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Russian Bond Market

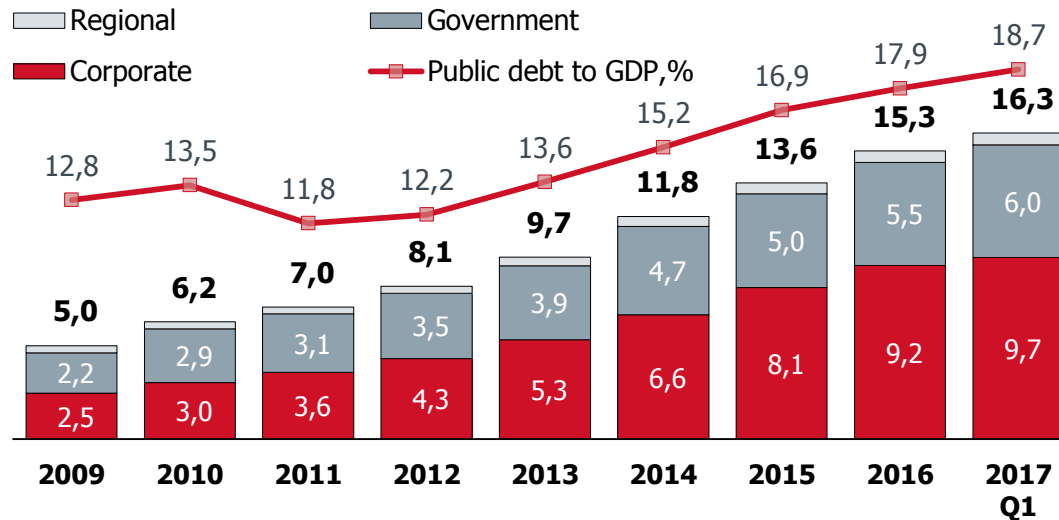
Gleb Shevelenkov

Director of Securities Market
Department

Bond market evaluation

Russian bond market outstanding

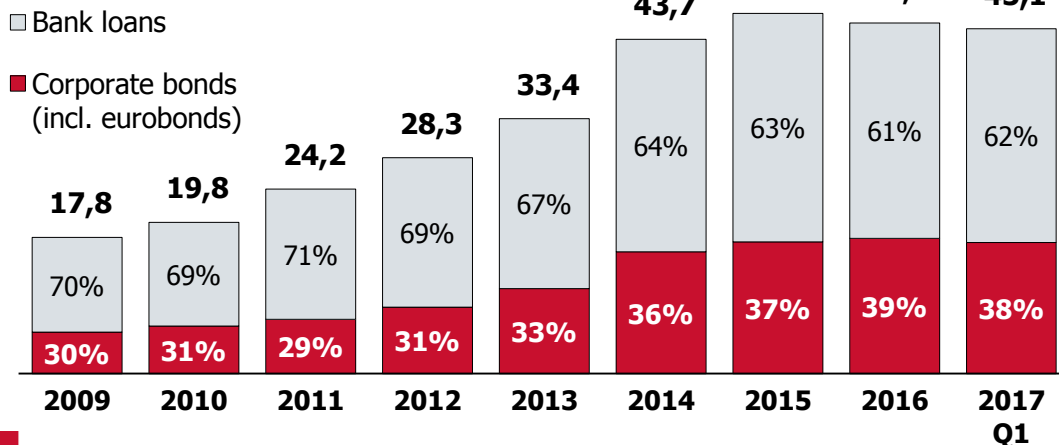
RUB tn (year end)



- Russian bond market is growing faster than GDP
- The share of bonds in corporate debt has been growing from 31% to 39% over the last 6 years
- Bonds account for 45% in the corporate long-term debt

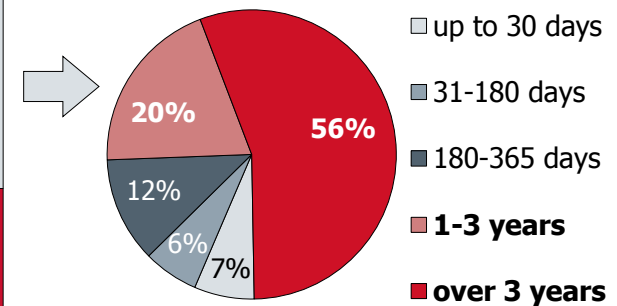
Corporate bonds vs loans

RUB tn (year end)



