

The Bretton Woods Committee

Symposium Strengthening Capital Markets in Emerging Market Countries

The Russian Capital Market

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Emerging Market Definition

- Lack of clear definition- pervasiveness of misleading statistics and studies
- Even in the IMF and the Economist Intelligence Unit, the list of countries considered to be Emerging Markets is not consistent
 - Statistics not comparable, conclusions not accurate
- Ignores the fundamentally different needs of Emerging Market, Developing and Underdeveloped countries

Emerging Market Definition

- a society transitioning from a dictatorship to a free market oriented economy, with increasing economic freedom, gradual integration within the Global Marketplace, an expanding middle class, improving standards of living, social stability and tolerance, as well as an increase in cooperation with multilateral institutions.

Role of Emerging Markets in the Global Marketplace (January 1, 2008)

81 countries

- **Territory: 46.45%**
- **Population: 68.32%**
- **Gross World Product: 49.67%**
- **Foreign Direct Investment inflow: 40%**

Impact of Russia's National Ideas on the Capital Market

- Power of the Territory
- Prevention of disintegration
- Russia as the Third Rome
- Ruler worship
- The Superior is always right
- Conspiracy Obsession
- Extensive not Intensive Economy

The Political Environment of the Russian Capital Market

- From Communist Dictatorship to Yeltsin's Anarchy to Putin's "Vertical of Power" (1989-2006)
- Western Misconceptions about Russia's pseudo-advocates of the free market (1989-2001)
- Liberalization of prices before Demonopolization (1992-93)
- Pseudo-privatization and the creation of the economic roots of corruption (1992-1995)
- The Crash of Russia's romantic image of capitalism and Americanism (1992-1995)
- Regional Decentralization of Russia- Governors as Godfathers (1995-2002)
- Corruption and Nepotism as a philosophy and image of Russian Business

Historical Developments of the Capital Market

1990

- Birth of Russian stock market: the USSR government issues two decrees:
 - “Regarding Share Holding Companies”
 - “Regarding Valuable Papers”
- First shares issued and actually sold: shares of Russian commodity exchanges, accounting for 80 per cent of all shares until November 1991.

Historical Development

1992

- Creation of The Moscow Interbank Currency Exchange, the Moscow Central Currency Exchange, the Russian Commodity Exchange, St. Petersburg Stock Exchange and the South-Ural Stock Exchange

1993

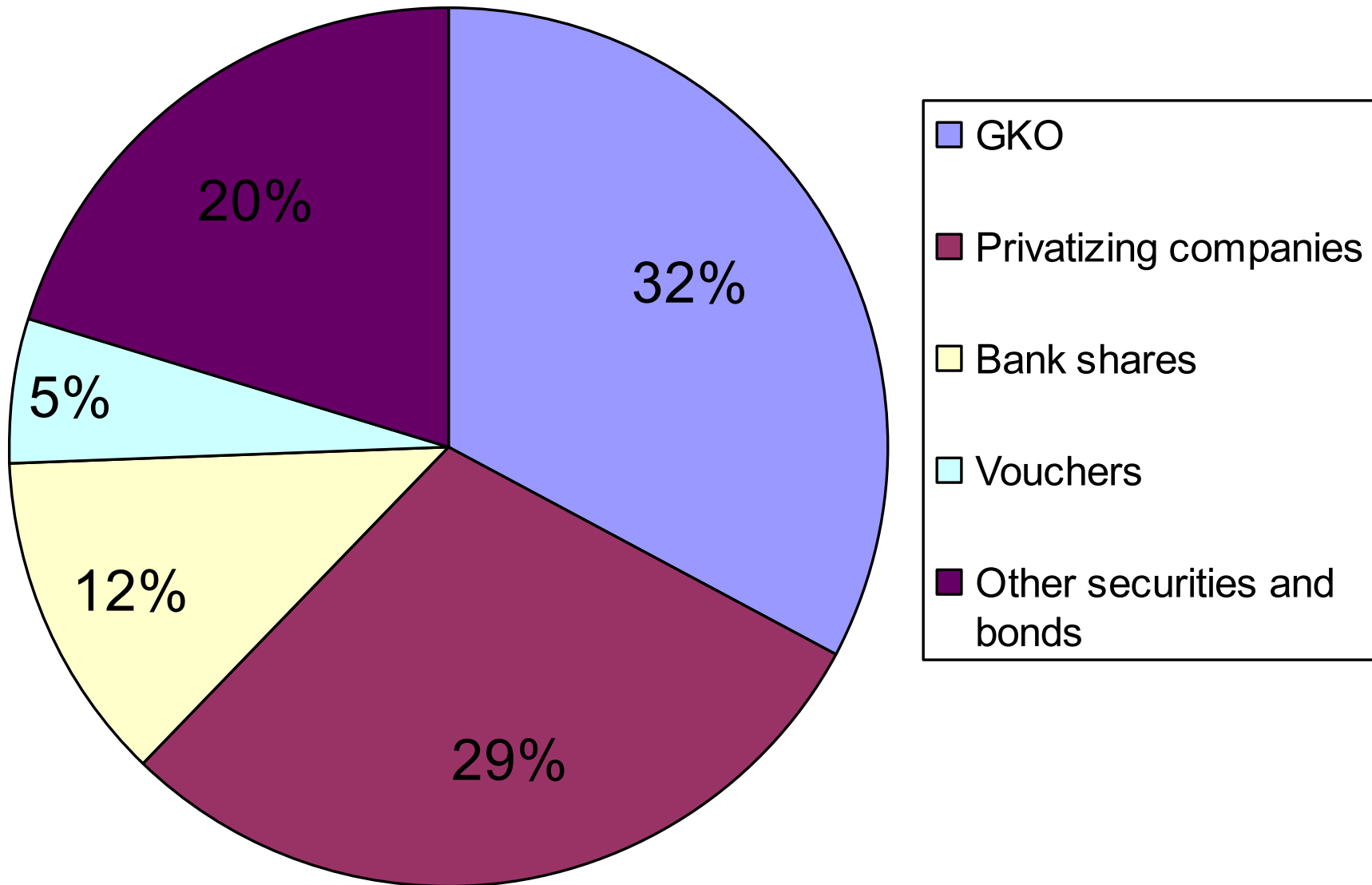
- Beginning of the sale of shares of privatizing companies
- Beginning of the state bond market- GKO

Historical Development...

