

Russian Capital Market
January – June 2008

Facts and Events

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AUTHORS:

- Alexey V. Timofeev – Chairman of Executive Board, NAUFOR
- Alexander Ya. Tregub – Councillor to Chairman of Executive Board, NAUFOR
- Elena A. Shabunina – Deputy Chairman of Executive Board, NAUFOR
- Dmitriy V. Shubochkin – Leading specialist, NAUFOR, Department of control and support of professional activities

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Introduction

This paper presents a review of Russian capital market in the first half of the year 2008.

Our purpose was to give a general idea of the Russian capital market and its key elements: its instruments, participants, infrastructure, regulation and supervision systems, as well as the main market events of the year.

The reports are issued by the National Association of Securities Market Participants with active participation of the Moscow School of Management SKOLKOVO.

Please note:

first, in this review we strived to avoid extensive comments and judgements, except for those necessary to understand the data contained in the present report, their dynamics, as well as the specifics of Russian capital market;

second, we used the data as of the end of the first half of 2008 whenever possible; however in some cases when such data were unavailable we used available data with the timestamp as close to this date as possible;

third, it was not our purpose to show a lengthy trend of the Russian market development prior to 2008. Generally, when using historical data, we limit ourselves with the information dating to no earlier than 2005;

fourth, the numerical data in the review are presented both in national and in foreign currency. This is due to peculiarities of trading and presenting the results;

fifth, sometimes we quote data from different sources to show the existing discordances in estimates or calculations.

Main indicators and trends for the first half of 2008

Stock market

The capitalization of Russian stock market is still around 1.3 trillion dollars. The number of issuers represented at stock exchanges decreased by about 10%, and the number of instruments in quotation lists increased by 10%. The concentration of stock market capitalization is still high: ten most capitalized Russian issuers account for 66% of the total capitalization. By industry, 50% of the Russian stock market capitalization is concentrated in the oil and gas industry companies. The internal exchange turnover of transactions with Russian companies' stocks (excluding repurchase transactions) decreases by about 4% per quarter, on the average, and amounted to around 8 trillion roubles according to the results of the half-year (0.34 trillion dollars). The share of repurchase transactions in the total exchange turnover is growing and has reached 60%. The internal exchange turnover of transactions with Russian companies' stocks (including repurchase transactions) amounted to around 20 trillion roubles according to the results of the half-year (0.85 trillion dollars). Public offerings of stocks by Russian companies have slowed down. One IPO was held in a foreign stock exchange (449 million dollars raised). Total raised capital including secondary offers amounted to 1.3 billion dollars.

Corporate bonds market

The total amount of corporate bonds in circulation is 1.5 trillion roubles. The number of issuers reached 468. The share of so-called non-market issues (issues that are not in circulation) experienced sharp growth. The total volume of IPOs for corporate bonds was 385 million roubles, including 7.5 million roubles for the exchange bonds. The estimated total transaction volume for corporate bonds (repurchase transactions not included) did not change compared to the same period of last year and amounted to around 1.3 trillion roubles according to the results of the half-year. The share of repurchase transactions in the total exchange turnover for corporate bonds is growing and has reached 78%. The internal exchange turnover of transactions with Russian companies' corporate bonds (including repurchase transactions) amounted to around 5.7 trillion roubles according to the results of the half-year.

Derivative market

The market of derivative contracts, whose underlying assets include securities and stocks indices, experiences active growth. Just under 90 types of contracts are offered. The total volume of the transactions was 6.4 trillion roubles, and the number of the transactions reached 11 million.

Stock indices

The main stock indices experienced slowdown and downtrend. The profitability (APR) by composite indices was 1.1% for the RTS Index and dropped to -14% for the MICEX index. All industry and capitalization indices, except oil and gas, metallurgy and mining, showed negative profitability. The biggest dropdown was seen in power industry index (-48%), telecommunications (-42%) and financial industry (-31%).

Individual Investors

The number of private investors operating at MICEX is growing and has achieved 472,000, including 68,500 active investors.

Collective Investors

The number of Unit Investment Funds (UIFs) remained almost unchanged and is around 1000. The total net value of UIF assets amounted to 841.5 billion roubles and grew because the total net value of closed-end UIFs, mainly the real estate funds, has grown. The total net value of opened-end UIFs decreased by 16.3 billion roubles, and that of interval funds – by 4.5 billion roubles. The opened-end UIFs registered a negative balance of net capital raising: the outflow amounted to 10.1 billion rbl.

Foreign investment funds

As currently estimated, about 2000 foreign funds (among those required to disclose the information on their activity) invest into Russian assets (stocks and depository receipts) A constant inflow of these funds' resources into Russian assets is registered. The total volume of Russian assets in which these funds have invested is estimated as 105 to 110 billion dollars. About a quarter of these assets was purchased in Russian stock exchanges.

1. Instruments

1.1. Stocks

Russian legislation requires registering all stock issues by all joint stock companies (including closed joint stock companies). The CJSC SKRIN database, as of the end of the first half of 2008, registered 127,408 stock issues by 86,657 issuers (including 23,531 open joint stock companies). The overwhelming majority of all these stocks is absolutely illiquid, and they are not traded in any secondary markets.

Only a very small part of these stock issues is traded on stock exchanges. See summary data on stocks offered at Russian stock exchanges in Table 1.

Table 1. Organized stock market.

	MICEX				RTS			
	2005	2006	2007	1H08	2005	2006	2007	1H08
Number of Issuers	163	190	208	185	261	281	302	265
Number of stock issues	256	325	309	334	383	398	413	343
of them, included in the quotation lists (common stocks/preferred stocks)	34/16	46/14	71/16	77/16	46/13	63/13	87/16	90/15

Sources: MICEX, RTS.

Therefore, less than 1.5% of all open joint stock companies are represented at stock exchanges.

The growth trend of the number of public issuers, typical for 2006 and 2007 (10% per year, on the average) changed to a downtrend in 1H08: the number of issuers dropped about 10% compared to the beginning of the year. It should be noted that the majority of the stock issues traded on organized markets (about 70% of their total number) refer to nonlisted securities, i.e. the securities that were allowed to be traded without undergoing the listing procedure. In 2005-2006 this statistics was higher, about 80%. The growth rate of the number of instruments included in the quotation lists of different levels in 2006-2007 was 30 to 35% annually. In the first half of 2008 this number grew up 7-10% compared to the beginning of the year.

A specific feature of Russian capital markets is the opportunity to conduct organized trade in securities of the same issuer simultaneously on several stock exchanges. Therefore a considerable part of the issuers is present at both of the principal Russian stock exchanges. Stocks of some Russian issuers in the form of depository receipts are traded at foreign exchanges as well. According to Standard&Poor's data¹, the number of Russian issuers with stocks listed at RTS, MICEX, NYSE, NASDAQ as well as entered in the LSE-listed S&P EMDB Russia index, was 309 as of December 2006, and 328 as of December 2007. In March 2008 this number dropped to 312.

Therefore, the first half of 2008 demonstrated the downtrend for the number of public issuers, for the first time over the last years.

¹ Emerging Stock Markets Review, S&P, 2006-2007 issues series.

The data on the Russian issuers stock market capitalization are shown in Table 2. Please note that at present there is no commonly accepted methodology for calculating Russian issuers stock market capitalization. Because of that, this report uses data from several sources.

Table 2. Russian issuers stock market capitalization.

Period	Units	2005	2006	2007	2008	
					Q1	Q2
MICEX ²	billion roubles	N/A/7 440	25 482/23 338	32 740/29 974	N/A/26 000	32 263/29 305
	billion dollars	N/A/259	966/885	1 329/1 217	N/A/1 106	1 375/1 249
RTS	billion dollars	329	966	1 329	1 232	1 375
Estimate by S&P ³	billion dollars	549	1 057	1 503	1 406	1 524
GDP	billion roubles	21 624	26 882	32 988		
Capitalization/GDP ⁴	%	34,41	94,79	99,25		

Sources: MICEX, RTS, FSSS, S&P.

In general, in the first half of 2008 the growth of Russian issuers stock market capitalization experienced a slowdown. In the first quarter of 2008 the capitalization dropped 7% compared to the previous quarter; at the end of the 2nd quarter, the capitalization was 3.4% higher than at the end of 2007. We should note that, while in 2005 the foreign trading floors share of Russian issuers' stocks capitalization was 40%, in 2006 – 1st half of 2008 it was 9-12%.

High concentration of capitalization is a specific characteristic of Russian capital market; it's true both for the issuers and for the industries they belong to.

Table 3 contains the list of top ten most capitalized companies, and Table 4 shows change dynamics of top ten most capitalized companies' share in 2006-2008.

Table 3. Most capitalized Russian issuers (Results for the first half of 2008).

Nº	Issuer	Capitalization (billion dollars)	Share in total capitalization (%)
1	OJSC "Gazprom"	345,0	27,61
2	OJSC "NK Rosneft"	110,5	8,85
3	OJSC "Lukoil"	84,0	6,73
4	OJSC "Sberbank"	70,6	5,65
5	OJSC "MMC Norilsk Nickel"	48,4	3,87
6	OJSC "Surgutneftegaz"	43,6	3,49
7	OJSC "Gazprom neft"	37,9	3,04
8	OJSC "Novolipetsk Steel"	33,2	2,66
9	OJSC "Uralkaliy"	30,5	2,44
10	OJSC "Severstal"	26,3	2,10
	TOTAL	830,1	66,44
	Total capitalization	1 249,3	100,00

Source: MICEX.

² MICEX appraises both the total capitalization of the share market (the numerator) and the capitalization of the issuers whose shares are circulating at the stock exchange (the denominator). This stock exchange also offers the capitalization estimates in national and foreign currency.

³ The estimate included Russian issuers with shares listed at RTS, MICEX, NYSE, NASDAQ as well as those featured in the LSE-listed S&P EMD Russia index.

⁴ The calculations took into account the capitalization of the internal capital market.

Table 4. The share of top ten most capitalized issuers in total capitalization of the capital market.

	2006	2007	2008	
			Q1	Q2
TOTAL (%)	78,50	68,46	66,65	66,44
Incl. OJSC "Gazprom"	30,70	27,27	26,98	27,61

Calculated using MICEX data.

Over the last several years, there was little change in the list of the most capitalized issuers: in 2006, OJSC "NK Rosneft" entered the list after an IPO, and upon the results of 2007, OJSC "VTB Bank", also after an IPO. In the first half of 2008, as a result of completed reorganization of the power industry, one of the most capitalized and liquid issuers, RJSC "UES of Russia" ceased its activities. A new highly capitalized issuer, OJSC "Uralkaliy", entered the list after an IPO; OJSC "VTB Bank" did not make it into the list of top ten most highly capitalized issuers. The decrease of concentration for issuers capitalization in the first half of 2008 compared to 2007 is very small; OJSC "Gazprom" accounts for about 30% of the total capitalization.

Table 5 shows the dynamics of the Russian market capitalization concentration by industry. In this Table, petrochemical industry and manufacturing of mineral fertilizers are categorized as Chemical industry, and the pharmaceutical industry as Other industries.

Table 5. Russian stock market capitalization by industry.

№	Industry	2006	2007	2008	
				Q1	Q2
1	Oil and gas	62,4	50,4	50,9	53,5
2	Finances	9,2	11,8	10,2	9,0
3	Power industry	11,9	12,5	11,6	11,0
4	Metallurgy	8,1	11,0	12,2	11,5
5	Communications	4,1	5,8	5,5	4,7
6	Food industry	1,5	1,3	1,2	1,1
7	Construction	0,0	1,3	1,2	1,2
8	Mechanical engineering	0,8	1,1	1,2	1,1
9	Transportation	0,8	1,2	1,1	0,9
10	Trade	0,6	0,7	0,7	0,7
11	Mining	0,3	0,7	0,9	1,2
12	Chemical industry	0,2	1,5	2,0	3,0
13	Other industries	0,2	1,0	1,1	1,1

Source: MICEX.

