

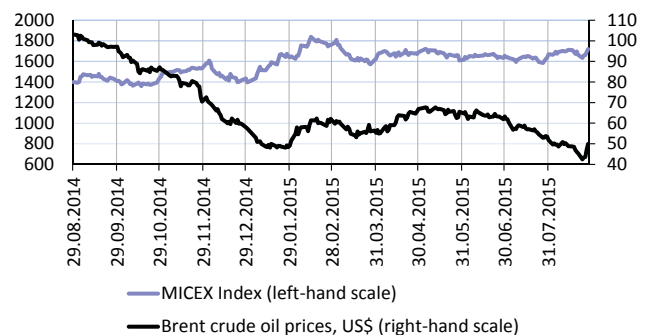
RUSSIA'S FINANCIAL MARKETS IN AUGUST 2015

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The MICEX Index in August showed a growth of more than 7% with an average of 1677 index points regardless of the fact that crude oil prices saw a downside trend. All of the Industry Indices were growing, of which the Chemical and Petrochemical Index advanced higher than others (+17.2%). Russia-focused mutual funds continued to see investments outflow for the fourteenth straight week, almost \$880m since the beginning of the year. The situation in the Russian domestic corporate bond market deteriorated gradually due to adverse trends in the external markets. The key adverse developments were driven by the weighted average yield rate of bond issuances, and issuers' defaults on obligations to bondholders still remained a problem. Nevertheless, the key market indicators such as the corporate bond market volume and index followed moderately positive dynamics; investors' activity in the primary and secondary markets was kept at an average level.

The dynamics of basic structural indices in the Russian stock market

After the 3% fall during the previous period under review the MICEX Index saw incremental advancement throughout the entire first half of August, reaching by 14 August 1712 index points¹ (a growth of 6.7% compared to the value seen in the beginning of the period under review²). Then by 24 August the Index reverted to its initial values driven largely by oil price fluctuations as a key factor. The plummeted oil prices on 24 August (the price on that date dropped by more than 6% to 42.44 dollars per barrel, lowest since 2009) had a strong effect on the Russian stock market quotations. Oil prices neared close to 50 dollars per barrel by the end of the period under review. The month-end fall of oil prices was 5.9%. In the last week of August the MICEX Index totally rebounded from the previous fall and ended the period with a total growth of 7.1%.



Source: Quote RbC, Finam.

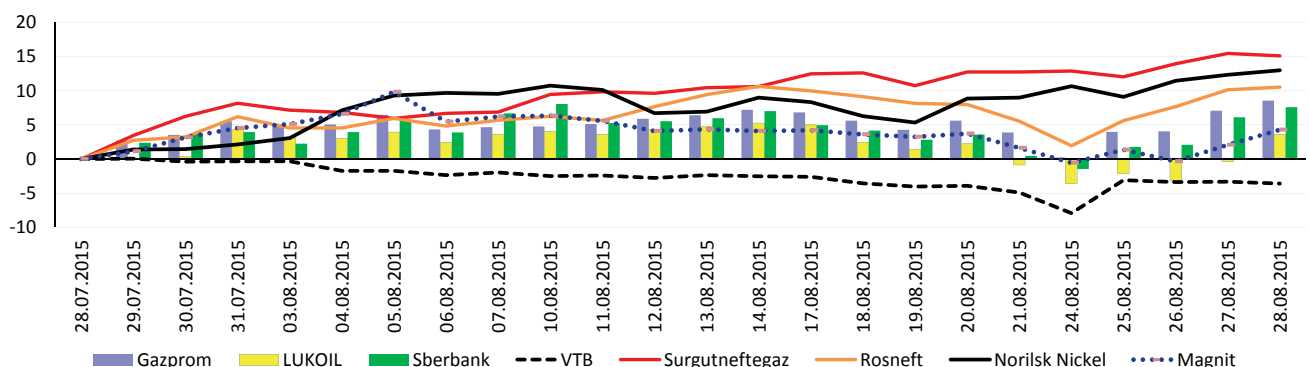
Fig. 1. The dynamics of the MICEX Index and futures prices of Brent crude oil in the period between 29 August 2014 and 28 August 2015

The current period under review, as opposed to the previous one, the shares of almost all highly liquid companies³ showed bottom-line growth of quotations. Surgutneftegaz's preferred shares (+15.1%), Norilsk Nickel's shares (+13.0%) and Rosneft's shares were

1 The data hereinafter are MICEX closing data.

2 The period under review refers to the period between 28 July 2015 and 28 August 2015

3 Companies with an average trading volume of more than Rb 1bn daily in the period under review.



Source: Quote RbC, author's calculations.

