

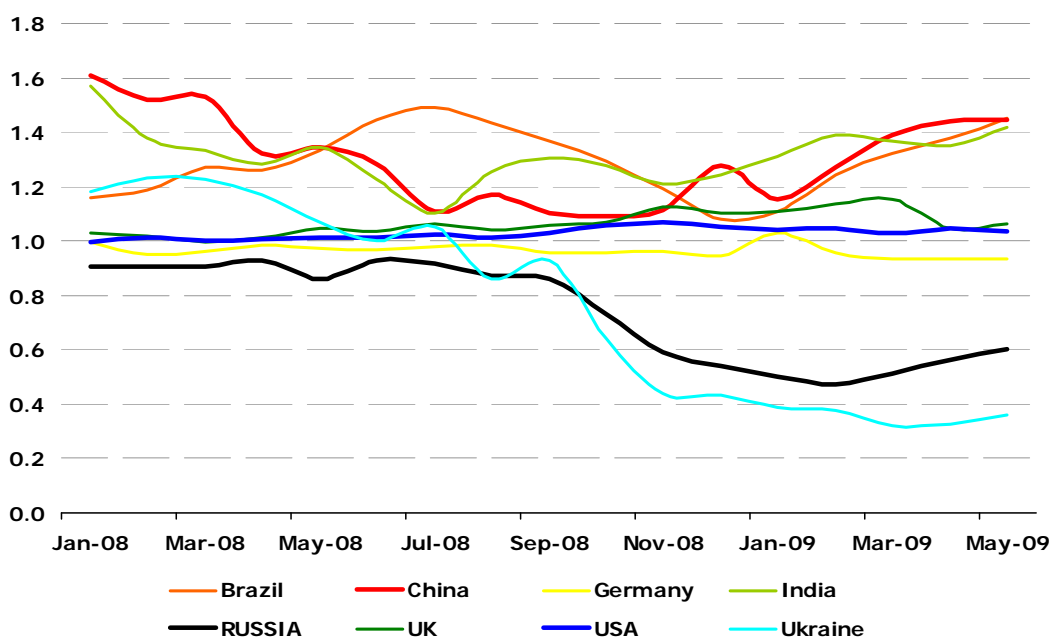
RUSSIAN STOCK MARKET: A 2009-2010 SCENARIO

RESEARCH
NOTE

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The Russian stock market witnessed one of the heaviest sell-offs during the ongoing global financial crisis started in 2008. The RTS index lost more than two thirds of its value in this time as investors withdrew their positions from Russian stocks and induced blockage on the inner financial system. Clearly the origins of the crisis lay outside the country borders and hence the national regulators don't possess efficient instruments to overcome the whole scope of problems faced. Moreover there's even no technical possibility to forecast the terms in which these problems could be resolved. In case of Russia this implies consequent fulfillment of at least three conditions. First, recovery of financing mechanisms and maintenance of liquidity turnover between production units. Second, resumption of foreign investments to the Russian fund market and achieving fair capital distribution with other markets. Third, halting the global recession and subsequent economic recovery. Few Russian companies can pretend on getting some fair levels of evaluation, unless these conditions are fulfilled.

Premium for investing in stock markets (mean level = 1)



Source: Sovlink estimates

* The premium value is estimated as weighted average of corporate key financial multiples to corresponding average industry values.

What do these conditions mean in practice?

1. The system of payments in Russia has traditionally rested upon a stable turnover of short-term bank credits. But maintaining this turnover became a true headache for bankers once they lost faith in their debtors. Consequently revival of cash flows requires rising the level of confidence in operations between financing institutions and the real sector of the economy. This process will most probably stretch over the 2009 and 2010 years. There exists some potential of making this process faster via implementation of an adequate state policy which is taking place since the beginning of the 2009 year. There's also some evidence of successful refinancing of several large loans (Mechel, Gazprom) which proves that financing issues are not unsolvable. Every new example of successful loan recapitalization is

important because it bears positive information to other creditors. On the other hand there's still a plenty of inefficient business units which can't pay for their loans because of the low market conjuncture. Their reserves may afford them extend the pay-off moment for some time, although in the long run bankruptcy is inevitable in case when commodities prices don't go up.

