

AB-ICI: Drops 2% on Global Trends

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Investment Summary

- The Alfa Bank Investor Confidence Index (AB-ICI) dropped 2% in July on weak FDI.
- Russian corporate sector to pay \$6 bln before YE2007, which will likely damage growth in CBR reserves

The AB-ICI down 2% on poor FDI in 2Q07

AB-ICI dropped 2% in July...

...while economic confidence slightly up

Foreign confidence damaged by poor FDI

Corporate spreads increase

Our AB-ICI index slid 2% in July, reflecting the slowdown in FDI inflows to Russia.

- The index's **economic confidence** went up in July due to the strong position of CBR reserves. However, this trend has reversed since mid-August and we do not anticipate it to improve quickly.
- **Foreign confidence** showed signs of diminishing in July, although the share of foreign banks in total assets remained unchanged. Some CBR officials claimed that it rose to 21% of the sector total, although their figure includes portfolio investments to Sberbank and VTB shares and thus cannot be used as a proxy for operational control of foreigners over Russian banks. FDI inflows to Russia dropped to \$6.1 bln in 2Q07 from \$9.8 bln in 1Q07, which exerted downward pressure on index growth.
- **Market confidence** was also down in July, indicating the beginning of market instability. The spread between corporate Eurobonds and the US market grew dramatically, which had a negative effect on this component of our index.

Figure 1: AB-ICI drops 2% in July on poor FDI



Source: Alfa Bank Research, New School of Economics

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Liquidity outlook crucial in coming months

Liquidity indicator slid at the end of June, with overnight rates jumping on August 16

The liquidity indicator began to decline at the end of June. However, as long as it remained above R1,000 bln (\$40 bln), the banking system did not suffer from a lack of liquidity. In the last days of July, the indicator dropped below its April level, indicating a liquidity outflow, although banks began suffering from a liquidity shortage only in mid-August when tax payments coincided with the outflow of capital from Russian markets. On August 16, overnight rates jumped to more than 6% in a single day, which is the level of repo operations with the CBR. The last time local rates were so high was in March, when the market was under pressure from falling oil prices.

Foreign debt about 15% of bank liabilities

An important consequence of the shortage in local liquidity for Russia's corporate sector is that companies will likely be unable to refinance their foreign debt. According to a recent statement from the CBR, some 15% of banking assets are financed with foreign debt, with some banks carrying even higher levels. The most active retail players, such as Russian Standard, URSA Bank, MDM Bank and Alfa Bank, have been diversifying their liabilities structure and aim to increase the maturity of their funds through access to international markets.

\$6 bln in foreign debt payments before YE2007, most of which are due in September

Before YE2007, Russian banks and companies will have to make about \$6 bln in principal and interest payments, with the bulk of this amount (almost \$2.5 bln) due in September, with a number of Russian banks redeeming their loans. From the standpoint of redemption, October will be the easiest remaining month in the year. In November and December, companies and banks will need to make payments in the amount of \$1.4 bln and \$1.3 bln, respectively.

Figure 2: Monthly foreign debt payments in 2007, \$ mln

	September	October	November	December
Russian Standard	300			
VTB	1,000			300
Alfa	220			340
URSA	110			
Gazprombank	171			
NSMMZ	100			
Seventh Continent	90			
Moscow Narodny Bank		200		
Open Investments			150	
Nutritek			100	
TNK-BP			700	
RMK				100
MDM				250
Coupon payments	455.8	461.6	487.4	285.9
Total	2446.8	661.6	1,437.4	1,275.9

*Note: This table contains information about securities and syndicated loans only
Source: Cbonds.Info., Alfa Bank Research*

CBR will likely have to continue injecting liquidity

The primary implication of the debt payment schedule above is that the local liquidity situation will likely not improve much in September, which suggests the CBR will have to continue its liquidity injections. We reiterate our view that ruble appreciation would be very helpful in reducing the speculative demand for dollars, although this would certainly slow growth in CBR reserves and have a negative impact on AB-ICI performance.

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