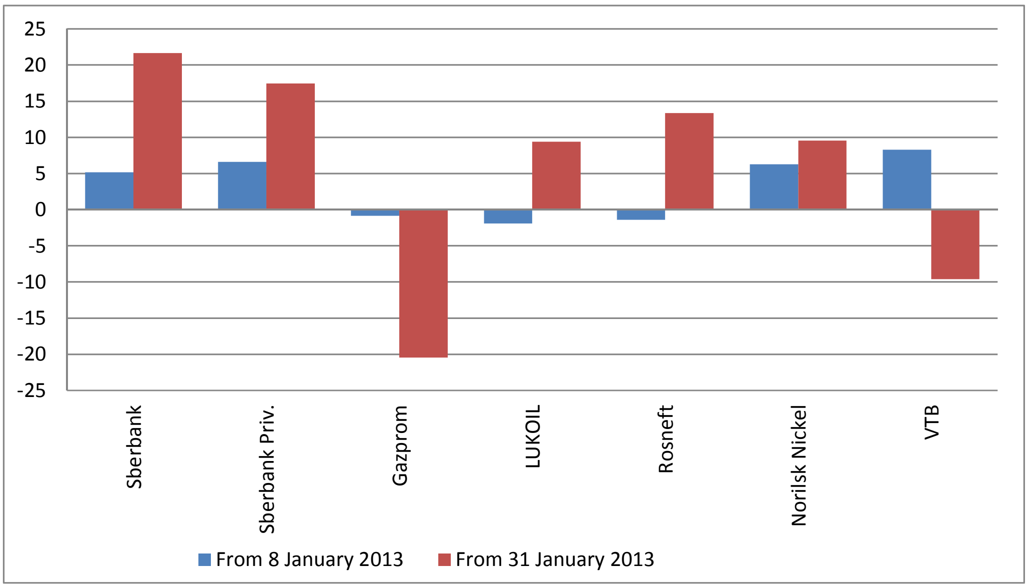
Nikita Andrievskiy, Elizaveta Khudko

Financial Markets

The new year's beginning was marked by a generally positive behavior of the stock market. The quotation changes displayed by major Blue Chips over January were multi-vectored. At the same time, it should be noted that the observed growth in prices was sustained by Russian investors, while foreign market participants continued to withdraw their resources from the Russian market. January also saw a rather favorable situation on Russia's domestic corporate bond market. The activity of the market's biggest bond emitters in registering their new issues hit its several-year high, while at the same time many big companies gave up their plans to place their previously registered bond loans, and so these issues were annulled.

The Movement of the Russian Stock Market's Main Structural Indices

In January (from 8th through 31st), the MICEX Index rose by 2.11% to 1,546.76 points, which is 2.16% above its value as of 31 January 2012. The movement of the main Blue Chip stocks over that month was multi-vectored. Thus, for example, *Sberbank*'s shares climbed 11%, *Norilsk Nickel*'s - 4%, and *VTB*'s – 1.6%. The value of shares issued by oil and gas companies over January moved in the other direction and on the average dropped by 1.6%. Thus, *Sberbank*'s shares in January demonstrated the highest yield per invested ruble – 11.4 kopecks; while the highest loss per invested ruble (3.9 kopecks) was on *LUKoil*' shares. In annual terms, however, their movement is somewhat different. Thus, the value of VTB's shares declined on its index as of 31 January 2012, and so the investors' loss amounted to 20.9 kopecks per invested ruble. The losses sustained by investors in *Gazprom* were somewhat greater – more than 22.7 kopecks per invested ruble as of 31 January 2012. The growth rate displayed by other companies' capitalization was from 3% to 21.5% per annum. This growth occurred in response to the positive stock movement on the world's major trading floors. In this connection it should be noted that the rising quotations were sustained by Russian investors, while foreign participants continued to steadily withdraw their resources from the Russian market.