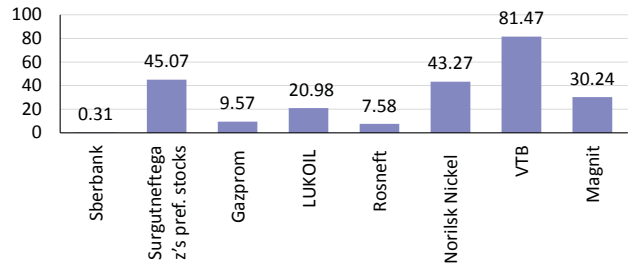
Fig. 2. Growth rates in quotations of Russian highly liquid stocks in the Moscow Exchange in the period between 28 July 2015 and 28 August 2015

among the top3 leaders during the month (+10.5%). VTB was the only one in the red line at the month's end (-3.6%). The fall of quotations which in the fourth week of August affected first of all oil producing companies and banking sector companies was driven by plummeting oil prices and the ruble exchange rate. Oil prices were corrected rapidly as was the case with quotations of stocks. Even LUKOIL which early in the month was hit most by the slump of oil prices (-3.5%) managed to end up at a positive level the period under review.

VTB Bank still remained the ROE leader (+81.5%) thanks to an unprecedented growth which took place in May 2015. Surgutneftegaz's preferred shares were 2nd in terms of annual return among the blue chips (+45.1%), Norilsk Nickel moved down at the bottom of the top3 (+43.3%) from the 2nd in the previous period under review. Additionally, it is worthwhile noting that Magnit's shares advanced more than a 30%. Sberbank's shares for the first time over the last four months showed a positive return, a purely symbolic though (+0.3%).

The Chemical and Petrochemical Index was leading for the second straight month among the industry indices, this time mostly due to a more than 20% growth of Uralkali's shares. The Index closed 17.2% at the end of the month. It should be noted that none of the industry indices was found to be in red at the end of the period under review. The least successful industries such as the Energy Index and the Finance Index advanced 1.6% and 1.8% respectively. The shares of companies operating in the oil & gas, transport and telecommunications industries, as well as the metal & mining industry showed a growth of 7-8%.

The Moscow Exchange's (MOEX) turnover increased for the first time after the three previous months of fall, reaching the last year level (in terms of par value of securities). The MOEX turnover in the period between 28 July and 28 August amounted to Rb 767.3bn, being equal to Rb 32.0bn daily turnover, i.e. more than 20%



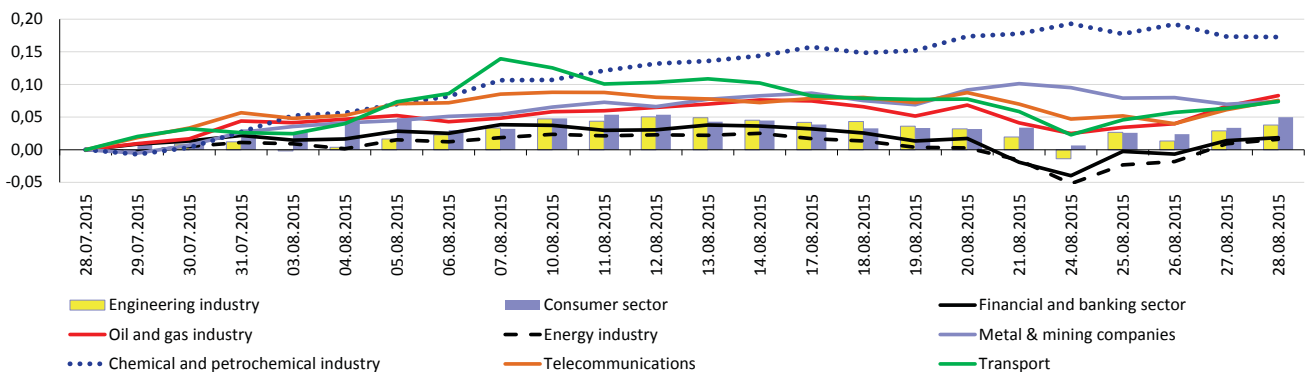
Source: Quote RbC, author's estimates.

