TECHNOLOGY OF SUCCESS
As of today, over 10 million individuals and about 110 thousand businesses have made their choice in favor of Alfa-Bank. We are grateful to our customers for their trust and intend to do, both now and in the future, our utmost to have our customers not only satisfied with the quality of our services, but also recommending us to their friends and partners.

Mikhail Fridman
Chairman of the Supervisory Board of Alfa Group Consortium, Member of the Board of Directors of Alfa-Bank

ALFA-BANK 2013

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<td>countries</td>
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<td>branches and offices</td>
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<td>employees</td>
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<td>total assets, USD million*</td>
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* For the purposes of this report, the term “Alfa-Bank” is used to describe ABH Financial Limited and its subsidiaries.
**ALFA-BANK’S AWARDS IN 2013**

**12.2013**

Alfa-Bank was named the Best Retail Bank in 2013. RETAIL FINANCE AWARDS for the second time in a row named Alfa-Bank Best Retail Bank in 2013 and Customer Service Quality Leader. The awards are given by editors of The Retail Finance magazine based on their own vision and analysis of the retail financial market.

**12.2013**

Alfa-Bank again won its annual award in the category Private Banking & Wealth Management within SPEAR’S Russia Wealth Management Awards 2013 — first Russian annual award in Private Banking & Wealth Management. This year Alfa-Bank won in the category «Most Innovative Bank».

**12.2013**

Alfa-Bank is Russian Internet Bank Development Benchmarking Leader. For the second time in a row Forrester Research named Alfa-Bank Russian Internet Bank Development Benchmarking Leader.

**11.2013**

«Alfa-Click» — Best Internet Bank Global Financial Market Review named «Alfa-Click» Best Internet Bank in 2013. Ranking leaders were defined by the expert council of independent editors and by subscribers’ voting results.

**11.2013**

Alfa-Bank ranked First for the Efficiency of Tablet Computer Mobile Applications. Markswebb Rank & Report ranked Alfa-Bank first for the efficiency of tablet computer mobile applications in its Tablet Banking Rank 2013. The survey covered 11 iPad applications offered by largest Russian banks. As a result, among all iPad applications graded by their efficiency, functionality and convenience Alfa-Bank’s Tablet Bank was named the best, almost completely replicating the functionality and interface capabilities of Alfa-Mobile for iPhone. Tablet Banking Rank 2013 — is an addition to the annual survey of Mobile Banking Rank 2013 covering all banking applications for tablet computers.

**10.2013**

09.2013

Alfa-Bank ranked first among mobile and Internet banks in Russia winning in three categories according to Markswebb Rank & Report and COMNEWS. Diplomas were awarded at the conference «E-payments Russia 2013 — Electronic Payment Systems, Mobile Payments and Systems in Russia». Alfa-Bank is the winner in the categories:

- best in efficiency overall grade;
- best in user convenience;
- best mobile bank for Android.

07.2013

Alfa Mobile Banking Ranked Best Again Markswebb Rank & Report ranked Alfa Mobile Banking best in terms of its efficiency for individual customers. The assessment was carried out among 30 largest expert graded banks, covering 93 functionalities and 80 convenience criteria. Rank winning is evidence that today Alfa Bank has most advanced mobile banking system. For the last six months Alfa Mobile has won over 35% new customers.

04.2013

Alfa-Click was named «Best Internet Bank». Markswebb Rank & Report in its Internet Banking Rank 2013 again named Alfa-Click «Best Internet Bank» by its functionality and convenience among other Russian banks. The survey covered 40 internet banking systems, of which 30 are among top banks leading in loan and deposit volumes, with 10 expert chosen banks based on their interface and usability tests. Methodology included interface examinations and a number of usability tests.
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THE BOARD OF DIRECTORS REPORT ON ALFA-BANK’S RESULTS IN ITS PRIORITY BUSINESS AREAS

We are glad to present to you Alfa-Bank’s 2013 Annual Report. Assessing the past year results, we can proudly say that 2013 became a successful continuation of the Bank’s multi-year history, during which we based our work on the needs and expectations of our customers at each stage. Our strategy has proved to be efficient as evident from our financial performance in the past year. It was a year of dynamic implementation of the Bank’s Strategy for 2012-2015 approved in 2012, and we succeeded in achieving high results in all business lines. To begin with, a special reference should be made to a stable growth of the customer base both in Retail and Corporate Banking. As of today, over 10 million individuals and about 110 thousand businesses have made their choice in favor of Alfa-Bank. We are grateful to our customers for their trust and intend to do, both now and in the future, our utmost to have our customers not only satisfied with the quality of our services, but also recommending us to their friends and partners.

Focus on customers and technological efficiency as well as competent risk management and overall performance of each of the Bank’s subdivisions are our competitive strengths, which have a special significance amid an economic growth slowdown. All banking units and business lines operate as a coherent team for achievement of the high targets set by the Bank’s management. In 2013, we were able not only to achieve the planned performance, but also to exceed a number of targets and to beat the market in terms of average trends.

Thus we should note the accomplishments of the Corporate-Investment Bank, which achieved an exceptionally high ROE of over 20% and increased the risk-free revenue in the overall portfolio. Great advances were reached by the Mass Corporate Business, which customers grew more than by half last year despite an overall decrease in the number of such companies nationwide. Special mentioning goes to the Retail Banking, which retained its top-3 position in the individual demand deposit sector and added to its credit portfolio and was again named Russia’s best retail bank by RETAIL FINANCE AWARDS experts.

Another significant event that marked the past year was an official acknowledgment of Alfa-Bank’s technological leadership. Alfa-Click Internet bank and Alfa-Mobile bank received several awards in various nominations of the leading Russian ratings. Pooling of resources of all banking units in 2013 was an accomplishment to guarantee that the Bank will retain its focus on the development and introduction of up-to-date solutions aimed at making the world of finances more simple and convenient.

Finally, by developing new products, services and facilities Alfa-Bank continues to lay a special emphasis on streamlined management of operational risks and reducing the level of overdue loans. A smart risk-management policy ensured growth of the Bank’s revenue amid lowering marginality and customer quality.

An efficient and successful conduct of business and care for its customers and staff are the Bank’s priority tasks tackled daily. However, great efforts being made in this direction do not prevent Alfa-Bank from remaining a socially responsible financial entity. The Bank is actively engaged in charity and lends support to cultural and educational initiatives. This applies both the Bank and its employees. Support to the Life Line fund, which collects money for treatment of critically ill children, and to the World Wide Fund (WWF), as well as volunteer efforts and assistance to vulnerable social groups are only a few of Alfa-Bank’s charity projects. An important direction of Alfa-Bank’s internal policies is social support to its own staff and development programs for talented youth. We should not forget about cultural projects, which include not only assistance to local theaters, museums and educational establishments, but also organization of tours of domestic and international stars throughout Russia.

In conclusion we would like to say that customers’ expectations from the Bank, with which they are prepared to cooperate, grow each year. We are aware of this fact and accordingly endeavor not only to offer our customers solutions to any financial tasks from expedient handling of current operations to financing and implementation of major projects, but also to foresee their future needs and expectations. We make relations with the Bank understandable, transparent and predictable, but at the same time we are always ready to please our customers and partners with surprising offers of still better ways to satisfy their requirements of financial services. We work every day to ensure that each of our customers can take pride in having the best financial partner — Alfa-Bank.
We managed to expand cooperation with our existing clients, partly thanks to improved models of account management for individuals, companies and private entrepreneurs. We were rewarded by the growth of the Bank’s market share in demand accounts — of corporate clients as well as individuals.

Regarding 2013, several external factors need to be mentioned that influenced the Bank’s performance to some degree. Even though individual consumer spending continued to grow, as did the credit market (by 29% on average across the country, according to the Central Bank of Russia), the economy slowed down in general, corporate clients’ revenues suffered, and the GDP improved weakly. In that situation quality customer management, the ability to find appropriate solutions for every need and every client, business efficiency — all the things Alfa-Bank had been developing year after year — meant more than ever.

Another important trend was strengthening of the regulator’s role, which, among other things, resulted in purging the banking systems of financial organizations involved in shady activities. In the existing situation Alfa-Bank has maintained its positions as the largest private bank in Russia, trusted by its customers, as well as those many who flocked to the Bank from other banks, mostly small regional ones.

The regulators also kept their last year’s promise to hold back retail credit growth. Even though this will affect business only in 2014-2015, when the changes come into full effect, we can already observe slower growth rates in retail lending. This forces players in the segment to change their business model as their profits are decreasing. Alfa-Bank, however, is protected better than its competitors, because in the retail segment we de-
derive the most revenues from transactions rather than loans. Alfa-Bank is the best bank for everyday life, specializing in sophisticated management of current accounts. With such a competitive edge, the Bank does not need to change its business model in retail.

Finally, in 2013, we continued to prepare for the new regulating standards passed by the Basel Committee on Banking Supervision (Basel II and Basel III). Alfa-Bank is following the Strategy in doing everything necessary to work under the new system.

Whatever changes occur in the Russian economy, the Bank’s stable and professional team will unfailingly provide excellent service and keep its competitiveness in any situation. Our employees and corporate culture are the foundation of our competitive advantage — the capital Alfa-Bank treasures the most. Our effective strategy for developing and retaining staff, a transparent motivation system, our social policy and training are the achievements that have allowed the Bank both to win loyalty of the currently working employees and attract new, the most gifted and skilled talents. This refers to frontline employees and top management alike.

Last year Alfa-Bank’s team was augmented with several excellent specialists. Alexey Tchoukhlov became Chief Financial Officer, David Brown became Chief Risk Officer, Maria Shevchenko was appointed Chief Operating Officer. Our thoughtful personnel policy is one of the advantages that in 2014 still allows Alfa-Bank to maintain the best ratings among private banks in Russia and the CIS on the backdrop of banks’ ratings downgrades triggered by the Ukrainian events.

The impeccable professionalism of the risk management team helped the Bank not only to avoid financial losses, but also to increase profits even as economic growth slowed down. Operational risk management at Alfa-Bank is configured to minimize its exposure to any internal and external hazards.

As for Operations, Maria Shevchenko’s efforts to implement project and process culture and improve project efficiency make Alfa-Bank stand out among Russia’s financial institutions and adds an even greater competitive advantage.

An important element of the Strategy is to develop the technological advantage. Alfa-Bank has always spearheaded the sector in business technologies. In 2013 its status was acknowledged by both customers using our remote services and experts: Alfa-Bank took the top in three nominations of the Markswebb Rank & Report’s rating and COMNEWS portal’s rating of Russian mobile and online banks. Alfa-Click (online banking service) was in 2013 awarded Russia’s best online bank by the Global Financial Market Review.

Developing the technological leadership, last year the Bank started another important and interesting project — Alfa-Lab. It is a special division of Alfa-Bank focused on innovative digital solutions and products. Another fact worth mentioning is that 2013 saw integration of the Bank’s technological resources, and now Alfa-Lab’s team administers software development both for the retail and corporate segments. This should make synergistic use of the divisions’ expertise and preserve high standards throughout.

Development of its competitive advantages, effective risk management and teamwork on every stage let the Bank set new financial performance records. According to IFRS in 2013, Alfa-Bank raised its net profit to USD 900 million, equity to 4 818 million, loan portfolio to 33 958 million. All divisions showed excellent results.

For example, operating profit of the Corporate and Investment Bank exceeded the goals with an exceptionally high ROE of more than 20%. This was made possible by a thorough optimization of the Bank’s corporate business. Even with the economy slowing Alfa-Bank has been able to increase the number of corporate customers and balances on their accounts. Further increase in fee and commission income was another important factor. For instance, in the mass corporate segment the share of interest income amounts to only 15%, the rest is attributed to risk-free fee and commission income. Given that quality of corporate clients tend to decline, this becomes especially valuable.

In the retail segment Alfa-Bank remains the only private player among the top three banks of the demand accounts market, and our share in this segment has approached 7.0%. According to IFRS, the amount of term deposits raised by 28.2%, which is well ahead of the market growth. Our retail credit portfolio reached USD 6.2 billion according to IFRS in 2013 — this means 32.7% higher than in 2012. Customers and experts again recognized the Retail Bank’s performance. For two years in a row, Alfa-Bank has been winning RETAIL FINANCE AWARDS’ top prize in the Best Retail Bank category, and taking the first place in the retail bank ranking by customer service.

Finally, the 2014 Private Banking and Wealth Management Survey by Euromoney declared Alfa-Bank Russia’s best private bank. We are proud that our work and customer-oriented approach have earned a favorable appraisal from such a reputable European magazine as Euromoney. We constantly improve our service, introduce innovative prod-
ucts, making the world of finance simpler and more convenient and we are glad that this was noted by experts.

2014 is shaping up to be a difficult year for the banking sector, and in current vulnerable environment customers’ trust is more important than ever. Even in conditions of economic uncertainty, Alfa-Bank has always maintained steady progress ahead of the market, and we are confident it will this time as well. Stable customer base growth that took place in 2013 will continue in 2014, because it is the customer that all our products, strategies, services and technologies are intended for. Our mission is to make the world of finance simpler and more convenient, and we move in that direction every day. Speed, flexibility, out-of-the-box thinking, technological advantages plus top-notch service and strong risk management let us increase customer confidence and year after year stay the country’s number one private bank.

TECHNOLOGY OF SUCCESS
EFFICIENCY

Increasing efficiency is one of the main vectors of our development in a competitive environment. Performance indicators and financial results that were relevant two or three years ago could be obsolete tomorrow. Each of us can contribute to improving business efficiency of the whole Bank. We qualitatively enhance the value of our company, while implementing a large-scale changes as well as many small innovations every day.
RUSSIAN ECONOMY AND BANKING SECTOR OVERVIEW

Global environment remains rather favorable

There were significant changes in global environment in 2013 that were not actually too negative for Russia. Firstly, global growth prospects started to improve mid-2013, reacting to the faster-than-expected recovery in Eurozone and global economy. EU countries that were in a recession in 2012 showed improving economic growth rates, returning to positive growth in 2H13, indicating an end of intense stage of the crisis.

