production companies (including their affiliates) showed highest growth (more than 4 p.p.), namely Open Joint-Stock Company Agency for Housing Mortgage Lending, OJSC ALFA-BANK, OJSC Gazprombank, PJSC Zenit Bank, OJSC Metalloinvest Holding Company, OJSC VympelCom, OJSC RUSAL Bratsk Aluminum Smelter, JSFC Systema.

At the same time, despite the adverse market trends, the interest rates on certain high-rated loans began to decline. High-tech companies saw the most marked downtrend (by 3 p.p. on average) among liquid securities. The yield rate on securities in the production and energy segments saw a less market downtrend (by an average of 1.0 p.p. and 0.7 p.p. respectively). The financial segment saw the largest pressure on the yield rates: on average, the yield rate on financial companies' liquid securities remained unchanged, although there was a visible downtrend in the yield rate on certain issues of securities. At the same time, investors were relatively less interested in financial companies as well as regional energy operators¹.

Despite high yield rates, issuers were fairly active in new fundraising late in December 2014 – early in January 2015, although registration figures declined several times compared to the record figures seen in the previous month, owing to a seasonal downtrend in the market activity and a great deal of holidays. For instance, nine issuers registered 14 bond issues at an aggregate par value of Rb 110,9bn in the period beginning on December 20, 2014 and ending on January 22, 2015 (to compare, 50 bond issues at an aggregate par value of 994,3bn Rb were registered in the period between November 25 and December 19 last year)². Major bond issues were registered by CJSC Mortgage Agent Absolut, The State Company Russian Highways (Avtodor), CJSC Mortgage Agent AIJK 2014-2. Stock-exchange traded bonds accounted for less than one fourth of registered bond issues, while a few debut issues were also registered in the period under review.

The situation in the primary market was optimistic again, although it cannot be compared with the latest record, because the bond placement statistics at that time were drastically influenced by a major market player. For instance, in the period beginning on December 20, 2014 and ending on January 22, 2015 25 issuers placed 35 bond issues at an aggregate par



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

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

value of Rb 214,3bn (to compare, 54 series of bonds at a record par value of Rb 751,1bn were placed in the period between November 25 and December 19 last year, although as early as the end of October – early in November the volume of issues amounted to only Rb 42,3bn) (Fig. 2). Major bond issues were placed by CJSC Mortgage Agent Absolut, LLC VTB Leasing Finance, PJSC Khanty Mansi Bank Otkrytiye³. Stock-exchanged traded bonds accounted for almost two thirds of the bond issues placed in the period under review, and quite a few number of debut issues were placed. Despite the complex situation faced by the financial markets, most issuers managed to borrow for a long term, namely four mortgage agents raised funds for a period ranging between 19 and 43 years, one issuer for 15 years, and another seven issuers borrowed for 10 years.

Late in December 2014 – early in January 2015, the Bank of Russia declared void 12 corporate bond issues for non-placement of securities or issuers' giving up their fundraising plans, and hence cancelled registration of these issues (all of the issues offered in the primary market in the same period last year were placed with success)⁴. The financing plans were revised due to the drastic increase in interest rates in the debt market.

Despite the complex economic situation, all 14 issuers repaid their 16 bond issues at an aggregate par value of Rb 34,5bn in the period between December 20, 2014 and January 22, 2015 (all issuers honored their obligation in due time in the preceding period). Sixteen corporate bond issues at a total of Rb 69,5bn, as well as a single bond issue of \$500m⁵ are to be repaid in February 2015.

1 According to the data provided by Finam Investment Company.

2 According to the data provided by Rusbonds Information Agency.

3 According to the data provided by Rusbonds Information Agency.

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

5 According to the data provided by Rusbonds Information Agency.

The situation with issuers' failure to discharge their obligations to bondholders saw some worsening late in December 2014 – early in January 2015. Only a single issuer announced a technical default on coupon yield payment accrued on its two issues (a few technical and real defaults were announced in the pre-

ceding period)¹. At the same time, no real defaults² on coupon yield payment and early redemption(s) of securities on the put date and full repayment were announced in the bond market in the period under review. ●

1 According to the data provided by Rusbonds Information Agency.

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