As one may see from Table 5, the 2007 trend for the decrease of oil and gas industry share did not develop further. More than a half of Russian stock market capitalization is still concentrated in the oil and gas segment. A positive tendency in the industry structure that emerged in 2007 was the increase of the financial companies' share. This tendency is related to the large offerings of stocks by two financial organizations, OJSC "Sberbank" and OJSC "VTB Bank". However, in the first half of 2008 the share of financial companies in the total capitalization dropped back to the 2006 level.

No new segments emerged in the capitalization structure by industry, with a possible exception of construction industry. A relative increase of the share of chemical industry enterprises also worth noting.

Table 6 shows transaction volumes for Russian companies' stocks at the leading stock exchanges.

Table 6. Russian issuers' stocks trading volume.

Period	Units	2005	2006	2007	2008		1H08
		Total	Total	Total	Q1	Q2	Total
MICEX ⁵	billion roubles	4 025,0	14 859,6	30 927,1	9 570,2	10 249,6	19 819,7
<i>share of repurchase transactions in the total volume of stocks transactions at MICEX</i>							
	%	18,5	25,6	50,5	58,0	62,4	60,3
RTS classical market ⁶	billion dollars	7,7	16,1	14,6	3,6	3,1	6,7
<i>share of repurchase transactions in the total volume of stocks transactions on RTS classical market</i>							
	%	0,0	0,0	0,0	0,0	0,0	0,0
RTS exchange market ⁷	billion roubles	82,0	27,3	23,5	4,9	7,4	12,3
<i>share of repurchase transactions to the total volume of stocks transactions on RTS exchange market</i>							
	%	0,6	12,0	36,3	48,3	44,6	46,1
SE SPB ⁸	billion roubles	936,8	1 205,9	64,2	21,1	18,0	39,1
<i>share of repurchase transactions in the total volume of stocks transactions at SE SPB</i>							
	%	17,5	25,1	64,8	89,9	86,5	88,4
Exchange rate of US dollar for the last day of the period (informational)							
		28,78	26,33	24,55	23,52	23,46	23,46
Total (estimated) including repurchase transactions							
	billion roubles	5 264,0	16 516,8	31 383,5	9 679,8	10 348,6	20 028,4
	billion dollars	182,9	627,3	1 245,4	411,6	441,2	852,8
Total (estimated) not including repurchase transactions							
	billion roubles	4 354,1	12 415,6	15 713,0	4 110,5	3 934,2	8 044,4
	billion dollars	151,3	471,5	621,2	174,8	167,7	342,9
As estimated by S&P	billion dollars	159,3	514,4	754,5	222,0	214,5	436,5
Turnover ratio (annual)⁹							
	%	45,98	48,81	46,74			
Turnover ratio (quarterly)							
	%				14,19	12,20	

Sources: Bank of Russia, MICEX, RTS, S&P.

Trading volumes for the stocks of Russian companies have sustained strong growth in 2005-2007. Thus, the volume of trade in the leading trading floors has, on the average, tripled in 2006 compared to 2005; in 2007 the annual increase was lower, around 30%. In the first half of 2008 the growth has slowed down, and the quarterly transaction volume (not including repurchase transactions)

⁵ Including auction mode, negotiated deals mode, IPO and repurchase transactions.

⁶ Including market deals, OTC deals and repurchase transactions.

⁷ Including market deals, OTC deals and repurchase transactions.

⁸ Including market deals, OTC deals and repurchase transactions.

⁹ Here, calculated as the ratio of the transactions volume (not including repurchase transactions) for a period (a quarter or a year) to the capitalization as of the end of this period.

has dropped, on the average, by 4%. The turnover ratio for the stock trade at stock exchanges has dropped accordingly.

It worth noting that, starting from 2007, the share of repurchase transactions with stocks has changed significantly. While in 2005 it constituted 17% of the total volume of stock exchange trade of stocks, and in 2006, 25%, by the end of 2007 it reached a significantly different level of 50%. In the first half of 2008 the share of repurchase transactions in the internal market grew further and reached 60%; at some stock exchanges it even reached 80% i.e. was an overwhelming majority. Thus, over the last years the internal stock exchange market is more and more used as secured credit money market.

The trade in stocks is concentrated on a rather limited set of instruments. Table 7 shows the list of issuers whose stocks were traded most actively at MICEX in the first half of 2008¹⁰.

Table 7. Issuers whose stocks were traded most actively at MICEX (Results for the first half of 2008).

Nº	Issuer	Share in total turnover (%)
1	OJSC "Gazprom"	33,9
2	OJSC "Sberbank"	12,6
3	OJSC "MMC Norilsk Nickel"	10,1
4	RJSC "UES of Russia"	9,0
5	OJSC "Lukoil"	8,8
6	OJSC "Surgutneftegaz"	4,8
7	OJSC "Rostelecom"	4,8
8	OJSC "NK Rosneft"	4,3
9	OJSC "VTB Bank"	3,7
10	OJSC "Tatneft"	1,2
TOTAL		93,2

Source: MICEX.

The turnover concentration has an insignificant downtrend (the share of top ten most liquid issuers was 96.6% in the end of 2006 and 94.8% in the end of 2007¹¹). Over the last few years, there was little change in the list of the most liquid issuers: in 2006, OJSC "NK Rosneft" entered the list after an IPO, and in 2007, OJSC "VTB Bank", also after an IPO. Characteristically, according to the results of the first half of 2008, compared to the end of 2007, RJSC "UES of Russia" moved from 2nd to 4th place in the list of the most liquid issuers.

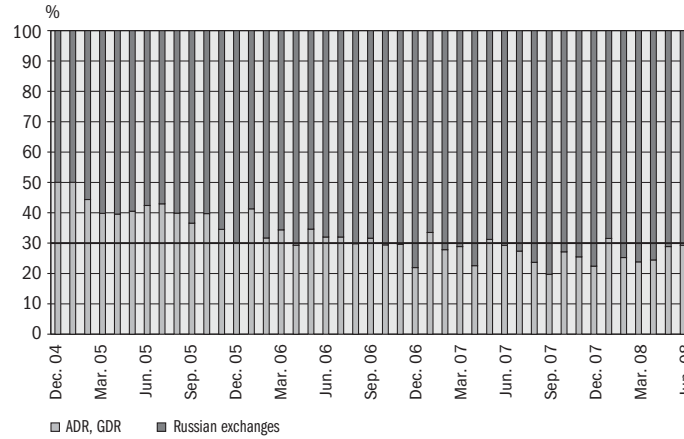
An important issue for the Russian capital market is the distribution of trading volume between domestic and to foreign exchanges.

Foreign trade in depository receipts far exceeded domestic trade in these instruments in the late 1990s. At the end of 2004, however (see Fig. 1) domestic exchanges have restored the parity with foreign exchanges and in 2006 have established the average ratio of 70% to 30%. In 2007 and the first half of 2008 this ratio remained more or less unchanged fluctuating slightly up and down.

¹⁰ Including repurchase transactions.

¹¹ Calculated using MICEX data.

Figure 1. The amount of stocks and depository receipts trades of Russian companies, which depository receipts are traded on foreign exchanges



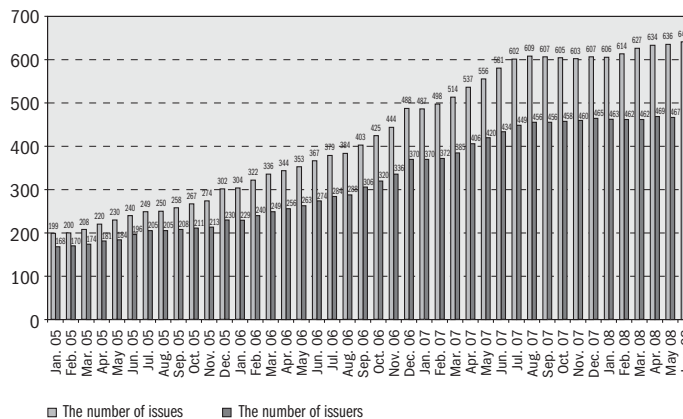
Source: MICEX.

1.2. Corporate bonds

Unlike many other national bond markets, the Russian domestic corporate bonds market developed predominantly as an exchange market from the very beginning. Development of the corporate bonds market for the last few years shows a stable increase in the numbers of issuers and issues, as well as growth of trading volumes.

According to the CBONDS agency, as of the end of 1H08, there were 642 corporate bonds issues of 468 issuers in circulation, exceeding the 1H07 figures by 10.5% and 7.8% respectively. As you can see on Figure 2, starting from July 2007 the growth rates for the numbers of stock issues and issuers have dropped abruptly (in 2005 they were 52.7% and 36.3%, in 2006 – 61.6% and 60.9%, in 2007 – 24.4% and 25.7%).

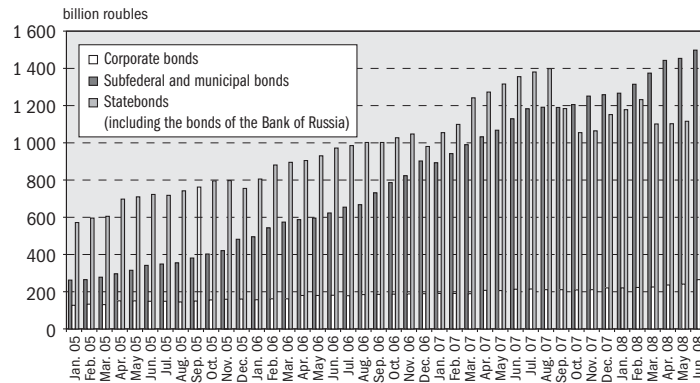
Figure 2. The numbers of corporate issuers and issues in domestic debt instruments market.



Source CBONDS

According to CBONDS agency, the total volume of Russian corporate bonds in circulation as of the end of 1H08 amounted to 1497.11 billion rbl. at par, which is an 32.7% increase compared to the same period of 2007 (see Figure 3). This growth rate is low compared to the previous years (which was 88.3% in 2005 and 87.4% in 2006, and dropped to 39.2% in 2007).

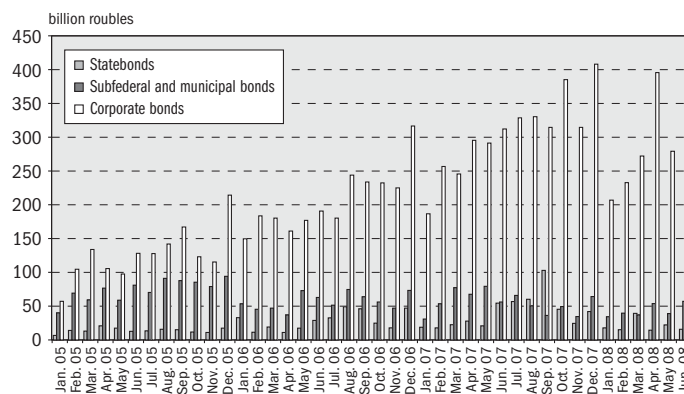
Figure 3. The volume of the domestic debt market (at nominal value).



Source CBONDS

The share of so-called non-market issues (issues that are not in circulation) for 2006-2007 stayed more or less the same, in the range of 0.25-0.4%. In the 2nd quarter of 2008, however, according to the CBONDS agency data, this share experienced a sharp growth and reached 3.0-4.5%, the level of early 2005. According to experts, this is related to the large non-market offerings of corporate bonds that took place.

