

AB-ICI June: Down As Expected

Natalia Orlova

(7 095) 795-3677

NORlova@alfa-bank.com

July 26, 2005

www.alfa-bank.com

Moscow

Investment Summary

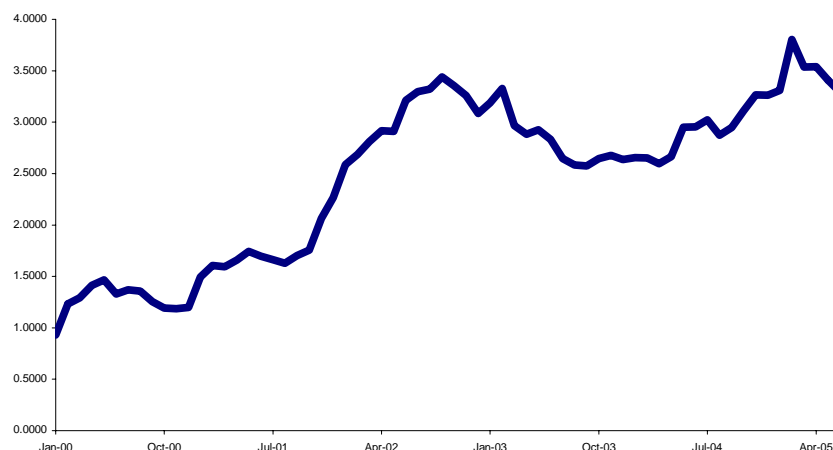
- AB-ICI down 3.5% in June, reflecting poor domestic liquidity and market concentration
- Decline in CBR reserves on PC payments to be compensated by faster dollar accumulation
- Pension and salary indexation in August-September will support Index recovery

AB-ICI declined 3.5% in June on poor liquidity

AB-ICI suffered from a lack of good news

The AB-ICI declined 3.5% in June, largely due to the lack of positive fundamental changes rather than any negative news. First, the CBR's recalculation of the 1H05 balance of payments suggested a higher than expected capital outflow that accelerated last month. Second, on the corporate bond market the share of small and medium-sized enterprises (SMEs) continues to decline, while state-run companies and banks (such as VTB) are assuming leading positions. In short, the Index last month suffered from a lack of positive news.

Figure 1. AB-ICI declined 3.5% in June, as expected



Sources: New School of Economics, Alfa Bank

Pension/salary indexation from August will allow an increase in banking liquidity

In the coming months we expect the upward trend to resume. The planned increase in pensions from August 1 and the 10-30% indexation will inject a few billion dollars into the banking system. As a result, we believe that current liquidity in banking accounts (~\$20 bln) will rise starting from September.

China's revaluation means a stronger ruble rate, and thus greater capital inflows to Russia

Another point with regard to banking liquidity is that the CBR is currently paying \$15 bln ahead of schedule to the Paris Club, and this has already resulted in a near \$10 bln decline in reserves. This led to market expectations that the monetary authorities will have to purchase dollars more aggressively from the market, and thus a large number of participants began switching from rubles into dollars, thereby reducing ruble liquidity. However, after China's announcement of 2.1% revaluation of the yuan followed by weakening of the dollar on foreign markets, we believe that the Russian public will be less