Corporate loans by term to maturity

As of 01/03/2017



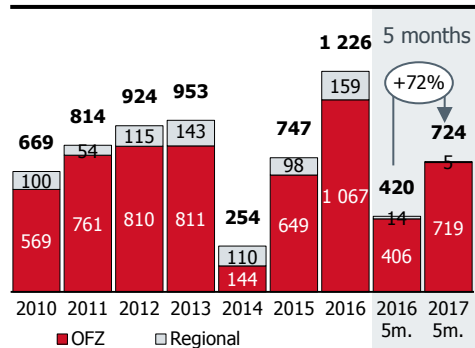
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Source: Bank of Russia, Moscow Exchange, CBonds

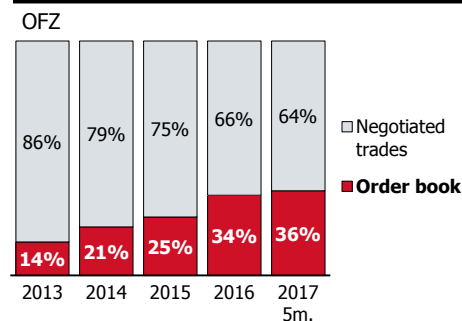
Government bonds – two years of growth

OFZs and regional bonds

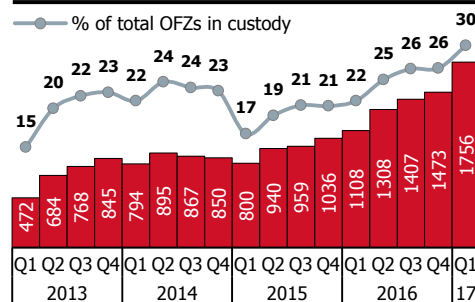
Issuance, RUB bn



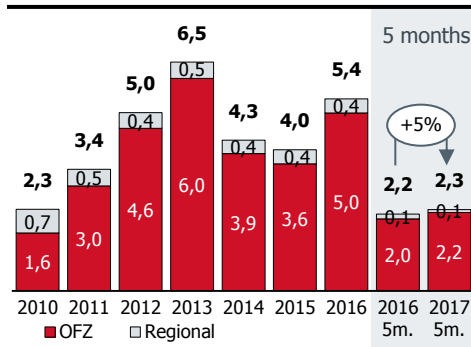
Share of "order book" in secondary trading



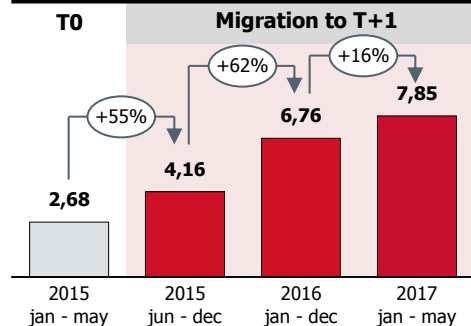
Foreign nominee account balances in NSD, RUB bn



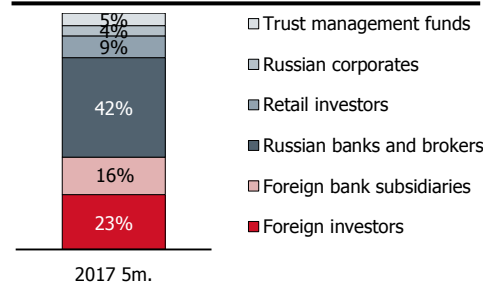
Secondary trading, RUB tn



OFZ - 2 years in T+1 order book, ADTV RUB bn



Trading activity in client groups



- OFZ secondary market growth in 2016-2017 was driven by:
 - Government borrowings increase. Estimated OFZ issuance growth of 75% in 2017 (up to RUB 1.75 tn)
 - On-exchange OFZ trading migration to T+1 in 2H 2015 (partial collateral, T+1 settlement)
 - Swap of illiquid OFZ (RUB 63.7 bn, September 2016).
 - OFZ tick size optimisation and market-making program (2017). Orders execution has grown by 17% this year.
- International investors' holdings account for 30.1% of amount outstanding.
- Expected regional bonds issuance value – 200-250 RUBbn in 2017 driven by:
 - CBR's key rate decline expectations;
 - The policy of the Ministry of Finance on stimulating regional borrowings