US growth rates also improved during the year, with GDP growth of 1.9% in 2013, exceeding market expectations. US debt figures showed improvement. Deleveraging over the past five years helped to curb the level of household debt from 100% of GDP in 2008 to 80% of GDP in 2013. Also, US budget deficit was only 4% of GDP last year against 7% of GDP in 2012 and 8% in average for the period from 2009 to 2012, being a positive sign.

The better growth outlook positively effected on energy prices. Combined with support from geopolitical factors, oil prices were remarkably stable last year ranging from $100 to 120/bbl. The fear of the shale oil and gas revolution failed to affect market sentiment last year. The only concern was that as opposed to the oil market, metal prices were under pressure because of increasing concerns over the sustainability of Chinese growth.

Concerns over China target not only risks of the country’s economic model, but also reflect increasing nervousness over the attractiveness of emerging markets as an asset class. Better growth in US economy and strong job creation allowed the Federal Reserve to initiate tapering of the previously launched quantitative easing. The tapering itself was preannounced in the mid-2013, but actual implementation was delayed until December last year because of the US budget crisis. The change in US monetary policy pressured all emerging markets currencies, causing indices to decline, interest rate to increase and economic growth rates to decelerate in these countries. Capital outflow from emerging market countries is likely to continue in 2014 and it remains major risk factor.

All things being equal, neither Fed tapering nor concern on China have a visible effect on Russia, while oil prices remained consistently high, having a rather favorable effect on Russia’s economic trend last year and supporting financial stability. In addition to high oil prices, poor development of local debt market also turned to be an advantage in the period of the capital outflow. The share of Russia’s state debt in total GDP is 10% that is one of the minimum rates of emerging markets.
Growth rate disappoints

The key surprise in 2013 was Russia’s inability to benefit from global economic recovery. Russian growth did not accelerate in 2H13, as had been expected, thereby raising more concerns about internal growth constraints. The full-year GDP growth rate was only 1.3% y/y — well below the 3.4% growth in 2012 — triggering a reconsideration of Russia’s growth case that now suggests the rate will likely remain rather limited in the mid- and possibly long-term. Even the government’s long-term official forecasts have been lowered, taking into account this new reality. In the end of last year expected average annual growth rates until 2030 were slashed to 2.8%, while the initial official forecasts were in average 1.5x higher.

However, growth was buoyed on the consumption side. Even though retail trade decelerated from 6.3% y/y in 2012 to 3.9% in 2013, local consumers appeared to be in a comfortable position. Real salaries continued growing last year, mainly due to indexation in public sectors. In 2013, the average salary grew by 12% y/y in nominal terms, while salaries were up 20% y/y in public sector. The demographic factor played strongly in favor of income growth. The unemployment rate last year
RUSSIAN ECONOMY AND BANKING SECTOR OVERVIEW

Macro picture is eroding

With the slower economic growth rate, idea of revisiting Russia’s macro fundamentals is more and more often coming to the minds of investors. Indicators suggest a material deterioration compared to 2008. Firstly, Russia’s image as a country with a very low debt burden has started to erode. Overall foreign debt is 35% of GDP, which is in line with the pre-crisis level; however, the growth composition was close to the historical low rate at 5.0-5.5%, reflecting stagnation in labor force due to poor birth rate in the 1990s. Number of young people aged under 20 years are currently 14 mln less than in the end of 1980s, which is a strong factor supporting salaries growth. Despite decelerated inflation, population still has rather low preference for savings, with a ratio of only 9%, which is as low as the pre-2008 high-growth years. Finally, the retail loan market grew by 29% y/y in 2013, providing additional support for consumer trend.

At the same time, what is good for consumers is negative for producers. Industrial output was up only by 0.3% y/y in 2013, stagnating for the main part of the year. The share of wages as a share of GDP reached a post-crisis high of 52% last year, while the share of corporate profit declined, reaching a historical low of 29%. Not surprisingly, companies in this environment cut capex and investments declined by 0.2% y/y for FY2013, driven by a decrease in construction. The capacity utilization in the Russian industry has recently reached its pre-crisis high, limiting the upside to the industrial output going forward.

The limited business growth opportunity remained a strong factor for net capital outflow, which was the only 2013 economic indicator that did not decline from 2012’s level, accelerating in 2H13 on fears that US monetary tapering would render access to foreign debt refinancing more difficult. For the full year, net capital outflow was $63bn, exactly the same as in 2012, and for the last five years, accounting for $290bn.

RUSSIAN ECONOMY AND BANKING SECTOR OVERVIEW
RUSSIAN ECONOMY AND BANKING SECTOR OVERVIEW

Banking system: NPLs are the key risk factor to watch

The appointment of new governor of the CBR marked the beginning of a sharp increase in CBR activity to clean up the banking sector. The number of banks in Russia is still very high at around 900, and this number has started to decline more quickly than previously, indicating very favorable process in the banking area. However, as this coincided with the beginning of Federal Reserve tapering, active license revocations fuelled some nervousness in the banking sector. As a result, consolidation of the banking sector received additional boost.

While in the previous years the potential shortage of financial resources to finance economic growth was a major cause of concern, in 2013 it became clear that the banks’ funding growth is not an issue. Overall, despite cleaning of the banking system, the deposit market growth was a positive surprise last year in both the retail and corporate sides. In 2013, funding growth exceeded our expectations. Corporate deposit growth reached 16% y/y, as the anticipation of US Fed-tapering-induced turmoil on the markets has pushed companies to accumulate additional financial cushions. The slow GDP growth environment and heavy pressure on the ruble have aggravated this trend. Retail deposit growth also surprised on the upside last year and reached 19%. We expect income growth to continue supporting retail deposit growth; however, ruble instability creates the risk of a higher preference for foreign currency savings. Though stable in 2013, the share of retail forex deposits jumped to a post-crisis high of 20% at the beginning of this year. In order to offset the faster dollarization of the banks funding

RUSSIAN ECONOMY AND BANKING SECTOR OVERVIEW

Secondly, budget stability has also deteriorated greatly. Russia faced the 2008 crisis with huge state reserves of $225bn, including $140bn in the Reserve Fund. As of end-2013, state savings accounted for only $175bn, including $87bn in the Reserve Fund, while a large portion of the National Welfare Fund already is or is expected to be spent on infrastructure projects. The key worry is that due to slowing economic growth and aggressive government social policies, the budget now requires a $114/bbl. oil price to balance, while in 2008, $62/bbl. was sufficient. The increased budget breakage oil price indicates increased vulnerability to negative developments on the commodity markets.

Finally, Russia’s balance of payments now looks more vulnerable. In 2013, the current account surplus was $33bn under a $110/bbl. average oil price, which was far below the $104bn under $94/bbl. in 2008. This deterioration reflects fast growth in imported goods and services, stagnation in non-oil exports, and an increased foreign debt payment burden. The persisting net capital outflow at 3-5% of GDP per annum is additional factor adding pressure to the balance of payments and causing nervousness on the financial markets.

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is a concern. While state foreign debt is only 4% of GDP (vs. 2% in 2008), quasi-sovereign debt of state-owned companies and banks has doubled from 7% GDP in 2008 to 14% GDP. Russia’s total foreign debt is now $732bn vs. $464bn at the beginning of 2008 and almost 80% of its growth in the last two years is due to the quasi-sovereign and sovereign borrowing. As a result of fast foreign debt growth CBR reserves cover only 70% of overall foreign debt, while on the eve of 2008, they covered over 100%. The decline in the debt-coverage ratio is a big concern, pointing to a dilution in previous macro achievements.

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Figure 9: Corporate net profit and GDP growth, % y/y

Figure 10: Corporate net profit and GDP growth, % y/y
RUSSIAN ECONOMY AND BANKING SECTOR OVERVIEW

In 2013, the CBR and Finance Ministry were proactively providing banks with ruble liquidity. In 2013, their presence in the banking sector liabilities was up by RUB1.4 tr. At the same time, the lending markets are causing more concern. Concerned with rapid 39% retail loan growth in 2012, including a 90% increase in credit card debt, the CBR tightened the non-collateralized debt regulation in Q1, which led to a sharp deceleration in short-term retail loan growth. By the end of 2013, credit card debt growth halved to 45% y/y, point of sale lending also slowed materially to 11%, and as a result, overall lending growth slowed to 29% in 2013. Even if the retail lending market growth rate stays at 20-25%, CBR monitoring and control in the segment will remain tight. Corporate loan book growth remained at 13% y/y in 2013 (unchanged vs. 2012). Combined with the poor economic growth environment, this suggests more concerns regarding loan quality and lower demand for loans in the corporate segment. Even if the current NPL level appears manageable and even declined from 4.6% to 4.1% throughout 2013, poor economic growth suggest that this improvement might be temporary.

If in the retail segment deceleration of the market growth rates was rather positive for the loan quality, the risks of corporate NPLs would be mounting.

The loan quality is an important area to focus on this year, and clearly only acceleration of the economic growth rate could be a positive catalyst. It became obvious in 2013 that Russia is challenged by structural constraints, which makes monetary tools of support irrelevant and do not allow the local economy to benefit from the better global environment. Thus, in the near term, the mood on the local financial markets and the wellbeing of the banking sector will largely depend on the government’s success in addressing internal structural constraints.

Figure 11: NPLs by segment, RUB bn and % of portfolio

Source: CBR, Alfa Bank

Corporate NPLs, RUB bn (LHS)
Corporate NPLs, % of portfolio
Retail NPLs, RUB bn (LHS)
Retail NPLs, % of portfolio

Our main goal — employees who are constantly evolving based on our corporate values and models of leadership competencies. Priority in our future work is development of capacity and performance of our employees and our corporate culture. Customer orientation is a quality that is necessary for each of our employees. This quality together with desire to achieve results, desire for self-development and co-operation determine the success of the organization. Bank gives these people the opportunity to realize their potential, because Alfa-Bank — the place of action for each of us.
2013 became a new successful milestone in Corporate Investment Bank’s development. Year-end operating profit surpassed the planned figures and ROE (return on equity) exceeded 20%, thus indicating the bank’s high efficiency. Net profit before tax, received by Corporate-Investment Bank in 2013, amounted to $803mln in accordance with IFRS accounts. A slight decrease in net profit before tax compared with previous year results ($834mln) was mainly caused by increased provisions charges in amount of $85mln. In 2013 Corporate-Investment Bank achieved significant increase in corporate client base. As of 1st of January, 2014 Alfa-Bank served about 109,200 clients compared with 82,000 clients at the beginning of 2013. Corporate-Investment Bank loan portfolio increased by 2% and amounted to $27.8bn in accordance with IFRS results. Current accounts of corporate customers grew by 18% and constituted $4.6 bn.

In recent years, corporate sector of the economy has been characterized by enhanced competition for quality clients. Owing to its competitive advantage and particular attention to the loan portfolio quality, Alfa-Bank achieves strong performance in this area. One of the priorities in 2013 was improvement of loan portfolio quality. This work has yielded the results. Despite the worsening economic situation share of overdue loans in total corporate loan portfolio remained stable and amounted to 1.2% by the end of the year. This figure is one of the lowest in the Russian banking market. Due to additional provisions created in 2013 overdue coverage ratio amounted to more than 340%.

Last year was an important step for the Bank’s Development Strategy, approved in 2012, and the year’s results show that business is moving in the right direction. There have been significant changes in Corporate Investment Bank team, with the purpose to increase its efficiency; work patterns have been restructured and systematized in accordance with the Strategy. Much has been done to make the changes occurring in the Bank more understandable and transparent, to convey to each of its employees the goals and objectives of changes. Much attention was paid to assessing the effectiveness of the Bank’s processes as well as the operation of its departments and their employees.

Many significant steps have been made in client relations. One of them, planned within the Strategy, was customer base segmentation by revenue. Particular attention was paid to corporate customers with revenues between $10mln and $100mln. Significant growth is planned for this particular segment and it is an important objective for the Bank next year 2014. Working with major corporate customers has always been and still is one of Alfa-Bank’s strong points. Today corporate divisions are facing an important task to apply the successful large business service models to the segment of customers with revenues between $10mln and $100mln. Much was done in this regard last year.

As for major client relations, Alfa-Bank has serious advantages over its competitors in this segment, as it had before. In particular, great importance is given to the Bank’s ability not only to meet the clients’ needs but also to anticipate and even form them. Individual approach to customers, analytics and industry expertise, prompt decision-making and broad range of products are the advantages that make Alfa-Bank an attractive partner for the most exacting customers. Investment and retail business product sales to corporate clients, as well as sales of Alfa-Insurance products, were another goal in 2013. In addition, growing risk-free transaction revenues in the major client segment remained a priority. In accordance with IFRS net fee and commission income of Corporate-Investment Bank increased by 23.3% to $228mln.

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Regional Development

As part of the Strategy, significant changes in the business model and organizational structure of Corporate Investment Bank were initiated. First and foremost, these changes are related to the interaction between the central and regional offices. It should be noted that, as before, Alfa-Bank is actively working on maintaining a large share of market presence in each region, in each industry in the region and in each customer segment in

MAXIM PERSHIN
Member of the Executive Board, Co-Head of Corporate and Investment Banking
In 2013 Alfa-Bank attracted a lot of new customers. A significant number of transactions were organized and carried out, including sale of complex structured products. A few transactions of the past year deserve a special mention. In February 2013 the deal on the debt restructuring of Chelyabinsk Pipe Rolling Plant Group went through. Chelyabinsk Pipe Rolling Plant Group is one of the largest pipe manufacturers in the Russian Federation. Alfa-Bank acted as a lender and one of the arrangers of two syndicated loans for a period of 7 years. Total volume of syndicated loans amounted to RUB86.5 billion. Active position of Alfa-Bank in the negotiation process as one of the arrangers of the transaction significantly improved the conditions of syndicated loan for all creditors. During transaction execution agreements between the borrower and other lenders regarding increased interest rate changes in security composition were reached between borrower and lenders along with substantial changes envisaging special points of syndicated lending market both Russian and international were introduced to the loan documentation.