Figure 4. Total trading volume on the domestic debts instruments market (by months)



Source CBONDS

It worth noting that in September 2007 the volume of corporate bonds exceeded the volume of the Federal bonds, including these of the Bank of Russia. Since then, the gap has been increasing.

It is worth noting that the share of the financial industry in the total corporate bonds turnover volume experiences constant growth¹²: at the end of 2005, it was 20.7%, at the end of 2006, 26.3%, in 2007 it reached 32.4% and by the end of 1H08, 36.7%. It means that the finance companies, and first of all the credit institutions, increasingly use the debt market as a source of additional debt financing.

The total volume of IPOs for corporate bonds in 1H08 is estimated¹³ at 385 million roubles, including exchange bonds.

The trading volume at the secondary corporate bonds market¹⁴ (exchange and off-exchange in total) is permanently growing (see Figure 4). There are, however, significant changes in monthly turnover from month to month; thus, the seasonal factors became visible in the last years: there is a significant activity in December and a slump in the beginning of each year. The end of 2007 and the beginning of 2008 are similar to other periods in this aspect, except for the sharp outlier in April 2008.

The total volume of secondary market transactions with corporate bonds for 2005-2008 is represented in Table 8.

Table 8. Volume of transactions with corporate bonds.

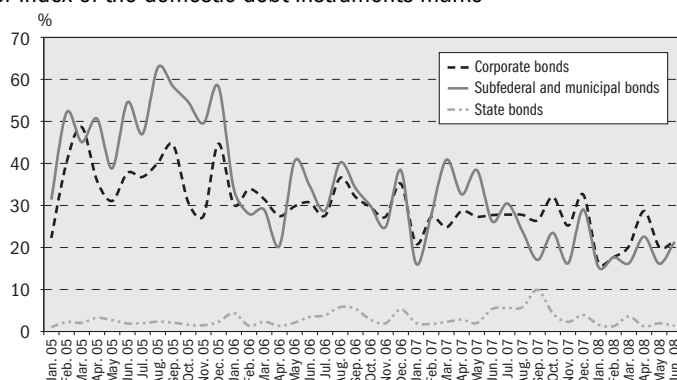
Period	Units	2005	2006	2007	2008		1H08 Total
		Total	Total	Total	Q1	Q2	
Total turnover	billion roubles	1 514,3	2 437,5	3 669,5	711,8	984,4	1 696,2
The share of e transactions at organized marketplaces in the total turnover	%	60,31	72,19	73,92	70,63	77,63	74,69

Source: CBONDS.

As it follows from the Table 8, the volume of transactions with corporate bonds is constantly growing: the total turnover for 2006 was 61% higher than for 2005, and in 2007 the transaction volume grew by 51%. In 2008, the growth rate has slowed down: the transaction volume for 1H08 is only 6.8% higher than for the same period of 2007. Characteristically, the share of exchange transactions in the total turnover is growing steadily; it reached 74% in 2007 and did not change in the first half of 2008.

The corporate bonds market is rather liquid (see Figure 5).

Figure 5. Turnover index of the domestic debt instruments market



Source CBONDS

¹² As estimated by CBONDS.

¹³ As estimated by GK "Region".

¹⁴ From here onwards, the repurchase transactions are not included in secondary market volume estimates for all types of bonds, unless stated otherwise.

The corporate bonds turnover index¹⁵ is subject to considerable changes, including seasonal changes; however its median value is permanently decreasing: from 37.3% in 2005 to 20.3% in the first half of 2008.

Corporate bonds are traded at MICEX and RTS. Table 9 contains summary data on corporate bonds (including stock exchange bonds) offered at Russian stock exchanges, and Table 10 contains data on bonds traded at MICEX¹⁶.

Table 9. Organized corporate bonds market.

	MICEX				RTS			
	2005	2006	2007	1H08	2005	2006	2007	1H08
The number of bond issuers	202	316	445	456	4	77	79	78
The number of bond issues	250	414	577	601	4	118	120	113
including these in the quotation lists (issuers/issues)	46/62	69/98	149/207	184/250	1/1	0/0	0/0	0/0

Source: MICEX, RTS.

Table 10. MICEX bonds transactions volume¹⁷.

Period	Units	2005	2006	2007	2008		1H08
		Total	Total	Total	Q1	Q2	Total
Corporate bonds without repurchase transactions	billion roubles	900,4	1 801,3	2 700,5	500,7	763,0	1 263,6
Corporate bonds with repurchase transactions	billion roubles	1 249,7	3 665,1	9 374,4	2 268,57	3 450,7	5 719,3
Share of repurchase transactions to the total volume of corporate bond transactions	%	27,95	50,85	71,19	77,93	77,89	77,91

Source: MICEX.

Therefore, as follows from Figure 2 and Table 9, currently about 95% of all the bond issues are represented at organized market. At the same time, despite the permanent growth of corporate bond exchange transaction volumes in the absolute figures, their growth rate decreases. Thus, while in 2006 the numbers doubled in comparison to 2005, the year 2007 showed only 50% growth. For the first half of 2008, the volume of stock exchange transactions with corporate bonds was comparable to the same period in 2007 (the growth is only 5%).

A new tendency of the last few years is the rapid growth of the share of repurchase transactions in the total secondary turnover of the corporate bonds. Thus, over the 2 years from 2005 to 2007 this index grew 2.5 times and exceeded 70%. The volume of repurchase transactions in 1H08 reached 78%.

¹⁵ In this case calculated as the ratio of the monthly transactions volume to the total volume of corporate bonds in circulation, at nominal value, for this month.

¹⁶ The data on RTS bond trading is not shown in this table and Table 15, it being relatively small (in 2005, the total transaction volume at Classical and Exchange markets of RTS with corporate, subfederal and municipal bonds including market deals and two-sided deals amounted to 0.15 billion roubles, in 2006 – 8.24 billion roubles, in 2007 – 1.23 billion roubles, and in the first half of 2008 – 3.05 billion roubles).

¹⁷ Including auction mode and negotiated deals mode. Initial offerings are not included.

Thus, the organized corporate bonds market, as well as the stock market, is more and more used as secured credit money market.

A notable characteristic of the corporate bonds market, and an advantage over the stocks market, is the low concentration of its trading volumes. Table 11 contains data on ten bonds issues with the highest transaction volumes in 1H08¹⁸.

Table 11. Corporate bonds issues that were traded most actively at MICEX
(Results for the first half of 2008).

№	Security	Issuer	Доля в общем обороте (%)
1	BankMosk-2	OJSC "Bank of Moscow"	2,82
2	FGC UES - 02	OJSC "FGC UES"	2,03
3	RZhD-06obl	OJSC "Railways of Russia"	1,87
4	Hydro OGK - 1	OJSC "UK HydroOGK"	1,59
5	IKS5Fin01	LLC "IKS 5 FINANS"	1,46
6	FGC UES - 05	OJSC "FGC UES"	1,43
7	VTB - 5 ob	OJSC "VTB Bank"	1,33
8	TsentrTel-4	OJSC "Tsentrtelecom"	1,21
9	StrTrGaz02	OJSC "StroyTransGaz"	1,13
10	RusAlF-3v	LLC "Russian Aluminum Finances"	1,11
		TOTAL	15,98

Calculated using MICEX data.

Therefore, the secondary bonds market is much less concentrated on particular instruments. It should be noted that the concentration of corporate bond transactions tends to decrease: according to the results of the first quarter of 2007, the share of top 10 most traded bonds in the total turnover was 26.1%, and at the end of 2007 it was 20.1%. We should also emphasize that the list of most liquid corporate bonds is subject to significant changes. Thus, of the 10 issuers listed in Table 11, only 4 were present in the similar list for 2007.

In March 2008, a pilot offering of exchange bonds was held at MICEX. The total volume of IPOs for exchange bonds in 1H08 was 7.5 million roubles.¹⁹ To issue exchange bonds, the issuer does not have to register the issue with the State and report the issue results: these functions are delegated to the stock exchange, significantly shortening the interval between the decision to issue bonds and the start of secondary trading. For the exchange bonds to be admitted to a stock exchange, the issuer must comply with a number of requirements, including the following:

- this issuer's stocks must be included in this stock exchange's quotation lists;
- the issuer must have existed for at least 3 years and must have properly approved annual financial statements for at least 2 complete fiscal years;
- the bonds' maturity date cannot exceed one year after the offering date.

In the first half of 2008, five exchange bonds issues of two issuers were traded at MICEX; the total transactions volume (including repurchase transactions) amounted to 21.86 billion roubles.

¹⁸ Including repurchase transactions.

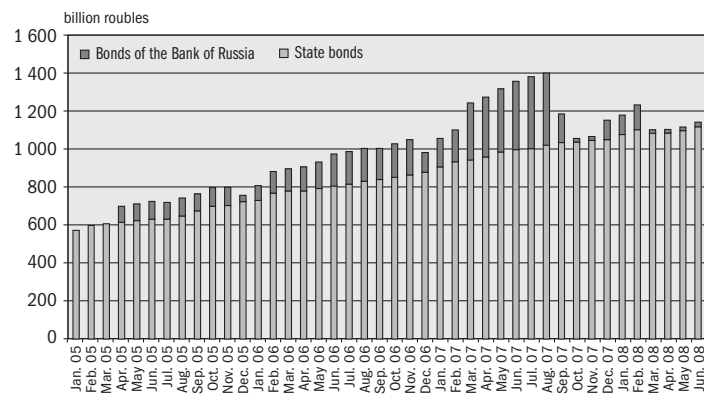
¹⁹ As estimated by GK "Region".

1.3. State, subfederal and municipal bonds, bonds of the Bank of Russia

The first State bonds of the Russian Federation were issued in 1991. Rapid development of the domestic exchange market transactions with these bonds (GKO, i.e. State Credit Bonds, and OFZ, i.e. Federal Loan Bonds) took place in 1993–1998, but was interrupted by the default that occurred on August 17, 1998, and since then this market has not recovered neither the volumes nor the role in the financial system that it held before the crisis. The bonds of the Bank of Russia, issued since 2005, formally are not State securities, even though they have the same reliability level. They are short-term securities and are used by commercial banks for liquidity management; the other investors are not allowed to acquire them.

The trading volume of the federal bonds market has been increasing over the last years (see Fig. 6).

Figure 6. The volume of the domestic debt market (at nominal value).



Source CBONDS

According to the CBONDS agency, the volume of the State bonds circulating in the domestic market as of the end of 1H08 amounted to 1115.5 billion rbl. at par, an increase by 12% compared to the same period of 2007 (for comparison, in 2006, the increase was 21.4%, and in 2007, 19.6%). At the same time, the volume of the secondary market and the liquidity of State bonds are small compared to those of the corporate bonds market (see Figures 4 and 5). The state securities market is organized at MICEX. Table 12 contains data on state bonds market turnover.

Table 12. Transaction volumes of state bonds.

Period	Units	2005	2006	2007	2008		1H08
		Total	Total	Total	Q1	Q2	Total
Turnover	billion roubles	166,16	335,01	491,45	71,60	51,67	123,27

Source: CBONDS.

Having compared Tables 8 and 12, we see that despite of commensurability of the par value offering volumes, the turnover of the State securities is almost ten times less than that of the corporate bonds, and the turnover rate is, accordingly, much lower. The interest towards the state bonds market is falling.

While in 2006 there was a 101% increase in the transaction volume, in 2007 it halved to 46.7%. In the first half of 2008 the turnover drops 23% compared to the same period in 2007.