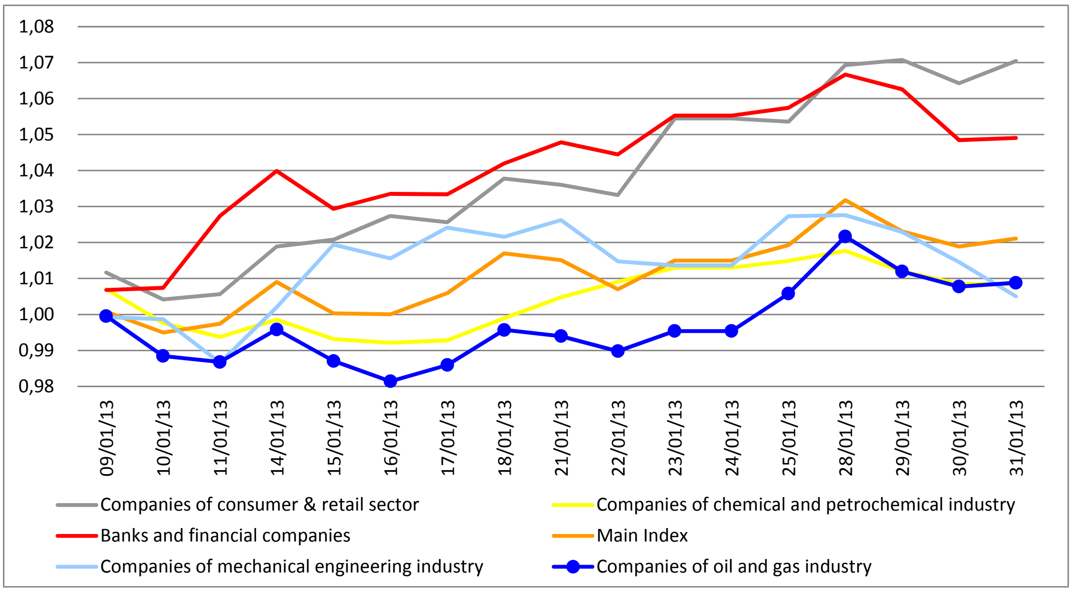


Source: Quote.rbc.ru; the author's calculations.

***Fig. 1.* Growth Rate of Blue Chip Stocks on the MICEX, %**

December 2012 saw only one placement of Russian shares – the shares in Open-end Joint-stock Company *Multisistema*, a holding company specializing in the construction, assembly and maintenance of engineering systems, and also the equipment for the housing and utilities sector. The total face value of the placed shares is Rb 9.8m, which in no way influenced the stock market's structure over that month (the MICEX's total capitalization in Q4 2012 amounts to more that Rb 24 trillion). The total face value of shares placed on Russia's domestic stock market in 2012 is Rb 49.6bn (for reference: the total face value of shares placed on foreign markets is Rb 267bn).

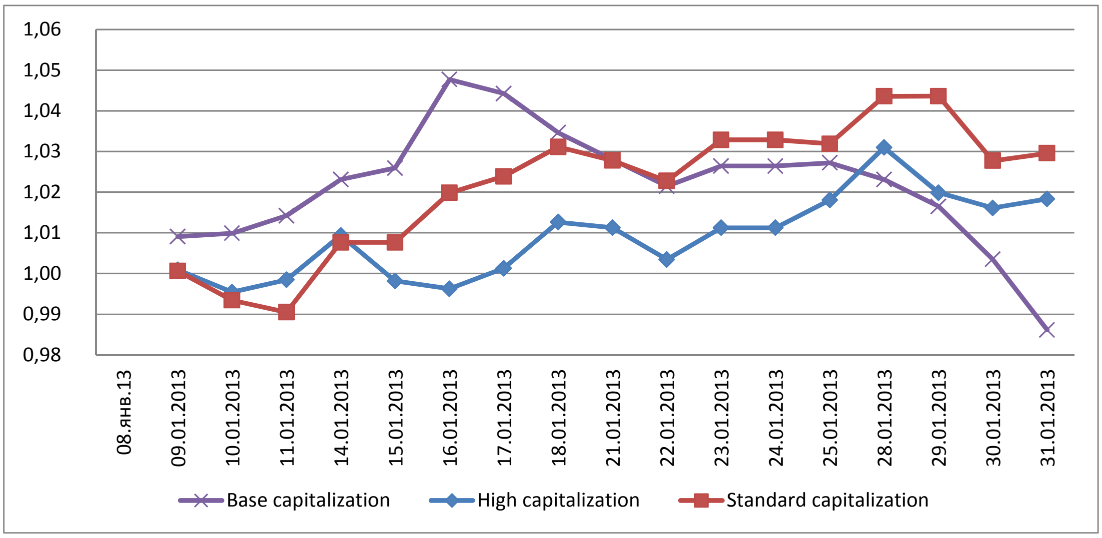
The beginning of the new year on the stock market was marked, on the whole, by a positive movement of stock indicators. The Main Index of the Moscow Exchange over the period from 8 through 31 January 2013 rose by 2.11%, while displaying noticeable variances in its behavior in different sectors (*Fig. 2*).



