

“We are neither optimistic nor pessimistic – we are Russia realists”



Michael Cole-Fontayn



Gregory Roath

Photos: Alexey Kudikov

Five of the top DRs programmes in Russia are in the top ten globally. The Review spoke to Michael Cole-Fontayn, Managing Director, Global Issuer Services, Bank of New York and Gregory Roath, Vice President, Bank of the New York, which is depository bank for 80% of all Russian DR issuers about increasing investor and issuer demand, even in the fact of political turmoil

It was thought that in the Yukos Affair, as long as the rule of law was observed, that foreign investors would remain sanguine. Are they furious now?

Michael Cole-Fontayn: Minority investors are certainly enraged. The Russian government took their actions under Russian law and that is their prerogative. However, you can see from the very well-orchestrated minority shareholder press activity that there is a heightened level of concern. Yet for old Russia-hands, for investors in Russia, there have been significant dips in the market that have provided buying opportunities. That has been reflected in activity in the DR programmes for our

major Russian clients. We consider that for our business in Russia, volatility in equity markets is positive and we have seen the opportunity for long-term investors to selectively increase and consolidate positions. Newer investors have, obviously, taken flight and a lot of the investment committees have been questioning whether it is timely or appropriate to allocate funds to Russia, especially if you are a pension fund.

Gregory Roath: One could look at December 2004 as a whole when there was the not just Yukos but also Vimpelcom and Mechel stories, which took a dip. There was also a \$1.7b placement from MTS – an accelerated

book-build that took a matter of days, so there is still demand and an appetite despite the other stories that are going on.

MCF: Certainly there were a number of very good investment stories during the year. Russian business is becoming increasingly international. You only have to look at the role that Norilsk Nickel has played recently in business affairs in South Africa. The Russian government is very aware of its position as an alternative supplier of oil and gas, which is being eagerly courted by China and Japan as much as it is by other parties. We continue to be very positive on our DR business in Russia. There is



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also, for the first time, the opportunity to invest in the Russian property market via Open Investments, which is part of the Interros Group and a pretty successful transaction.

We have seen the continuing establishment of new Level I programmes for companies such as Irkut. We have a number of other companies in our pipeline to come to market. The MTS transaction was very successful. I think the message to investors is that they need to look at investments selectively and do their due diligence carefully – to know who the principles are behind a company and understand them and form a relationship. We are neither optimistic nor pessimistic – we are Russia realists, and it is a reasonable good time for our business

Back in first half of 2004 it was expected that there would be a significant increase in ADRs – based on the growth of Russian economy, on the fact that the Russian stock market had outperformed rivals over the preceding five years and because US-based investors would want to diversify their holdings and would therefore look to Russia. Six months on the situation looks very different ...

MCF: The second six months of 2004 was very different from the first six months – it was a year of two distinct halves. The Russian economy minister is on record as predicting a slow-down in the Russian economy so that is a government confirmed fact.

The head of the FSFM has been reasonably vocal on this point: it is hard to determine what the government's national economic policy is. Russian business is looking for a lead around a coherent economic strategy, and wants to hear it repeated on a fairly regular basis. The stock market will go up and down, but it is heavily underpinned by natural resource stocks. Long-standing Russian investors want to be able to invest in other sectors of the economy. There is a mutual interest for the Russian government and for investors to see development of the small and medium sized enterprise sector, who will provide the potential to come to market in the future. We are aware that it is the Russian government's aim to stimulate

that sector but it is always a challenge.

We identify three types of investors – you have investors who are based in Russia, who really understand the Russian market and have a preference for investing in DRs. They are exceptionally sophisticated, connected, understand their rights and have over the years been very successful investors. Then there are the emerging market investors who are predominately based in Europe, who are Russia realists and know and understand the markets pretty clearly and those trends are reflected in the US as well. There are, to date, only six Russian companies that are fully registered with the SEC and listed on US stock exchanges. Those are the companies that are deemed to have the highest level of transparency and corporate governance. Mechel Steel joined that group last year which was positive for Russia and for the market.

I think US investors are still cautious – and probably rightly so for the moment because they haven't had experience of doing due diligence in Russia. Certainly there is a lot of noise in the press about concerns and the investment opportunity and knowing your investment and company management is very important – that isn't to say that there aren't a very high number of good opportunities for both direct and portfolio investors.

Vimpelcom are clients of Bank of New York. How did you interpret the developments in December 2004, concerning the tax bill which was sprung on the company?

MCF: The quick downward revision of the tax bill, which was demanded of Vimpelcom, was positive although perhaps pointed to a lack of cohesion between government departments. Vimpelcom is a good example of the way in which Russian corporates are looking to improve their business processes, which is good for long term investors. Interestingly when they were in the midst of their 'tax issue' Vimpelcom were communicating the news with their investors in multiple media. They were web casting their conference call, which had close to 700 participants listening in. It was an example of a well-orchestrated communication strategy, reaching out to investors. 