In June 2013, Alfa-Bank acted as one of the arrangers of four-year syndicated loan to RESO-Leasing. The loan size is RUB5 billion, may be increased to RUB8 billion. Alfa-Bank acted as a underwriter, paying agent and security agent. VTB, VTB Capital PLC and GLOBEXBANK acted as co-arrangers of transaction. Latham & Watkins LLP was a legal advisor. The loan is secured by property rights under leasing contracts as well as by the leased property. Structure of the transaction also envisages use of the borrower’s special account with a special mode of funds allocation. This deal has become significant for the Russian debt market both in terms of security structure and the amount of financing taking into consideration size of the borrower’s business. In October 2013, Alfa-Bank, jointly with VTB Bank, VTB Bank (Deutschland) AG, AKA Ausfuhrkredit-Gesellschaft m.b.H., OJSC Promsyuzbank, CJSC ACB NOVIKOMBANK, and CJSC Asian-Pacific Bank, signed a one-year USD63.5 million syndicated loan agreement in favor of OJSC Belagroprombank (Belarus). The loan may be extended for a subsequent year. This transaction confirms the possibility of the syndicated lending market development by attracting the borrowers from the CIS financial markets.

Among other significant events, it is worth to note the participation of Alfa-Bank as a consultant in the merger of two major pharmaceutical brands: A.v. E and the 36.6 pharmacy chain. This is a landmark transaction for the whole market, as merged company became the largest pharmacy chain in Russia in terms of revenue and market share. In order to maximize effect from the merger for both companies, it was very important to organize and carry out the transaction as quickly as possible. Due to operational and well-coordinated work of Alfa-Bank, the transaction was carried out in the shortest possible time.

Successful completion of the transaction has once again evidenced high professional expertise of the Bank’s team, its ability to carry out complex transactions as well as its competence in the field of equity transactions. These advantages of the Bank, in conjunction with a broad product range, strong financial possibilities and prompt decision-making, make it an attractive partner for any company in trade and commerce industry.
INVESTMENT BUSINESS

2013 was a challenging year for investment business. It was marked by continued limited access to liquidity sources in all financial markets combined with active lending in the domestic market. This has led to two expected consequences: reduced income from trading instruments and structured transactions. Alfa-Bank quickly responded to the situation and took steps to improve efficiency of investment business. These measures resulted in the successful completion of the year with the financial results remaining at the level of the previous year, 2012.

Investment unit operation, as well as entire work with corporate clients, was performed in line with Alfa-Bank’s Strategy. Focus on the client, special attention to the team, improving efficiency and technology as well as risk control — all these priorities are reflected in the investment business development strategy. First, a major restructuring of the unit started in 2013. It is aimed at optimizing the unit operation in accordance with the market situation and the expected profitability of various business segments. The priority areas were currency markets, bond portfolio management and sales of structured products.

In sales of structured products, cooperation with a large number of counterparties became more intense, and therefore new financial structures relevant for the needs of such counterparties were created. The work resulted in overachievement of the target plans and increase in number of customers by approximately 20%. Also, number of customers of the Bank’s electronic platforms increased by 15%.

Another product actively sold in 2013 is a structured deposit. We can confidently say that this product was in great demand. Many customers who used it returned to the Bank again. And, of course, special attention was paid to improvement of customer service. To this end, measures were taken to improve the investment unit employee involvement in collaboration with colleagues from the corporate unit. An initiative called «joint business» was developed in Corporate Investment Bank. As part of the initiative, the Bank set up special working teams, which included employees from various departments. Each group faced general objectives on seeking new development opportunities for current customers and on attracting new customers. This work format proved its efficiency, led to new transactions, and improved the efficiency of interaction between various Bank’s departments.

Several special formats of communication have been created within the framework of cooperation of corporate and investment business experts. The first of them is the «four», i.e. a group consisting of several representatives of four departments: customer, credit, investment and banking, and investment. Group meetings discuss trends in each direction, prospects and development opportunities. In addition, special groups were set up for each customer. The objective of each group is to anticipate customer’s needs and offer it a profitable and convenient solution. An important initiative was creating the technological development plan of Corporate Investment Bank. Its mission is to create an electronic platform for investment business development using existing Bank’s systems and methods as well as to enhance the efficient use of information technology in 2014-2016.

It is also worth noting that in 2013 the Bank introduced a new version of OPICS system. Necessity to upgrade the system was mainly caused by increased volume of transactions and the number of customers, but developed system also ensured the Bank’s compliance with new regulatory requirements of the Central Bank of Russia.

Debt Market

For many years Alfa-Bank has already been one of the leading players in the debt market. In 2013, it participated as arranger in some significant bond placement transactions. Thus, the Bank acted as the organizer of the first transaction in the Russian debt market on securitization of the bonds, secured by consumer loans, for LLC HC Finance. The transaction amounted to RUB5 billion. Credit ratings of Standard & Poor’s at BBB level and Moody’s Investors Service at Baa3 level were assigned to the bonds issue. This transaction is a landmark in the Russian debt market. Compared to mortgage bonds, which until now have been the only covered negotiable instrument in local debt market, new bonds of LLC HC Finance, secured by consumer loan portfolio of HCF Bank, have several advantages: a shorter duration and no planned depreciation; higher interest on loans and, as a result, a higher excess spread. HC Finance bonds meet all the formal requirements for inclusion in the Lombard List of the Central Bank, as well as investment of pension funds, and provides a reduced burden on the banks’ capital.

Last year saw another significant placement with Alfa-Bank’s participation. Together with Promsvyazbank, Alfa-Bank successfully placed the bonds of Alfa Ukrfinance , series 01, worth RUB3 billion, with a maturity of 3 years. International rating agency Fitch Ratings assigned B rating to the bond issue. The series 01 bonds meet the requirements essential for inclusion to the Bank of Russia Lombard List.
Alfa-Direct

In 2013, we launched a new, more investor-friendly version of online trading system — Alfa-Direct. The final version of this world-class system will be released in mid-2014. To date, it has no equivalents either in Russia or abroad.

Conference «Russian Banking Sector: Slowdown. Seeking Solutions»

On October 17, 2013, Alfa-Bank held VIII Conference for mass media: «Russian Banking Sector: Slowdown. Seeking Solutions». More than 130 representatives of federal and regional mass media took place in the Conference. The speakers at the conference were: Petr Aven, Chairman of the Board of Directors of Alfa-Bank Group, Anatoliy Aksakov, Deputy of the State Duma, President of the Association of Regional Banks of Russia, Vladimir Nazarov, Director of the Scientific and Research Finance Institute of the Ministry of Finance of Russia, Mikhail Kovrigin, Director of Department for Supervision over System Critical Important Credit Institutions of the Bank of Russia, Sergey Moiseyev, Acting Director of the Financial Stability Department of the Bank of Russia, Evgeniy Yasin, Supervisor of the Research and Scientific Institute «Higher School of Economics», etc.

At the Conference, the representatives of the largest financial institutions, state bodies as well as regional and federal media once again discussed the present and future of the industry. The participants of the Conference got an insight into the financial and economic situation in the country, the current state of the banking sector, and asked questions to experts, economists and bankers.

Forecasts for 2014

The complex task of Corporate-Investment Bank for 2014 is preservation and development of its competitive advantages, satisfaction of clients’ needs, technology development, synergy of Bank’s teams, further straighten of Bank’s position in major corporate clients segment by offering them integrated solutions based on massive industry expertise, and use these successful patterns in other customer segments. As for investment business, 2014 will be complicated enough. This is due both to the local geopolitical situation and to the global situation in emerging markets. Ruble weakening, which occurred early in the year, may have a positive impact on the development of the Russian economy. However, it will also cause a drop in purchasing power of the country’s population. Thus, the only right decision of the Bank in such circumstances is to adapt strategy of business at the investment market to the current situation and to continue improving business efficiency. Alfa-Bank is the largest private bank in Russia that is why it is the best possible partner for customers who expect the Bank’s flexibility and individual approach to their financial objectives. In the next year, the Bank will continue to develop a comprehensive approach to each customer aimed at meeting its current and anticipating future needs. 2014 will be a year of new challenges and achievements for Corporate Investment Bank, but constant attention to customers and high quality of service will remain unchanged.

The basis of our strategy — is exceptional skill in building the relationships with different customer segments. The ability to speak with each client on the language he understands is our strategic competitive advantage. We are constantly looking for ways to make our customers’ lives easier and more convenient, thanks to the range of tools that we use, including modern and safe technology. We pay particular attention to feedback from our customers, as it helps us to monitor the effectiveness of our services. In any situation, the Bank aims to be understandable partner and to be as useful as possible for the customer.
RETAIL BANKING

The year 2013 ended very successfully for Retail Banking, which has accomplished many ambitious goals. Good operating results are best illustrated by the fact that number of the Bank’s customers exceeded 10 million and the market share increased in all core businesses, such as retail on-demand deposits, credit cards, loans (excluding mortgages). Despite sustaining growth in this market nationwide, the Bank demonstrated impressive results in this segment which is an indicator of clients’ trust and confidence to the Bank. Lending segment demonstrated significant growth in all key indicators.

Key financial indicators are in line with impressive results achieved over the year. By the end of the year the average market share of retail on-demand deposits increased to 6.99%, which exceeds the beginning of the year rate by 0.49 p.p. Alfa-Bank preserved its positions as the only private bank entering top three in this segment. In accordance with IFRS accounts term deposits increased by 28.2% compared with previous year results and amounted to $7.2 bn., exceeding an market average growth.

Alfa-Bank’s retail loan portfolio demonstrated a 32.7% increase according to IFRS and reached $6.2bn. In 2013, Consumer loans portfolio grew by 13.9% constituting $1.6bn. Considerable growth was demonstrated by all segments of retail lending. Thus, Alfa-Bank’s credit cards and cash loans portfolio grew significantly, surpassing the previous year’s result by 46.9% and amounting to $4.3bn. In this segment Alfa-Bank also demonstrated better dynamics than market. By the year-end Alfa-Bank took the fifth place in terms of credit card portfolio. The market share in accordance with RAS amounted to 5.55%.

Within the payroll projects, the Bank issued more than 700,000 bank cards in 2013. In the past year Alfa-Bank established a new record in terms of the number of acquired payroll customers.

And finally, the total number of Alfa-Bank’s retail customers increased by 19.3% in comparison with 2012 and amounted to 10.6 million.

Bank Development Strategy

In accordance with the Retail Business Development Strategy adopted in 2012, last year Alfa-Bank continued to work towards maintaining leading positions in the area of customer experience and technologies for retail customers, as well as increasing the number of active clients. An important component of this Strategy is work in accordance with segment-oriented approach aimed at meeting the customers’ current and future needs and expectations. Customers in each segment should receive offers corresponding to their requirements, expectations and preferences which is the main goal of the Retail Bank in the nearest future.

Regional Development

Developing of a profitable branch network and increased payroll projects are the major sources of growth in the number of active customers. Currently quality banking services still present high demand in the Russian regions. This is the need Alfa-Bank aims to satisfy by creating presence in new locations.

Alfa-Bank has significantly expanded its presence over the last year. Alfa-Bank opened 46 new fully-fledged customer service branches, having increased total number of offices by over 20%. Thus, at the end of the year the Bank’s network consisted of 270 fully-fledged branches, with 67 of them being located in Moscow and 203 in the regions, as well as 18 «light» offices located in the regions (4 with cash services and 12 without). Alfa-Bank’s branches first appeared in Zelenograd, Lyubertsy, Yakutsk, Abakan, Novocherkassk, Taganrog, Berdsk, Linevo, Ulyanovsk, Ilyichinsk, Petrozavodsk, Miass, Yasny, Penza, and Pskov. In addition, a new A-Club office was opened in Krasnoyarsk.
Employee Relations

Retail Bank’s employees are the capital which is of particular importance for Alfa-Bank, as they represent the Bank in the eyes of customers. Therefore, the development and retention of staff became one of the most important points of Alfa-Bank’s Development Strategy. In 2013 Alfa-Bank achieved success in this area. Comparing with the previous year, staff turnover in the Retail Bank decreased by 6%. To a great extent, this is the result of HR strategy. The most significant achievements are development and introduction of career models for the mass divisions; the new system of staff performance management and special incentive programs; additional attention to the adaptation of new employees; implemented social policy programs as well as a comprehensive training program, taken by more than 9,500 employees.

Alfa-Bank gives everyone the opportunity to realize their potential, achieve personal success, and make a contribution to the Bank’s success at the same time. Alfa-Bank’s employees are active, initiative, curious, striving for continuous self-development. They successfully work as a team and achieve their objectives together. Retail Bank’s staffing strategy allows employees to achieve more while Alfa-Bank provides high quality services to clients.

Technological Effectiveness

Traditionally, Alfa-Bank’s strong point is development of innovative technologies. As Russia’s leading private bank, we always offer the market advanced solutions and new technological approaches to organizing customer interface channels, primarily via the Internet and mobile phones. In an increasingly competitive environment, we constantly improve our processes and technology to create a more efficient customer service package. In 2013, Alfa-Bank announced a new version of the Alfa-Click online banking service with a completely updated platform and design. The service now offers additional features and has become even more advanced and user-friendly. Among other things, there is now a traffic ticket payment function. In addition, Alfa-Bank customers can now transfer money via the Alfa-Click online banking service and the Alfa-Mobile banking service. To make a transaction, the user only has to enter the transfer amount and the recipient’s mobile number or e-mail address. Alfa-Click offers My Expenses — a new expense and the recipient’s mobile number or e-mail address. Alfa-Click offers My Expenses — a new expense monitoring function which presents graphically all items of the customer’s expenses. With this service, the Alfa-Bank’s clients will be able to view expenses with a breakdown by items for a certain period, which means easier monitoring of finances.

Alfa-Bank’s customers use remote access for 90% of their various transactions, and we are glad to provide them with this opportunity, while constantly improving the technical level and functionality of our online banking service. Last year, the total number of customers using Alfa-Click passed a serious milestone of 3 million people, while the number of corporate payment recipients has exceeded 11,000. According to this figure Alfa-Bank is the second largest bank in Russia. The Alfa-Click banking service has not only been praised by the customers, but also recognized by the professional community. It became Russia’s best Online Banking Service in 2013, according to Global Financial Market Review. The leaders were determined by the expert board of independent guest editors, as well as by subscriber voting.