Source: Quote.rbc.ru; the author's calculations.

***Fig. 2.* Movement of the MICEX Stock Indexes**

Thus, the New Year holidays and the expectations of incomes from 'holiday sales' pushed up the consumer & retail sector index by 15.4. The value of shares in mechanical engineering companies, as well as that of banking and finance sector shares, grew above the prescribed 10% threshold. It may be assumed that this result was achieved due to the high return on equity demonstrated by Russia's biggest banks and the underestimated value of the shares issued by the mechanical engineering industry's companies throughout the year 2012. The rate of growth displayed by the latter category of shares was, in fact, even higher than that of the shares in oil & gas companies. At the same time, the growth rates of the stock indices of chemical and petrochemical companies have been fluctuating around zero. Such values of these indices point to a low degree of investors' interest in the shares issued by companies belonging to that sector – mainly because they are part of vertically integrated holding companies, which do not permit the issuance of a more or less significant number of securities.

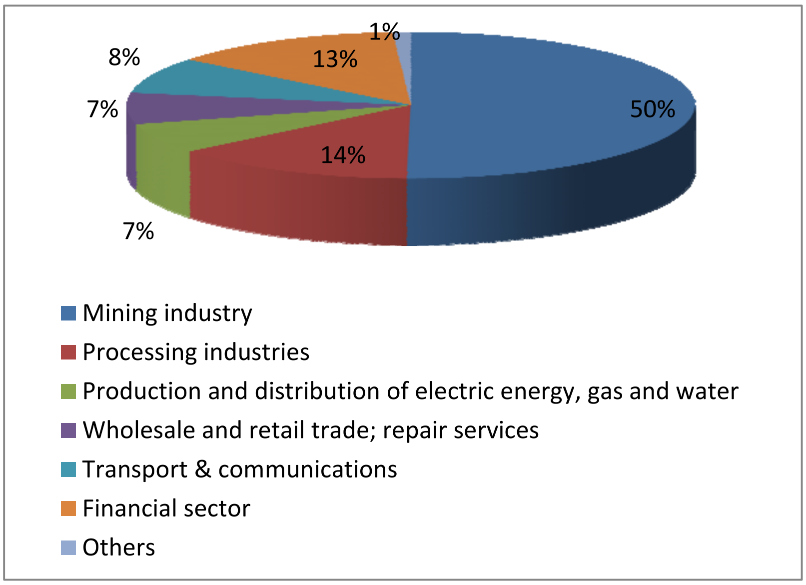


Source: Quote.rbc.ru; the authors' calculations.

***Fig. 3.* Changes in the Capitalization Indices of the Stock Market**

MICEX MC, the index of shares in Russian companies with standard capitalization (30 companies with an aggregate market capitalization of Rb 12.3 trillion and an average market capitalization of Rb 412bn), had caught up with MICEX LC, the index of shares in Russian companies with high capitalization, which grew at a rate of 7.9%. Thus, the rise in the capitalization of the companies included in MICEX MC amounted to 8.1%. Meanwhile, over the course of December 2012 and the first two weeks of January 2013, MICEX SC, the index of companies with base capitalization (50 companies with an aggregate market capitalization of Rb 16.6 trillion and an average market capitalization of Rb 333bn), increased by 12.7%.