2. The Russian fund market became one of the leaders in decrease of capitalization relative to corresponding revenue and capital values during the autumn of 2008. Panic and uncertainty over further perspectives were among the main reasons for an accelerating flight of portfolio investments to more reliable assets. But we have evidenced a visible improvement in transparency of prospects since then meanwhile stabilization of production takes place. Moreover Russian companies stand on a more solid ground in some positions than their competitors abroad, benefitting from permanently low production costs and currency devaluation. This is a valid argument for redirecting investments towards more profitable and reliable Russian producers. It is especially important for export-led companies which are less vulnerable to inner solvency issues.

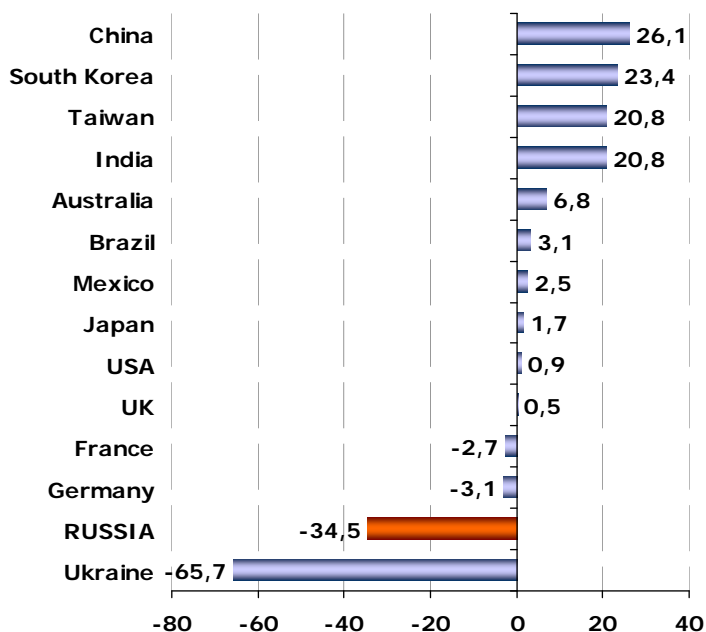
3. At last, the end of the global recession would become the main driving force for reincarnation of all stock markets including the Russian one. Although this factor is expected to obtain importance only since 2010, its role shouldn't be undervalued as it would lead to the fastest growth at all markets. Mining assets (including those located in Russia) would benefit mostly from it as they would also be the first to feel improvements at commodities market.

When we estimate the fund market midterm growth prospects, the first two factors should be highlighted and taken into account, since they would have the strongest impact during this and the 2010 years. Solving mutual payments troubles and making foreign investing to Russia attractive again are both truly feasible tasks for our country. And consequently they comprise the leading growth potential at this moment.

In order to measure this potential we have to give a certain estimate value of the losses incurred by our market relative to the markets of other countries. **In the base point before the crisis (July, 2009) an average Russian nonfinancial company had been valued some 10% below its average competitor in the same global industry sector.** But the situation has become much worse six months later and the corresponding discount for Russian equities equaled already 50%. The outflow of investments from Russia coincided with their redistribution towards safer assets and also stocks of foreign producers. Most of them are located in Asia, in countries like India and China. They have also suffered heavily from the crisis, although its aggregate impact was moderate and the process of recovery followed sooner.