Volumes of issues of these bonds by the Bank of Russia were growing very fast in 2005 and 2006, except for the traditional December slump; for example, in the year 2006 the volume grew by 35.2%. However, the tide turned in 2007-2008 (see Figure 6). According to CBONDS, the total amount of circulating bonds issued by the Bank of Russia as of the beginning of 2007 was 104.2 billion rbl., and as of the end of the year, 102.9 billion rbl. However, in October and November it dropped to 20 billion rbl. In February 2008 this volume amounted to 131 billion roubles, and then it dropped abruptly and stayed at around 20 billion roubles till the end of the first half of the year.

Subfederal and municipal bonds have smaller volumes of issue than state and corporate bonds, and they do not show any significant change tendencies (see Figure 3). According to the CBONDS agency, the volume of the subfederal and municipal bonds circulating in the domestic market as of the end of 1H08 amounted to 265.1 billion rbl. at par, a 24% increase compared to the same period of 2007 (for comparison, in 2006, the increase was 17.8%, and in 2007, 16.2%).

Total volume of transactions with subfederal and municipal bonds for years 2005-2007 is shown in Table 13.

Table 13. Subfederal and municipal bonds transactions volume.

Period	Units	2005 Total	2006 Total	2007 Total	2008		1H08 Total
					Q1	Q1	
Total turnover	billion roubles	890,1	682,8	663,54	110,08	149,19	259,27
The share of exchange transactions in the total turnover	%	70,00	79,90	83,18	86,13	92,27	89,93

Source: CBONDS.

Therefore, as follows from Table 13, the total subfederal and municipal bonds transaction volume is decreasing from one year to another. It dropped 23% in 2006 and 3% in 2007. In the first half of 2008 the turnover drops 28% compared to the same period in 2007.

Exchange trade for subfederal and municipal bonds is effected at MICEX and RTS. Table 14 contains summary data on subfederal and municipal bonds (including stock exchange bonds) offered at Russian stock exchanges, and Table 15 contains data on trade for these bonds at MICEX.

Table 14. Organized market of subfederal and municipal bonds.

	MICEX				RTS			
	2005	2006	2007	1H08	2005	2006	2007	1H08
The number of bond issuers	41	50	59	52	2	14	16	15
The number of bond issues	90	105	116	115	16	35	30	27
including these in the quotation lists (issuers/issues)	22/53	22/49	27/49	28/51	1/1	0/0	0/0	0/0

Sources: MICEX, RTS.

These bonds have rather high liquidity despite of the small volumes of circulation. Comparative analysis of Tables 8, 12 and 13 shows that subfederal and municipal bonds, having essentially smaller volumes of issue than corporate bonds, in 2005-2008 had a higher turnover rate than the State securities.

The values and trends of the subfederal and municipal bonds turnover rate (see Figure 5) are rather similar to these of the corporate bonds. The share of the subfederal and municipal repurchase transactions in the total exchange turnover has significantly changed over the last years (see Table 10): the increase over 2005 was 2.5 to 3 times, sometimes exceeding 85%. Thus, the organized subfederal and municipal bonds market, like the stock and corporate bonds markets, becomes more and more like a secured credit money market.

Table 15. MICEX subfederal and municipal bonds transactions volume²⁰.

Period		Units	2005	2006	2007	2008		1H08
			Total	Total	Total	Q1	Q2	Total
Subfederal bonds	without repurchase transactions	billion	556,7	520,1	496,8	87,0	98,6	185,6
	with repurchase transactions	roubles	773,2	1 301,9	2 478,2	537,7	707,1	1 244,9
<i>Share of repurchase transactions to the total volume of RF constituent entities bond transactions</i>		%	28,00	60,05	79,95	83,82	86,05	85,09
Municipal bonds	without repurchase transactions	billion	24,0	24,0	28,3	4,5	3,4	7,9
	with repurchase transactions	roubles	35,0	41,3	84,6	16,3	13,3	29,6
<i>Share of repurchase transactions to the total volume of municipal bonds transactions</i>		%	31,52	42,05	66,54	72,22	74,60	73,29

Source: MICEX.

1.4. Investment units

The secondary market of investment units has completed its development and has a tendency to grow. Investment units are traded at MICEX and RTS. Table 16 contains summary data on IUFs offered at Russian stock exchanges, and Table 17 contains data on the trading volumes of investment units.

Table 16. Organized investment units stock exchange market.

	MICEX				RTS			
	2005	2006	2007	1H08	2005	2006	2007	1H08
The number of management companies	33	48	88	97	6	10	15	20
The number of UIFs	69	114	219	279	18	22	38	43
including these in the quotation lists (management companies/UIFs)	3/4	4/4	20/30	24/43	1/1	3/3	6/7	6/6

Sources: MICEX, RTS.

The number of UIFs admitted to circulation at stock exchanges experienced significant growth over the last years (more than 60% growth in 2006, more than 90% in 2007). The growth for the first half

²⁰ Including auction mode and negotiated deals mode. Initial offerings are not included.

of 2008 is lower, 10-15% compared to the beginning of the year. Currently around 1/4²¹ of all functioning UIFs are represented at stock exchanges. The exchange turnovers of the investment units grow very fast: they grew 4.7 times in 2006, 3.7 times in 2007, and for the 1st half of 2008 the transaction volume has already reached 77% of the entire previous year. However, not all UIF investment units have high liquidity. The concentration of transactions with investment units is very high: in 2007, top ten most liquid UIFs accounted for more than 80% of the total investment units turnover. In the 1st half of 2008 this share dropped a little, to 78%.

Table 17. Investment units stock exchange transactions volume.

Period	Units	2005	2006	2007	2008		1H08
		Total	Total	Total	Q1	Q2	Total
MICEX	million dollars	43,8	186,0	790,0	248,0	382,0	630,0
RTS	million dollars	1,7	30,9	27,9	N/A	N/A	N/A
TOTAL	million dollars	45,5	216,9	817,9	248,0	382,0	630,0

Sources: MICEX, RTS, NLMC.

1.5. Futures and options on securities and market indices

Currently the market of derivative instruments that use underlying assets such as securities and stocks indices is concentrated at the derivative market, FORTS of RTS. Besides derivatives based on securities and stocks indices, this market also transactions in contracts for gold, currency, oil and so forth; the share of transactions for these contracts, however, is relatively insignificant, in spite of its growth trend, and amounts to less than 4–7%, depending on the type of volume indicator.

The instrumental base of the derivative market becomes increasingly complex. In 2006, FORTS market offered 18 types of derivatives (12 futures and 6 options) based on securities and stocks indices. By the end of 2007, their number increased to 53 (36 futures and 17 options). In 1H08 it reached 85 (44 futures and 41 option). Therefore, the number of types of derivatives based on securities and stocks indices is growing over the last years (in 2007, the increase was 194%, and in 1H08, 60%.) Characteristically, while in 2006–2007 the ratio of futures and options was, on the average, 65 to 35%, in the first half of 2008 the options share increased: 52 to 48%. In mid-2007 MICEX introduced its the first index derivative, a futures contract based on the MICEX index. The transaction volumes for this instrument, however, are still low: it amounted to 1.76 billion roubles by the end of 2007 and 0.72 billion roubles in the first half of 2008.

Tables 18 and 19 summarize the data on FORTS market for index derivatives for 2005-2008.

As follows from Table 18, the FORTS market has experienced fast growth in 2006: the total transaction volume has increased almost fourfold, and the number of transactions grew by 164%. In the year 2007 the growth continued: the total volume of derivatives instruments trade (in monetary value) has increased by 170%, and the number of concluded transactions grew by 130%. In the first half of 2008 the growth did not change (compared to the same period of 2007, the trade volume in monetary value showed a 180% increase, and the number of transactions – 159% increase). The ratio of futures to options stayed the same as in 2007: futures account for 82% of transaction volume and 97% of the transactions.

²¹ As estimated by NLMC.

Among all the derivative contracts, the interest towards stock index contracts is growing steadily. In 2007, the transaction volume of these contracts amounted to 60% of monetary value, and in 1H08 this share increased to 77%.

Table 18. Contracts on securities and stock indices trading
futures and options on securities and stock indices.

Period	2005	2006	2007	2008		1H08
	Total	Total	Total	Q1	Q2	Total
FUTURES CONTRACTS						
Volume of trade, billion rbl.	607,8	2397,1	6052,4	2553,8	2710,9	5264,7
<i>of them, on index</i>	119,8	752,0	3587,1	2048,3	2199,1	4247,4
<i>of them, on stocks</i>	471,0	1 569,6	2389,2	501,8	510,9	1012,7
<i>of them, on bonds</i>	9,0	13,7	29,3	3,7	0,9	4,6
Trading volume, million cont.	46,0	78,9	114,6	41,9	44,9	86,7
<i>of them, on index</i>	2,3	9,0	34,7	20,7	20,5	41,2
<i>в т.ч. на акции</i>	42,6	66,3	75,5	20,8	24,3	45,1
<i>of them, on bonds</i>	0,8	1,3	2,8	0,4	0,1	0,5
Number of transactions, million pcs.	1,8	4,9	11,3	5,3	5,5	10,8
<i>of them, on index</i>	0,1	0,7	4,3	2,9	3,1	6,0
<i>of them, on stocks</i>	1,7	4,1	7,0	2,4	2,4	4,8
<i>of them, on bonds</i>	0,0	0,0	0,0	0,0	0,0	0,0
OPTION CONTRACTS						
Volume of trade, billion rbl.	79,3	311,4	1 300,2	513,89	605,50	1 119,4
<i>of them, on index</i>	2,6	84,3	758,7	341,2	312,6	653,9
<i>of them, on stocks</i>	76,6	226,9	541,4	172,7	292,9	465,5
<i>of them, on bonds</i>	–	–	0,0	–	–	0,0
Trading volume, million cont.	7,3	10,7	25,0	10,9	17,3	28,2
<i>of them, on index</i>	0,0	1,0	7,1	3,4	3,0	6,4
<i>of them, on stocks</i>	7,2	9,7	17,8	7,5	14,3	21,8
<i>of them, on bonds</i>	–	–	0,0	–	–	0,0
Number of transactions, million pcs.	0,1	0,2	0,3	0,1	0,2	0,3
<i>of them, on index</i>	0,0	0,0	0,1	0,1	0,1	0,2
<i>of them, on stocks</i>	0,1	0,1	0,2	0,1	0,1	0,1
<i>of them, on bonds</i>	–	–	0,0	–	–	0,0
TOTAL						
Volume of trade, billion rbl.	687,1	2 708,5	7 352,6	3 067,7	3 316,4	6 384,1
Trading volume, million cont.	53,3	89,6	139,6	52,7	62,2	114,9
Number of transactions, million pcs.	1,9	5,0	11,6	5,4	5,7	11,1

Source: RTS.

The proportion of security- and index-based derivatives market to the volume of stock spot market not including repurchase transactions (see Table 6) is permanently growing: at the end of 2005, it was 15.4%, at the end of 2006, 21.2%, in 2007 it reached 46.3% and by the end of 1H08 it reached 79.3%.

The volume of open positions and their distribution over different types of instruments has changed significantly (see Table 19). Thus, in 2005 futures accounted for 64% in the total volume of open positions, but later their ratio started to decrease: 54% in 2006, 38% in 2007, 23% in 1H08. Therefore, options lately become increasingly more popular in market risk management. The ratio of open positions and transaction volumes for futures and options differs significantly. While for futures

this ratio is in the range of 2-5%, for options (according to 2007-2008 data) it stays at around 35-55% during the first half of the year and drops to 15% by the end of the year.

Table 19. Open positions on securities and stock indices future contracts at FORTS derivative market.