In 2012, the by-sector capitalization structure on the Russian exchange continued to be dominated by companies belonging to the extracting sector (50.2%), followed by the financial sector (13.3%) and the processing sector (13.9%), which indeed correlates with the by-sector structure of the real sector.



Source: the MICEX's official website; the authors' calculations.

***Fig.* 3. Structure of Capitalization of the MICEX Stock Market, by Type of Economic Activity**

The Corporate Bond Market

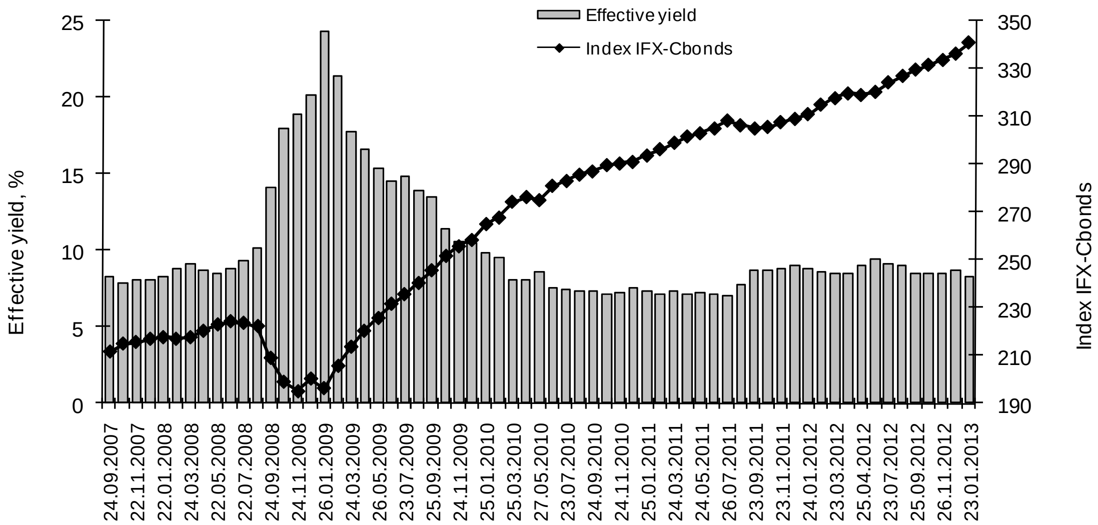
At the beginning of 2013, the volume of Russia's domestic corporate bond market (by the nominal value of ruble-denominated securities in circulation) continued to grow, reaching the level of Rb 4,147.5bn, which represents a 2.7% rise on the end of December 2012 (in the previous several months, it had been growing at an average rate of 1.5% per month)[1]. The increase in the volume of the market was once again caused by growth in the number of issued bond loans (894 ruble-denominated corporate bond issues vs. 881 issues as of the end of the previous month). At the same time, the number of emitters represented in the debt segment remained almost unchanged (337 vs. 338 in December). The ruble-denominated bond issues in circulation included several bond issues of foreign emitters (the International Finance Corporation, the European Bank for Reconstruction and Development, and *Uranium One Inc*.). Several U.S. dollar-denominated bond issues and one yen-denominated bond issue were still in circulation.

In late December 2012 and January 2013, the secondary corporate bond market saw a rise in investment activity, mainly accounted for by the final trading days of last year. Thus, from 24 December through 23 January, the combined volume of exchange transactions carried out on the Moscow Exchange amounted to Rb 146.5bn (for reference: from 26 November through 21 December, the trade turnover was Rb 129.1bn), while the number of transactions carried out over the period under consideration amounted to 26.5 thousand (vs. 27.5 thousand in the previous period)[2].

The IFX-Cbonds index of the Russian corporate bond market continued to rapidly rise. By late January 2013, it had climbed up by 4.4 points (or 1.3%) from the end of 2012. Having slightly increased in December, the weighted average effective yield on corporate bonds considerably dropped – from 8.67% as of the end of the previous month to 8.29% (*Fig. 5*). Both the rise in the yield at the end of a year and its drop at the beginning of a year are the seasonal phenomena that have been repeatedly observed in recent years[3].