Alfa-Bank’s customers can perform even more transactions using their mobile phones. Nearly all of the Bank’s customers carry a mobile phone today. So, if the Bank is “in the phone”, it can provide a maximum number of services to its customers through the latter. Therefore, Alfa-Bank assigns great importance to development of mobile banking. The Bank’s customers actively use its offers. In 2013, the number of Alfa-Mobile users exceeded 400,000. The figure is significant. It allows Alfa-Bank to remain a trendsetter in this segment. One of the exciting developments in this area was last year’s free mobile application “Oh/tpp” for iOS, which allows money transfers between different bank cards. This convenient and fast application is available to cardholders of any bank.

Alfa-Bank’s achievements in mobile banking were noted by the experts. According to research made by Deloitte, Alfa-Bank is one of the leaders in mobile applications in the Russian market. The company has tested 25 mobile banks, most of which belong to the largest lending institutions in the country. Deloitte experts noted that Alfa-Bank’s mobile apps offer the most advanced services to its customers. For instance, when they have downloaded the application to their phones, customers can make transfers between accounts simply by touching two smartphones together. The application also supports the “augmented reality” function enabling search for ATMs and offices when scanning the area within walking distance.

Moreover, Alfa Bank took the first place in the mobile and online banking rating in Russia. It was rated the best in three categories by Markswebb Rank & Report and COMNEWS: best for total efficiency, best for convenience, best for Android mobile banking service. Heading the rating is another confirmation of Alfa-Bank’s leading position on the mobile banking and online banking market.

Another area where Alfa-Bank firmly holds leadership is Internet acquiring. Profound experience in this field allows Alfa-Bank to constantly serve companies of any size, regardless of the volume of their business. The main advantage of Alfa-Bank Internet acquiring is that the processing of transactions and card payments is on the side of the Bank, i.e. is carried out without the involvement of intermediaries, which ensures a high level of payment security. A multilevel system of fraud prevention and risky operation monitoring, introduced in the processing center of Alfa-Bank, allows users to control and prevent even complex fraudulent transactions. Security of online payments is certified by international payment systems using 3D-Secure: Verified by Visa and MasterCard SecureCode and takes place up to the world-class standards.
Today, Alfa-Bank’s market share in this segment is 32.3%, i.e. about a third of all transactions are carried out through Alfa-Bank. The Bank has over 300 corporate strategic partners — prominent players in all business areas, many occupying leading positions in their respective markets.

Retail Lending

Retail lending development in the past year was quite active: consumer lending market grew by 29%. Retail banking has shown good results in this area and has achieved its goals. For example, in the segment of consumer lending, Alfa-Bank continued to develop partnerships both with major federal retailers, such as «M.Video», «Eldorado», «DNS», «Svyaznoy», «Euroset», as well as small regional companies and local retail chains specializing in the sale of tourist services, electronics, household appliances, furniture and other goods and services. In 2013, Alfa-Bank started lending to the online store «Sotmarket», one of the largest players in the market of e-commerce in Russia.

It is worth noting that last year Alfa-Bank changed POS-loans sales technology at the points located in its partner’s stores. Now, the customers can process at these points not only loans for goods, but also process credit cards or get a cash loan. By the end of the year the number of such retail points was more than 2,770.

Another important event in the field of consumer lending in 2013 was the creation of an innovative product — the «My purchases» card. To date, approximately 25-30% of consumer loans sales points across Russia use this product. The partner of the project at the federal level is Russia’s largest network of home appliances and electronics «M. Video» and at the regional level — the store of digital equipment DNS and other leaders in consumer lending. The peculiarity of «My purchases» is that the customer receives a credit card instead of a term consumer loan for the purchase of goods. A required amount is debited from the card account and with the loan repayment the funds are returned to the card and become available again. At the same time the amount of payment varies when using the card, the payment date remains unchanged and the available limit on the card can be increased by the Bank with time. The card allows to attract the customer for a longer period: the term of a consumer loan is 10 months on the average, while the card is valid for 3 years. The card received by the customer has broad opportunities. In the near future it will allow to withdraw cash, pay for the goods and services and spend money at your own discretion.

Last year, Alfa-Bank launched another interesting project for retail customers — a credit card online store Alfacards.ru. It is a user-friendly, clear and bright store where you can choose a credit card for any purpose and for all occasions. Having chosen a card, the customer can apply for it using online questionnaire and then only needs to wait for the decision of the Bank and come for the card to the office a few days later.

The service allows each person to choose a credit card in accordance with their goals and needs, as online store provides not just the opportunity to fill in an application for a loan product but provides each user of the website a full service allowing to compare and choose card settings. This is another way to make the Bank easier and more convenient for all its customers.

Customer Feedback

Alfa-Bank traditionally focuses on obtaining feedback from its customers as it is the most important source of information assisting in improving the quality of customers’ experiences. The same was in 2013. The Bank actively used all channels of feedback: feedback on the website of the Bank, its own page on Banki.ru portal, reviews left in the offices and, of course, communications through social networks, where the number of users associated with the Bank grew by 76% over the past year.

The Bank’s objective is to respond promptly to the feedbacks and make everything to ensure customers’ satisfaction with the Bank, their using of its services and their recommendation of the Bank to their friends. A significant point is the personal involvement of all participants of the process, starting from the rank and file employees to the management, in the work related to the improvement of the customers’ experiences. Last year the Bank firstly conducted a research using the NPS indicator — net Promoter Score. The results of two waves of research have shown that every second customer is ready to recommend Alfa-Bank, noting among its strengths the technological effectiveness and innovation. This is a good result, which shows that the Bank’s customers appreciate it and find it a reliable financial partner providing high quality services.

To receive feedback from the customers immediately after they leave the office and to respond to it promptly, the Bank last year launched the pilot of a new tool — sms to the Bank. These are the messages asking to assess the quality of service by the Bank’s employee, to which the customers can respond. The customers willingly use this tool. It also provides additional motivation for the Bank’s employees to provide the highest quality of service as they realize that they are assessed. Such an assessment is also of great importance for branch managers as it is a management tool for the situation and rapid response to customer’s complaints and dissatisfaction, preventing the claims to the Bank. In the departments participating in the pilot project the customers give a high rating to the level of service — about 75% of the reviews about the work of the Bank are positive.

Awards and Ratings

Achievements of the Retail Banking in 2013 were marked not only by the customers loyalty to the Bank, but also by the experts. For two consecutive years now, Alfa-Bank gets the highest award in the category...
RETAIL BANKING

«Best Retail Bank» according to RETAIL FINANCE AWARDS and also takes the first place in the ranking of retail banks in terms of customer service. The award was created to distinguish the most worthful representatives of the retail banking business. That is why, it is of great importance for the Bank that it received this award again in 2013.

Last year the Bank again was a finalist of SPEAR’S Russia Wealth Management Awards 2013 — Russia’s first annual award for private banking & wealth industry professionals; the Bank received the award of Visa for quality customer service in the category «The highest international level of an issuer of debit cards approvals» and two consecutive years now has become a leader in the field of Russian Internet banking according to the analytical research agency Forrester Research.

Forecasts for 2014

The 2014 priority for Alfa-Bank retail business is growing faster than the market in the key product directions: lending, including credit cards, on-demand deposits and savings accounts.

The priority is also given to the development of our distribution network, both physical and alternative channels. This year we plan to scale a new format of our offices based on a segmental approach. From the perspective of alternative channels of sales and service we develop our processes and technology to deliver leading solutions for online and mobile banking. Consistently high levels of ATM network and call-center customer accessibility are also of great importance for us.

We continue to be customer-oriented. The main focus of the Bank is to build long-term relationships and increase customer loyalty. Our basic tools are the introduction of segment-oriented strategy, which takes into account the needs and expectations of each segment in terms of product and service standards, as well as the improvement of customers’ experiences. In the near future the competition in the Russian banking market will continue growing, so the success will belong to the bank that can provide the highest quality service, not only satisfying but also anticipating the customers’ needs. This is what Alfa-Bank does and will do going forward.

Our Bank’s objective is to be a reliable financial partner for the residents of Russia, participating in their daily lives. This is because none of our customers operate such terms as banking relationships. They are ordinary people who have a variety of needs — to make a payment, to obtain financing for any purpose or to preserve and increase their finance. Banks provide the tools to implement these or those needs, help their customers maintain a high degree of financial freedom. And we see our mission to become the main everyday bank for our customers — the best bank for daily life.

Risk management — our core competence and strategic competitive advantage. The success of the Bank’s strategy implementation depends on it. We do not aspire to but we are able to make decisions under uncertainty thanks to a competent evaluation and analysis of all available information we have. We are able to determine the degree of risk that we can and must afford.
MASS BUSINESS

Historically, Alfa-Bank focused primarily on individual clients as well as medium and large corporate businesses. However, the market situation has changed lately, and the serious potential of small business segment has become apparent. A few years ago, the Bank started to actively develop this business, and in 2010 the segment of small businesses and individual entrepreneurs (companies with annual revenues of up to RUB150 million, and since 2014 — RUB300 million) was restructured as a separate banking unit — Mass Business. Over the years, the unit has demonstrated excellent revenue growth in priority areas, exceeding average market growth. And finally, this year we would like to present the results of Mass Business unit in the Annual Report.

Last year results have shown that even against the reducing number of companies in this segment in Russia, Alfa-Bank’s competitive advantages have allowed it to increase number of customers. Thus, by the end of 2013 number of clients in small business and individual entrepreneurs (with annual revenues of up to RUB150 million) segments exceeded 90,000, which is 57% higher than in 2012. This enabled the Bank to almost double its market share by number of customers, (growth constituted 2.21%). Alfa-Bank’s fee income in the small business segment grew by 45% and amounted to USD58.2 million, while the average monthly call deposits on customers’ accounts increased by 41% compared with the previous year and amounted to USD852 million.

Although our main priority in this segment doesn’t relate to credit products, mass business loan portfolio increased by 30%. However, the share of interest income in Alfa-Bank’s Mass business segment is only 15%, while the rest is attributed to risk-free fee and commission income. By the beginning of 2014, just three years after the Bank started working with small businesses and entrepreneurs, the share of this segment in transaction income of the Bank’s entire corporate business reached 50%.

These achievements are particularly noticeable against the background of market changes that occurred in 2013. During that year, number of small businesses decreased by approximately 20% — from 5 million companies early in the year to 4 million by the end of the year. This is primarily due to the increased tax burden on small businesses. Extremely low unemployment rate (below 5%) was another factor contributing to the slowdown in the development of small business, as stable employment opportunities prevent people from opening their own businesses.

However, Alfa-Bank actively attracted customers throughout 2013. Even against the background of stagnation, number of customers and balances on their accounts have grown practically one-half. Over past three years, number of customers has increased fivefold. By 2016 we expect to attract up to 5% of total number of companies in this segment, i.e. about 200,000 customers. The Bank managed to keep high business growth rates, mainly due to effective sales system and development of non-banking services attractive for small businesses. In addition, tightening of regulatory requirements to banks is driving non-compliers from the market, while customers of troubled banks are choosing reliable partners, such as Alfa-Bank.

Alfa-Bank’s Strategy. Client Relations

In 2013 all Bank’s business units including Mass business actively implemented their strategy. One of mass business strategy key points was an active increase in market share and, respectively, number of customers. In this respect, the Bank increased the number of sales managers and opened 38 new offices servicing small businesses and individual entrepreneurs, where customers can get a full range of products, services and advice. There are about 200 such offices in Russia today. The second important point was extra attention to client relations. Special stress was put on non-banking services, i.e. those that do not bring immediate profit to the Bank but increase customer satisfaction and improve the chance of their long-term cooperation with the Bank. Several such projects were launched in 2013, and they were all popular among the customers.
Quite often, banks do not pay enough attention to small businesses and entrepreneurs as opposed to large corporate clients and the quality of service for such customers is lower. Alfa-Bank’s approach to such customers is different. In early 2013, the institution of personal managers for this category of companies was established in 12 million-plus cities. Personal managers are the Bank’s employees who work with the customer, their goal being to develop relations with the customer, including the sale of new products and services. It means that every entrepreneur served by the Bank in these cities, regardless of the size of his/her business, now has a manager who can help with any matter anytime. Such an approach to direct client relations triggered growth of the customer base: the standard rate of customer turnover from the Bank of about 2.5% per month reduced 3 times after the introduction of personal managers. In 2014, the institution of personal managers will be introduced in all the cities where the Bank operates.

The second important point in working with clients was promoting cross-sales of additional products, including not only corporate products, such as loans, deposits and various payment services, but also those of priority for the Bank as a whole, for example, payroll projects. However, special attention was paid to development and implementation of non-banking services and projects as they enable to create added value offers for customers. Through this approach, the customers consider Alfa-Bank not just an institution allowing them to fill their financial needs, as usual banks do, but a partner that cares about them and offers them assistance and support where necessary. One of the most significant non-banking projects was the Customers Club in 2013.

Customers Club and Other Non-Banking Services

Customers Club is a unique customer support system developed by Alfa-Bank. In each city where the Bank operates it has partners in key sectors of B2B services and has reached agreements with these companies on substantial discounts for the Bank’s customers who have joined the Customers Club. Now an entrepreneur who needs to open an office or a retail outlet automatically receives a discount with all Alfa-Bank’s partners does when opening an account. When organizing the office operation, an entrepreneur may, through the Customers Club, save the amount that exceeds the cost of annual servicing at the Bank. If the Bank thus assists the entrepreneur in the launch of his/her business, it creates closer and trust relationship with the customer. The same scheme applies to other non-financial services available to customers of Mass Business owners — received a special present from the online accounting of regberry.ru. With the new service, users can quickly and smoothly prepare a set of documents required to register business. The system automatically generates a complete set of documents which only needs to be printed out. The service is useful not only for starter entrepreneurs but also for those who want to register a second or a third company. The documents are also accompanied by a detailed manual describing further steps necessary for registering as a limited liability company or individual entrepreneur. In addition, after entering all required information, a starter entrepreneur may send an application for opening an account with Alfa-Bank directly from the system. The Bank’s manager will contact the prospective customer and help him choose the best package of cash management services.