Fig. 3. Growth rates in the value of highly liquid Russian stocks in the Moscow Exchange in the period between 28 August 2014 and 28 August 2015

above the last month turnover, yet 4% lower than the average daily turnover in Q2 2015.

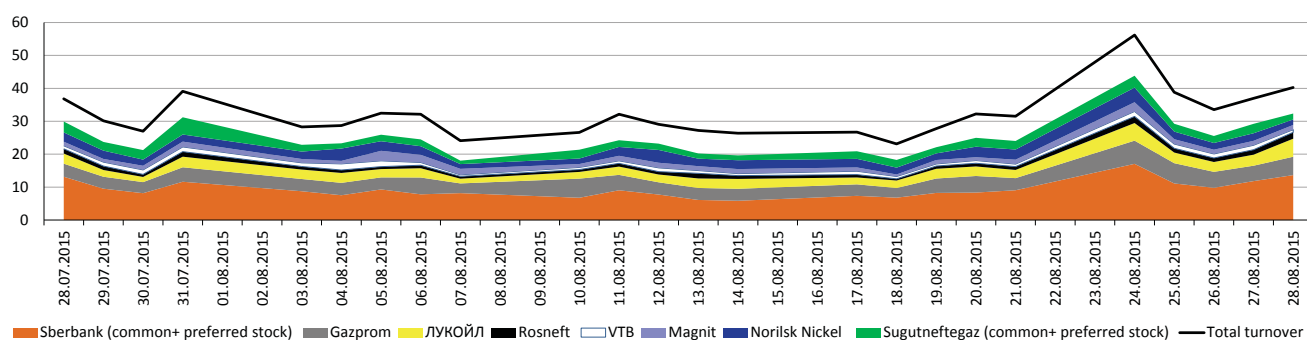
Sberbank's shares kept leading in terms of its share of MOEX turnover despite a loss of 2% of the total turnover vs. the previous month. The share of Sberbank in the MOEX turnover (28.6%) was twice as much as that of Gazprom which was second (13.5%) after Sberbank in terms of MOEX total turnover. Gazprom is followed by LUKOIL and Norilsk Nickel which had almost the same share of the MOEX turnover (8.6% and 8.4% respectively). The top-3 leaders accounted for 50.7% of the total MOEX turnover (almost 4% more than in the previous month), the next top5 accounted for another 27.4%. Collectively, the top-8 largest companies accounted for 78.1% of the turnover, up 1% compared to the value seen in the previous reporting period.

Russia-focused mutual funds continued to see investments outflow. According to the data provided by the Emerging Portfolio Fund Research (EPFR), within four weeks of August (from 30 July to 26 August) the total outflow amounted to \$630.4m, of which \$433.5m fell on the last week of the month (from 20 to 26 August), this is the biggest outflow of investment since the beginning of 2015. The outflow as of 26 August continued for the fourteenth straight week, and the total outflow amounted to near \$880m.



Source: Quote RbC, author's calculations.

Fig. 4. Growth rates in various sector stock indices in the Moscow Exchange in the period between 28 July 2015 to 28 August 2015



Source: RbK Quote, author's calculations.

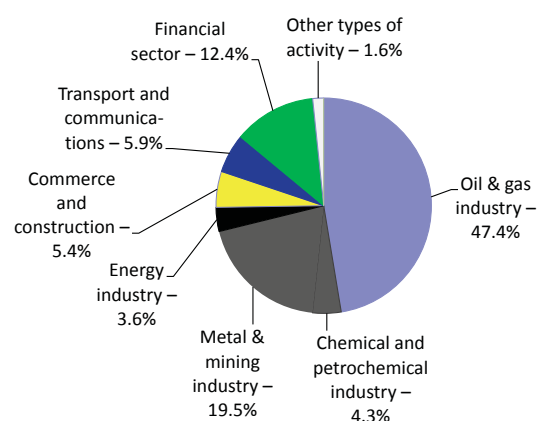
Fig. 5. The structure of Moscow Exchange trading volumes in the period between 28 July 2015 no 28 August 2015

The MICEX total capitalization as of 28 August 2015 amounted to Rb 29.19 trillion (40.9% of GDP), more than 8% above the value seen in the previous month. The metal and chemical industries continued for the second straight month to gain in terms of the share of MICEX capitalization (in August +1.0% and +0.6%, respectively), whereas the financial sector lost more than 1% of the capitalization. The oil & gas industry gained and the energy industry lost 0.3% of the capitalization. Other industries saw insignificant changes in their share of the MICEX capitalization.