RESEARCH DEPARTMENT

research@alfabank.ru

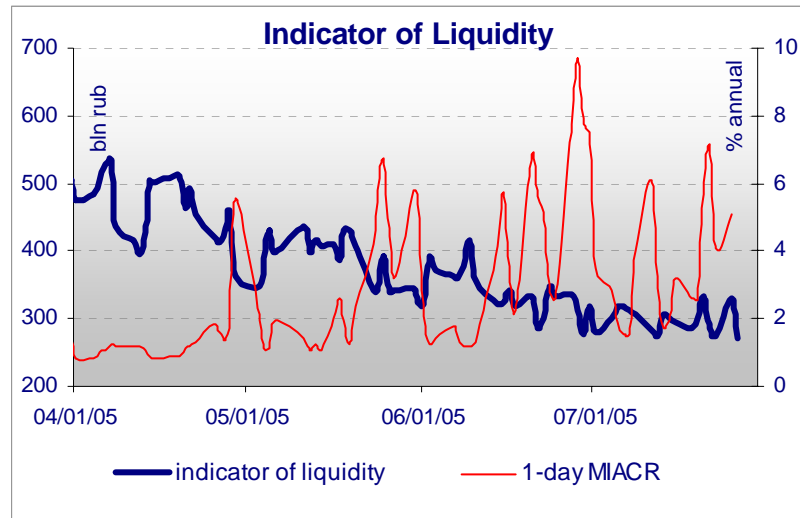
(7 095) 795-3676

Alfa Bank Group and/or its affiliates does and seeks to do business with the issuers covered in this research report. As a result, investors should be aware that Alfa Bank Group and/or its affiliates may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. For important disclosure information relating to Alfa Bank Group and/or its affiliates' investment banking relationships, if any, with the issuers mentioned in this report and regarding Alfa Bank Group and/or its affiliates' rating system, valuation methods, analyst certification and potential conflicts of interest, please refer to the Disclosure Section at the end of this report.



willing to maintain long positions in dollars. Also, the ruble's appreciation is seen as a powerful argument in favor of greater capital inflows to Russia.

Figure 2. Inerbank Rates Remain High and Volatile



Source: Reuters

The strength of state banks has led to higher interbank rates

An area of concern, however, is that Russia's banking and corporate markets have not seen significant structural changes. Quite the opposite – the position of state entities is now stronger. This has apparently resulted in a declining share of SMEs on the Russian corporate bond market. Another, less direct implication of this concentration of assets in state institutions is reflected in liquidity indicators. State banks, which mainly service the accounts of the largest state companies, are not allocating their excess liquidity to the interbank market, but rather to deposits with the CBR or to government bonds. Thus, given the increasing role of state institutions, it is unsurprising that the interbank market is now experiencing growth in interest rates despite high oil prices and good domestic liquidity.

Contact Information

Alfa Bank (Moscow)

Head of Equities
Telephone
Facsimile

Dominic Gualtieri
(7 095) 795-3649
(7 095) 745-7897

Research Department

Telephone
Facsimile
Head of Research, Telecoms
Strategy Team
Oil & Gas
Macroeconomics, Banking
Utilities
Telecoms
Metals & Engineering
Consumer Goods, Retail, Media
Russian Product
Fixed Income
Technical Analysis
Editorial Team
Translation Team
Production Team

(7 095) 795-3676
(7 095) 745-7897
Andrei Bogdanov
Chris Weafer; Erik DePoy
Anna Boutenko, CFA; Anisa Nagaria
Natalya Orlova
Vitaliy Zarkhin; Roman Filkin
Andrei Bogdanov; Svetlana Sukhanova
Maxim Matveev, CFA; Natalya Sheveleva
Svetlana Sukhanova; Elena Borodenko
Angelika Henkel; Vladimir Kravchuk
Ekaterina Leonova; Marina Vlasenko
Vladimir Kravchuk
Erik DePoy; Brendan Franich
Rinat Gainouline
Brendan Franich

Equity Sales & Trading

Telephone
Facsimile
International Sales
Domestic Sales
Equity Capital Markets
Address

(7 095) 795-3712
(7 095) 745-7897
Kirill Surikov, Mikhail Shipitsin
Oleg Martynenko; Alexander Nasonov;
Konstantin Shapsharov; Dmitri Sadoviy
Armen Petergov; Alexander Svinov; Elena Kapustina
12 Akad. Sakharov Prospect, Moscow, Russia 107078

Alfa Capital Markets (London)

Telephone
Facsimile
Sales
Equity Capital Markets
Sales Trading
Address

(44 20) 7588-8500
(44 20) 7382-4170
Maxim Shashenkov; Mark Cowley
Simon Roache
Steve Downer
City Tower, 40 Basinghall Street, London, EC2V 5DE

Alfa Capital Markets (New York)