Another unique project for small businesses offered by the Bank in 2013 is a special legal support program. Now every entrepreneur opening an account with Alfa-Bank receives a certificate for legal support of his or her business in one of the best companies in his/her city. Thus, by becoming an Alfa-Bank client, a business owner realizes not only his or her need for financial products and solutions, but also for legal and tax support. The purpose of the program is to support small businesses which traditionally face numerous legal and tax problems in their daily activities and, unlike large companies, cannot afford to employ a staff lawyer.

Last year, Alfa-Bank held another campaign for small businesses together with the online accounting office My Business. As part of the campaign, all the Bank’s customers — small businesses and individual entrepreneurs — received a special present from the online accounting office My Business: free sending of returns via the Internet to the Federal Tax Service and free use of all My Business services for three months. The campaign for small businesses took place within the strategic partnership of Alfa-Bank and My Business service. In the autumn of 2012 the integration of Alfa-Business Online Internet Banking with the online accounting office My Business was completed. This provided fully automatic data exchange between the Bank and the accounting service system. The integration has let entrepreneurs keep their books in the same window with Internet Banking: send payments, receive statements, generate tax payments. This makes it possible to automate the bookkeeping process and in some cases even do away with accounting services.

Last year the customers of the unit were offered a concierge service. Before only premium cards holders could use this service, but in 2013 it became available for small business owners. During the first two months more than 1,500 customers used Alfa Concierge service. Most popular requests are air or train ticket booking and flower delivery to partners and counterparties.

And, finally, last non-banking project that we would like to describe is joint campaign of Alfa Bank and Yandex. Direct. Companies and entrepreneurs who opened a settlement account with Alfa-Bank receive a certificate for advertising their business in the Yandex contextual advertising system. Joint campaign...
with Yandex.Direct is one of the projects aimed at assisting starter entrepreneurs in developing their business, as advertising is essential for any business regardless of its size. For many businessmen, work with Yandex.Direct became their first advertising campaign, as small businesses often even cannot imagine that they may advertise their business in Yandex. It is worth noting that cooperation with such a high-tech company was significant for Alfa-Bank, as it also pays great attention to development of the most up-to-date technologies to ensure convenience and safety of its customers.

In future we plan to create new non-banking projects that will make the work of small businesses even easier and more convenient. This is one of the priorities for our unit as we attach utmost importance to our customers’ loyalty and feeling of support that the entrepreneurs get through our services strengthen their relations with Alfa-Bank.

Employee Relations

Another important point of Alfa-Bank’s Strategy is particular attention to employees of each unit. For Mass Business unit, this work is directly connected with another postulate of the Strategy, i.e. improving unit efficiency. Our team is our most valuable asset. Great attention is paid to employee relations, to maintaining the internal corporate culture and development of each employee. Thus, various contests and team events are conducted within the Mass Business unit, cultivating and encouraging leadership behavior of employees. The Bank takes serious and successful measures aimed at reducing staff turnover, in 2013 staff turnover reduced twofold. The team stability has a direct impact on the efficiency of its work, as new employees always need time to start showing good results and, therefore, by reducing turnover we increased the efficiency of each account manager or sales manager. The unit objective, as well as the objective of the Bank as a whole, is to ensure that each employee performs his job as well and as efficiently as possible. This applies to all categories of employees: salespeople that attract new businesses to the Bank, account managers who work with existing customers, office staff that serve local customers. Every person employed by Alfa Bank can rely on assistance in professional development. And, of course, the effectiveness of employees increases due to the constant development of technologies used in the Bank every day.

High Technology

Alfa-Bank is a tech-savvy bank, which is one of the most important competitive advantages for Mass Business as well. Connection of effectiveness and new technologies is necessary to provide as many remote transactions as possible. This reduces the burden on branch employees and makes it more convenient for customers to cooperate with the Bank as they do not need to come to the office to perform most transactions. The Bank constantly analyzes the operation of its departments, and if we see that the customers visit us for routine operations that can be performed remotely or through an ATM, we inform the customers respectively and instruct them on how to use remote services.

For example, the latest version of Alfa Business Online is a new generation of online banking. Moreover, last year another high-tech service for small businesses and individual entrepreneurs was launched: Alfa-Business Mobile, an updated mobile banking service allowing customers to manage their funds via their phones. Alfa-Business Mobile application was developed for Android and iOS devices and provides access to customers’ settlement accounts via a mobile phone. With Alfa-Business Mobile on a smartphone, customers connected to Alfa-Business Online can make necessary payments to its counterparties via their phones, view account balance and receive statements on latest transactions. About 25% of new customers immediately connect to the rubles payment service. In addition, Alfa-Business Mobile provides corporate clients of the Bank with information and location-based services: addresses of branches and ATMs, with a navigation capability, as well as the Bank’s news. Over 12% of corporate customers connected to the Internet banking service use its mobile version and this share is constantly increasing. All these possibilities are now available for tablet users, including the popular iPad. Alfa-Bank was one of the first banks in Russia to implement such a project. It shows that we are ready to move forward and improve our services based on current trends and, most importantly, our customers' needs. We are pleased to offer our customers the latest technologies that will make interaction with the bank even more convenient and enjoyable.

Another popular product for small businesses is Alfa-Cash card. Entrepreneurs can use their cards to withdraw and deposit cash, which is immediately reflected on the company’s account. As of the beginning of 2014, the number of issued cards exceeded 25,500. Alfa-Bank’s ATM network with a cash-in function grew by 570 (to 1,745) during the year.

Another project — mobile card payment terminals — was created for small companies that would like to start accepting card payments thus increasing number of their customers. In fact, more and more customers prefer to pay by bank cards today: according to various studies, about 20% of customers refuse from a purchase if card payments are not accepted. This greatly hinders the development of small trading companies, which cannot afford acquiring. Alfa-Bank developed the Alfa-PAY service — accepting payments for goods and services using bank cards through mini terminals connected to smartphone or tablet — for such companies as well as for those who find acquiring inconvenient. Mini terminals contain a security chip, and data from payment cards are transmitted to the smartphone in an encrypted state and are not stored in it. Verified by Visa and MasterCard SecureCode are also used for authentication. Also, there is a system of company check before connecting a mini terminal and around the clock online fraud monitoring of each transaction takes place. Currently, the service is available both in Moscow and in the regions — in more than 50 cities where the Bank operates.
Settlement products the Bank creates for its customers are focused primarily on making the customer’s interaction with the Bank even more convenient. Alfa-PAY service helps the Bank’s clients simplify settlements with their customers, expand customer base and develop their business with a convenient and innovative tool. By launching this project, Alfa-Bank once again confirmed that it is an innovative and technologically advanced Bank, offering its customers banking products and services aimed at business development and sales growth. Of course, much attention is paid to security of all transactions conducted through the Bank. We are proud to note that during the entire 2013 there was not a single successful attempt of theft from the accounts of entrepreneurs in Mass Business segment. It shows that the funds of our customers are strongly and reliably protected.

Plans and Forecasts for 2014

Mass Business unit has set ambitious goals for 2014: to increase number of customers to 130,000 companies and entrepreneurs and market share up to 3%. The priority is still given to development of risk-free business and risk-free product sales related to daily maintenance of transactions, settlements and cash services. Another important objective in 2014 is to increase number of products per active customer. Finally, much attention will be given to further enhancing the effectiveness of each manager working at the Bank and maintaining team stability.

We do not expect an increase in number of small businesses next year. To the contrary, the trends that we see today enable us to predict a certain narrowing of the market. However, it will not affect the ability to reach the goals of the unit and to achieve scheduled targets. Alfa-Bank is well aware of customers’ needs in this segment. Namely for this, not putting priority to small business lending, we pay great attention to development of non-banking services that are really in demand among our clients. In addition, the unit has a strong system of active direct sales, which is more typical for companies in the FMCG sector than for financial institutions. And, of course, our team is our additional advantage. Our employees are united by one goal, they like to work at Alfa-Bank, have opportunity to grow and develop their faculties. Strong corporate culture gives Alfa-Bank special advantages over competitors.

In conclusion, we would like to mention an interesting fact. A survey of small businesses has revealed that Alfa-Bank currently ranks among the top three banks which, according to the respondents, are actively cooperating with small businesses. The development of this customer segment has been continuing for three years, and during these three years Alfa-Bank managed to achieve significant progress both in actual performance and with regard to its image among the target audience. This means that in future small businesses will increasingly choose Alfa-Bank as their financial partner.
For Operational Department the year 2013 was very successful as we demonstrated outstanding performance results. Last year, there were many important processes taking place in Operational Department — rethinking the role of Operational Department within the Bank in line with the Strategy implementation, re-evaluation of Operational Department's current position and setting goals for the future.

The functionality of Department covers three areas:
- support and execution of the Bank’s day-to-day business operations;
- strategy implementation support through changing processes and developing of projects;
- control of operational risk processes and collection of overdue retail loans.

In view of the current year performance results, first of all we would like to note that we achieved significant reduction in personnel turnover — almost twice to 13%. Such results were achieved thanks to the system work aimed at employees involvement and launch of new communications. As of today there are 12 subdivisions engaged in Operational Department. The headcount of its staff exceeds 4 thousand people covering all banking operations geographically spread from Sakhalin to Kaliningrad. The quality and continuity of operations depend on their work. We estimate this achievement as significant.

Operational Department has undergone some structural changes: a new directorate of SAP implementation and development, processes directorate, and Project office were created. These changes confirm new role of Operational Department — transformation of the Bank in line with the Bank's Strategy.

In 2013, we achieved significant progress in the implementation of the Bank's process culture: updating of retail business credit process, implementation of Generator of Contracts — unique technology to create and handle contract documents on credit deals known as Generator of Contracts; implementing a complex of objectives to grow the number of automatically treated payments without employees participation; the rate of ATMs availability increased above 92%. A new strategy of process and project culture implementation was developed, and new top processes the transformation of which will make it possible to ensure stable competitive edge for the Bank were also selected.

Last year, there was number of other projects implemented with the aim to improve efficiency: centralization of certain functions in regional branches and automation of processes in the subdivisions of Operational Department. In spite of the growing number of transactions in 2013 by about 31% their cost dropped down to 12%. It points out that our work to achieve higher efficiency produced excellent result.

Once again, Alfa-Bank was honored for its high quality service of customer payments with Quality Recognition Award. This award is given by one of the largest American banks — JP Morgan Chase Bank. The Bank earned this appraisal for its automatic straight-through processing of customer payments with JP Morgan Chase Bank at the level of 98.16%. The Bank’s prestigious awards have become a good tradition. In addition to its annual recognition by JP Morgan Chase Bank, in October 2013 the Bank received STP Excellence Award 2012 from another world largest bank — HSBC. The Bank’s recognition on the part of our authoritative foreign colleagues is a result of our high level transaction service, flawless professionalism and responsibility of Operational Department employees consistently delivering the best performance results.

It should be mentioned that there is another important project started in 2012 — the Bank’s second operating regional center in Barnaul. The number of its active customers is constantly growing.
up together with the number of transactions performed by them. Several years ago the Bank adopted a new concept for opening operating centers in the regions to meet retail customer needs. Thus it possible to use the potential of highly educated employees in the regions as the level of competition for better staff in the regions is lower compared to Moscow, and we are eager to support the regions by retaining the talented youth locally. On the other hand, the Bank benefits due to economy of scale from the centralization of functionality, minimization of personnel turnover, and balancing the load between different centers. The capacity of new regional center in Barnaul is about 2,000 people. Since January, 3,130 new employees have already occupied their workplaces in the building joining the team of Operational Department.

Risk Management

Risk management is an important factor in operational activities of any financial institution. The objective of Operational Department is to minimize losses from risk occurrence. For instance, with overdue debt collection the default risk is the less when most of overdue loans are returned at the earlier stage within 30 days. Last year, we achieved good results in this area. One more task is work with operational risks in general. In 2013, Managing Operational Risk Committee was established in Alfa-Bank to handle system approach and monitor the processes where such risks may occur.

The Bank’s Development Strategy. Key Areas

Increased efficiency has become one of the priority objectives of the Bank to be implemented within its Strategy. So, in 2013 Operational Department worked on three key initiatives. First one is related to the implementation of the Bank’s project culture and increasing the level of project maturity. Today, a large-scale project is going on to develop unified banking methodology and common approach to assess project managers performance. This project was started last year and is planned to come to principally new level by the end of 2014. Thus the Bank will create an overall portfolio of Bank’s projects with priorities, a single model of assessing project managers, a program of their development and training, and a unified project methodology, including project launch, maintenance and closing down, as well as a unified model of project management.

Second initiative is related to the Bank’s process culture. This initiative can be divided into two parts: on the one hand it is implementation of the process culture in particular optimization of the Bank’s key processes. The work is performed as follows: finding the ways to increase the efficiency of processes, in view of higher quality for customers and lower operational risks as well as cost reductions. We emphasize not only optimization of processes but also implementation of the results monitoring system and quality control process. This is required to continuously monitor our work client assessment by the customers in particular the availability of services and observance of deadlines.

Third initiative is called Knowledge Management System. Under this initiative three projects were launched, the first one is aimed to grow our personnel expertise, providing people with quick access to all necessary working documents. The second one is related to the development of a single communication platform in the Bank — Alfa-Mir web portal. Active work on it began in 2013 and is going on. In 2014, the portal will be redesigned and provide full access to the new up-to-date services in line with the requirements and desires of the new generation. For instance, experts in different areas will have an opportunity to communicate on the same platform, and each division will be able to create its own site and share the required and interesting information through the news feed.

All processes launched within the Strategy have a direct impact perceive of Alfa-Bank by customers, since its make the work with Alfa-Bank easier and more convenient. For instance, the optimization of retail business credit processes has become not only economically effective, but also drew new customers to the Bank, because it minimizes credit approval time. Promptness is one of the determining factors for our customers; therefore this work will be going on. So, for instance, the Bank’s project culture will make it possible to implement new ideas in a faster way, with customers using new services and technological solutions.

Prospects for 2014

Under the Strategy through 2016 we consider not only our operations, but operating model of the Bank as a whole. We have to achieve maximum efficiency in the processes, projects, technologies and new developments. In highly competitive environments the efficiency is the key advantage of Alfa-Bank. The Bank must be sensitive to customer needs, offer better service, and at the same time use its own resources. Support units play a key role here, as we create additional value to the Bank’s customers by rendering assistance to business.