1994

- October, Black Tuesday- the dollar exchange rate collapses, cutting the purchasing power of the Russian Ruble in half.
 - **first** currency speculation in the Russian market
- MIBOR (seller' s rate of deposit) and MIBID (buyer' s rate) are adopted by the 9 biggest banks.

Russian Stock Market, 1994



Historical Development...

1996

- Establishment of the stock, currency, derivative, and interbank credit markets.
 - The biggest of these was the currency market.
 - Daily interbank credits reached the value of 300 billion rubles.
 - Due to the high risk of this market, securitization takes off

Historical Development...

1998

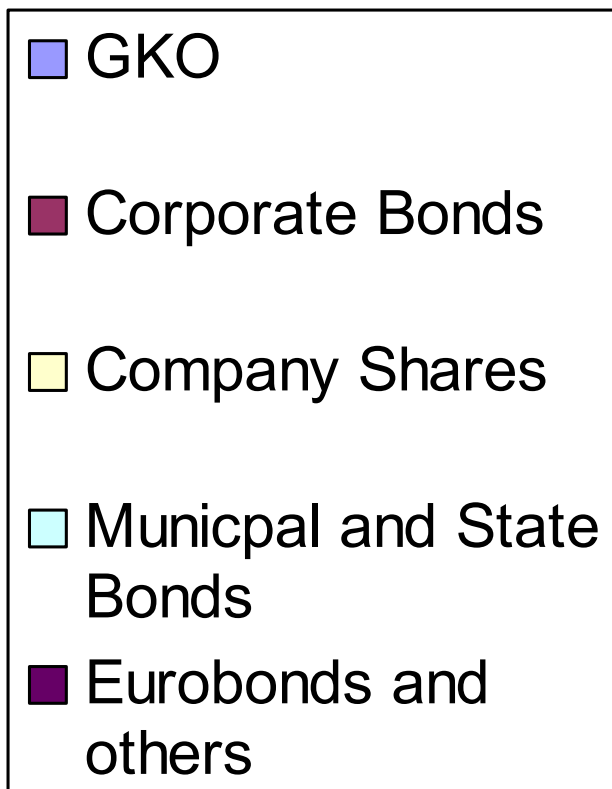
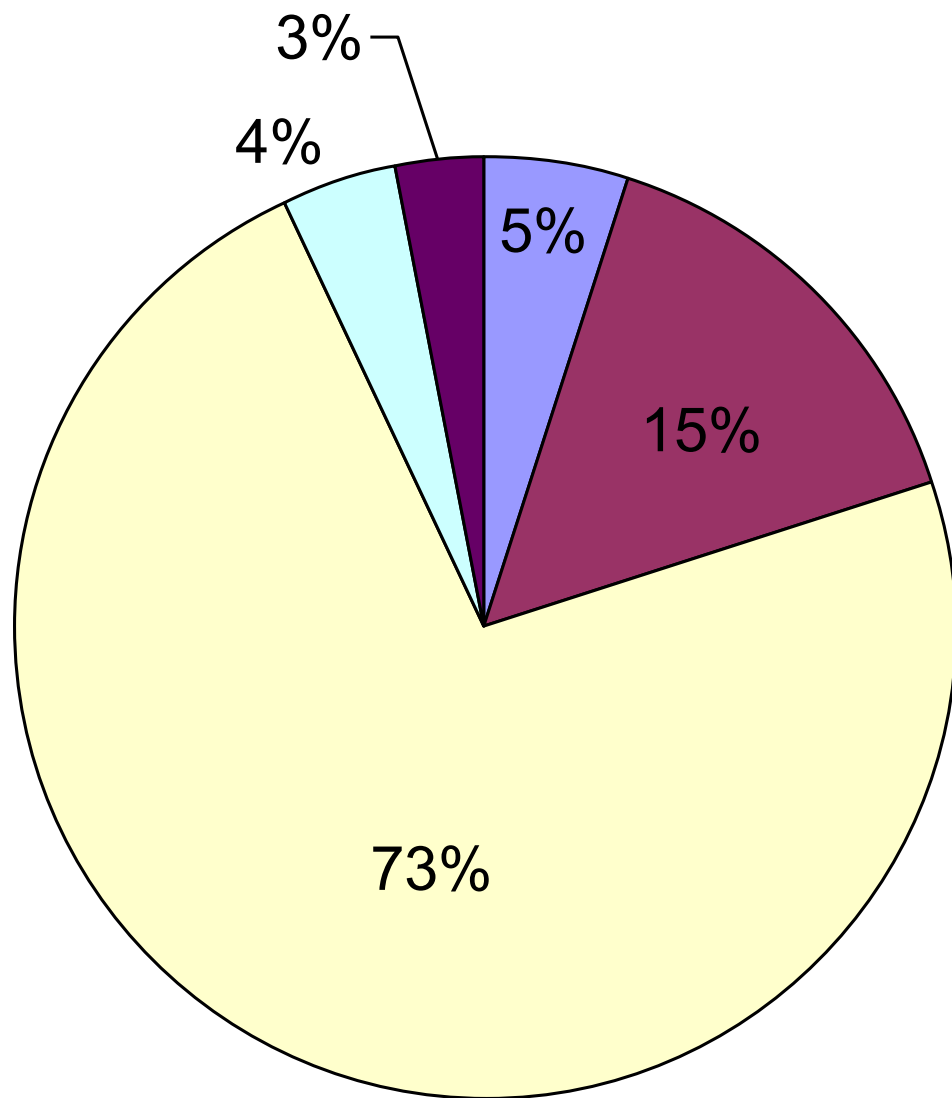
- Destabilization of the Russian stock market , following the Asian crisis.
- August 17- following payment crisis, Russian government declares **Ruble default** and a moratorium on private and state obligations to foreign creditors

10 years later...