For example, Chinese companies managed even to increase their premium relative to other competitors from +11% prior to the crisis to +15% by the beginning of 2009. This premium is estimated to be even higher currently: an average Chinese producer costs almost 40% above its average competitor. In the same way Indian companies gained in popularity amongst investors: their premium increased from +10% before the crisis to +33% today. Countries like South Korea (from -15% to +6%) and Taiwan (from +19% to +44%) followed the leaders. At the same time American securities demonstrated positive but less impressive performance. Although the USA are often described to be the predominant source of global financial cataclysms, the relative value of its equities has also increased from +2,1% before the crisis to +3,1% today. Although this change looks quite moderate, it is also very substantial because the relative weight of its stock market among the 62 countries chosen for our analysis is not less than 38%. Latin

Relative change of mean premium for different markets from June 2008 to 14.4.2009, % (pre-crisis level =100%)

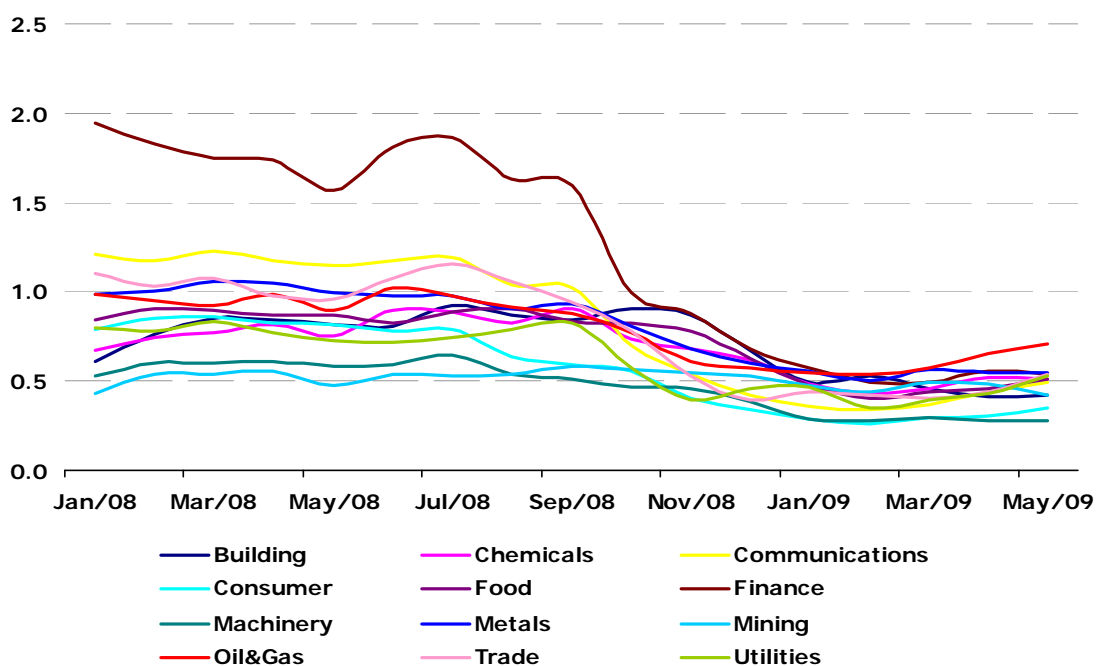


Source: Sovlink estimates

America has also succeeded in improving its relative positions in investor portfolios along with the USA. The premium for Brazil moved up from +49% to +53% and in Mexico — from +35% to +38%.

At the same time most European equities demonstrated negative trend, losing their relative attractiveness. Total weigh of European markets equals some 27% of the whole sample which makes it play the role of the largest donor of capital. Slow economic growth and inflationary pressures had provoked investors to keep distance from the Euro zone already before the crisis broke out. This resulted in a visible discount on local equities. But the discount increased even higher in recent half a year. In France — from -7,5% prior to the crisis to -10 today, in Germany — from -1,9% to -5%, in Switzerland the premium of +25% was replaced by only +20%.

**Russian stocks premium/discount relative to their foreign peers by sectors
(mean level for each month = 1) (*)**



Source: Sovlink estimates

* Premium value for a sector is estimated as an weighted average of corporate key financial multiples to corresponding average sector values.

The redistribution of capital between countries has reached its peak in the end of 2008 and since the beginning of this year the opposite process takes place. Its pace would play the dominant role in the resulting disposition of investments and their recipients by the end of the year. Russia is also moving in this direction: The Russian equities managed to curtail the gap to only -39,9% by mid-April. Nobody is entitled to proclaim that the discount would vanish by the end of the 2009 year for objective conditions. This would necessitate aggregate capitalization to grow by 53% given improvements within the one strictly contoured region. Of course this is possible in theory, but its probability is very small. Nevertheless, such growth might be real in case that the other markets also start to recover, because it would benefit Russian enterprises too.

