



Photo: Alexei Kudikov

**“We are building up our presence, not aggressively, but in a fairly ambitious way”**

## **Stuart Harley, Head of Equities, Russia, Citigroup, describes how even though the group may not be first to build up a trading platform in Russia, their entry is a long-term investment in an evolving market**

**In June 2004 Citigroup announced the plan to build up the equity trading platform in Russia. Why did you make the decision then?**

June was the statement of intent, which we have since followed through on. We have now made our hires, and have a core-team around the equity business, with only a couple more people to add. At the end of the year, we appointed Timur Nasardinov as Head of Equity Trading in Moscow. Most recently, we have made some additional hires, namely Kirill Gromov as Head of Domestic Equity Sales, Vladimir Tchikvadze in sales trading and Yuri Aldakimov in trading. Like the rest of the team, they are great individuals. I have been consistently impressed with the people we have hired, they are people who understand the market well and how to do business. I am very excited

that we managed to find these guys.

The recent research hires are Dimitry Vinogradov who is the senior Russian country analyst (specialising on consumer and financials), Mikhail Seleznev in basic materials, Alex Korneev in utilities and Andrei Machanskis in oils. The people that we have picked are those who we think will be the stars of the future. We have tried to look at people on the research-side who dovetail nicely into what we have in London. We don't them to be just Russia analysts, but analysts who can look at Russia in a global context and draw on the skills which we have around the world. This will give them more interest and give our product relevance in the global context.

**That almost sounds as though Citigroup is treating Russia as a normal country, which can fit quite neatly in**

**the Citigroup approach?**

I wouldn't say that Russia is a “normal” country yet, which is where the opportunity lies. Citigroup has identified Russia as one of the growth markets. We are not looking at it as just as a market on the equity side, but also on the consumer banking side. At the beginning of 2004 Citigroup employed just over 400 people; at the end of 2004 we were over 1000 people, and 1500 by the end of February 2005. It is a very fast moving market. We are building up our presence, not aggressively, but in a fairly ambitious way. The equities business is a small part of that expansion.

**You must be pleased that Citigroup decided to expand in this direction. It can't have been a foregone conclusion; and there must have been a great deal of internal debate, before the group**

**made this commitment to Russia?**

Absolutely. We looked very critically at how you can make money in a market and what the opportunity lies therein. We are conscious of the fact that we are late to the party, but we see it as a long-term investment, in a market that is evolving. It is a long-term commitment that we are making.

**Despite the sensation that progress in Russia is still 'two steps forward, one step back', do you believe that Russia's integration into the global economy is moving in the right direction?**

Exactly. It is moving in the right direction. Russia is not a market that anyone can ignore. It is an enormous economy, with huge potential and people with immense depth of skill who want to do well. I am very upbeat. It is not going to be a straight-line from here. The easy money may have been made, but that is also what makes it a challenge. We are well positioned, helped by the fact that we are part of the global Citigroup infrastructure.

**The Russian stock market still very concentrated in natural resource stocks...**

We expect the market to deepen. Yes, the market is concentrated, but in the platform that we are building will hopefully add to our coverage as well. We expect to see an expansion of the consumer plays. It is natural that there is a resource focus at the moment but that will change over time and that is where the opportunities are. We cover almost all of the MSCI at the moment, and we are putting the team on the ground to add to that coverage.

**Has Russia failed to diversify away from oil & gas?**

Russia hasn't failed to diversify – one thing is the market, and the other is the economy. If you have an economy that is so rich in natural resources, clearly that is where it is going to develop. There is the so-called Dutch disease and the crowding out of other export markets. That is something that Russia has to be wary of. There is the large stabilization fund in place, which is growing at \$10b a year, and I would hope that it is used to generate investments in infrastructure. There is still a concentration

of wealth in Russia. I would like to see it bare fruit in other sectors.

**Is the interest of local Russian portfolio investors growing?**

You have got, and this is not surprising, a very active professional investor base. It is very tough to put numbers on it (we think it is around \$30b, which is a fair sum for Russia). They are very serious investors who are becoming increasingly sophisticated. Clearly our focus will be Russia equities, but over time I would like to build an equities business in Russia, rather than a Russian equities business and bring with that some of the other areas of expertise in the firm. Also, the next wave will be the pension funds, which haven't even developed yet.

**How would you describe the competition between your team and the local equity brokerages that have grown up in the last 14 years in Russia?**

I have great respect for the local brokerage environment. You have some tremendously experienced and very profitable domestic brokers. That is what makes Russia slightly different from a lot of our region. For example, in central Europe there isn't that core of domestic brokers.

In Russia, over the last year, there was the deal between UFG and Deutsche Bank and UBS buying out the balance of Brunswick which they did not own. Renaissance Capital continues to be very strong. All of which is a good thing. There is a core of very well-established, competent, brokers. We are not going to go in and buy market share; we want to build this market and stimulate demand. Competition is good for the market, in terms of generating incremental interest. What distinguishes us from the locals is the global context – something that not all our competitors are able to provide.

**The RTS has languished over the last year. Do you expect the stock market to rally?**

Clearly the market has been overshadowed by the Khodorkovsky affair. Over the last 12 months there has been a significant net outflow from the market, about \$500m. The last spurt in

performance came from global sector funds coming into the market. They have come in, made some money and left. But the positive impact of that is that there is no hot money in the market waiting for an appropriate time to exit. The global emerging markets are under-weight. Equity risk premium in Russia has expanded and is one of the highest in emerging markets, which I don't think reflects reality. This will narrow again. Russia is not an expensive market.

However, it is not just a question of what happens with Russia and investor's views on the country, but more fundamental issues about emerging markets in this environment. For example, what is going to happen in the US bond market? If rates go up, risk-aversion issues come to the fore, which can impact asset allocation decisions. Equally currency moves versus both the USD and Euro. The deleveraging in Russia makes the economy less vulnerable than it has been in the past.

What we haven't seen is money coming off the table in emerging markets. We are not seeing net inflows, but nor are we seeing outflow. In those circumstances, and while there is a degree of uncertainty and people are sitting on their hands. Volatility has dropped but volumes have also dropped.

**What concerns you about Russia's economic development? Does it concern you that the government hasn't really made an effort to stimulate SME development?**

I don't think that the government's role is to encourage things or not encourage things, because you then create anomalies, which is unhealthy in the longer term. What the government have managed to do is encourage FDI flows, which have been extremely strong. In a negative environment, people always try to point to negative outflows but I think that a more fundamental view on risk is that there are large corporates making very large investments. Portfolio investors can come and go as the seasons pass but if you are a large corporate making a big investment, this represents a significant statement to confidence in the long-term future of the country. 