Period	2005	2006	2007	2008	
				Q1	Q2
FUTURES CONTRACTS					
Average volume of open positions, billion rbl.	11,5	34,6	74,7	57,2	60,7
<i>of them, on index</i>	0,6	7,9	33,5	26,9	28,6
<i>of them, on stocks</i>	9,5	20,9	38,9	29,6	31,7
<i>of them, on bonds</i>	0,7	1,6	2,3	0,6	0,5
Average volume of open positions, million cont.	1,0	1,2	1,9	1,9	2,2
<i>of them, on index</i>	0,0	0,1	0,3	0,3	0,3
<i>of them, on stocks</i>	0,9	0,9	1,3	1,5	1,8
<i>of them, on bonds</i>	0,1	0,1	0,2	0,1	0,0
OPTION CONTRACTS					
Average volume of open positions, billion rbl.	6,5	30,0	117,3	154,6	207,9
<i>of them, on index</i>	0,2	9,0	71,7	103,0	122,0
<i>of them, on stocks</i>	6,3	20,9	45,5	51,6	86,0
<i>of them, on bonds</i>	–	–	–	–	–
Average volume of open positions, million cont.	0,6	1,0	2,3	3,1	5,3
<i>of them, on index</i>	0,6	0,9	0,7	1,0	1,3
<i>of them, on stocks</i>	0,0	0,1	1,6	2,1	4,0
<i>of them, on bonds</i>	–	–	–	–	–
TOTAL					
Average volume of open positions, billion rbl.	18,0	64,6	191,9	211,8	268,6
Open positions volume over the year, million cont.	1,6	2,2	4,2	5,0	7,5

Source: RTS.

Night trade session was introduced at FORTS derivative market in 2008 (see section 2.3b for details). This mode was introduced in the end of May, so the accumulated statistical data is still insufficient for detailed analysis. We can say, however, that the median volume of a night session deal is 5% of the total daily trade volume for futures; on some outlier days it can reach up to 14.7%. For the options, median value is 2% with outliers up to 14.2%.

1.6. Stock indices

At present Russian and international organizations, such as stock exchanges, information agencies, investment banks, brokerage companies etc. calculate dozens of various indices of the Russian capital market. The most recognized of them are: for the stock market – RTS Index, MICEX Index, MSCI Russia Index; for the bond market – Corporate bonds Index RUX-Cbonds, Municipal bonds Index Cbonds-Muni, MICEX Corporate bonds Index, EMBI+ Russia Index; for the collective investments market – RUIF Indices calculated by National Rating Agency.

Traditionally, however, the most popular and quoted indices are these calculated by RTS and MICEX.

RTS Index is being calculated since 1995. It is a composite index currently based on 50 stocks of the most capitalized and liquid issuers. The list of stocks for indices calculation is revised once in three months.

Besides the main RTS Index, RTS Stock Exchange calculates RTS-2, an index of the second tier companies, since 2003.

Besides, the industry indices are also calculated since 2005-2007:

1. RTS – Oil and gas (RTSog) index
2. RTS – Metals and mining (RTSmm)
3. RTS – Telecommunications (RTStl)
4. RTS – Industry (RTSin)
5. RTS – Consumer goods and retail trade (RTScr)
6. RTS – Power Industry (RTSeu)
7. RTS – Finances (RTSfn).

The MICEX Index is calculated since 1997. Originally its basis included 21 most liquid stocks traded at the basic trade sessions of MICEX. In the first quarter of 2007 the basis for calculation of this index was extended to 30 stocks of the issuers representing main sectors of economy. The index basket is updated not more than once in a quarter based upon expert estimates of the Index committee.

Besides, MICEX also calculates the industry and capitalization indices since 2005-2007:

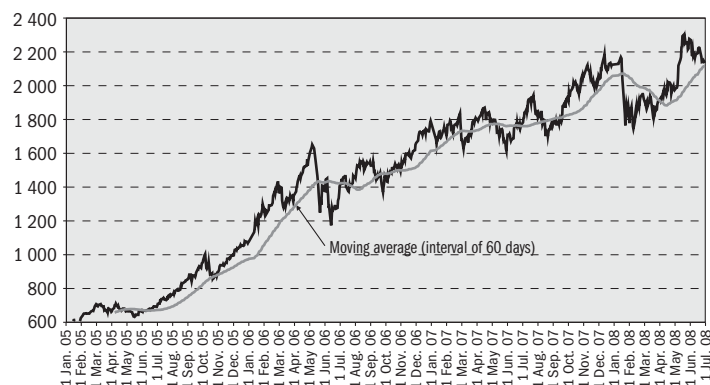
1. MICEX O&G – oil and gas companies stock index;
2. MICEX PWR – power industry companies stock index;
3. MICEX TLC – telecommunication companies stock index;
4. MICEX M&M – metallurgical and mining companies stock index;
5. MICEX MNF – mechanical industry companies stock index.
6. MICEX LC – high capitalization companies stock index;
7. MICEX MC – standard capitalization companies stock index;
8. MICEX SC – base capitalization companies stock index.

Among industry indices maintained by various stock exchanges, the similarity of calculation base (75%-80% of coincidence) can be observed for the oil and gas industry indices (RTSog, MICEX O&G), telecommunications industry (RTStl, MICEX TLC), power industry (RTSeu, MICEX PWR), as well as metallurgy and mining (RTSmm, MICEX M&M). RTSin and MICEX MNF indices demonstrate somewhat lower similarity.

Figures 7 and 8 represent charts of RTS and MICEX indices, respectively.

Table 20²² shows profitability data calculated according to RTS and MICEX indices for the last years.

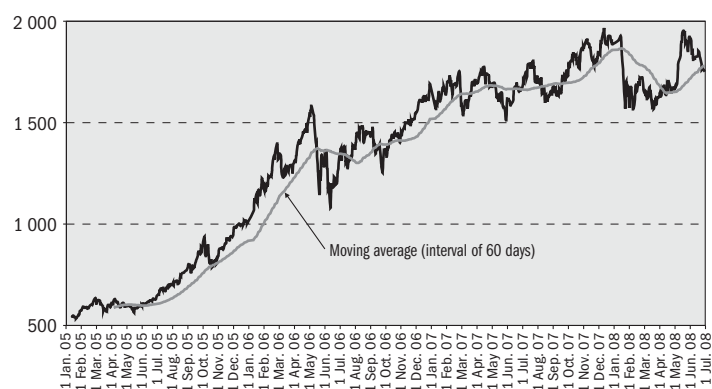
Figure 7. RTS index



Source RTS.

²² The profitability was calculated upon the range from the last trading day of the previous year to the last trading day of the appraised year based on the length of 365 days.

Figure 8. MICEX index



Source MICEX.

Table 20. Stock indices profitability (% per annum).

	2005	2006	2007	1H08
COMPOSITE INDICES				
RTS Index	83,52	70,94	19,23	1,11
MICEX index	83,08	67,69	11,57	-14,12
RTS2 Index	69,32	42,27	43,17	-3,95
INDUSTRY INDICES				
<i>Oil and Gas industry</i>				
RTSog	86,78	50,80	1,05	16,41
MICEX O&G	91,95	47,95	-3,57	8,31
<i>Telecom</i>				
RTStl	40,78	81,47	28,13	-33,04
MICEX TLC	39,10	65,98	14,56	-42,26
<i>Metallurgy and mining</i>				
RTSmm	53,18	52,42	54,00	23,40
MICEX M&M	74,60	51,69	42,61	15,79
<i>Power industry</i>				
RTSeu			31,96	-48,78
MICEX PWR	38,68	134,51	7,87	-48,34
<i>Industry</i>				
RTSin	40,50	73,76	66,83	3,85
MICEX MNF	28,90	69,62	60,57	-4,79
<i>Consumer goods</i>				
RTScr	92,51	51,24	29,31	-18,19
<i>Finances</i>				
RTSfn			14,30	-31,45
CAPITALIZATION INDICES				
MICEX LC			9,89	-12,11
MICEX MC			15,64	-15,91
MICEX SC			29,17	-19,33

Sources: MICEX, RTS.

As follows from these data, RTS and MICEX indices show very similar behavior. Significant growth of these indices which began in 2005, started slowing down gradually in 2007 and stopped in 2008, turning into decrease. In the first half of 2008 the indices demonstrated two opposite behaviour phases that defined the results of this period. The first was the tumble for 7 trade days in a row (January 15 to January 23; RTS Index showed a 19.2% drop, and MICEX Index a 18.7% drop). The biggest daily drop was witnessed on January 21 (both RTS Index and MICEX Index dropped 7.4%). Then, on January 24th, the maximum positive growth of the period was achieved (5.2% for RTS Index and 5.8% for MICEX Index).

The second phase was the growth phase. RTS Index demonstrated constant growth during 11 trade days, from May 4th to May 19, resulting in 17.2% growth. For MICEX Index this phase was shorter, from May 6th to May 14th, with 12.8% growth.

Between these two phases, there was a long sideways trend with high volatility.

The end of the 1H08 witnessed a downtrend for the composite indices.

All the indices, except oil and gas, showed lower profitability in 2008 than in 2007. However, we should take into account that oil and gas industry indices demonstrated the biggest slump of all in 2007. While in 2007, in spite of an evident slowdown, most indices nevertheless demonstrated positive profitability, in the first half of 2008 the majority of indices showed negative profitability. It amounted to -48% in power industry, -42% in telecommunications and -31% in financial industry. The most stable results over the last three and a half years were demonstrated by the indices related to metallurgy and mining (RTSmm, MICEX M&M).

As to the capitalization indices, their profitability was, independently of the capitalization level, negative in the first half of 2008.

The most stable results over the last three and a half years were demonstrated by the indices related to metallurgy and mining (RTSmm, MICEX M&M).

2. Institutional structure

2.1. Issuers

In Russia there are no precise statistics relating to securities issuers. Any joint stock company is an issuer because it issues and places stocks at the moment of its incorporation (and is required to register them). A limited liability company, and, in some cases, a non-profit organization can also be a bonds issuer. The CJSC SKRIN database, as of the end of 2007, contained entries on 86,591 issuers of stocks and bonds. By the end of 1H08 this number grew to 87,139. Summarized data on the numbers of issuers at organized markets are shown in Table 21.

Table 21. Issuers at organized stock exchange market.

	MICEX				RTS			
	2005	2006	2007	1H08	2005	2006	2007	1H08
The number of issuers (stocks and bonds)	385	539	670	592	262	332	354	332
of them, included in the quotation lists	93	127	229	235	46	64	88	91

Sources: MICEX, RTS.

According to current estimates, the stocks of approximately 70 issuers also circulate as depository receipts in foreign stock exchanges.

Therefore, only around 0.7% of all the stocks and bonds issuers are represented at organized market. For example, as follows from Table 22, the number of issuers in the organized market was growing steadily in 2005-2007. In the 1st half of 2008, however, the trend changed, and the number of issuers represented at the stock exchanges dropped 6-11%.

Public offerings

Placement of most stocks traded today at Russian stock exchanges happened during privatization of the 1990s. The first public offering of Russian stocks abroad was in 1996, and the first offering at a domestic stock exchange happened in 2002.

In 2006-2007 the volumes of the public offerings of Russian companies have drastically increased (see Table 22).

Table 22. Public offerings of stocks of Russian companies.

Period	2005	2006	2007	1H08
Volume of offerings (US\$ billion)	4,55	17,98	23,6	1,3
of them, in domestic market (%)	6	36	44	51
Number of companies	13	24	25	5

Sources: "offering.ru/IPO in Russia" project, "Alpha Bank", Ernst&Young.

At the time, Russia was a world leader both by the total offerings volume and by the volumes of capital raised by a single company. It should be noted, however, that this growth was largely caused, not by a large number of new companies entering the market, but by massive placement of stocks of several companies, mostly with the State's participation and support. The largest public offerings at the time were so-called "people's IPO": OJSC "NK Rosneft" (10.4 billion dollars), OJSC "Sberbank" (8.8 billion dollars) and OJSC "VTB Bank" (7.9 billion dollars).