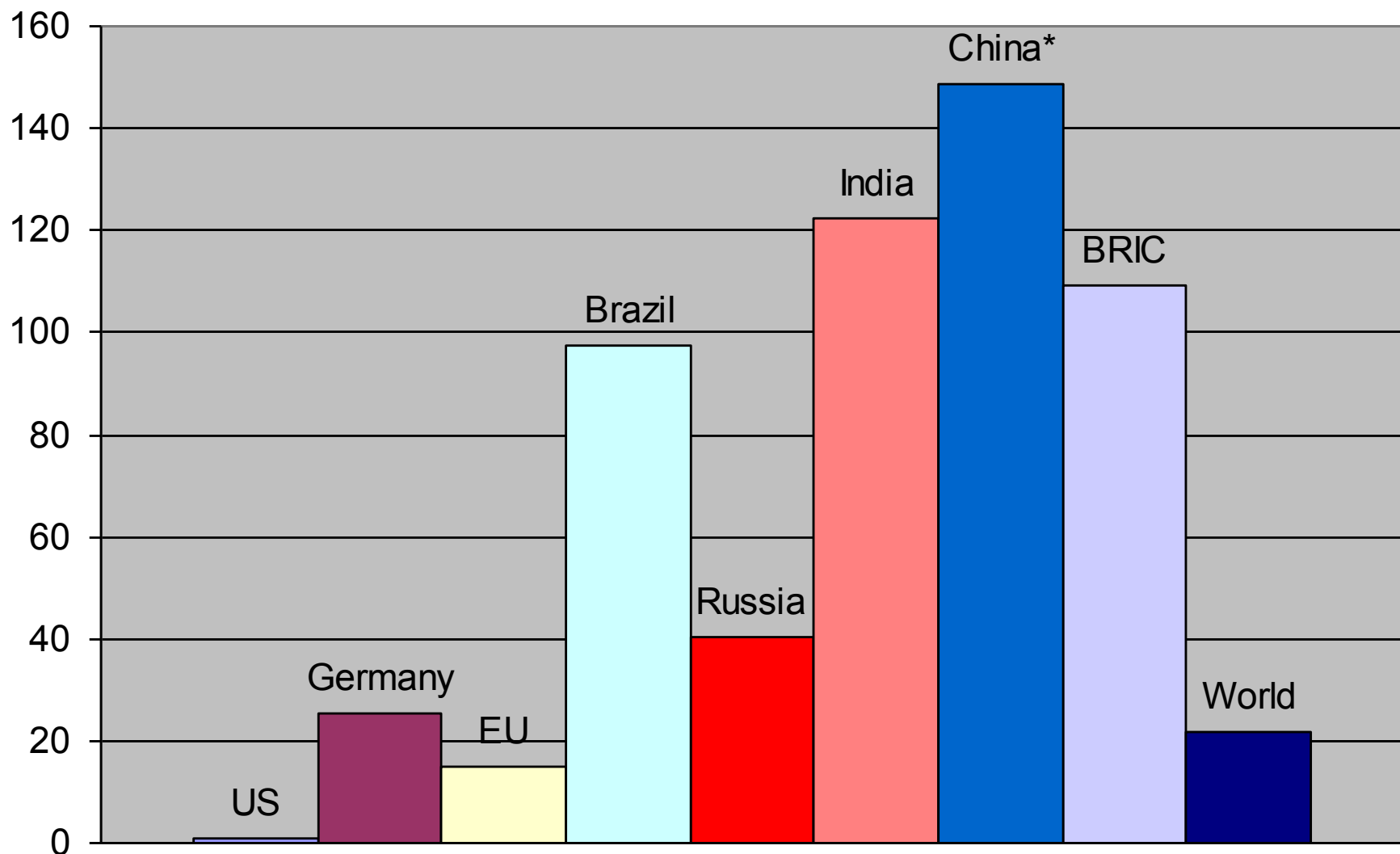
January 21, 2008

- Futures for Brent oil fall below \$88
- Shares of Oil companies fall between 5.27% (Rosneft) and 8.7% (Surgutneftegas)
- Capitalization of Vneshtorg Bank decline by 6.33% and Sberbank by 7.65%
- Telecom sector declines by an average of 7.5%
- Caused by uncertainty of US market and complicated by closing of NYSE (US National Holiday)

Russian Stock Market, 01.01.2007

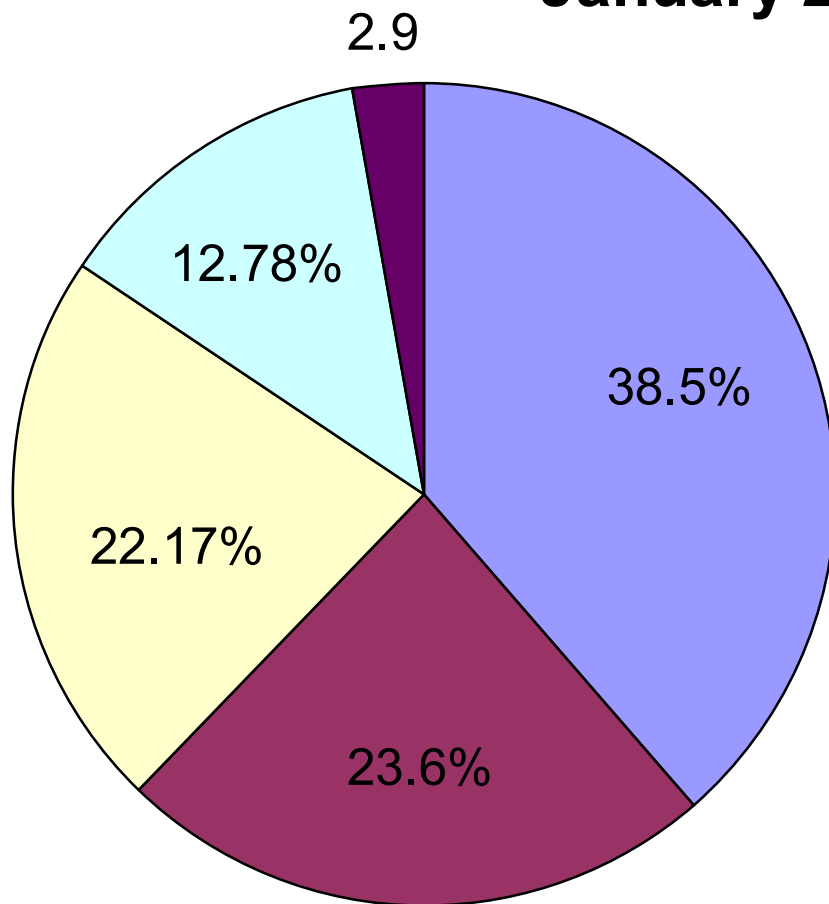


Capitalization Growth Rates, 2007



*including Hong Kong

Capitalization of the Global Marketplace, January 2008



- United States
- Global Emerging Market (without Russia)
- European Union (without EMCs)*
- Japan and Canada
- Russia

Capitalization in Russia

2007

- For the first time since 2000, Russia experienced a sluggish growth of capitalization and high volatility.
- 300 new companies went public bringing an additional \$121 billion. Only in December, 15 companies went public with a total market value of \$924 billion.