Corporate bond market

The volume of Russia's domestic corporate bond market (measured by the par value of outstanding ruble-denominated securities including those issued by non-residents) in August kept growing, though at a relatively slow pace. By the end of the month the volume hit again the all-time highest, reaching Rb 7654.4bn, 1.0% above the value seen as of the end of July¹. The past period saw no substantial changes in the number of both outstanding bond issuances (1149 corporate bond issuances denominated in national currency were registered versus 1144 issuances registered as of the end of July), and issuers represented in the debt segment (375 issuers against 374 companies in the previous month). Seventeen dollar-denominated bonds issuances of Russian companies (worth a total of more than \$2.4bn), one JPY-denominated bond issuance remained outstanding in the market.

Investors' activity in the secondary corporate bond market in August remained at its average annual level. For instance, the MOEX total trading volume was in the period between 23 July 2015 and 26 August 2015 was running at Rb 125.9bn (by contrast, the trading volume in the period between 23 June 2015 and 22 July 2015 was equal to Rb 124.3bn). Again the number of transactions in the period under review increased substan-



Source: The Moscow Exchange official website, Gaidar Institute's calculations.

Fig. 6. The structure of stock market capitalization by type of economic activity as of 28 August 2015

tially to 33,000 (by contrast 26,900 MOEX transactions were registered in the previous period), thus showing growing interest in securities by retail investors².

The Russian Corporate Bond Market Index (IFX-Cbonds) in August kept growing steadily. The Index increased 4.1 index points (or 1.0%) by the end of the month compared to the value seen at the previous month's end. However the corporate bond average weighted yield showed negative dynamics in the past period, increasing from 12.23% in late July to 12.33% by late August, still being much higher than the central bank base rate which in late July was cut from 11.5% to 11.0% (Fig. 7)³. The corporate bond portfolio duration was driven by negative dynamics for the fifth straight month – 380 days as of the end of August, 28 days less than that seen as of the end of July. In this particular case, these developments are the reflection of both shorter average maturity of securities in the market and a certain increase in the yield rate.

All in all, the most liquid segment of the corporate bond market saw some increase in the bond yield

1 According to the data provided by Rusbonds Information Agency.

2 According to the data provided by Finam Investment Company.

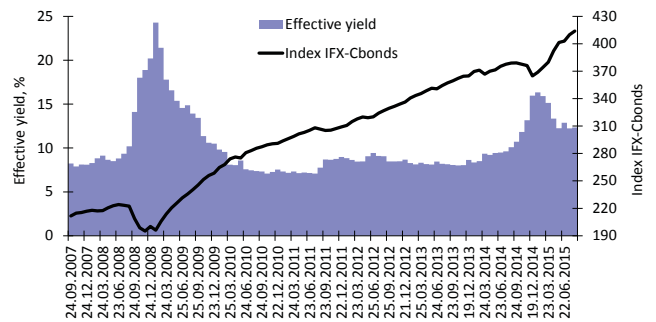
3 According to the data provided by Cbonds Information Agency.

rates. Securities of financial segment issuers were distinguished by high volatility. For instance, Bond issuances of the following companies saw most of the interest rate decrease (more than 2 p.p.): AO Alfa-Bank and OAO Binbank, whereas a substantial growth was seen at again AO Alfa-Bank and VTB Bank. In the past period however, like in the previous one, most liquid securities of production and financial companies showed stabilization in terms of the change in rates, and the yield increased substantially in the technology segment (by an average of 0.9 p.p.)¹. The energy sector was driven moderate growth in the yield, by an average of 0.3 p.p. Securities of financial and production companies, in particular the bonds of such issuers as Gazprombank, Russian Railways, VTB Bank, saw higher demand by investors. At the same time investors paid no attention to the securities of regional energy companies.

Issuers' activity in seeking new fundraising remained low in the period under review, which can be explained by a seasonal factor. For instance, five issuers registered 11 ruble-denominated bond issuances with an aggregate par value of Rb 51.2bn in the period between 23 July and 26 August (by contrast, 10 ruble-denominated bond issuances with an aggregate par value of Rb 71.3bn were registered in the period between 23 June and 22 July)². Two issuers – AO Freight One and ZAO O1 Properties Finance – accounted for the highest value of bond issuances. In addition, JSC Transcapitalbank registered a foreign currency bond issuance at a value of \$60m.