After a short period of growth at the end of 2012, the corporate bond portfolio duration index resumed its downward trend. As of the end of January, this index amounted to 571 days, which represented a 30-day drop on the end of December. That drop in the corporate bond portfolio duration index reflected a reduction in bond loans' periods of circulation in the corporate segment.

[1] According to data released by the Rusbonds information agency.
[2] According to data released by the Finam company.
[3] According to data released by the Cbonds company.



Source: According to data released by the Cbonds company.

***Fig. 5.* Behavior of the IFX-Cbonds Index of the Russian Corporate Bond Market and the Dynamics of its Weighted Average Effective Yield**

The most liquid bond issues demonstrated fall of their yields (by 0.3-0.4 pp., on average). The only exception was the Bank of Moscow's issue of Series 02 bonds. Like in December 2012, the biggest bond-yield losers (by more than 1 pp.) were securities issued by manufacturing and energy companies. By the end of January the yields on the bond issues of high-tech companies remained almost unchanged[4].

At the end of 2012 - start of 2013, bond issuance exceeded all forecasts, hitting a several year high. Thus, over the period from 22 December through 23 January, 14 emitters registered 99 bond issues with a total face amount of Rb 793bn (vs. 33 bond issues with a total face amount of Rb 148.4bn registered from 27 November through 21 December). However, it should be noted that in the main those record-high achievements resulted from the registration of the 51 commercial paper issues with a total face amount of Rb 500bn, released by JSC *Sberbank Rossii* [The Savings Bank of the Russian Federation]. Large issues of securities were also registered by JSC *AKB Bank Moskvy* [the Joint-Stock Commercial Bank of Moscow] (8 series of commercial papers with a total face value of Rb 60bn), LRC *EvrazHoldingFinans* [the Eurasian Financial Holding Company] (4 series of bonds with a total face value of Rb 50bn), JSC *Novolipetskii Metallurgicheskii Kombinat (NLMK)* [Novolipetsk Metallurgic Combine] (7 series of bonds with a total face value of Rb 50bn), JSC *RusGidro* [Federal Hydro-Generating Company] (4 series of bonds with a total face value of Rb 40bn)[5]. More than two-thirds of the registered issues were commercial papers.

While the end of a year is always a time of hectic bond registration activity (although last year's end has broken all records in this respect), placement of securities in the immediate pre- and post-New Year's eve period is usually a much more subdued and humble affair, which can be explained by low investor activity in January. Over the period from 22 December 2012 through 23 January 2013 11 bond emitters placed 14 bond loans with a total nominal value of Rb

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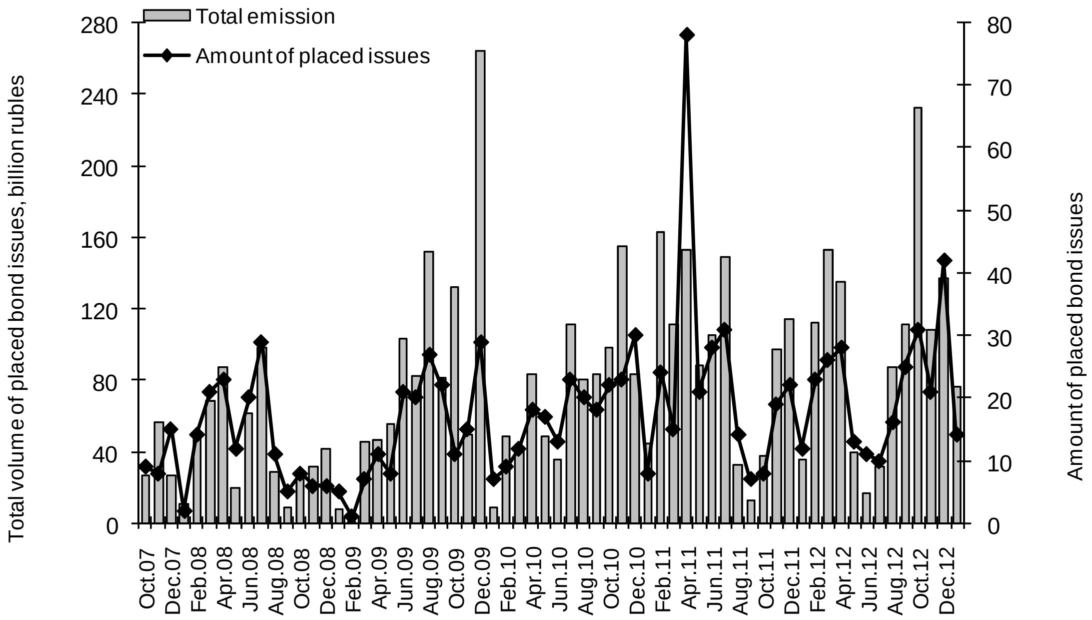
[4] According to data released by the Finmarket information agency.
[5] According to data released by the Rusbonds company.