Capitalization

2008

- Total capitalization of the Russian market: \$1.463 trillion.
 - Since 2003, market capitalization increased by a factor of ten.
- Contrary to popular opinion, the market capitalization of the oil and gas sector is a little lower (by \$6 billion) than capitalization of all other publicly traded companies.
- The 100 biggest publicly traded companies of Russia account for 92.12% of the total market capitalization

Quantitative Evaluation of the Russian Capital Market, 2008

- Out of 85,489 emitters in Russia, only 482 (0.56 per cent) have a presence in organized markets
- 95 % of market transactions are related to only 3% of available company shares
- Total face value of corporate shares on the market is 1,128.15 billion rubles
 - increased by 30% in 2007
- The percentage of transactions on stock markets relative to total transactions has surpassed 75%

Unique Characteristics of the Russian Stock Market

- **An emitter can have a presence at several different exchanges simultaneously**
- **Extremely high rate of growth-**
 - 2005: 150%
 - 2006: 200%
 - 2007: 10% (six months)
- **High concentration of capitalization in terms of emitters and industries**
 - Gazprom: 25.5% of the market.
 - The ten major companies, (Norilsk Nickel, Lukoil, MTS Telecom, and Sberbank, among others): more than 70%
 - Three industries- Energy, Financial and Metallurgy: 90%
 - Increasing role of the financial sector (3.5 times, 2007)
- **Declining role of depository receipts of Russian companies on foreign stock exchanges (since 2004)**

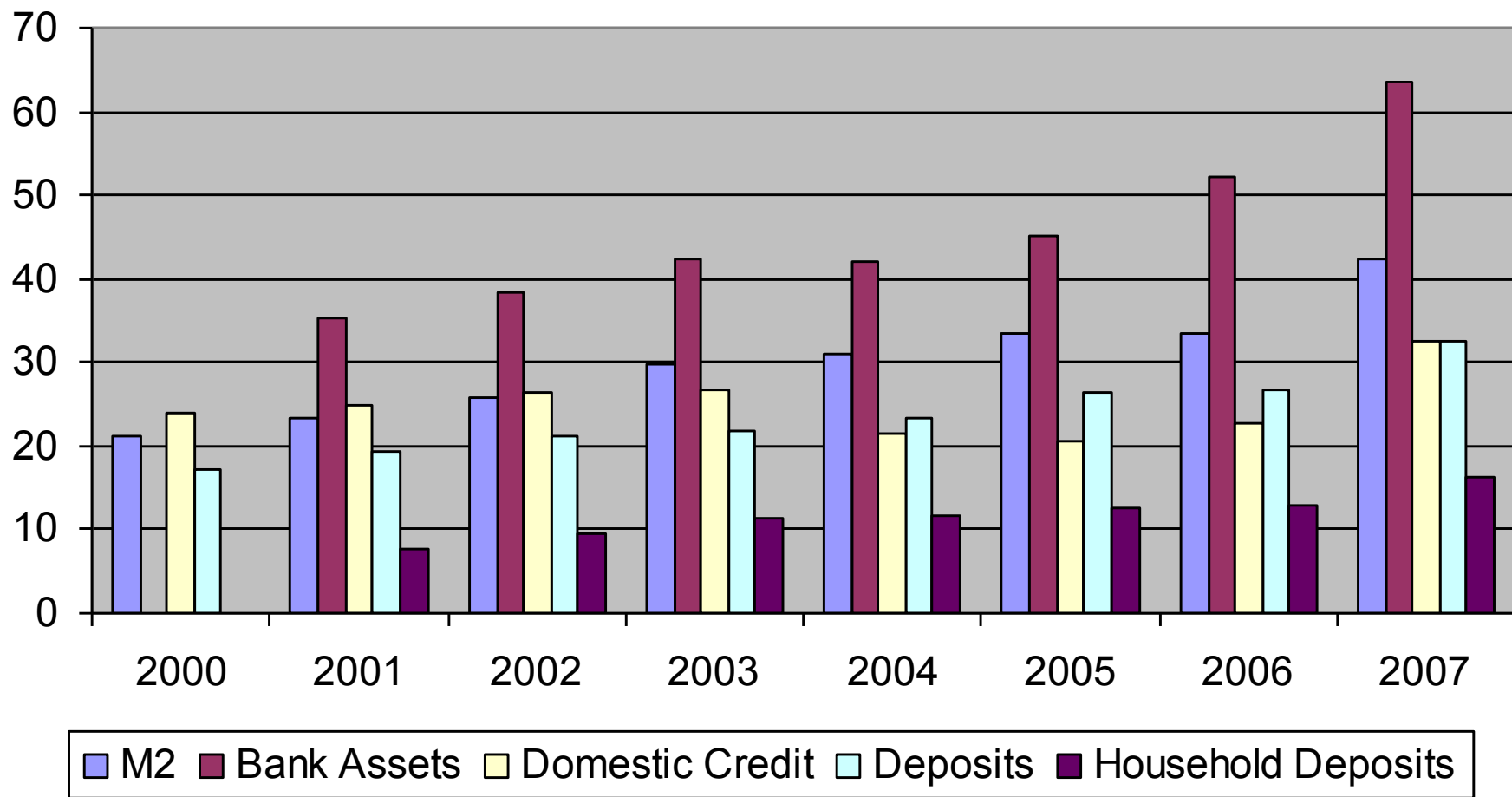
Russian Capital Market Trends 2008

- **Increasing debt of individuals and companies will have a substantial influence on the financial and banking sectors**
 - every Russian owes the banking sector of about \$1,000
 - Delinquent debt per person is 1,500 rubles (roughly \$60)
 - Lower credit discipline will negatively influence the credit debt market
- **Rapid development of banking sector despite decreasing number of banks**
 - Assets, capital and private bank accounts have increased by 30-40% annually (7 times faster than GDP)