In the first half of 2008 the public offerings of stocks of Russian companies have practically stopped because of the global crisis of this segment of the global financial market. Only one IPO (Globaltrans Investments at LSE, 449.4 million dollars) was performed. Many companies that had previously announced their plans for public offerings have canceled them, deferred them or made a private offering instead.

2.2. Investors

Investors are any individuals or institutions investing funds in securities for the purpose of gaining profit. There is no official systematized data available on the structure and quantitative statistics of the Russian capital market investor base. Nevertheless, lately professional securities market participants, self-regulatory organizations and research groups began working on listing and studying Russian investors.

a) Public

Here, the public includes "market" investors – individuals who have decided to work independently in the capital market and periodically use brokers' or trust managers' services, or are "market" clients of UIFs. The individual holders of stocks received in the course of the voucher privatization, as well as the shareholders of check investment funds, or holders of units in unit investment funds that have emerged as a result of transformation of the check investment funds, do not belong to this category.

There is no complete and authentic statistics on the quantity of the individuals engaged in securities market transactions in Russia. It is possible to create the following, far from complete picture by compiling data from various nonsystematic sources.

Since 2005, MICEX regularly publishes data on the numbers of individuals participating in the trades (hereinafter referred to as "MICEX clients"). We should say that in mid-2007 MICEX has adopted a new, more exact methodology of registering clients with their individual identification attributes (unique clients).

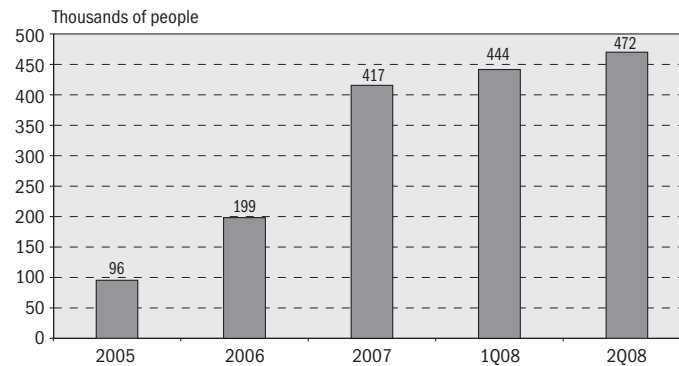
Figure 10 shows data on the quantity of individuals working at MICEX calculated using new methods, starting from 2005.

The number of individual clients at MICEX has increased by 108% in 2006. The estimated growth for 2007 is similar, 109%, however if we exclude the individuals who are OJSC "VTB Bank" IPO participants, the growth is 60%. Starting from the 3rd quarter of 2007, the growth rate of the numbers of individual MICEX clients dropped to 5-7% quarterly. In the first half of 2008 the increase was 28% compared to the same period in 2007.

An important characteristics of private investor base is the number of so called active investors who make at least one deal per month at the stock exchange. Figure 10 presents the available data on the active investors at MICEX.

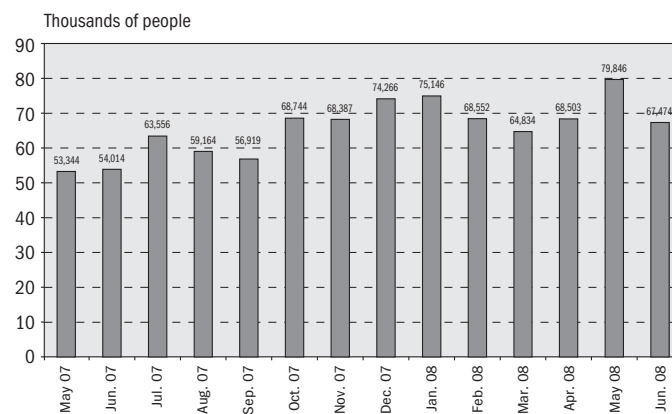
Therefore, as follows from Figure 9 and 10, the active investors – individuals account for 13-14% of MICEX's unique clients. It is remarkable that the number of active MICEX clients is very close to the difference between the total number of client accounts and the number of unique client accounts. This difference corresponds to the segment of client base that, for example, uses more than one broker company's services.

Figure 9. Participation of population in securities market investments (MICEX customers)



Source MICEX.

Figure 10. The number of active MICEX clients.



Source MICEX.

Between May 2007 (when publications of data on the number of active clients started) and the end of 2007 the number of active clients grew by 40%. At the same time, there was a lull in August and September that can be explained both by vacation time and by adverse securities market situation.

As of the end of the first half of 2008 no long-term trend for change in the number of active clients was identified. The median value stabilized at around 68,500 people. There were two growth spurts in January and May, coinciding with the market up- and downtrends.

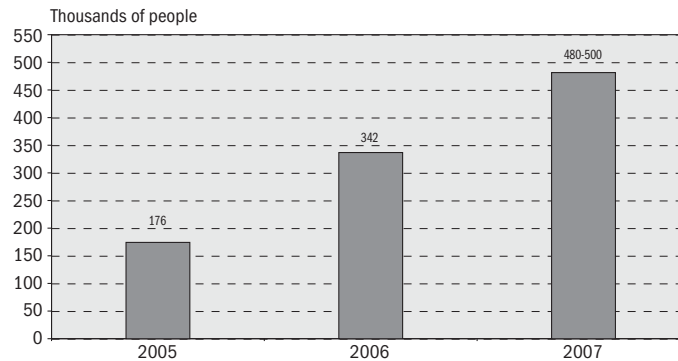
The National League of Management Companies has been estimating the number of accounts that belong to UIF "market" shareholders (see Figure 11) with nonzero accounts, since 2002.

According to these estimates, the number of the UIF unit holders increased by 94% in 2006 and by around 40% in 2007. There is no data for "market" shareholders' numbers available for the first half of 2008.

A new extensive group of private investors appeared in 2006-2007. It consists of the private individuals who participated in the so-called "people's IPO": OJSC "NK Rosneft", OJSC "Sberbank" and OJSC "VTB Bank". According to the data of issuing companies and mass media, the total number of such individuals was approximately 115 thousand at the Rosneft offering, 30 thousand at the OJSC "Sberbank" offering and 131 thousand people at the OJSC "VTB Bank" offering.

Currently, however, these investors, because of the weak investment results of the abovementioned offerings, largely joined other groups – some of them sold the previously purchased stocks, some quitted the "market" investors category and lost their interest towards the securities market.

Figure 11. Participation of the population in securities market investments (UIF customers).



Source NLMC.

b) Investment funds

23 contains summary data on the UIF numbers dynamics over the last three and a half years.

Table 23. Number of investment funds²³.

Period UIF type	2005	2006	2007	2008	
				Q1	Q2
Opened-end	201	299	455	487	486
Interval	59	86	95	101	101
Closed-end	121	234	398	466	468
<i>of this, real estate</i>	73	152	269	335	336
TOTAL	381	619	948	1054	1055

Source: NLMC.

There were 948 functioning UIFs in Russia by the end of 2007, which is 53.2% more than in the beginning of the year. Considering that in 2006 the number of UIFs has increased by 60.7%, it is necessary to note that in 2007 the growth rate of the number of UIFs has somewhat decreased. In the first half of 2008 the number of UIFs remained more or less the same. It does not signify any market trends. The explanation is that in 2008 some amendments to the law "On investment funds" were introduced but not supported by the necessary bylaws, and the registration of new funds was suspended.

Table 24 contains summary data on the UIF net asset value dynamics over the last three and a half years.

²³ Only the funds whose formation is completed are included in the statistics.

Table 24. UIF net asset value dynamics (billion roubles)²⁴.

Period UIF type	2005	2006	2007	2008	
				Q1	Q2
Opened-end	30,8	91,1	134,8	124,2	118,5
Interval	38,7	59,6	43,8	38,6	39,3
Closed-end	163,4	268,1	604,2	634,1	684,6
<i>of this, real estate</i>	24,9	69,0	189,9	223,1	251,8
TOTAL	233,0	418,8	782,8	797,0	842,5
UIF net assets value / GDP (%)	1,08	1,56	2,37	-	-

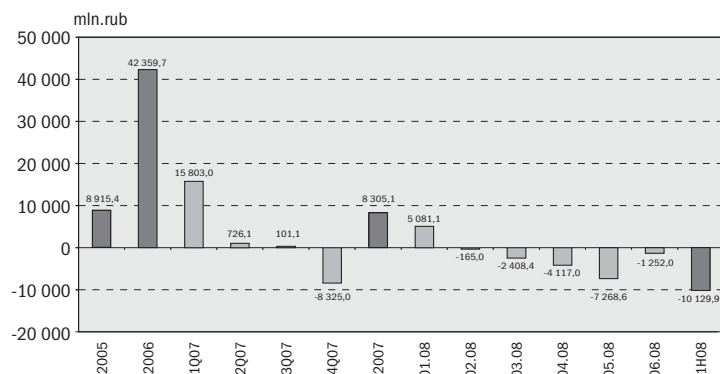
Source: Federal State Statistic Service, NLMC.

The value of the UIFs' net assets as of the end of 2007 was 782.8 billion rbl., which is 87% more than in the beginning of the year. In 2006, the increase was 80%. The value of the UIFs' net assets in the 1st half of 2008 reached 842.5 billion rbl., which is 31.7% more than in the same period of 2007. This increase is mainly explained by growth of the total net value of closed-end UIFs, mainly the real estate funds (the net asset value of the real estate funds increased by 141%).

Simultaneously, for the first time over the last few years the net asset value of opened-end UIFs has decreased (by the end of 1H08, the decrease was 12% compared to the beginning of the year, or 16.3 billion roubles in absolute values). The downtrend for net asset values of interval UIFs has already emerged in early 2007, and in the 1st half of 2008 the decrease was 10%, or 4.5 billion roubles in absolute values.

Besides net asset value, one of the most important UIF characteristics is the volume of net funds raised. These data are most important for the opened-end UIFs that accept requests for investment units issue and redemption daily. Figure 12 shows data on net funds raised by opened-end UIFs.

Figure 12. Volume of raised capital in UIFs.



Source NLMC.

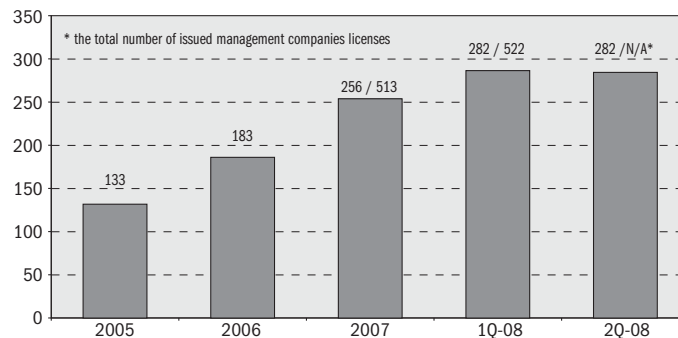
As one may see from Figure 12, over the last three and a half years 2006 was the record-setting year for net funds raised – the volume of net funds raised amounted to 42.4 billion roubles. In 2007 there is a significant cash inflow in the 1st quarter and an outflow in 4th quarter; summarily over the year the volume of the net funds raised amounted to only one fifth of the previous year, 8.3 billion roubles.

²⁴ Only the funds whose formation is completed are included in the statistics.

In the first half of 2008 there was a characteristic cash inflow in January and a steady outflow in February to June; in May, compared to the market's uptrend, this outflow (the purpose of which was probably the fixation of the financial result) was quite significant. As a result, over 6 months of 2008 the balance of net capital raising was negative: -10.1 billion dollars.