76.4bn (vs. 42 loans with a total nominal value of Rb 137.1bn placed from 27 November through 21 December) (*Fig. 6*). Commercial papers accounted for one-third of the placed issues. The largest bond loans were placed by Oil Transporting Joint-Stock Company *Transneft* (2 series of commercial papers with a total face value of Rb 34bn) and JSC 'Bank VTB' (1 series of commercial papers with a total face value of Rb 15bn)[6]. Two mortgage agents, *Aziatsko-Tikhookeanskii Bank* [Asian-Pacific Bank] and *Evropa 2012-1* [Europe 2012-1] managed to attract finance in the form of 32-year and 30-year loans respectively.



Source: According to data released by the Rusbonds company.

***Fig. 6.* Dynamics of the Primary Placements of Issues of Ruble-Denominated Corporate Bonds**

The low indices of primary placements can largely be explained by the fact that many big bond emitters changed their previous plans of attracting resources from the debt market. Thus, over the period under consideration, that is, from 22 December through 23 January, 16 bond issues were annulled by the Federal Financial Markets Service of Russia (FFMS) due to failure to place even a single security; their State registration was also annulled (for reference: over several previous months, no more than 6–8 issues had been annulled)[7]. Among the issues thus annulled there were, for examples, the bonds issued by *TGC-1, Mobile TeleSystems (MTS),* the Novolipetsk Metallurgic Combine *(NLMK),* and *VimpelCom*.

Over the period from 22 December through 23 January, all the bond emitters redeemed their 6 bond issues with a total face value of Rb 8.6bn in due time, i.e., without declaring a technical default, which is exceptional in view of the history of the last four years. In February 2013, the redemption of 15 issues of corporate bonds with a total face value of Rb 60.9bn is expected.[8]

[6] According to data released by the Rusbonds information agency.
[7] According to data released by the Federal Financial Markets Service of Russia.
[8] According to data released by the Rusbonds company.

The situation with regard to real defaults (when an emitter is unable to fulfill current obligations against a bond loan even in the next few days after the planned redemption date) has remained stable for several months. Thus, in the period from 22 December through 23 January only one bond emitter defaulted on the payment of the coupons to the securities holders. As in the previous months, all the bond emitters redeemed the face value of their bond loans before their maturity by means of a buyback offer to their current holders in due time or, at least, within the framework of a technical default.[9]

In late 2012, some measures designed to further develop the investment instruments were implemented. Thus, among other things, the RF Government approved a decree whereby the formerly imposed ceiling (30%) for the share of infrastructure bonds of one bond emitter in the general pension saving investment portfolio of a government asset manager was abolished[10]. Alongside that measure, the government introduced more precise guidelines for *Vneshekonombank*'s activities associated with investing pension savings in bonds secured by RF government guarantees, and also in bonds rated at or above the sovereign credit rating and issued with the purpose of providing funding for nationwide infrastructure projects.

[9] According to data released by the Cbonds company.
[10] According to data released by the Cbonds company.