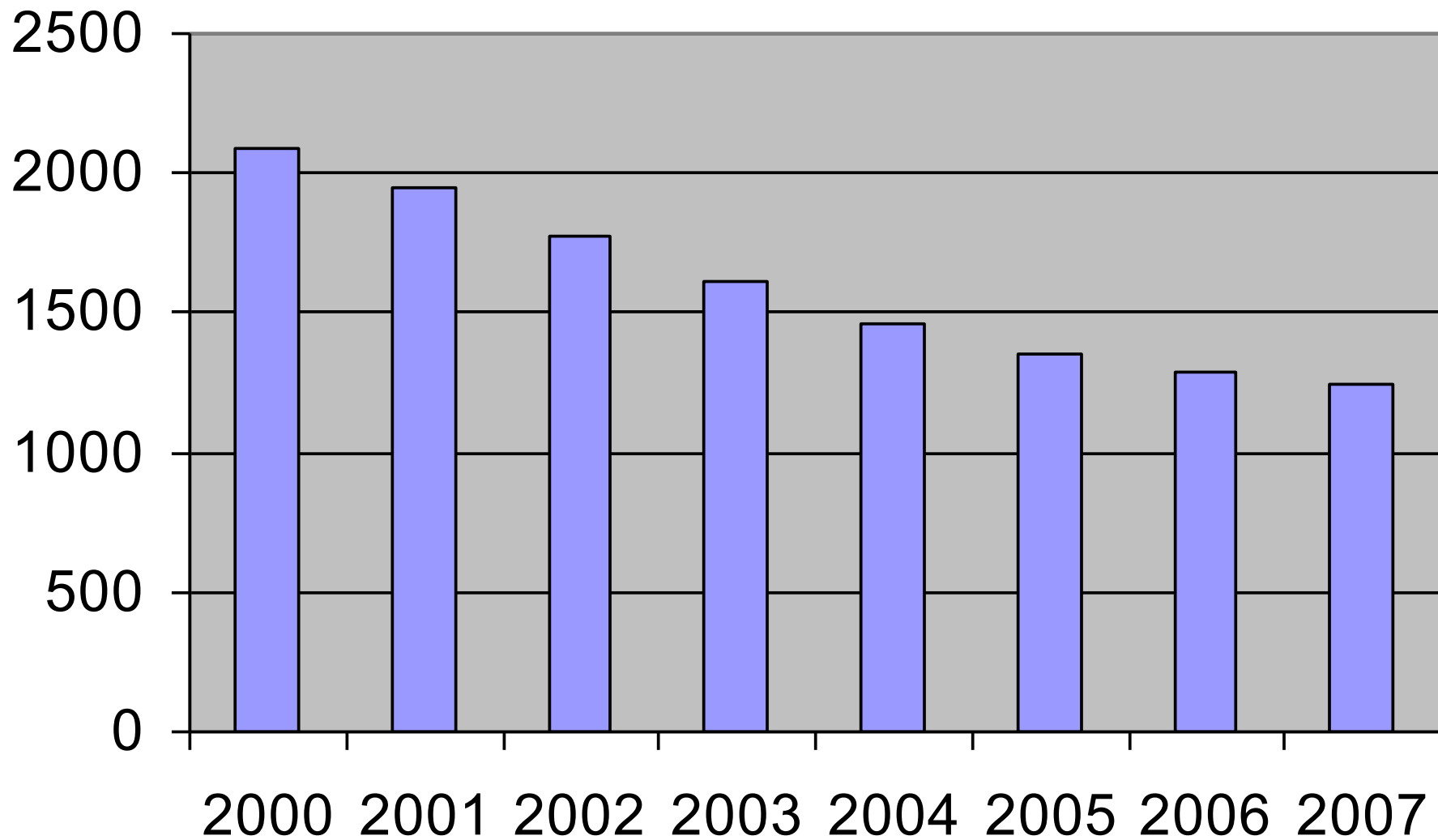
Status quo of Russian Banking Sector, 2008

- 1,243 registered banks
 - Total registered capital of 731.74 billion rubles
- 1,092 banks licensed to conduct banking transactions
- 199 banks licensed to operate with precious metals
- 906 banks licensed to operate with foreign currency
- 202 banks with foreign capital
 - 63 banks (with 169 branches) that consist of 100 per cent foreign capital
 - 23 banks with more than 50 per cent foreign capital
- 909 banks with governmentally insured accounts
- Since 2003, 1,419 bank licenses were revoked
- More than 90 per cent of all transactions (60 per cent of in terms of value) are conducted via internet trading