There's much more rationale in suggesting that the recovery terms would appear considerably longer and it would take at least two years to return to the original levels of market evaluation (relative discount to competitors – -8,2%). In this case annual market growth rate which is required to reach this level would equal 27,5% until the end of 2010. **This scenario suggests that the RTS index achieves about 970 points by the end of the 2009 year.** Its fundamental prerequisite states that the rest of the world remains stationary in this period and only the process of capital redistribution takes place. This redistribution has to provide Russia with sufficient capital inflow owing solely to the factor of its relative cheapness at the moment. Certainly this precondition can't be fulfilled in practice and we can only expect that the global recovery pace would remain rather slow in this year while overcoming the recession would require considerably longer period of time. Based on this we may suggest that the global fund market



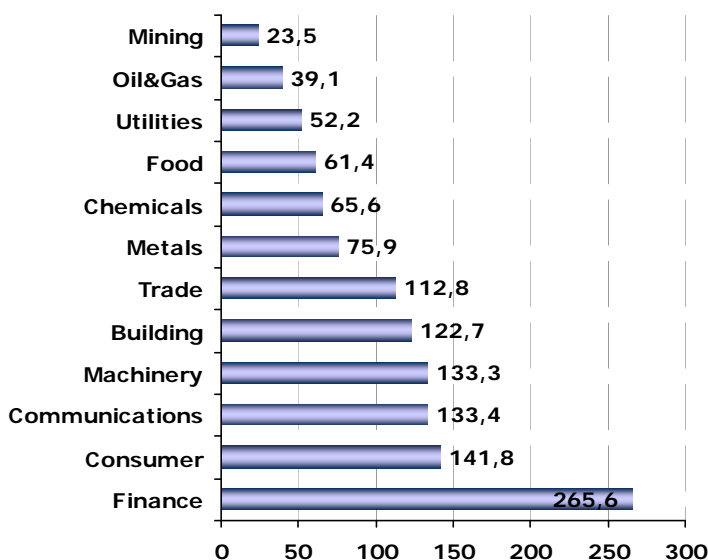
doesn't pretend to demonstrate serious recovery this year. But if this possibility becomes real, there's a chance that the Russian stocks would also gain much more from reinstatement of confidence. **In this situation the Russian RTS index might achieve a level of about 1250 points and even higher already by the end of the 2009 year.**

While projecting any growth potential one should also take into account increasingly higher volatility levels which carry substantial risk to markets. Whenever capitalization growth and stock buying restoration go faster than fundamental economic factors afford, exchanges would suffer new downside corrections. They would neutralize excess cash influx and provoke new indices crashes. Deep declines would only postpone the final recovery moment. While smaller corrections are inevitable and might provide even some positive clearing function and help boost subsequent development.

The prospects of particular companies and sectors in Russia are highly correlating with their liquidity supply and scale of debt load. For example the Oil&Gas sector pretends to rely on stable cash flow from export activity, which guarantees its relatively high evaluation by the market. The sector had a -2% discount relative to its competitors before the crisis and today it is about -30%. This decrease is the smallest among Russian sectors, second only to the mining industry. The metal-producing companies also had a -2% discount earlier, but today its value increased to about -44%. Most large metal industry representatives took active participation in merger and acquisition deals in recent years which resulted in substantial debt load on their balance sheets. Their ability to cope with interest and principle payments would remain questionable unless commodities markets restore. Other industries have also suffered heavily from capital flight. Relative discount for Russian utilities companies increased from -25% to -51%, for manufacturing enterprises — from -36% to -72%, for construction companies — from -8% to -58%. The financial sector went under the highest pressure: its original premium of +86,5% transformed into a -49% discount today. This is a direct consequence of the debt crisis which broke out in Russia. These figures provide solid ground for estimating the extents of possible rehabilitation which can take place in every sector of the economy. This doesn't mean that the discount should necessarily disappear at all (it would be wrong to claim so, because there exist permanent risks specific for Russian equities which diminish their value), but rather return to the pre-crisis levels of evaluation.