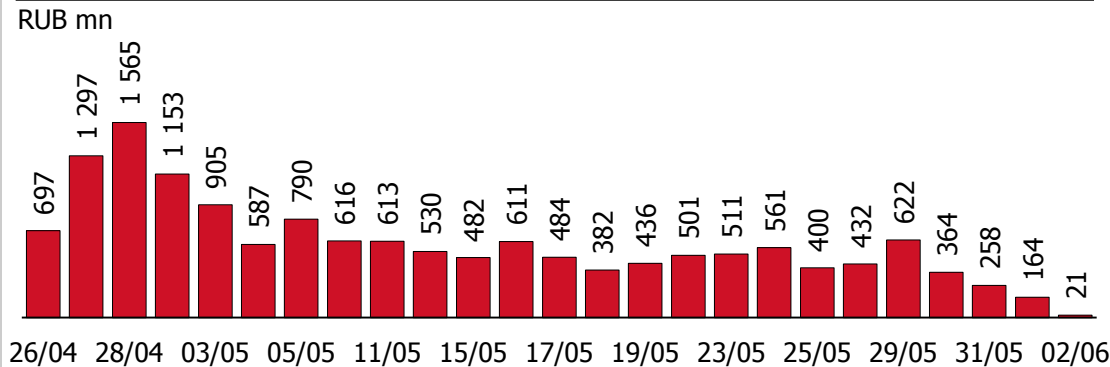
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Source: Moscow Exchange

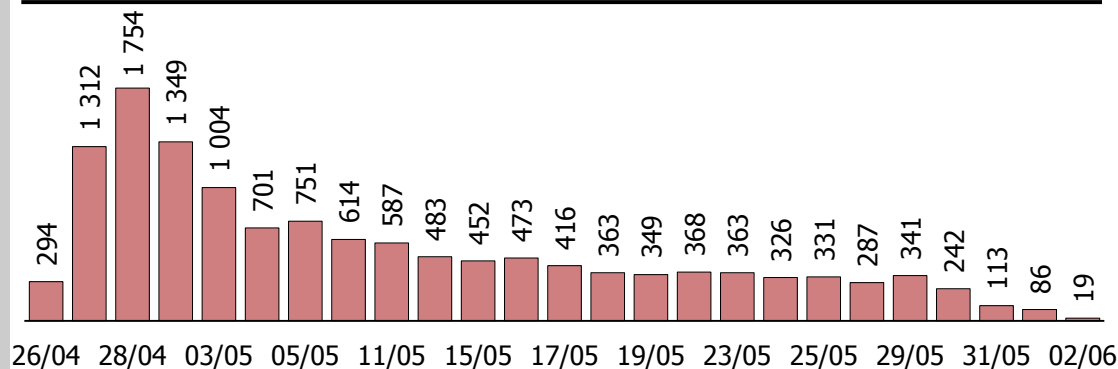
OFZ for individual investors (1st tranche)

| Issued value | Investors number | Average trade value |
|-----------------------|--|----------------------|
| RUB 15 billion | 12,756 individual investors 10,184 (80%) – new investors | RUB 1 million |

Daily issuance



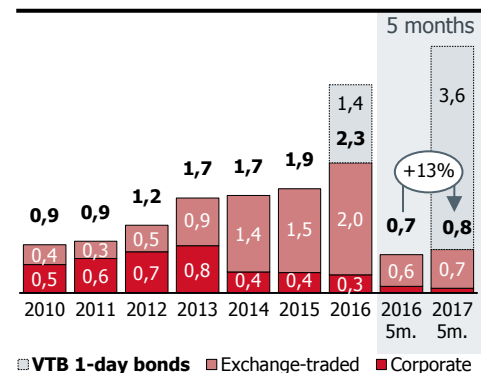
Daily investors base



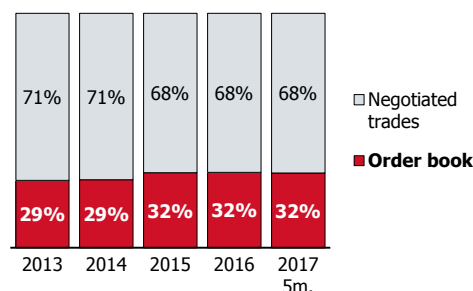
- 26/04/2017 Ministry of Finance launched new OFZ for individuals (53001)
- Principal RUB 15 bn, maturity 3 years, coupon 7.5% - 10.5% (avg. 8.92%)
- Minimal size – 30 bonds, maximal size 15,000 bonds
- Agent banks: Sberbank, VTB 24
- 1 471 (14%) of new individuals have additionally opened Individual Investment accounts (IIA)