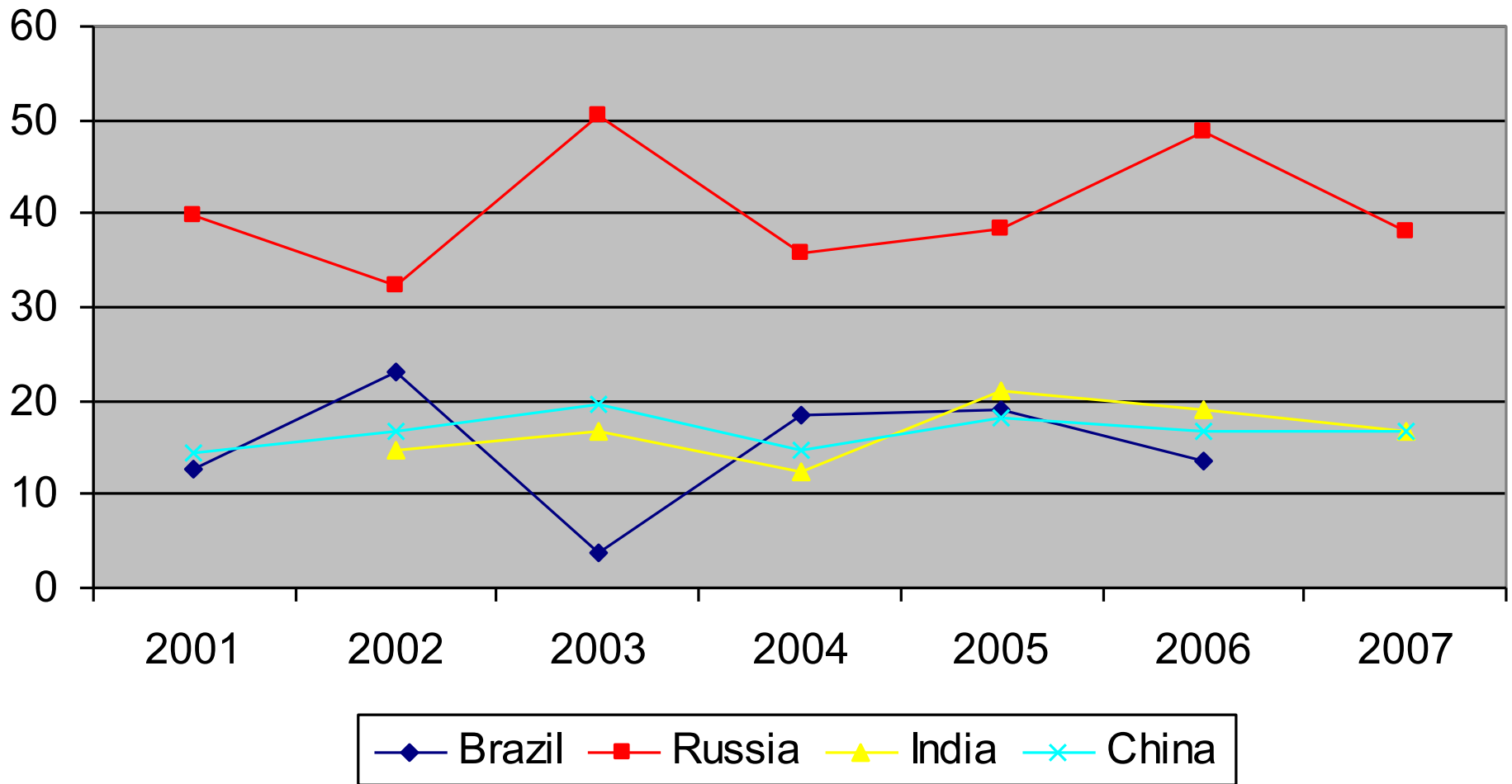
Selected Financial Indicators of Russia as % of GDP