As for the team of Operational Department, the priority is to ensure further increase of personnel expertise. In this regard we plan to perform overall performance appraisal and additional training of staff to meet high quality standards within the expected professional competence. In our relations with customers specific attention will be paid to the creation of a new quality assessment system that will take into consideration the customers’ opinion. In the context of processes and technologies the important factor will be the increase in the level of process maturity and getting maximum effect from the implementation of processing structure in key banking processes.
As before, significant efforts will be made to manage efficiency. This is an important but not the only one aspect for Operational Department. In 2014 we plan a number of system improvements through the use of most up-to-date technologies. Specific attention will be paid to project management enhancement — our objective is to implement at least 90% of the Bank’s strategic projects in good time and at a high quality level. By year-end we intend to grow efficiency to a considerable extent in all our divisions.

In terms of risks our priority objective is to provide higher quality of the operational risk management system, focusing on the collection of overdue debts.

Many employees in Operational Department have a direct contact with customers, for instance those working in collection of overdue debts or in exchange control. Therefore, in 2014 we will focus on a better customer-oriented approach as the way our officers communicate with customers determines the perception of the Bank in general.

And finally, next year Operational Department will follow not only the Bank’s Strategy, but develop its own strategic plan so that each division would have a clear picture of its objectives, priorities and values in working with customers, continuously striving for higher efficiency, supporting our unique corporate culture, and be an integral part of Alfa-Bank’s team. Only the teamwork, cooperation and partnership with our colleagues from all banking units will make it possible for us to achieve highest results, thus making Alfa-Bank private bank No.1 in Russia.

Alfa-Bank attaches great importance to proper financial risk management. The main purpose of Alfa-Bank’s risk management is to achieve the optimum ratio of risk-return ratio for its operations. In 2013, Alfa-Bank also paid great attention to improving risk management as a key element for its development strategy implementation while Russia’s economic growth is slowing. During the year, Alfa-Bank evaluated internal and external risk factors, both in the existing Alfa-Bank’s portfolio level and in potential future transactions. This helped Alfa-Bank to avoid financial losses and ensure the stable level of loan portfolio quality and revenue growth in current economic environment.

We now apply a uniform risk management policy to our entire product line involving management of financial risks (including credit, market, currency, liquidity and interest rate risk), as well as operational risk management. Financial risk management involves determining appropriate risk limits and ensuring that the risk of potential losses does not exceed these limits. Operational risk management means ensuring the proper functioning of internal processes and procedures to minimize Alfa-Bank’s exposure to other internal and external risk factors.

Alfa-Bank’s risk management strategy consists of several basic components: risk management, risk identification, risk assessment and risk monitoring.

Risk Management: Organizational Structure

Alfa-Bank’s the Board of Directors has overall responsible for overseeing the risk management structure and monitoring management key risk. Its duties also include approving transactions that pose a significant capital risk. The Audit Commission is responsible for overseeing the internal control framework, assessing the adequacy of risk management, as well as developing compliance supervision.
policies and procedures. The committee meets on a regular basis. It meets regularly and makes recommendations to the Board regarding the development of the risk management structure, the quality thereof and relevant regulatory requirements.

The Bank’s Executive Board is responsible for monitoring and implementing risk-mitigation measures as well as controlling over compliance with the existing risk profile. The Risk Management Department together with the Retail Risk Division are responsible for the operation of the risk management system, thus ensuring that general risk management principles are followed, risks are limited and reports on them are submitted.

Credit, market and liquidity risks both at the portfolio level and the transaction level are managed and controlled through a system of Credit Committees, the Treasury, Risk Management Directorate, Retail Risk Division and the Asset and Liability Committee («ALCO»). In order to facilitate effective decision-making, Alfa-Bank has established a hierarchy of credit committees and individual limits, depending on the type and amount of the exposure. Within the Risk Management Department, the Credit Risk Department deals with credit risk for corporate clients, financial institutions, SMEs. There are also the business units in charge of market and operational risk management. The Retail Risk Division deals with credit risks inherent in such products as credit cards, cash loans and consumer loans with special purpose, automobile loans and mortgage lending.

Risk Identification

Within its organizational structure as a whole, Alfa-Bank identifies both external and internal risk factors, as well as how to manage them. Particular attention is paid to developing risk overviews that are used to identify the full range of risk factors and serve as a basis for determining the required risk mitigation procedures. A brief survey of the key risks is regularly reported to the Executive Board and the Board of Directors of Alfa-Bank.

Risk Assessment, Risk Management and Risk Control

Alfa-Bank’s risk assessment, reporting and control procedures vary by type of risk but share a common methodology developed and updated by the Risk Management Department and the Retail Risk Department. Compliance with Alfa-Bank’s standards is supported by periodic reviews undertaken by the Internal Audit Department. The results of review are discussed with the heads of the relevant business units and presented to the Audit Committee and senior management of Alfa-Bank.

In 2013, there were no material changes in the risk management system compared to 2012. However, due to slowdown of Russia’s economic growth, Alfa-Bank modified its lending policies and certain risk management procedures in order to maintain and strengthen its position on the banking market.

Credit risk

As a financial institution, Alfa-Bank takes on exposure to credit risk — the risk that the counterparty will be able to pay its obligations in full when due. Credit risks are structured according to the product, borrower, industry sector, etc., with a risk limit set for each parameter. Such risks are constantly monitored and regularly reviewed.

Analysis of the credit quality of financial assets is based on their stratification by established limits: higher limits are assigned to those counterparties whose credit quality is better. The exposure to any one borrower, including banks and brokers, is further restricted by sub-limits covering off-balance-sheet exposures and daily delivery risk limits in relation to trading instruments such as forward exchange contracts.

Credit risk exposure is managed through regular analysis of the ability of borrowers and potential borrowers to meet their interest and principal repayment obligations and by changing these lending limits where appropriate. Credit risk exposure is partially managed by obtaining collateral and corporate and personal guarantees.

Alfa-Bank defines its risk appetite by approving its Lending Policy, assigning authority to decide on risk-taking issues to committees, and granting specific approval of large transactions. The Lending Policy sets forth the framework for monitoring exposure to credit risk, including portfolio concentration limits and definition of responsibilities. In 2013, Alfa-Bank revised its credit policy to ensure it meets the current risks and market situation.

Alfa-Bank’s Credit Committees are responsible for approving the volume of credit risk. Each credit committee operates under special instructions approved by the Board of Directors.

• Depending on the credit risk amount, decisions on transactions with corporate clients are approved either by the Main Credit Committee or Supplemental Credit Committees. The maximum risk exposure is approved by the Executive Board: these include most major transactions with a value of over $200 million. Under certain conditions, loans approved by the Main Credit Committee have to be approved by the Executive Board or the Board of Directors.
• The Retail Credit Committee approves the credit policy regarding retail business, retail loan product parameters and pricing requirements (interest rates, the fees and fines), approves the process of loan product issuance, and the basic risk control procedures for retail business. The Committee meets monthly, and its members include representatives of all major Alfa-Bank retail departments.

Credit risk monitoring

Exposure to credit risk is subject to constant monitoring on a regular basis.

The Corporate Lending Department identifies potential problem transactions using a unique set of criteria for assigning the status of «questionable» transactions, as well as escalating procedures based on status of problem. Any significant exposer per customer with deteriorating creditworthiness are reported to and reviewed by the respective Credit Committee.

In order to manage credit risks, Alfa-Bank separates the loan portfolio into the following pools:

• Current loan pool includes current loans and loans overdue less than 14 days.
• Problem loan pool includes loans showing early signs of potential deterioration in credit quality and require more attention from management.
• Problem loan pool includes loans overdue for more than 14 days, or loans transferred to the unit that works with problem asset to devise restructuring plans, exercise of security, the initiation of judicial proceedings, etc.

Depending on the credit quality of the customer and the extent of the risk, the customer sales, margin and dynamics of the loan portfolio are analyzed on a monthly / quarterly basis.

The Retail Risk Department monitors retail loan portfolios on a regular basis. Such monitoring includes tracking of the following indicators: approval/decline indicators for all segments (products, customers), days overdue (both at different times and at the same time), prolongation indicators (overdue debt transferring to various stages), contacts and promises indicators in order to monitor debt recovery effectiveness; loan loss rate at various stages per product and per approval type, special pilot programs, maximum limits set for each retail portfolio, write-off of bad debts for each product portfolio, debt recovery for each product portfolio, risk assessment procedure stability and the statistical models and figures used to all products, for which the such models are used, as well as the effectiveness of applicant information verification procedures.

Portfolio concentration limits are checked weekly and the results are reported to the Main Credit Committee. In addition, the Committee is informed of the situations when the maximum limit is approached. The Main Credit Committee ensures that the impact of new transactions on the loan portfolio concentration corresponds to Alfa-Bank’s risks appetite and the portfolio limit structure.

Throughout 2013, Alfa-Bank paid special attention to the processing of doubtful and problem loans. Moreover, the Committee on Corporate Customers’ Bad Loan Recovery monitored bad loans: the outlook for their repayment, exercise of security, legal proceedings pertaining to debt recovery, terms of loan restructuring and requirements to provide additional collateral for loans.

Credit Risk Monitoring

The measures taken to control credit risk are aimed at securing adherence to the policies and procedures employed by Alfa-Bank. Thus, Alfa-Bank has implemented the credit risk regulation mechanisms, which facilitate effective risk management.

Credit Risk Mitigation

Alfa-Bank employs a variety of methods in order to mitigate credit risk of its lending operations, thus monitoring the loss factors (such as losses from retail transactions, probability of default and cross-default) and the scope of risk in the event of default, as well as the system risk indicators based on the portfolio.

At the transactional level, an assessment of a borrower’s ability to service the proposed level of debt is performed. Also, Alfa-Bank obtains loan collaterals, such as mortgage, floating charge or pledge of tangible assets. Various forms of legal protection are used, such as mutual settlement agreements, obligations under commercial lending agreements as well as credit support methods.

The credit exposure is actively managed. There are procedures ensuring early identification and prompt response to transactions showing the signs of deterioration. Such response includes credit exposure mitigation, additional collateral, restructuring or any other measures that may appear necessary.

A credit risk premium is included in the risk assessment and lending decisions. The credit risk premium seeks to provide fair compensation for the amount of each credit risk assumed by Alfa-Bank. At the portfolio level, credit risk is diversified in order to prevent excessive concentration. The portfo-
Financial Risk Management

Lien concentration limit includes the maximum exposure per borrower, industry concentration, maturity concentration limit, the limit of unsecured loans, and the internal ratings limit. In 2013, the two last limits were non-binding but subject to monitoring in financial statements. Alfa-Bank’s maximum credit exposure is included on the balance sheet value of the financial assets in the consolidated financial statement. For issued guarantees and other credit obligations, the size of the maximum credit risk must equal the size of liabilities.

Market Risk

Alfa-Bank takes on exposure to market risks, i.e. risks of changing in Alfa-Bank’s position values as a result of changing market indicators: issue securities values, stock indexes, exchange rates, book prices on precious metals, interest rates.

Alfa-Bank’s overall position is split up into the position of bank service provision to corporate and retail customers and investment activity position.

Market risk of Investment Activity

Alfa-Bank’s exposure to market risks inherent in investment business is managed based on the position amount limits and statistical metrics limits established for both aggregate position of the investment business in shares, fixed income instruments, in foreign currency and derivatives (treated as separate ‘trading positions’) and for managing individual sub-portfolios.

In addition, sublimits are set for the risk amount pertaining to different types of securities (including shares and debt securities) and markets, as well as position limits per issuers and individual instruments. The securities position limits are approved by ALCO. Additional limits for issuers pertaining to debt securities are approved separately by the respective Credit Committees.

Statistical risk measures employed:

- Value at Risk (VaR) 99% with 1 day time horizon and 99% degree of credibility.
- Liquidity adjusted Value at Risk (liq.-adj. VaR) with 99% 99% degree of credibility.
- Severe losses measure.

It is important that employment of this approach does not prevent losses outside of such limits in case of more material, extremely unlikely market movements.

Limits that are based on statistical risk levels are monitored on a daily basis by the Risk Management Directorate on the level of trading portfolios. Aggregate risk for investment business positions is monitored by the Risk Management Department on a weekly basis.

Market Risk of Banking Activity

Exposure of banking service provided to corporate and retail customers to market risks is managed through a system of limits controlled by the Treasury.

Currency Risk

Alfa-Bank’s Treasury is responsible for the centralized management of foreign exchange risk of its balance sheet position. ALCO sets an open currency position limits monitored daily by the Treasury on the basis of provided management reports on the open currency position. Alfa Bank uses derivatives to manage the current and projected size of the risk arising from its open currency positions.

Interest Rate Risk

Alfa-Bank is exposed to interest rate risk, which mainly results from difference in terms of raising and placing fixed rate securities by Alfa-Bank and floating interest rate schedules for floating rate securities raised and placed by Alfa-Bank.

Alfa-Bank’s interest rate risk is managed by the Treasury within the limits set by ALCO separately in Russian rubles, US dollars and euro, and for the overall exposure of Alfa-Bank.

Two sets of metrics are used as the interest rate risk metrics:

- metric of bank «present value» sensitivity to interest rate shift by 100 basis points (PV1%),
- metrics of expected net interest income sensitivity within 1 year horizon to interest rate shift by 100 basis points (EaR1%).

The limits are controlled by the Treasury’s Asset and Liability business unit on a weekly basis. The Treasury also uses foreign exchange forward contracts to control interest rate positions in various currencies and interest rate derivatives, such as interest rate swaps in US dollars and Russian rubles. Liquidity risk.
Liquidity risk is defined as the risk of a company facing hardships when performing its duties related to financial commitments. Every day Alfa-Bank has to satisfy payment demands in respect of funds received from overnight deposits against current accounts, maturing deposits, loan disbursements, the margin and other demands related to financial instruments. Alfa-Bank does not maintain the amount of available funds necessary to meet all these demands, as experience suggests that the minimum level of reinvestment of maturing funds can be forecasted with a high degree of probability. Liquidity risk is managed by Alfa-Bank’s Treasury and ALCO.