Corporate bond as an alternative for bank loan

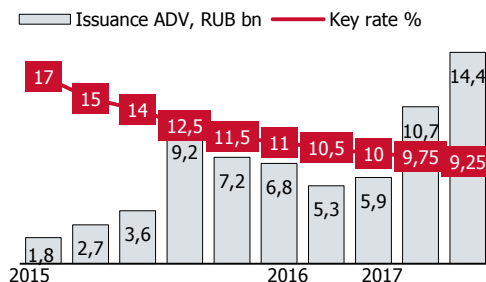
Issuance, RUB tn



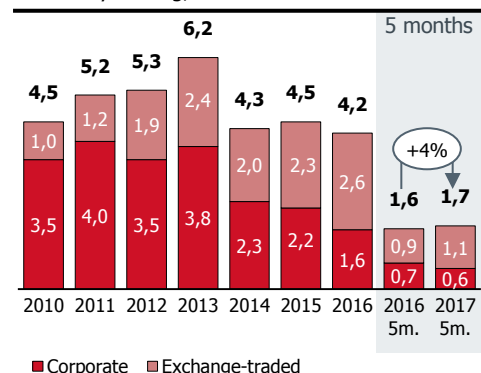
Share of "order book" in secondary trading



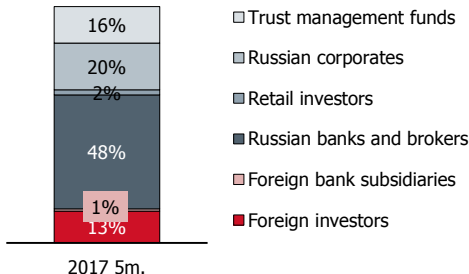
CBR's key rate and corporate bonds issuance



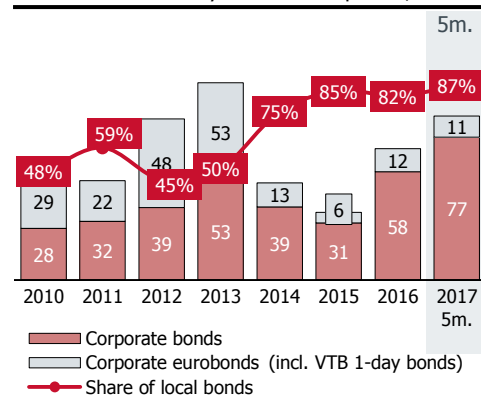
Secondary trading, RUB tn



Trading activity in client groups



Issuance of bonds by Russian companies, USD bn



Main findings:

- Bank loans are substituted by public debt. Over the last 6 years, the share of bonds in corporate debt grew from 31% to 39%
- Intense substituting of external debt with internal in 2014-2016, the average current share of local borrowings is 77% compared with 50% in 2010-2013.
- Key rate reduction (optimistic scenario: 8%-8.5% by the end of 2017)
- Liquidity surplus in the banking system
- Non-state pension funds investments in corporate bonds (RUB 234 bn in march 2017).
- Reinvestment flow (coupons, amortizations, redemptions ~ RUB 2.5 trillion)

Source: Bank of Russia, Moscow Exchange, CBonds

New bond market instruments 2016-2017

Short-Term bonds (< 1 year)

2016 PGK, Binbank, Carcade, Gazprombank, Sberbank

Ultra-Short-Term bonds (< 1 week)

2016 VTB – RUB 3.6 tn (97 issues) in 2017 YTD

FX domestic bonds

2016 VEB – USD 600 mn, Uralkali – USD 800 mn, Avenir – USD 20 mn, Eximbank of Russia – USD 150 mn

Retail bonds

2017 OFZ for individuals (53001)

TBA Regional and corporate issuers

High-yield bonds

??? Small and medium-size businesses



High yield & risk bonds – is there a value to the market?

Potential of the segment

- 230,000 small and medium-size businesses (SMBs) in Russia
- Need for borrowings ~RUB 300-500 mln per company

Major obstacles

- Complicated requirements even for a small issuance
- High entry cost to public placement



Searching for comfortable solutions

- Low disclosure and listing requirements for small issuances?
- Direct infrastructural link between issuers and retail investors?

