



AB-ICI April: Entering a Difficult Period

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Investment Summary

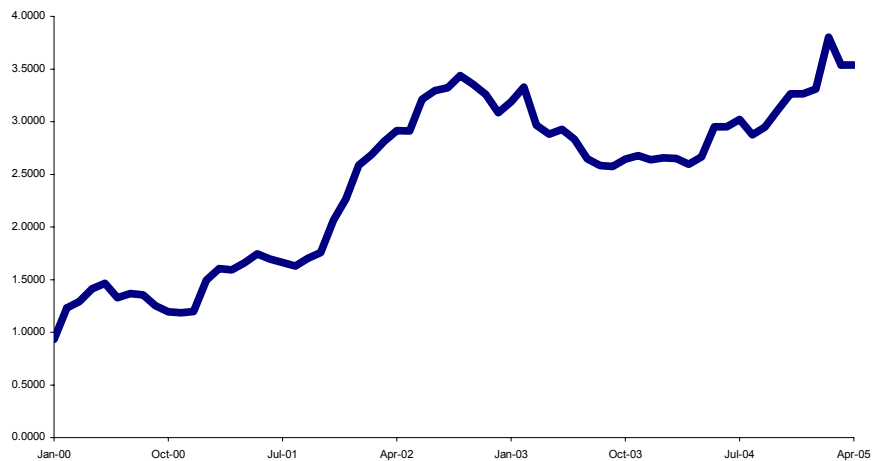
- AB-ICI remained virtually flat in April; recovery unlikely in coming months
- Redemption of Paris Club debt will negatively affect Index due to pressure on liquidity
- Depositors not well-informed about deposit insurance; banks must work to improve trust

AB-ICI flat, negative trend on the horizon

AB-ICI flat in April as IPOs were offset by weak markets

The Alfa Bank Investor Confidence Index (AB-ICI) was virtually flat in April, reflecting the mixed trend in the economy and on financial markets. The positive effect of two recent IPOs – by Severstal-Avto and Pyaterochka – was offset by a decline on the equity market and a widening of Russian bond spreads versus international benchmarks. The economic index remains depressed, as Russia experienced a capital outflow over the past few months.

Figure 1. AB-ICI flat in April – IPOs offset by weak markets



Sources: New School of Economics, Alfa Bank

Interest rates picked up on lower liquidity; \$15 bln to be paid to Paris Club will weigh on Index performance

In the coming months we do not expect the Index to recover rapidly, mainly because of market weakness. On the one hand, banking liquidity began to decline a month ago, which has exerted selling pressure on a number of Russian assets. While the situation does not signal the likelihood of any new banking crisis, the increase in interbank interest rates is an area to watch. The decision to pay \$15 bln in Paris Club debt ahead of schedule in June-August, while not directly affecting banking liquidity, is likely to prevent CBR reserves growth and thus weigh on our Index performance.

Weaker ruble may trigger sell-off on ruble bond market

Another factor is that the recent ruble depreciation has already rattled nerves on ruble-denominated bond markets, as the return in the past was largely generated by nominal ruble appreciation. Thus, market participants will be demanding higher ruble yields in the future.

RESEARCH DEPARTMENT

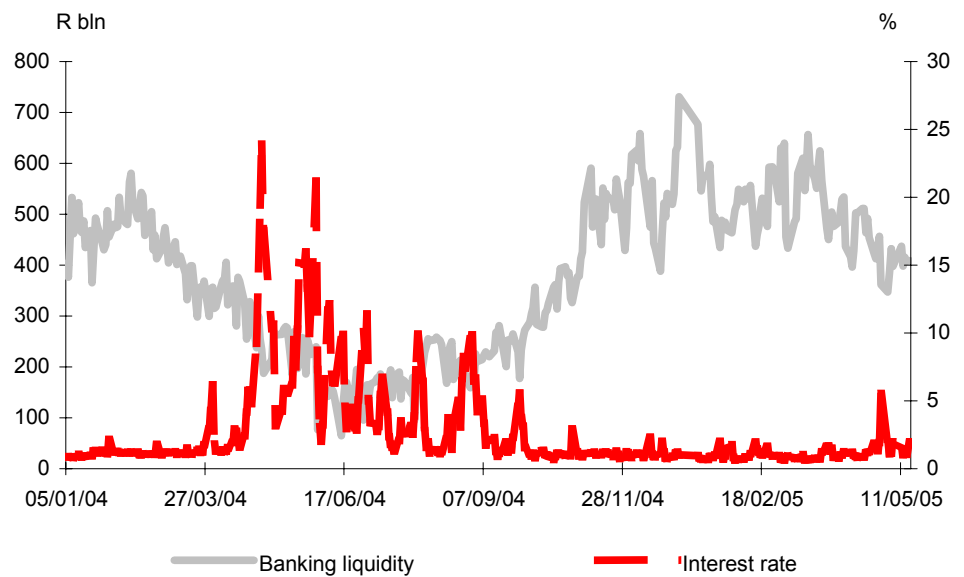
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Figure 2. Overnight Interest Rate and Banking Liquidity



Source: Reuters, Alfa-Bank estimates

95% of banking deposits are below \$3,500 – the minimum level covered by deposit insurance

We reiterate our view that confidence in the banking sector remains a stumbling block for better Index performance. The recently created Agency for Deposit Insurance recently conducted a poll suggesting that only 30% of respondents know about the Deposit Insurance Law and that 24% of respondents do not trust it. Depositors with Sberbank were particularly disappointed with the Law and noted a decline of confidence in the banking sector.

At the same time, the poll suggests that the average value of deposits in 1Q05 was only \$850, and that 95% of total deposits were below \$3,500 – the amount guaranteed by the Law. The conclusion is that the confidence problem is mainly psychological in character, and that private banks can improve trust if they manage to educate their retail clients about the advantages of deposit insurance.

Figure 3. Results of Poll Conducted by Agency for Deposit Insurance

- Only 32% of respondents have deposits with banks
- Only 30% of participants know about deposit insurance
- 35% did not alter their trust in banks
- 24% do not trust the Deposit Insurance Law
- 82% of poll participants keep money with Sberbank, 20% in private banks and 6% in other state-owned banks. Foreign banks received only 2%.
- Sberbank depositors noted a decline in trust in the banking sector after introduction of the Law
- In 1Q05 deposits averaged \$850 per capita
- 95% of deposits are below \$3,500, the minimum level covered by the Law
- Potential depositors may bring \$16 bln to the banking sector

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