Alfa-Bank is committed to maintaining a stable funding base comprised primarily amounts due to corporate and retail customer deposits, as well as debt securities in issue and due to other banks, and maintaining adequate diversified portfolios of liquid assets in order to be able to respond promptly and smoothly to unforeseen liquidity requirements.

Alfa-Bank’s liquidity management requires a consideration of the level of liquid assets necessary to settle obligations as they come due; maintaining access to a number of funding sources, having plans for financing in case of an emergency, and monitoring liquidity ratios to be recorded in accordance with regulatory requirements. Alfa-Bank calculates liquidity ratios on a daily basis following the requirements of the CB RF.

The said requirements are as follows: acid ratio (N2) calculated as the readily obtainable assets to demand liabilities ratio; current liquidity ratio (N3) calculated as the liquid assets to liabilities maturing within 30 calendar days; long-dated bank-liquidity (N4) calculated as the assets maturing within one year to the regulatory capital and liabilities maturing after one year.

The Treasury prepares the liquidity profile of financial assets and liabilities, as well as builds an adequate portfolio of short-term liquid assets, largely made up of short-term liquid trading securities, deposits with banks (including central banks) and other inter-bank credit facilities in order to maintain sufficient liquidity.

Liquidity is monitored daily, and liquidity stress testing is carried out regularly under a variety of scenarios involving both normal and more severe market conditions. The Treasury builds a forecasted liquidity model on a daily basis. Various scenarios are monitored including or excluding projected new lending. In order to forecast liquidity, information on overdue payments is updated on a regular basis.

Operational Risk

The operational risk is defined by Alfa-Bank as the risk of direct or indirect losses/profits from inadequate or erroneous internal processes for banking activities and transactions, personnel actions, IT systems and external developments.

Alfa-Bank basis its operational risk monitoring on the instructions of the Bank of Russia and the Basel committee’s recommendations.

Alfa-Bank has established the Operational Risk Steering Committee for reviewing operational risks and decision-makings.

Operational risk management encompasses risk identification, assessment, monitoring, control and/or mitigation of Alfa-Bank’s exposure to operational risk.

Alfa-Bank uses the following instruments to control operational risk:

- Acquiring data on the events of operational risk implementation.
- System of key risk indicators.
- Assessing operational risks for processes, products.
- Insuring operational risks.
ALFA-BANK’S COMPLIANCE WITH THE CODE OF CORPORATE CONDUCT

The Bank observes recommendations of the Code of Corporate Conduct. To maintain the standards of corporate governance and improve its system, the Bank’s Code of Corporate Governance was approved at the Extraordinary General Shareholders Meeting in late 2013 (Minutes No. 02-2013 dated 02.12.2013), which was developed in compliance with the provisions of the current legislation of the Russian Federation, regulations of the Bank of Russia and the requirements of the Code of Corporate Conduct recommended by Directive of the Federal Commission in the Russian market of securities No. 421/р dated 04.04.2002 «On the recommendations to use the Code of Corporate Conduct», Articles of the Bank and the Bank’s internal documents. The Bank’s Code of Corporate Governance takes into account the provisions of the Code of Corporate Governance recommended by Letter No 06-52/2463 of the Bank of Russia dated 10.04.2014.

The Bank’s Code of Corporate Governance is an internal regulatory document, which defines the fundamental principles, rules and standards of corporate governance to be adhered to by the Bank when carrying out its business activities, covering the following areas: protection of lawful rights and interests of the Bank’s shareholders, organization of activities of the Board of Directors and executive bodies, strategic management, risk management and internal control, prevention and regulation of conflicts of interests, disclosure of information, along with securing procedures related to significant corporate activities.

When carrying out its business activities in accordance with the Code the Bank commits itself to follow the below general principles of corporate governance:

- compliance with the legislative requirements, other standard rules, Articles and internal documents of the Bank;
- ensuring and protection of rights of the Bank’s shareholders;
- providing equal (in view of the requirements of standard rules) attitude to all shareholders of the Bank;
- ensuring that the Board of Directors is accountable to shareholders of the Bank;
- strategic management by the Board of Directors of the Bank’s operations;
- efficient control by the Board of Directors over performance of the Bank’s executive bodies;
- providing governing bodies with an opportunity to perform efficient control over current activities of the Bank based on the principles of rationality, good faith, exclusively in the Bank’s interests, and ensuring that executive bodies are accountable to the Board of Directors and to shareholders of the Bank;
- ensuring efficient risk management and internal control of the Bank;
- ensuring timely disclosure of complete and reliable information on the Bank;
- ensuring openness and transparency in performing significant corporate activities subject to the compliance with and protection of rights of the Bank’s shareholders.

In compliance with the legislation, Articles of the Bank and Regulations on the governing bodies of the Bank, the Bank has put in place the system of its corporate governance, including distribution of roles and authority among its governing bodies: the Bank’s General Shareholders Meeting, Board of Directors, Executive Board and Chairman of the Executive Board. The Bank’s governing bodies operate and exercise their authority strictly within the authority set out in the said documents.

Activities of the Bank’s Board of Directors are organized and carried out in strict compliance with the current legislation, Articles of the Bank, Regulations on the Bank’s Board of Directors, and Regulations on the committees of the Board of Directors. The said documents regulate the authority of the Board of Directors, requirements to the members of the Board of Directors and the procedure of their authority application.

The Bank’s Board of Directors approves of the Bank’s Strategy, and monitors its implementation. The Bank’s Strategy for 2012-2015 approved by the Board of Directors (Minutes No, 11-2012 dated 19.06.2012) was in effect in 2013. Early in 2014, due to certain forecasted changes in the economic situation on 23.01.2014 the Bank’s Strategy for 2014-2016 was approved at the meeting of the Board of Directors (Minutes No. 01-2014 dated 23.01.2014).

The Bank’s Board of Directors acting in accordance with the Articles of the Bank and Regulations on the Bank’s Board of Directors is responsible for the work on risk management, setting up and implementation of efficient internal control, and approval of the transactions that put at risk a considerable part of equity.

The Bank’s Executive Board acting in accordance with the Articles of the Bank and Regulations on the Executive Board is responsible for the fulfillment of resolutions of the Board of Directors, determination of risk management policy and maximization of revenues; it approves regulations related to the work of committees and other collegiate bodies of the Bank. The Bank’s Executive Board is responsible for monitoring and implementing efforts to mitigate risks, and control over the compliance with certain risk parameters.

Risk Management Directorate acting in accordance with its Regulations is responsible for the operation of the Bank’s risk management system, securing the fulfillment of general risk management principles,
including identification of risks and limitation on risk size, with the related information submitted to higher collegiate bodies.

Risk Management Directorate monitors and evaluates the level of bank risks, suggests measures to mitigate and minimize risks, and is responsible for the implementation of these measures within the specified roles of various divisions of the Directorate. To this end, the Directorate develops Policies for the Bank’s risk management, with its officers in charge being members of the profile committees and other collegiate bodies of the Bank.

Credit, market and liquidity risks, both at portfolio and transactions level, are controlled through Credit Committees and Asset and Liability Committee.

The Bank’s Board of Directors approved Procedure on the prevention of conflict of interests that defines measures on the prevention of conflict of interests when carrying its business activities. In addition, in order to prevent conflict of interests, shareholders of the Bank on a regular basis at the Annual General Shareholders Meeting approve the expected interested party deals in the normal course of business, indicating permanent partners of the Bank with their governing bodies including members of the Bank’s governing bodies.

In order to prevent conflict of interests, the Bank has also developed and approved Regulation on the terms and procedure of making interested party deals by Alfa-Bank’s employees and/or their affiliated persons (Addendum No.1 to Bank Order No. 1206 dated 03.12.2010.).

In accordance with the current legislation, information on the beneficiaries of the Bank and on its affiliated persons is available both to members of the Bank’s Board of Directors and to the unrestricted number of all interested persons; it is disclosed in due time through posting on the Bank’s web-site being fully available to the public and is regularly updated.

The Board of Directors has at its disposal all the necessary information in order to observe the requirements envisaged by Articles 78-84 of the Federal Law «On joint-stock companies» related to large-size and interested party deals.

Alfa-Bank’s Code of Corporate Ethics was approved by the Board of Directors and posted on the Bank’s web-site fully available to the unrestricted number of all interested persons. Employees of the Bank and members of the Bank’s governing bodies have familiarized themselves with the rules personally.

To implement the provisions of the Code, the Compliance Directorate monitors the observance of its requirements in the Bank. The Bank ensures the disclosure of information on its operations in accordance with laws of the Russian Federation based on the principles of reliability, regularity, timely publication, balance between the openness of the Bank and protection of its lawful interests.

In order to fulfill its obligations in full on the disclosure of information in a proper and timely manner the Bank has approved the following documents:

- Order «On the procedure of information disclosure on OAO «ALFA-BANK» No. 261 dated 16.03.2012;
- «Regulations on intra-company interaction when disclosing information during the issue and circulation of bonds of OAO «ALFA-BANK» (with all additions and amendments thereto) (approved by Order of the Bank No. 813 dated 17.07.2012);
- «List of information of the Bank, related to insider information» (approved by Order of the Bank No. 1267 dated 14.12.2011);

In order to monitor and supervise the Bank’s internal control system the Board of Directors approved the following documents have been approved:

- Regulations on Internal Control Department of OAO «ALFA-BANK» (approved by the Board of Directors, Minutes No. 05-2011 dated 22.02.2011).
- Policy for internal control of OAO «ALFA-BANK» (approved by the Board of Directors of OAO «ALFA- BANK», Minutes No. 05-2011 dated 22.02.2011).

The Bank’s Board of Directors on a regular basis monitors the work of the Bank’s Internal Control by review and approval of semi-annual and annual Internal Control Performance Reports and Action Plans.

The Bank will continue to improve its corporate governance system in order to comply with all changes to the current legislation of the Russian Federation introduction of new corporate governance standards and international practice and appearance of new shareholders, the Bank and all other interested persons.
AlfaStrakhovanie Group

AlfaStrakhovanie Group combines AlfaStrakhovanie PLC, AlfaStrakhovanie-Life LLC, Medicine AlfaStrakhovanie LLC, AlfaStrakhovanie-OMS LLC.

It is part of the Alfa-Group industrial and financial consortium, which includes companies such as Alfa-Bank, Alfa-Capital, Alfa Capital Partners, A1, Rosvodokanal, X5 Retail Group N.V. and other.

AlfaStrakhovanie Group’s equity exceeds RUB 8.5 billion. Under its license, the Group offers more than 100 insurance products, including life and accident insurance. It has more than 400 regional offices in Russia.

AlfaStrakhovanie Group is accredited by major banks, including Sberbank of Russia, VTB, VTB24, Gazprombank, Alfa-Bank, Russian Agricultural Bank, Raiffeisenbank, Bank of Moscow, MDM Bank, Unicredit, and is included on the official list of organizations as their insurance partner.

In 2013 the market share of the AlfaStrakhovanie Group reached 6.3% and its premiums counted 130.8 bln RUR, the premiums excluding obligatory medical rose up to 51.5 bln RUR and the market share up to 5.7%.

Main principles

Alfa Insurance Group has reputation of stable and reliable company. High reliability of insurance operations is further supported by the reinsurance programs of the largest global players, including Munich Re, Swiss Re, Hannover Re, SCOR, GenRe, and Partner Re, as well as Lloyd’s of London, with which Alfa insurance partners via international brokers Willis Limited, Marsh, AON Benfield and others.

AlfaStrakhovanie Group is one of the five leaders of the insurance market. In May 2014 Expert Rating Agency confirmed the A++ rating assigned to AlfaStrakhovanie Group in 2003. AlfaStrakhovanie Group is rated by Fitch Ratings at AA- on the national scale and BB on the international scale.

The Group works hard on improving service and developing new, custom-made insurance products. Recognition from market professionals validates the strategy. In 2013, AlfaStrakhovanie again won the main Russian award in the field of insurance — «Golden Salamander» award, and its management continued taking the leading positions of the Top 1000 Russian Managers rating produced by the Russian Managers’ Association and the Kommersant Publishing House.

Clients

The Group serves over 20.4 million individual clients and over 440,000 companies including leading banks, major vessel owners and carriers, firms in the atomic energy sector, metallurgical and engineering companies, offices of major foreign companies, public and government agencies and organizations: Aeroflot, Alfa-Bank, Magnitogorsk Metallurgical Factory, RusHydro, Sheremetyevo International Airport, Vimpelcom, Yokohama, Volgotanker and many others.

Recognition

In 2013, for a tenth year in a row, top-managers of AlfaStrakhovanie held the leading positions of the Top 1000 Russian Managers rating produced by the Russian Managers’ Association and the Kommersant Publishing House. For six years now, the Group has been awarded the Golden Salamander, the national Russian award to insurance providers.

In 2013 AlfaStrakhovanie won the annual Global Banking & Finance Review award, given to financial...
companies in various countries of the world for achievement and innovation, in the Best Insurance Provider Russia 2013 category.


Alfa-Capital Management Company

Founded in 1996, Alfa-Capital is one of the Russia’s market leaders in asset management. Alfa Capital’s major business lines include managing the assets of mutual funds, non-state pension funds, insurance companies and corporations, as well as individual trust management for large private investors. The Alfa Capital brand is synonymous with high-quality services in the asset management market.

According to Expert RA rating agency, Alfa-Capital is one of the top 10 companies by total amount of funds under management and is ranked first on the market in trust management for retail customers. It is in the top 5 by net asset value among PIFs and IPIFs: www.alfacapital.ru

2013 — strengthening leadership

In 2013 the company concentrated on developing its retail business, strengthening its position in trust asset management sector for individual clients, including corporations, improving customer service, developing new technological platforms for customers, creating and maintaining loyalty programs. In respect to staff, the company mainly focused on corporate culture, staff training, boosting the HR brand.

Retail business

In 2013 Alfa-Capital accepted four «retail» mutual funds from Renaissance Asset Management in order to manage. The total amount of funds is about RUB 650 million. The deal corresponds to the company’s development strategy which stresses improving Alfa-Capital’s position in the retail segment.