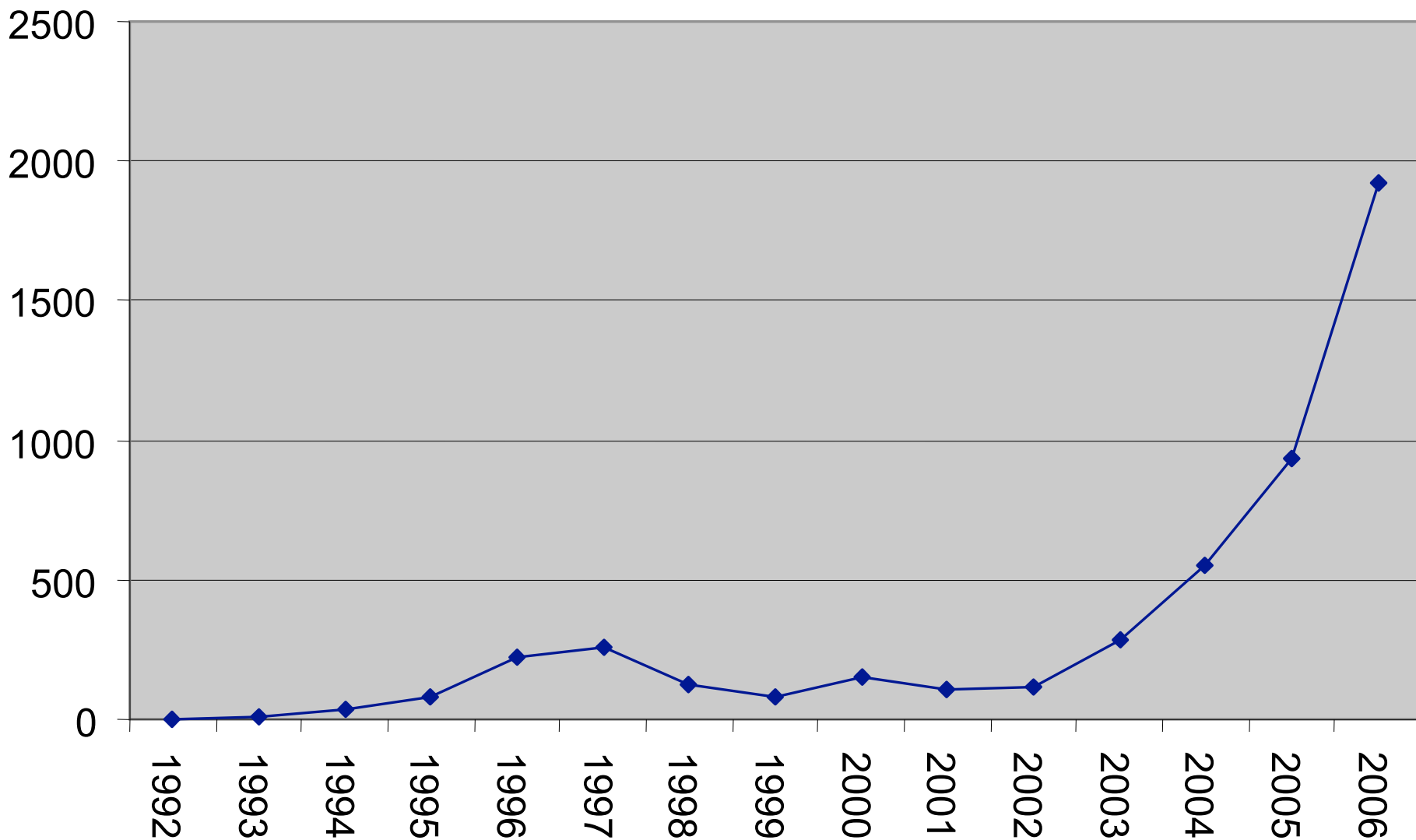
Number of Banks in Russia



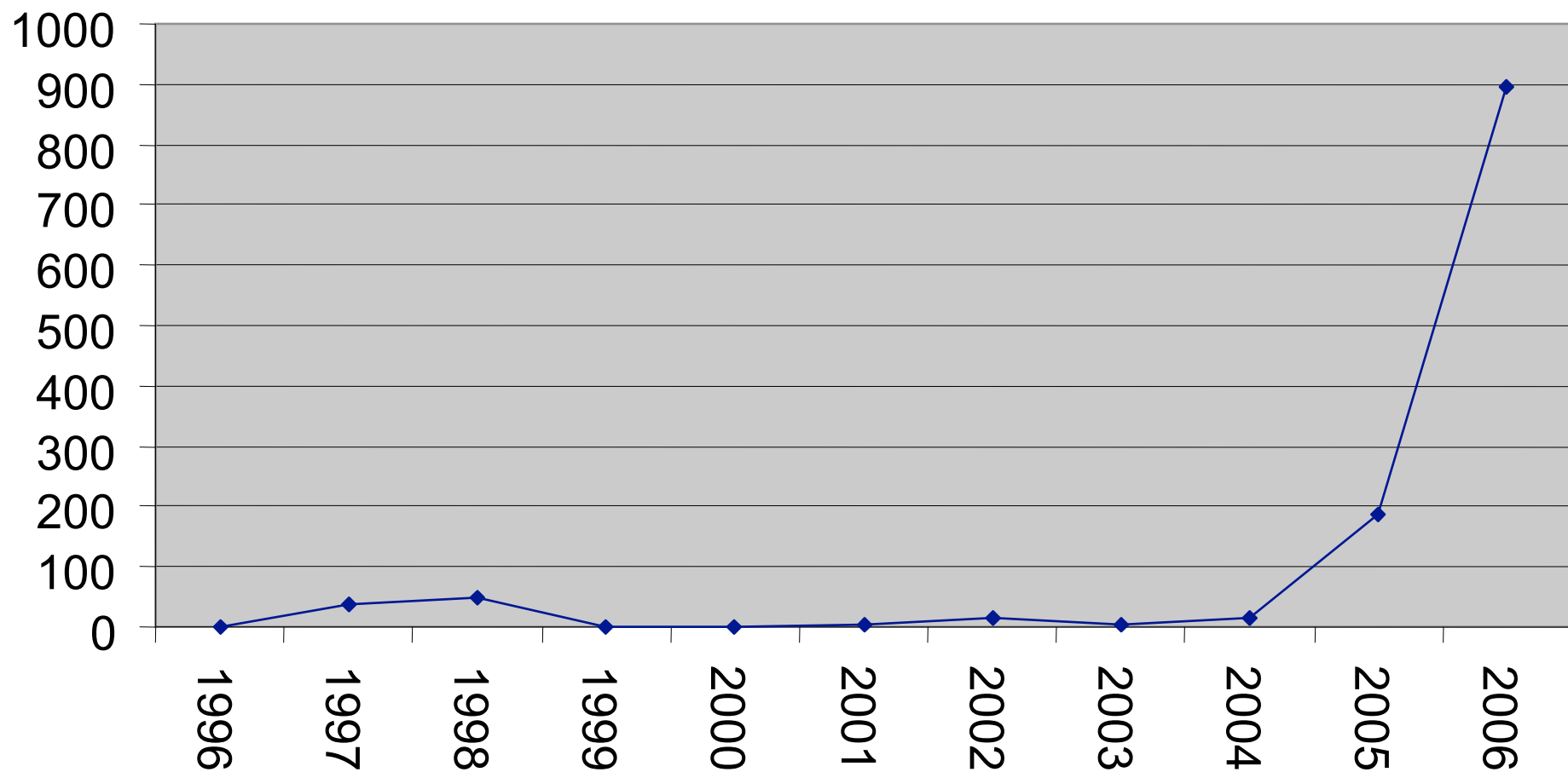
M2 Growth Rate (%) in BRIC



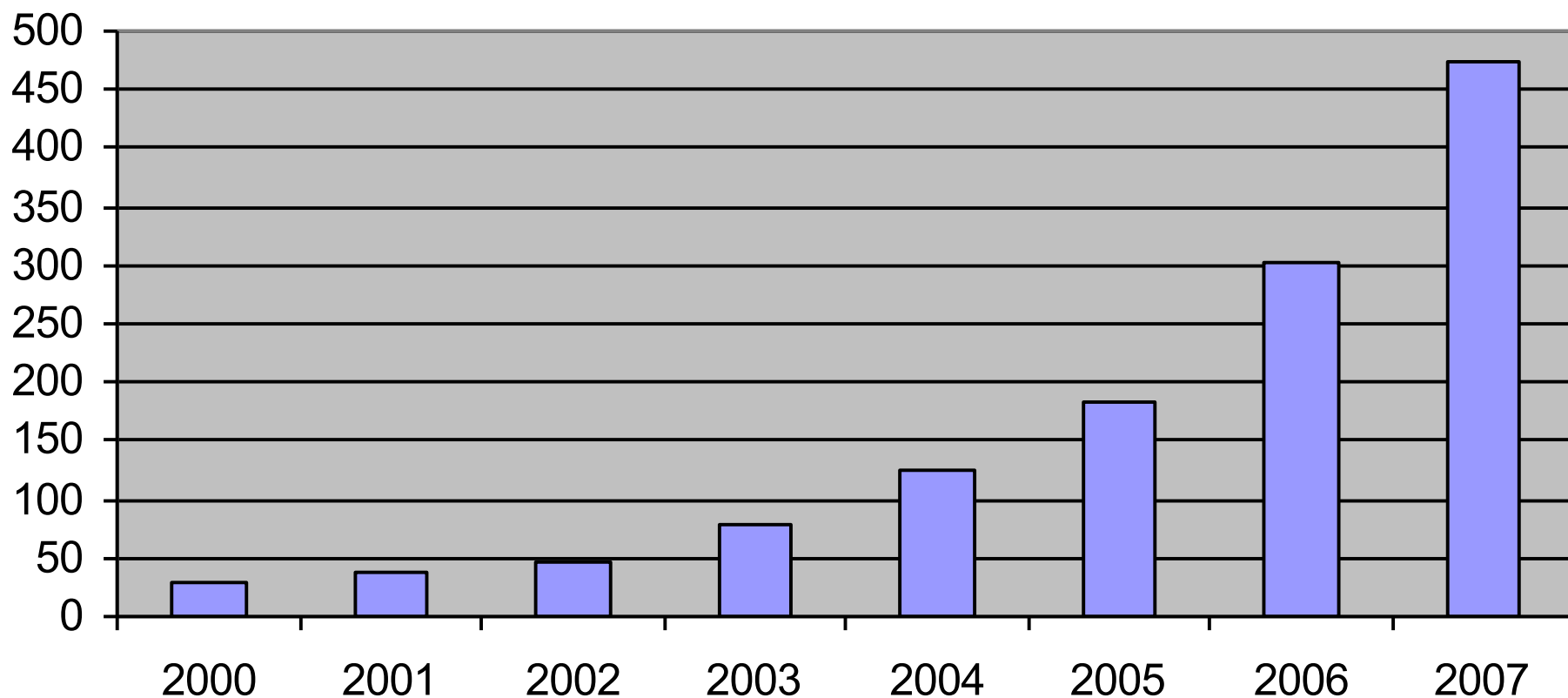
Annual Trading Volume, Total Turnover of the MICEX (blns US \$)