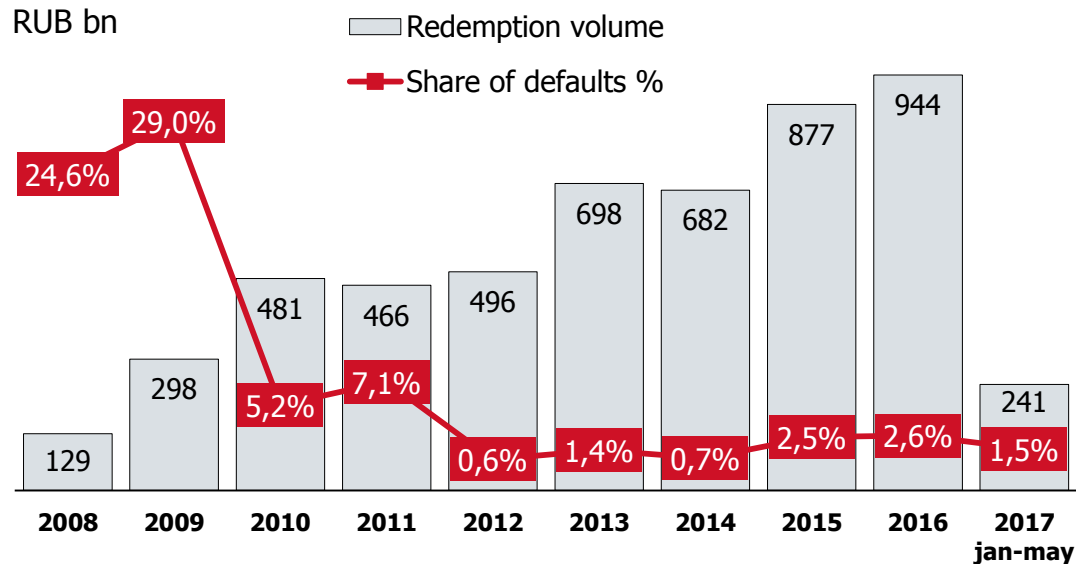
How to reduce risks?

- Restriction on the issue size?
- Maximum value of a purchase in “one hand”?
- Specially dedicated trading mode?
- Segregated bond segment?



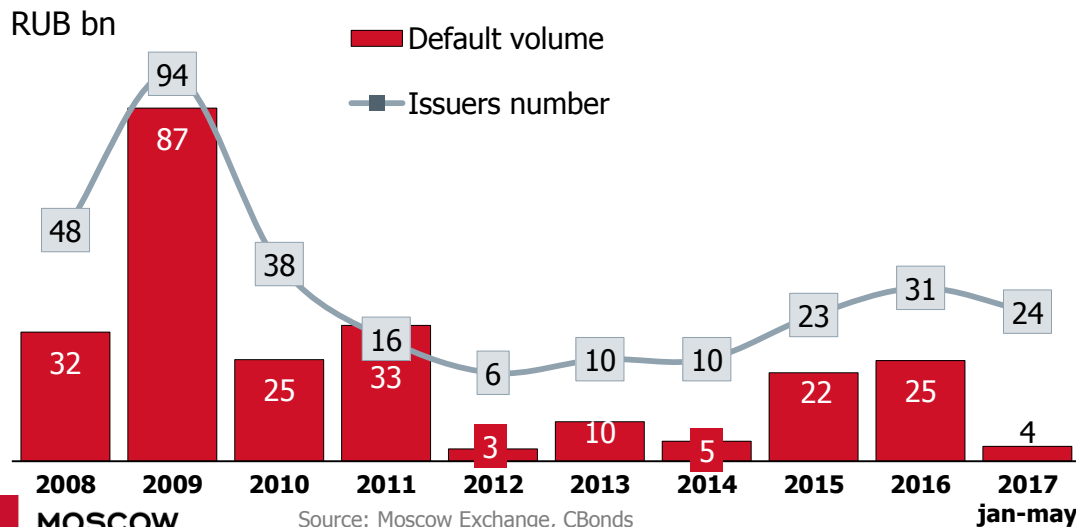
Defaults in the market

Corporate bond redemption volume



- The biggest redemption size in the market was in 2006...
- ... and the number of default cases decreased by 3 times from those in 2009
- In 2017 the share of problem bonds is ~1.5% of current redemption