Telephones
Facsimile
Sales
Sales Trading
Address

(212) 421-8564 / 1-866-999-ALFA
(212) 421-8633
Sabrina Ricci
Harold Warren
540 Madison Avenue, 30th Floor, New York, NY 10022

Copyright Alfa Bank, 2005 All rights reserved

This report and the information contained herein are the exclusive property of Alfa Bank. Unauthorised duplication, replication and dissemination of this report, in whole or in part, without the express written consent of Alfa Bank is strictly prohibited. This report was prepared by Natalya Orlova. Alfa Bank operates a policy to ensure the independence of its research. A copy of this policy is available on request from any of the Alfa Group firms that distribute this research. Under this policy the views expressed by the authors in this report accurately reflect their own personal views about the securities and issuers covered in the report. No part of their compensation was, is or will be related to the specific recommendations in this report either directly or indirectly. The authors do not report to Alfa Bank staff who have investment banking relationships with any of the issuers mentioned in the report. Where Alfa Bank or its affiliates have a relationship with any of the issuers covered in this report, the research in this report is produced separately from that relationship. Alfa Bank operates a system of "Chinese Walls" – information barriers to ensure that such relationships are excluded from published research. This publication has been approved for distribution in the United Kingdom by Alfa Capital Markets ("ACM"). ACM is regulated by the Financial Services Authority ("FSA") for the conduct of UK investment business and is the trading name of the UK branch of Alfa Capital Holdings (Cyprus) Limited ("ACC") which is authorised by the Cyprus Securities and Exchange Commission. **This document has not been approved for distribution to private customers as defined by FSA Rules and may not be communicated to such persons.** Although the information in this report has been obtained from, and is based on, sources the Alfa Bank believes to be reliable, no representation or warranty, express or implied, is made by Alfa Bank, ACM or the authors. ACM and its officers and employees do not accept any responsibility as to the accurateness or completeness of any information herein or as to whether any material facts have been omitted. All information and opinions stated herein are subject to change without notice. ACM makes no warranty or representation that the securities and/or opinions referred to herein are suitable for all recipients. This publication and its content are for information only and are not intended as an invitation, inducement, offer or solicitation to buy or sell securities or other financial instruments, or to engage in investment activity. Alfa Bank, ACC and their associated companies, officers and directors, from time to time, may deal in, hold or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to the securities, financial instruments and companies mentioned in this report, or may have been, or may be represented on the board of such companies. Alfa Bank has financial interests in Vimpel Communications and Golden Telecom. Vimpel Communications is a NYSE listed company. Alfa Bank and its affiliates will only accept unsolicited orders for this security. Alfa Bank is employed by Unified Energy System ("UES") in an advisory relationship. Research is produced independently from this relationship. Some investments may not be readily realisable as the market in such securities may be illiquid and therefore valuing the investment and quantifying the risk to which customers are exposed may be difficult. Some investments may be subject to sudden and large falls in value and on realisation customers may receive less than originally invested or, in some cases, be required to pay more. Foreign currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or price of the investment, or the income derived from it. In addition, investors in securities such as ADRs, the values of which are influenced by foreign currencies, effectively assume currency risk. Investing in Russia and Russian securities involves a high degree of risk and investors should perform their own investigations and due diligence before investing. Investors should consult with their professional advisors as to the risks involved in making such a purchase. Alfa Bank, ACM, ACC and their associated companies may issue this publication in other countries. The distribution of this publication in such other jurisdictions may be restricted by law, and persons coming into possession of this document should inform themselves about, and observe, any such restrictions. Any failure to comply with these restrictions might result in a violation of the securities laws of such jurisdictions. **Additional note concerning United States securities laws:** This publication is distributed in the United States by Alfa Capital Markets (USA) Inc ("Alfa Capital"), a subsidiary of Alfa Bank Group, to certain US persons to the extent permitted by US securities laws and other applicable laws and regulations. In connection therewith, Alfa Capital has accepted responsibility for the content of this research. US persons receiving this document and wishing to effect a transaction in any security or financial instrument discussed herein should only do so by contacting a member of Alfa Capital in the US. Any failure to comply with these restrictions may constitute a violation of US securities laws.