These discount values corresponds to a high potential of capitalization growth in most sectors. So, the Oil&Gas Industry can gain some 39%, the metals industry — 76%, the utilities — 52%, the manufacturing companies can grow 2,33 times and the financial sector — 3,6 times from the current ground. These estimates suggest that Russian equities manage to restore their level of evaluation relative to foreign competitors which existed before the crisis. It may require considerably long period of time. **Only a limited portion of this potential can be reincorporated in the near prospect (until the end of 2009). The major part of it would be embodied only together with a parallel growth on foreign stock markets. This certainly requires global recovery process to begin, which may start not sooner than the 2010 year.**

Russian stocks recovery potential to pre-crisis comparative valuations, %



Source: Sovlink estimates

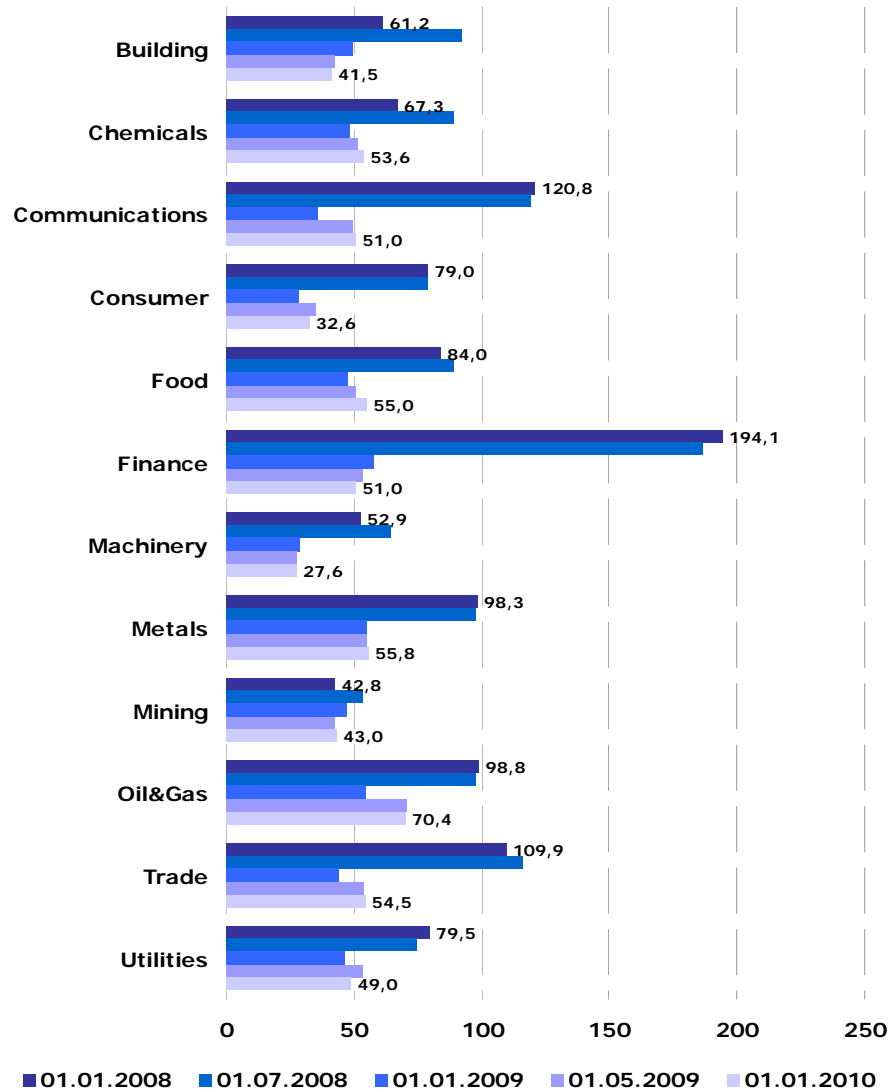


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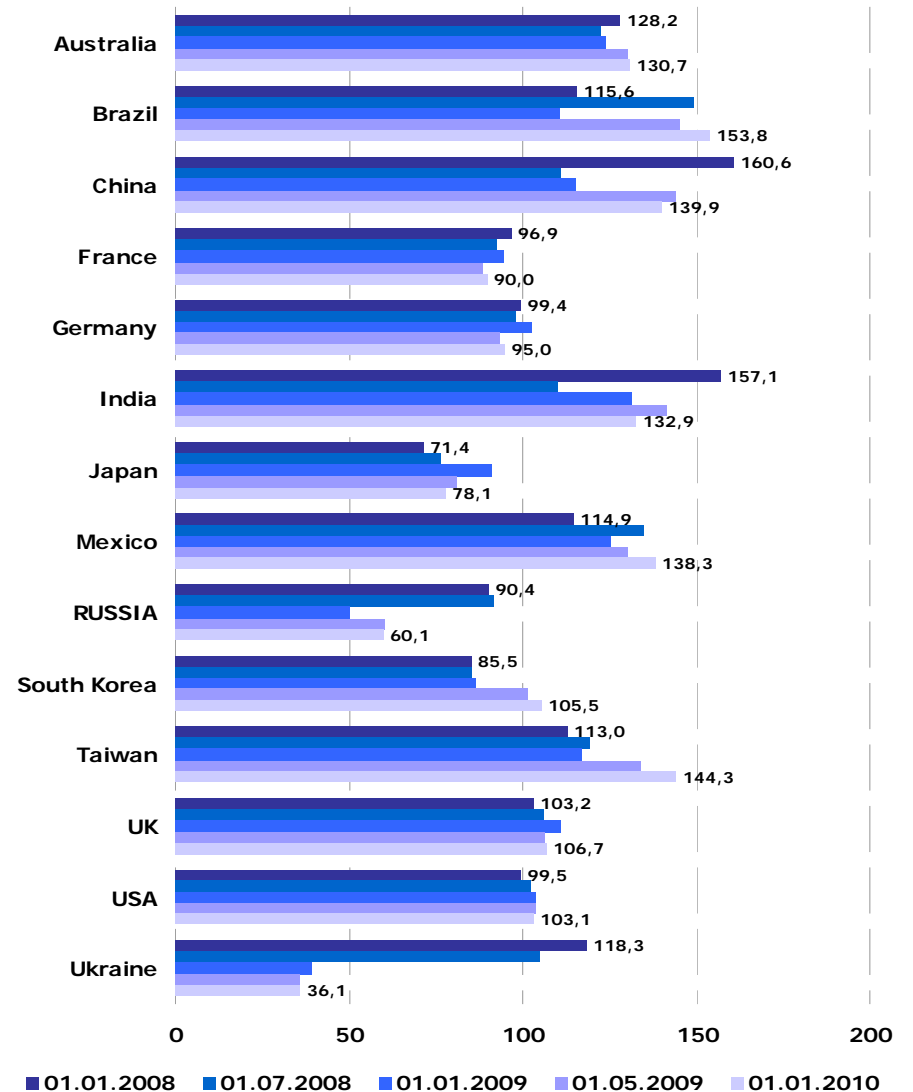
YOUR FIRST CALL - FOR THE SECOND TIER

April 22, 2009

Russian stocks relative valuation by sectors, % (mean world level =100%) (*)



Mean national companies valuation relative to their global peers, % (mean world level =100%) (*)



Source: Sovlink estimates

* Values from 01.01.2009 to 01.01.2010 are based on current capitalization and consensus analytic estimates for companies in corresponding sectors and countries.

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BUY:	Upside between 15 and 25%; confidence level - high / upside between 25% and 100%; confidence level - low
HOLD:	Upside of less than 15%; confidence level - high / upside of less than 25%; confidence level - low
SELL:	Target price at or below current price levels

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