A UIF is a property pool and not a legal person. The leading element in UIF structure is its management company. Figure 13 depicts summary data on the quantity of management companies controlling UIFs over the last three and a half years.

Figure 13. The number of the management companies controlling UIFs



Sources: FFMS, NLMC

The number of the management companies controlling UIFs has increased by 36.6% in 2006, and by 39.9% in 2007. Such growth statistics of 2006-2007 were noticeable against the changes in the other aspects of securities market activities and proved that there was a considerable interest towards the collective investments industry. In the first half of 2008 the growth of numbers of management companies controlling UIFs has stopped, especially in the 2nd quarter. This is most likely explained by the fact that no new UIFs were registered. About the half of all the organizations that own management companies licenses are involved in managing UIFs. The rest are engaged only in pension funds assets management and in other projects. There are also some companies that have no activity.

c) Bank-managed mutual funds

Bank-managed mutual funds (BMMF) are an investment product that credit organizations can offer according to the rules established by the Bank of Russia²⁵. A BMMF is a property complex that consists of property placed into trust management by several persons, as well as the property acquired by the trust manager in the course of exercising the trust management. An investor who has invested finances into a BMMF receives a participation certificate that is not a security. The requirements for BMMF's asset composition and structure are less restrictive than the UIF requirements. According to the existing data, around 30 credit organizations are involved in BMMF management. The data on the number of funds and net asset values over the last three and a half years are shown in Table 25.

As one may see from the Table 25, there are significantly fewer BMMFs than UIFs, and they have much lower total net asset value. While in 2006 the BMMF were growing rapidly (their number increased by 44%, and their total net value by 98%), in 2007 the growth was insignificant (1.2 and 1.3% respectively). In the 1st half of 2008 the growth of the BMMF numbers stopped, and their net asset

²⁵ The Bank of Russia instruction of July 02, 1997, "On the Order of Exercising Trust Management Transactions and Accounting for Such Transactions by Credit Organizations in the Russian Federation".

value dropped by 4 billion roubles (around 20%) since the beginning of the year. The summarized data on the number of BMMF investors are not disclosed. Some experts estimate this number at 30,000.

Table 25. Bank-managed mutual funds.

Period	2005	2006	2007	2008	
				Q1	Q2
The number of funds	108	156	174	174	185
<i>of this, roubles</i>	65	97	112	112	118
<i>of this, currency</i>	43	59	62	62	67
Net asset value (billion rbl.)	9,45	18,72	21,08	18,15	17,02

Source: *investfunds.ru*.

d) Private pension funds

According to the FFMS²⁶, 253 organizations had licenses for Non-governmental pension funds as of the end of 2007, and 126 of them were allowed to participate in mandatory pension insurance program. In May 2008, the number of valid private pension licenses dropped to 247, and the number of funds allowed to participate in mandatory pension insurance program grew to 127.

The data on funds' assets related to private pensions and mandatory pension insurance are shown in Table 26.

Table 26. Private pension funds' investment resources (billion roubles).

Period	2005	2006	2007	2008	
				Q1	Q2
Pension reserves	277,34	405,18	472,89	485,06	502,45
Pension savings	2,01	9,96	26,76	42,56	43,07
TOTAL	279,35	415,14	499,65	527,62	545,54
PPF Investment resources/GDP (%)	1,29	1,54	1,51	-	-

Source: *www.investfunds.ru*

As one may see from the Table 26, while over 2006 the PPF pension reserves have experienced 1.5 times growth, in 2007 they increased only slightly, by 16.7%. The pension savings had a spurt of growth in 2006, having increased fivefold, and in 2007 they have increased 2.7 times. In the 1st half of 2008, compared to the same period of 2007, the growth of pension reserves and pension savings was 16.5% and 116% respectively.

e) Pension savings investment

The insured persons, i.e. employees for whom their employers make contributions to the Pension fund of Russia and who therefore have pension savings may transfer their pension savings to a PPF or put them in trust for a management company – either private or state-owned. The first tender among private management companies for the right of participation in the investment of pension savings was held in 2004 and attracted attention of both professional community and interested public.

²⁶ *www.fcs.m.ru*

55 companies were admitted to the management of pension savings assets. Meanwhile, later private companies lost all interest towards this project. The functions of the state management company are currently performed by the OJSC "State corporation "Bank of Foreign Trade Activities and Development" ("Vneshekonombank").

As a state management company, "Vneshekonombank" has a right to invest pension savings only in state securities. The private management companies have wider range of investment opportunities.

The data on the pension savings amounts transferred into PPF are shown in Table 26. Table 27 shows data on the net asset value of the pension savings entrusted to "Vneshekonombank" and private management companies.

Table 27. UIF net asset value for the assets in which Pension savings are invested (billion roubles).

Period	2005	2006	2007	2008	
				Q1	Q2
"Vneshekonombank"	176,35	267,07	362,87	348,68	353,70
Private management companies	5,58	9,37	12,21	12,06	N/A
TOTAL	181,92	276,45	375,08	360,74	N/A
Management companies Investment resources/GDP (%)	0,84	1,03	1,14	-	-

Sources: VEB, Pension fund of Russia, www.investfunds.ru.

As follows from Table 27, the overwhelming majority (about 97%) of the pension savings volume of insured persons transferred for trust management was entrusted to "Vneshekonombank".

In the first half of 2008 the volume of assets entrusted to management companies decreases; this can be explained by redistribution of the pension savings in favor of NPF, as well as by the negative investment results of the management.

f) Commercial banks

Many Russian banks act as professional participants of the securities market as well as investors.

Summary data on the volumes of various types of securities in the assets of credit organizations for the last two and a half years are shown in Table 28²⁷.

Table 28. Various types of securities in the assets of credit organizations (billion roubles).

	2005	2006	2007	2008	
				Q1	Q2
Securities* (total)	1 400,1	1 745,4	2 250,6	2 252,5	2 347,5
including					
Debt instruments*	998,0	1 251,4	1 541,4	1 563,9	1 608,6
Equity securities*	127,1	185,0	316,3	285,5	290,9
A portfolio of controlling shares in daughter and affiliate JSC	64,9	79,8	141,9	144,6	176,9
Discounted promissory notes	210,1	229,2	251,1	258,5	271,1
Repurchase agreement securities (repurchase transactions)	139,3	215,9	304,1	-	-

* Before February 1, 2008, not including repurchase securities.

Source: Bank of Russia

²⁷ Securities purchased on both internal and external markets are counted.

In 2006-2007 the volume of securities in the assets of credit organizations had, on the average, 25% annual growth, however in the first half of 2008 the growth slowed down. The average relative share of securities in the assets of credit organizations (not including repurchase transactions) is around 14 %–16 % and has a tendency to fall.

The average share of debt securities in the composite securities portfolio of credit organizations is around 68%-71% and has a tendency to fall. On the other hand, the share of stocks (not including stocks of affiliated and daughter companies) shows a certain growth, from 9 to 12%. The share of promissory notes dropped from 15 to 12%.

g) Foreign investment funds

Russian capital market attracts foreign investment funds. According to "Interfax Business Service"²⁸, in 2007 and early 2008 about 2000 foreign funds (among those required to disclose the information on their activity) invest into stocks and depository receipts of Russian companies. The volume of investments into Russian companies' securities (both as local stocks and as depository receipts) experiences permanent growth. It reached 22.8 billion dollars in 2005, 49.5 billion dollars in 2006 and 73.4 billion dollars in 2007. At the same time the share of Russian assets is small – on the average, they account for 3.3% of the summary portfolio of the funds. The number of funds that specialize in Russia (i.e. those that have more than 75% Russian assets in their portfolios) is not too high, 25 to 30. By the end of 2007 they accumulated summarily around 7.3 billion dollars. The number of global funds with 10% or less of Russian assets is much higher. By the end of 2007 there was more than 1000 of such funds, and the total volume of Russian assets they owned was 37.5 billion dollars.

In the 1st half of 2008, according to existing estimates, the volume of foreign funds' investments into Russian assets grew by 31²⁹–39³⁰ billion. Summarily, the ratio of foreign funds' investments into Russian assets through Russian and foreign stock exchanges is 25 to 75%.

Besides foreign investment funds required to disclose the information on their activity, foreign hedge funds are investing in Russian assets as well. These funds are much less transparent, thus making it impossible to estimate their investments.

2.3. Professional securities market participants

Summarized, systematized and detailed data on professional participants of the Russian capital market are not published. According to FFMS³¹, the total number of professional market participants dealing in securities on the basis of appropriate licenses amounted to 1711 organizations as of the end of 2006. According to our estimates, about 40% of them are credit organizations.

There was no data on the total number of professional securities market participants for 2007 and the first half of 2008 available at the moment when this report was written.

a) Brokers, dealers, trust managers

Russian legislation regulates three kinds of intermediary activities in the capital market – brokerage activity, dealer activity and equity management activity. The definitions of these kinds of activities are more or less the same as in the developed markets, with the following amendments:

- The brokerage activity as such does not imply control of the customers' rights on securities, therefore brokers wishing to carry out such control should receive a separate license on depository activity;

²⁸ IPO in Russia: pro and contra. "Interfax Business Service" LLC, July 2008.

²⁹ As estimated by "Interfax Business Service".

³⁰ FFMS annual report, 2006.

³¹ FFMS annual report, 2006.

- The dealer activity includes only sale and purchase of securities accompanied by public announcement of the bid and/or sale prices; therefore the companies and persons who regularly deal in securities but do not announce the prices, including even those publicly offering to purchase or sell securities, are exempt from this regulation;
- Securities trust management formally differs from trust management of UIF and private pension funds; two different types of licenses exist for these similar kinds of activity.

The data on the numbers of valid licenses for professional brokers are presented in Table 29.

Table 29. Licenses for professional brokers.

Activity type	2005	2006	2007	1H08
Brokerage	1 379	1 433	1 445	1 488
Dealer activity	1 398	1 394	1 422	1 480
Securities management	1 022	1 100	1 169	1 269

Source: The FFMS of Russia.

As one may see from Table 29, over the last three years the distribution of professional market participants is more or less the same, and their numbers have a small uptrend. Please note that this is the number of issued licenses, but not the number of organizations that work as brokers in the capital market. Most professional securities market participants have three or four licenses.

The stricter requirements for the professional securities market participants' own capital, introduced in the beginning of 2008, have not so far affected the list of professional securities market participants and did not lead to reduction in their numbers, mergers or acquisitions.

In the first half of 2008 the number of issued licenses for securities trust management grew by 100. Considering the slowdown of the growth rates of the number of management companies (see Figure 13) this may be a reaction to the temporary limitations in UIF registration, as the trust management services were still in demand.

b) Trade and settlement infrastructure

The professional securities market participants that constitute the trade and settlement infrastructure of the Russian capital market conduct the following activities:

- organizing trade in the capital market (including stock exchanges);
- clearing activity;
- depositary activity as settlement depositaries.

Besides, the nonbanking financial entities engaged in settlement operation are also a part of this infrastructure.

According to FFMS data, as of the end of 1H08 there were 9 organizations with trade organizers' or stock exchange licenses; 1 organization had its stock exchange license suspended till the end of 2008. 12 organizations had clearing house licenses: two of them obtained these licenses in 2007 and one in 2008.

However, due to market competition and external integration processes two de-facto leading infrastructural centers, MICEX Group and RTS Group, were formed, that actually constitute the organized market for trading in securities and derivatives in today's Russia.

The MICEX Group is an integrated trade and settlement infrastructure including, among other organizations:

- CJSC "Moscow Interbank Currency Exchange";
- CJSC "MICEX Stock Exchange";
- Noncommercial partnership "National Depositary Center";
- Nonbanking credit company "MICEX Settlement House" (CJSC);
- CJSC JointStock Commercial Bank "National Clearing Centre".