Also, in order to develop its retail business, the company will cooperate with leading commercial banks. In 2013 Alfa-Capital and Citibank signed an agency contract, and now Alfa-Capital's products will be offered to customers at Citibank offices.

Trust management for individuals

For three years in a row, Alfa-Capital has remained the unquestioned leader in trust management for individuals (according to Expert RA). Last year the company received several prestigious awards. During the 3rd annual «Asset Management in Russia» conference, the National Rating Agency gave Alfa-Capital a «Quality Asset Management» award; NAUFOR’s «Securities Market Elite» competition judged it the best management company; SPEAR magazine named it the best management company for high net worth individuals (HNWI).

Corporate and institutional clients

In 2013 Alfa-Capital continued to expand on the endowment fund market with a contract for trust management of MGIMO’s target fund and the Urals Federal University’s endowment fund. It also took the non-government pension funds of Akvilon and Russian Standard for management. Alfa-Capital was commended for its involvement in establishing a special endowment fund for support and development of the Skolkovo Institute of Research and Technology.

Marketing and education

In 2013, Alfa-Capital attracted more clients for its mutual funds by conducting the large-scale «Mutual Test-Drive» advertising campaign. Leading business media supported the promotion. The purpose of promotion is improving investors’ financial literacy and positioning mutual funds as transparent and popular retail product.

Alfa-Capital started an educational video project — PRO Capital, which is oriented at both customers and beginner investors. In regular video updates Alfa-Capital’s investment experts explain how to make money on the securities market.

Financial indicators

The assets managed by the company grew by more than 10% to RUB 97.2 billion as of 31.12.2013. The number of clients in trust management grew by 53% in comparison with 2012. There were 4,249 non-zero accounts of individual clients by the end of the year. Positions in the endowment sector improved. The decision to invest in fixed-income instruments proved entirely correct and brought 26% more net revenue in 2013.
Staff management

During the past year Alfa-Capital’s HR department continued to implement its personnel development program. It developed wide-ranging incentive programs for employees, including non-material incentives, regular group classes and training seminars. The company focused on performance management to help employees achieve their best. As part of this, the Department carried out a 360-degree assessment and comprehensive evaluation of staff performance, with each employee receiving an individual development plan. In 2013 Alfa-Capital’s volunteers ran 10 large charity events using employees’ donations.

Client loyalty program

Traditionally, Alfa Capital has made a concerted effort to develop its client services and maintain customer loyalty. The Personal Profile service continues to improve. It allows customers to control their portfolios in real time. Also important was the Alfa Wealth loyalty program, providing premium services to wealthy clients at a number of partner companies. In 2013 1000 HNWI clients joined the Alfa Wealth program, while total assets doubled and exceeded USD 1 billion.

Market recognition

Alfa-Capital’s professionalism in 2013 was highly appreciated by experts:

- AAA individual rating from National Rating Agency (NRA) for the highest reliability.
- «A++ Rating. Exceptionally high / highest level of reliability and service quality.» from Expert RA rating agency.
- NAUFOR’s «Securities Market Elite» contest acknowledged it the best management company.
- Alfa-Capital’s online portal won the «Best Intranet Russia 2013» award.

Outlook for 2014

The company has set ambitious goals for 2014. Priority segments remain: HNWI clients, retail and corporate customers.

In trust management segment, Alfa-Capital plans strengthening positions of corporate customers. In trust management for individuals the goals are priority service for HNWI, developing Alfa Wealth, improving service quality. In retail, the company will focus on better management quality and staying in the Top 3 in terms of revenues from the 5 largest mutual funds.

The «Mass Trust Management» segment will be represented with Alfa-Profit product strategy.
Independent Auditor’s Report

To the Shareholders and Board of Directors of ABH Financial Limited:

1. We have audited the accompanying consolidated financial statements of ABH Financial Limited and its subsidiaries (the "Group") which comprise the consolidated statement of financial position as at 31 December 2013 and the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

Management’s Responsibility for the Summary Financial Statements

2. Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s responsibility

3. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity’s preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

5. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

6. In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2013, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

28 March 2014
Moscow, Russia
### CONSOLIDATED STATEMENT OF FINANCIAL POSITION

<table>
<thead>
<tr>
<th>In millions of US Dollars</th>
<th>31 December 2013</th>
<th>31 December 2012</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>5 925</td>
<td>5 218</td>
</tr>
<tr>
<td>Mandatory cash balances with central banks</td>
<td>355</td>
<td>444</td>
</tr>
<tr>
<td>Trading securities</td>
<td>1 493</td>
<td>1 098</td>
</tr>
<tr>
<td>Repurchase receivables relating to trading securities</td>
<td>1 881</td>
<td>1 869</td>
</tr>
<tr>
<td>Due from other banks</td>
<td>3 638</td>
<td>3 298</td>
</tr>
<tr>
<td>Loans and advances to customers</td>
<td>32 507</td>
<td>30 564</td>
</tr>
<tr>
<td>Investments</td>
<td>1 161</td>
<td>1 963</td>
</tr>
<tr>
<td>Other financial assets</td>
<td>607</td>
<td>555</td>
</tr>
<tr>
<td>Other assets</td>
<td>412</td>
<td>364</td>
</tr>
<tr>
<td>Premises and equipment</td>
<td>668</td>
<td>559</td>
</tr>
<tr>
<td><strong>TOTAL ASSETS</strong></td>
<td>48 647</td>
<td>45 932</td>
</tr>
</tbody>
</table>

| **LIABILITIES**           |                  |                  |
| Due to other banks        | 7 239            | 5 502            |
| Customer accounts         | 26 725           | 26 842           |
| Debt securities issued    | 6 504            | 5 949            |
| Syndicated and other debt | 350              | 125              |
| Subordinated debt         | 2 057            | 2 170            |
| Other financial liabilities| 463              | 741              |
| Other liabilities         | 408              | 361              |
| Deferred tax liability    | 83               | 90               |
| **TOTAL LIABILITIES**     | 43 829           | 41 780           |

**EQUITY**

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share capital</td>
<td>1 265</td>
<td>1 265</td>
<td></td>
</tr>
<tr>
<td>Fair value reserve for investments available for sale</td>
<td>-</td>
<td>68</td>
<td></td>
</tr>
<tr>
<td>Revaluation reserve for premises</td>
<td>43</td>
<td>25</td>
<td></td>
</tr>
<tr>
<td>Cumulative translation reserve</td>
<td>(442)</td>
<td>(403)</td>
<td></td>
</tr>
<tr>
<td>Retained earnings</td>
<td>3 952</td>
<td>3 196</td>
<td></td>
</tr>
<tr>
<td>Net assets attributable to the Company's owners</td>
<td>4 818</td>
<td>4 151</td>
<td></td>
</tr>
<tr>
<td>Non-controlling interests</td>
<td>-</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL EQUITY</strong></td>
<td>4 818</td>
<td>4 152</td>
<td></td>
</tr>
</tbody>
</table>

**TOTAL LIABILITIES AND EQUITY**

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>48 647</td>
<td>45 932</td>
<td></td>
</tr>
</tbody>
</table>

These consolidated financial statements were approved for issue by the Board of Directors of ABH Financial Limited on 28 March 2014 and any further changes require approval of this body.

### CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

<table>
<thead>
<tr>
<th>In millions of US Dollars</th>
<th>2013</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Interest income</td>
<td>4 090</td>
<td>3 110</td>
</tr>
<tr>
<td>Interest expense</td>
<td>(1 801)</td>
<td>(1 395)</td>
</tr>
<tr>
<td>Expenses directly attributable to leasing and deposit insurance</td>
<td>(43)</td>
<td>(37)</td>
</tr>
<tr>
<td><strong>Net margin</strong></td>
<td>2 246</td>
<td>1 678</td>
</tr>
<tr>
<td>Provision for loan impairment</td>
<td>(565)</td>
<td>(95)</td>
</tr>
<tr>
<td><strong>Net margin after provision for loan impairment</strong></td>
<td>1 681</td>
<td>1 583</td>
</tr>
<tr>
<td>Fee and commission income</td>
<td>1 023</td>
<td>769</td>
</tr>
<tr>
<td>Fee and commission expense</td>
<td>(243)</td>
<td>(189)</td>
</tr>
<tr>
<td>Gains less losses arising from trading securities</td>
<td>(32)</td>
<td>-</td>
</tr>
<tr>
<td>Gains less losses arising from interest based derivatives</td>
<td>15</td>
<td>8</td>
</tr>
</tbody>
</table>
These consolidated financial statements were approved for issue by the Board of Directors of ABH Financial Limited on 28 March 2014 and any further changes require approval of this body.
CONSOLIDATED STATEMENT OF CASH FLOWS

<table>
<thead>
<tr>
<th>In millions of US Dollars</th>
<th>2013</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash flows from operating activities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest received</td>
<td>4 074</td>
<td>3 108</td>
</tr>
<tr>
<td>Interest paid, other than on debt securities issued, syndicated and other debt and subordinated debt</td>
<td>(1 175)</td>
<td>(902)</td>
</tr>
<tr>
<td>Expense directly attributable to the lending operations</td>
<td>(43)</td>
<td>(37)</td>
</tr>
<tr>
<td>Fees and commissions received</td>
<td>1 013</td>
<td>787</td>
</tr>
<tr>
<td>Fees and commissions paid</td>
<td>(240)</td>
<td>(193)</td>
</tr>
<tr>
<td>Net loss received from trading securities</td>
<td>(27)</td>
<td>(31)</td>
</tr>
<tr>
<td>Net loss received from trading in foreign currencies</td>
<td>(57)</td>
<td>(176)</td>
</tr>
<tr>
<td>Net income received from interest rate derivatives</td>
<td>8</td>
<td>3</td>
</tr>
<tr>
<td>Other operating income received</td>
<td>18</td>
<td>24</td>
</tr>
<tr>
<td>Staff costs paid</td>
<td>(801)</td>
<td>(595)</td>
</tr>
<tr>
<td>Other operating expenses paid</td>
<td>(461)</td>
<td>(352)</td>
</tr>
<tr>
<td>Income tax paid</td>
<td>(237)</td>
<td>(235)</td>
</tr>
<tr>
<td>Cash flows from operating activities before changes in operating assets and liabilities</td>
<td>2 072</td>
<td>1 401</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Challenges in operating assets and liabilities</th>
<th>2013</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net change in mandatory cash balances with central banks</td>
<td>61</td>
<td>(104)</td>
</tr>
<tr>
<td>Net change in trading securities and repurchase receivables</td>
<td>(534)</td>
<td>(1 104)</td>
</tr>
<tr>
<td>Net change in due from other banks</td>
<td>(509)</td>
<td>(984)</td>
</tr>
<tr>
<td>Net change in loans and advances to customers</td>
<td>(3 858)</td>
<td>(7 792)</td>
</tr>
<tr>
<td>Net change in other assets and receivables</td>
<td>(240)</td>
<td>(185)</td>
</tr>
<tr>
<td>Net change in due to other banks</td>
<td>1 860</td>
<td>2 932</td>
</tr>
<tr>
<td>Net change in customer accounts</td>
<td>1 131</td>
<td>7 633</td>
</tr>
<tr>
<td>Net change in other liabilities and payables</td>
<td>28</td>
<td>66</td>
</tr>
<tr>
<td>Net cash from operating activities</td>
<td>11</td>
<td>1 863</td>
</tr>
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</table>

Cash flows from investing activities

<table>
<thead>
<tr>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acquisition of investments available for sale</td>
<td>(504)</td>
<td>(1 366)</td>
</tr>
<tr>
<td>Proceeds from disposal and redemption of investments available for sale</td>
<td>1 214</td>
<td>847</td>
</tr>
<tr>
<td>Acquisition of investments at fair value through profit and loss</td>
<td>(14)</td>
<td>(19)</td>
</tr>
<tr>
<td>Disposal of investments at fair value through profit and loss</td>
<td>101</td>
<td>14</td>
</tr>
<tr>
<td>Acquisition of investments held to maturity</td>
<td>(50)</td>
<td>-</td>
</tr>
<tr>
<td>Proceeds from redemption of investments held to maturity</td>
<td>35</td>
<td>47</td>
</tr>
<tr>
<td>Acquisition of premises, equipment and intangible assets</td>
<td>(257)</td>
<td>(281)</td>
</tr>
<tr>
<td>Proceeds from disposal of premises, equipment and intangible assets</td>
<td>35</td>
<td>17</td>
</tr>
<tr>
<td>Dividend income received</td>
<td>-</td>
<td>1</td>
</tr>
</tbody>
</table>

Net cash from/(used in) investing activities | 560 | (740) |

Cash flows from financing activities

<table>
<thead>
<tr>
<th>1</th>
<th>2</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proceeds from syndicated and other debt</td>
<td>346</td>
<td>-</td>
</tr>
<tr>
<td>Repayment of syndicated and other debt</td>
<td>(116)</td>
<td>(279)</td>
</tr>
<tr>
<td>Interest paid on syndicated and other debt</td>
<td>(13)</td>
<td>(18)</td>
</tr>
<tr>
<td>Proceeds from debt securities issued</td>
<td>3 221</td>
<td>2 597</td>
</tr>
<tr>
<td>Repayment of debt securities issued</td>
<td>(2 505)</td>
<td>(1 394)</td>
</tr>
<tr>
<td>Interest paid on debt securities in issue</td>
<td>(427)</td>
<td>(341)</td>
</tr>
<tr>
<td>Proceeds from subordinated debt</td>
<td>-</td>
<td>758</td>
</tr>
<tr>
<td>Repayment of subordinated debt</td>
<td>(38)</td>
<td>(13)</td>
</tr>
<tr>
<td>Interest paid on subordinated debt</td>
<td>(159)</td>
<td>(114)</td>
</tr>
</tbody>
</table>

Net cash from financing activities | 309 | 1 196 |

Net increase in cash and cash equivalents | 880 | 2 319 |

Cash and cash equivalents at the beginning of the year | 5 218 | 2 707 |

Effect of exchange rate changes on cash and cash equivalents | (173) | 192 |

Cash and cash equivalents at the end of the year | 5 925 | 5 218 |

These consolidated financial statements were approved for issue by the Board of Directors of ABH Financial Limited on 28 March 2014 and any further changes require approval of this body.
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