It should be noted that the practice of registering programs of exchange-traded bonds has in recent months been spreading wide among large bond issuers. For example, the Moscow Exchange as early as the beginning of August registered VTB Bank's program of exchange-traded bonds worth Rb 1 trillion (or an equivalent value in the foreign currency) with up to 30 years of maturity and Uralkali's program of exchange-traded bonds at Rb 100bn (or an equivalent value in the foreign currency) with up to 10 years of maturity. In the near future this trend will be further developing. For example, JSC Binbank approved a program of exchange-traded bonds with a volume of up Rb 200bn (or an equivalent value in the foreign currency) with up to 30 years of maturity. A similar large-scale program was approved by the management of Polyus Gold.

Considering popularity of the practice of registering programs of exchange-traded bonds, the Russian Ministry of Economic Development (MED) has suggested that the practice should be applied to mort-

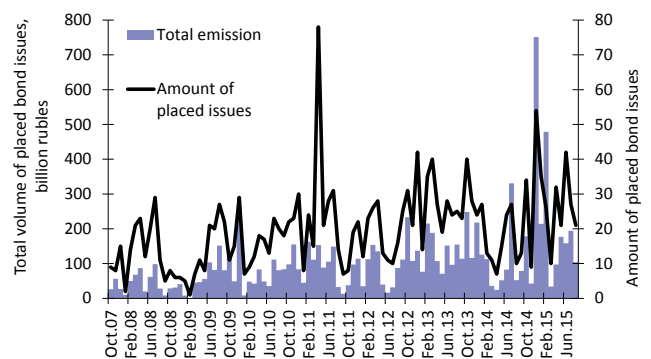


Source: According to the data provided by Cbonds Information Agency .

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

gage securities for the purpose of reducing the term and simplifying the procedure for issuing residential mortgage-backed bonds, because under the applicable law mortgage bonds must have separate issuances. It is the MED's opinion that the emergence of the new instrument for mortgage securities will result in a higher level of standardization of mortgage-backed securities, which will ultimately have a positive effect on the liquidity of instruments and the value of resources raised in the mortgage sector³.

Investors' activity in the primary market decreased too, remaining at its average annual level. For instance, in the period between 23 July 2015 and 26 August 2015 15 issuers placed 21 ruble-denominated bond issuances with an aggregate par value of Rb 104.0bn (by contrast, 27 bond issuances with an aggregate par value of Rb 194.2bn were placed in the period between 23 June 2015 and 22 July 2015) (Fig. 8). Large bond issuances were placed by OAO Russian Agricultural Bank, OAO PIK Group of Companies, JSC Otkritie Holding⁴.



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

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

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 Interfax Information Agency
4 According to the data provided by Rusbonds Information Agency.

In addition, OAO VEB Leasing placed bonds denominated in foreign currency at a value of \$200m. Half of the bonds placed in the period under review were exchange-traded bonds. Despite a tough situation in financial markets and shortening duration, most of bond issuers managed to raise funds with quite a long maturity: Eclipse-1 Mortgage Agent issued bonds with a maturity of more than 32 years, Lenta Company did the same with a maturity of 15 years, another 8 issues issued bonds with a maturity of 10 years.

None of the corporate bond issuances was cancelled in August by the Bank of Russia on the grounds that not a single security was placed (a record number of 32 corporate bond issuances were cancelled in July, 2-3 bond series were cancelled on the same grounds in a few previous months)¹. This suggests that companies are still waiting for better market conditions to be able to issue bonds.

In the period between 23 July 2015 and 26 August 2015, all of the nine 9 bond issuers redeemed their

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

ruble-denominated debts with an aggregate par value of Rb 56.7bn (in the previous same period, all of the bond issuers met their obligations in due time, and no technical defaults occurred). Eighteen corporate bond issuances worth a total of Rb 72.5bn are due for maturity in September 2015²

However, issuers' failure to meet obligations to bondholders was still a problem: Utair Finance (Limited Liability Company) declared actual default apart from a few technical defaults³, failing to redeem bond issuances on put date and a few coupon payments (a few technical and actual defaults on coupon yield payment and redemption of the par value were announced in the previous same period.⁴) ●

2 According to the data provided by Rusbonds Information Agency.

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

4 According to the data provided by Rusbonds Information Agency.