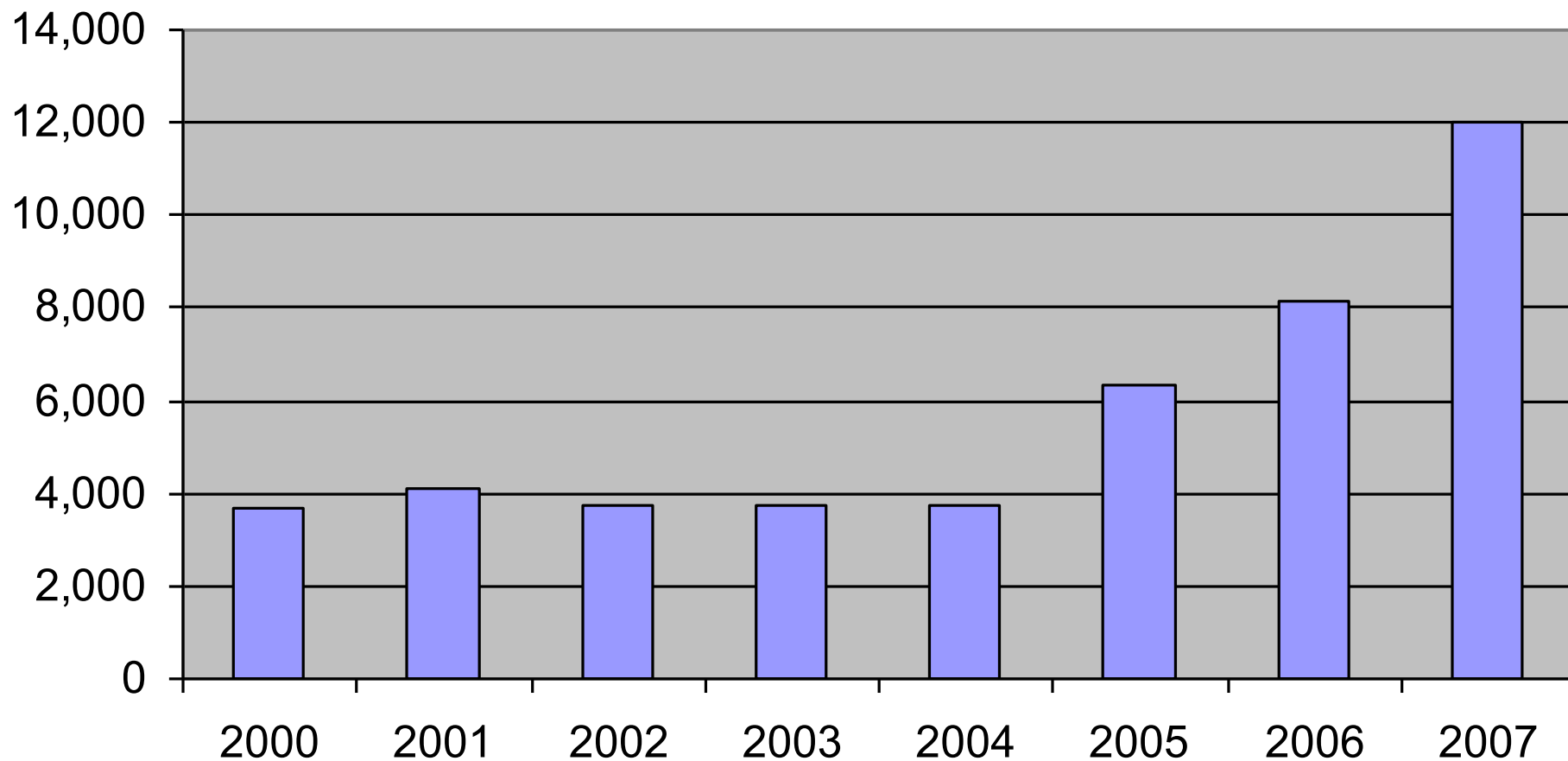
Annual Trading Volume, Derivative Market of the MICEX (blns denominated rubles)



International Reserves of Russia (Blns US \$)



Gold Reserves of Russia (Mlns US \$)



Priorities for Russian Capital Market's Improvement

- Establishment of Law of Protection of Minority Shareholders' Rights
- Enforcement of legal rights of minority shareholders
- Improved access of medium and small companies to capital market
- Continuation of the increasing role of the public sector in the Russian capital market
- Prevention of federal and regional governments from breaching of contracts
- Increasing level of convertibility of the Ruble
- World Trade Organization membership and improvement of capital controls