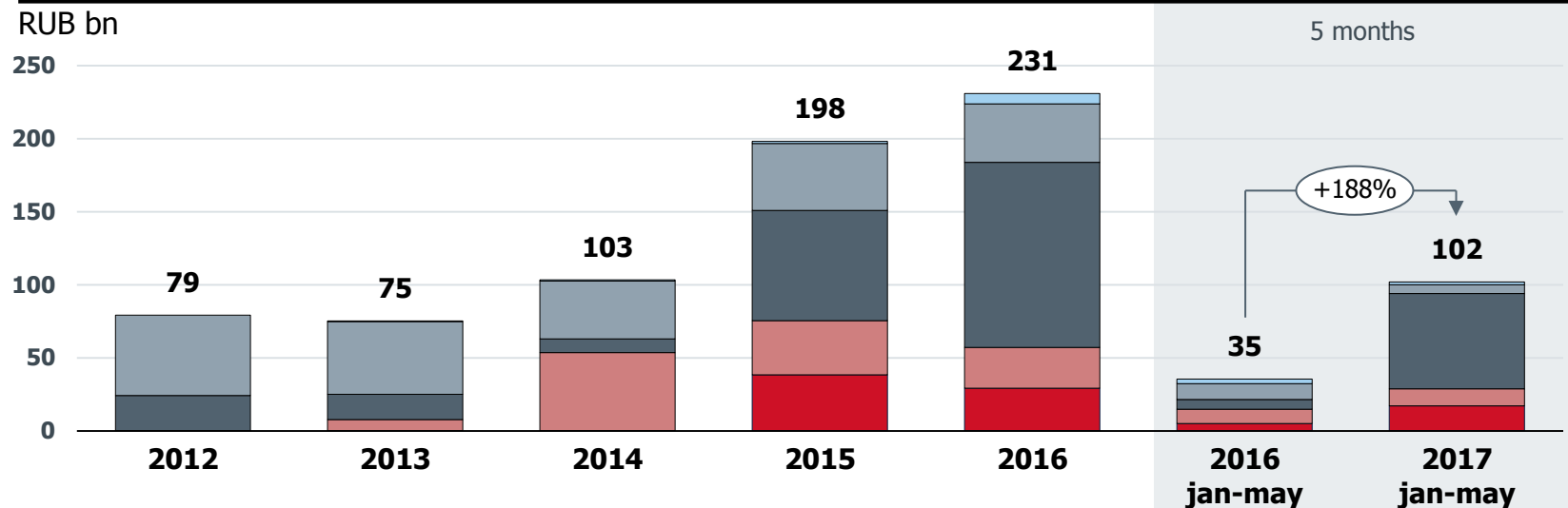
Default volume



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FI market instruments in a foreign currency

Trading value (primary and secondary markets)



Corporate Eurobonds

- 52 issues
- 20 of them trading with minimum lot USD 1,000

Government Eurobonds

- 12 issues (Russia)

Corporate bonds in a foreign currency

- Veb-leasing (15 iss.)
- Veb (1 issue)
- Uralkali (2 issues)
- Avenir (1 issue)
- Eximbank of Russia (1 issue)

Bonds of international Financial Institutes

- 19 issues

Bond ETFs

- US Treasury Bills ETF (RUB)
- Russian Eurobonds ETF (RUB/USD)



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Source: Moscow Exchange

Projects and regulatory initiatives

Clearing

- Single pool of collateral
- New trading vs clearing membership structure

Bond Market

- On-exchange book building (prefunding/compensation)
- OFZ market spreads
- Bond put/call- option optimization
- New instruments - Ultra-Short-Term bonds, High-yield bonds, Securitization, etc.
- Swap technology development

Securities Market

- Increase of the maximum IIA contribution to RUB 1 million per year
- Reduction of the term of ownership from 3 to 1 year for tax deduction
- New taxation of coupon payments
- Eligibility restrictions removal for non-state pension funds (IPO/SPO, REPO)
- Issuance simplification
- "Russian Basel" (N1, LCR) adaptation for more flexible bond accounting



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- changes in (a) domestic and international legislation and tax regulation and (b) state policies related to financial markets and securities markets;
- competition increase from new players on the Russian market;
- the ability to keep pace with rapid changes in science and technology environment, including the ability to use advanced features that are popular with the Company's and its subsidiaries' customers;
- the ability to maintain continuity of the process of introduction of new competitive products and services, while keeping the competitiveness;
- the ability to attract new customers on the domestic market and in foreign jurisdictions;
- the ability to increase the offer of products in foreign jurisdictions.

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