In June 2008 a specialized company, CJSC "MICEX – Information technologies" was founded within MICEX Group. The company specializes in development and support of software and technical solutions for connecting participants to the MICEX trading system.

The **stock market of MICEX** (where the trade is organized by CJSC «MICEX Stock Exchange») functions on the basis of "order-driven market" principle where the transaction is made automatically if there are corresponding anonymous bids. Transactions are carried out on the "delivery versus payment" principle with 100 % preliminary assets deposit. Transactions are executed on the date of their conclusion (T+0).

In the negotiated transactions mode the traders have an opportunity to quote securities by making nonaddressed bids (invitations to offer for all traders) and to make a transaction on bilateral (not anonymous) principle using corresponding addressed bids (an offer for a deal from one trader to another). At that, the traders define the appropriate date of fulfillment of their obligations ranging from the current business day (T+0) to 30 calendar days after the transaction (T+30). This mode of trade allows the traders to make transactions either with complete control of backing or without the control of backing.

Clearing on MICEX Setock Exchange transactions is carried out by CJSC MICEX. The settlements of the net obligations of traders on their transactions are effected based on settlement documents issued by CJSC MICEX as a clearing centre, in "MICEX Settlement House" (settlement organization on monetary assets) and in NP "NDC" (settlement depository for securities). In March 2008 a new service was introduced that allows to settle transactions and fulfill obligations on transactions made earlier by simple clearing, using the "delivery versus payment" principle, during the business day and not upon its end.

A Sector of innovative and growing companies (IGC) was formed within the MICEX Group in 2007. Besides, a futures market started its activities, offering a settlement future based on stock index.

The summary of MICEX Group trade in the non-state securities in 2005-2008 are shown in Table 30³² both in roubles and in foreign currency equivalent.

Table 30. MICEX trade results.

Period	2005	2006	2007	2008		1H08 Total
	Total	Total	Total	Q1	Q2	
Trade volume (billion dollars)	225,6	754,9	1 708,9	516,2	618,0	1 134,2
Trade volume (billion roubles)	6 400	20 380	43 500	12 500	14 650	27 150

Source: MICEX.

The RTS Group is an integrated trade and settlement infrastructure including, among other organizations:

- Noncommercial partnership "Russian Trading System Stock exchange";
- OJSC "Russian Trading System Stock exchange";
- Noncommercial partnership "Saint Petersburg Stock exchange";
- CJSC "RTS Clearing Centre";
- Nonbanking credit organization "RTS Clearing house" (LLC);
- CJSC "Depository and Clearing Company".

The RTS Group supports several trading modes:

- Classical market
- Exchange market
- FORTS market of futures and options.

³² Including transactions with stocks, corporate, subfederal and municipal bonds, investments units, including repurchase transactions.

The trade is organized by OJSC "SE RTS". NP "Saint Petersburg Stock exchange" trades the stocks of OJSC "Gazprom".

Within **RTS Classical market** two models of trade are used:

- Classical market with nonanonymous trade: the transactions are based on non-anonymous quotations ("quote-driven market"), there is no preliminary assets deposit; the quotations are made in US dollars and it is possible to choose the settlement date (from T+0 to T+30), the method of settlement ("delivery versus payment" or free delivery), the currency of settlement (roubles or foreign currency). Neither clearing centre nor settlement depository are used here. Money settlements in "delivery versus payment" mode are effected through NFE "RTS Clearing house" or J.P Morgan Chase Bank, and the settlements in free delivery mode are effected through any bank.
- Classical market with anonymous trade: this means anonymous auctioning of bids (order-driven market), partial preliminary deposit of assets; the method of settlement is "delivery versus payment" on T+4 basis; the quotations and settlements are made in US dollars. The clearing centre used is NP "SE RTS", the settlement depository is CJSC "DCC", the settlement credit institutions – NFE "RTS Clearing house" or J.P Morgan Chase Bank.

RTS Exchange market works on the following principles: anonymous bids auction (order-driven market), 100% preliminary assets deposit; the settlement method is "delivery versus payment" on T+0 basis, the quotations and settlements are made in roubles. The clearing centre used is NP "SE RTS", the settlement depository is CJSC "DCC", and the settlement financial organization is NCO "RTS Clearing house".

In September 2007, a technology of "central counterpart for transactions" was launched at the stock market, where NP "SE RTS" functions as a counterpart for all the transactions. In June 2008, the netting technology for stock market settlements in the mode of "central counterpart for transactions" was introduced.

In May 2008 RTS Board of Directors made a decision to transfer the securities clearing from NP "SE RTS" to OJSC "RTS Clearing Center" effective on September 1, 2008.

The **FORTS derivative market** is based on anonymous bids auctioning (order-driven market). Settlements and delivery are effected after the end of term of the contract circulation. Quotations and settlements are made in roubles. The clearing centre is OJSC "RTS Clearing Center", the settlement depository is CJSC "DCC", and the settlement financial organization is NFE "RTS Clearing house". Since September 2007, the intermediate clearing started at the FORTS market (14:00-14:03).

Night trade session was introduced at FORTS derivative market in May 2008. The main session ends at 5.45PM, after which the clearing session is held. The night session is on from 6PM to 11.50PM; the settlements for the session transactions are effected at 2PM on the next day.

Besides within RTS there is an indicative quotations system, RTS Board, based upon the following principles: displaying indicative quotations on securities not admitted to trade at RTS stock exchange; no preliminary securities and money deposits required; the quotations are made in US dollars; it is possible to choose the settlement date (from T+0 to T+30), the method of settlement (delivery versus payment or free delivery), the currency of settlement (roubles or foreign currency). Neither clearing centre nor settlement depository are used here. Money settlements in "delivery versus payment" mode are effected through NFE "RTS Clearing house" or J.P Morgan Chase Bank, and the settlements in free delivery mode are effected through any bank.

A special segment, RTS START, was created within RTS Group in 2007 for the companies with small and medium capitalizations.

The summary results of RTS Group trade at different markets in 2005-2008 are shown in Table 31³³.

³³ Including transactions with stocks, corporate, subfederal and municipal bonds, investments units, including repurchase transactions. For FORTS derivative market, the futures and options deals for all types of underlying assets were included.

Table 31. RTS trade results

Period		2005	2006	2007	2008		1H08 Total
		Total	Total	Total	Q1	Q2	
RTS classical market							
Trade volume	billion dollars	7,7	16,1	14,6	3,6	3,1	6,7
RTS exchange market							
Trade volume	billion roubles	82,0	27,3	23,5	4,9	7,4	12,3
SE SPB exchange market							
Trade volume	billion roubles	936,8	1 205,91	71,2	21,1	18,0	39,1
FORTS derivatives market							
Trade volume	billion roubles	687,1	2 708,5	7 531,2	3 195,7	3 453,7	6 649,4
RTS Board							
Trade volume	million dollars	324,0	544,8	751,9	199,1	141,2	340,2

Source: RTS.

According to the Regulation for information disclosure³⁴ the stock exchanges collect information on over-the-counter transactions with securities included in the stock exchanges' quotation lists, provided that the fulfillment of obligations under the deal includes transfer of ownership for the security. In the first half of 2008 the total volume of over-the-counter transactions reported through MICEX and RTS was around 3.7 trillion roubles.

c) Registration system

There are two alternative methods to register rights on securities in the Russian capital market: on depo accounts with a depository and on personal accounts in the register keeping system. Both methods have equal legal weight. Depositories, registrars and issuers who keep a register of their shareholders by themselves, together constitute the capital market registration system. Depository and registry activities are subject to licensing.

Depositories render services of registering and certifying rights on securities, registering and certifying transfer of securities, as well as custody of securities (if issued in documentary form). A depository carries out its activity on the basis of agreement with the owner of securities or the person having other rights on securities (depository agreement).

In Russia depositories are divided into settlement and custodial as it is generally accepted in the world practice. Settlement depositories are those that make settlements with securities upon the results of clearing and conduct all operations on capital market participants' custody accounts for executing transactions made through trade organizers. All other depositories are custodial depositories.

A registrar is a professional participant of securities market who carries out activities related to keeping a register of the securities owners (data collection, recording, processing, storage and provision of data that constitute the system of maintaining the security owners register). The registrar works upon an agreement with the security issuer. The individuals who open accounts in the register do not conclude an agreement with the registrar. An issuer with 50 or fewer shareholders can keep the register by himself or have an agreement with a registrar. If the number of the shareholders exceeds 50, the issuer is required to delegate the register keeping to a registrar, even though the issuer is still responsible for the register-keeping.

The data on the numbers of valid licenses for depositories and registrars are presented in Table 32.

³⁴ The FFMS Order of June 22, 2006 No. 0667/pz-n «On approval of regulations on disclosing information on transactions».

Table 32. Licenses for depositaries and registrars

Activity type	2005	2006	2007	1H08
Depositary	743	831	787	800
Registry	82	73	65	60

Source: *The FFMS of Russia*

Therefore, as follows from Table 32, over the last three years the number of depositary licenses was subject to increases and decreases; the number of registrars, however, has a pronounced downtrend.

3. Legislative base and regulation

The legislative base regulating capital markets in the Russian Federation is mainly developed by now. It comprises several dedicated laws ("On Securities Market", "On protection of rights and legitimate interests of investors in the securities market", "On mortgage securities") which define general rules for the capital market, and by numerous bylaws (predominantly decrees of the Government of the Russian Federation and internal orders of the FFMS) establishing special rules and norms.

The functioning of particular institutions is regulated by special laws: "On investment funds", "On non-state pension funds", "On investment of assets for financing the savings part of labor pension", "On savings and mortgage system of military men's housing" which are also accompanied by numerous bylaws.

It should be noted that in December 2007 the federal law "On updates to the Federal Law "On investment funds" and several legislative acts of the Russian Federation" introduced important changes into regulating the investment funds' activities in Russian Federation, including these directed at regulating the investment funds' activities for qualified investors; at the same time, the concept of a "qualified investor" was introduced into the securities market legislation. These updates are in agreement with the international tendencies of regulating the financial markets. In the first half of 2008, the work on improvement of regulations for the investment funds activities in the Russian Federation by legislation issued by FFMS. The Regulation on procedure for becoming a qualified investor was approved.

In the first half of 2008 no amendments for federal laws regulating legal relationships at financial markets were adopted. However, some legislation acts issued by FFMS, regulating a number of important issues, were approved or came into effect On February 1, 2008, the "Provision on qualification of foreign financial instruments as securities", approved by an order of FFMS of Russia, came into effect. This Provision regulates the procedure of qualification of foreign financial instruments as securities depending on the CFI (Classification of Financial Instruments) code.

Besides, in the 1st half of 2008 FFMS of Russia has approved the new "Provision on audit procedures in the organizations monitored and supervised by FFMS of Russia" and "Provision on the procedure for maintaining the register of owners of Russian depository receipts".

In the end of 2007, FFMS of Russia has issued an order "On requirements to the order of keeping the register of owners of registered securities by issuers of registered securities". By the Supreme Court's decision of May 16, 2008, this regulation was nullified.

General provisions of the Civil Code of the Russian Federation and norms regulating joint-stock companies established by the law "On joint-stock companies" are also very important for the Russian capital market.

Taxation of capital market activities

The Russian Federation is a country with traditional taxation system, i.e. it does not position itself as a tax shelter country.

Table 33 lists the main taxes that apply to profits (the income of enterprises who carry out activities subject to taxation in the Russian Federation, relevant to securities trade or to individuals' income).

Russian Federation has double taxation treaties with 67 countries of the world. According to these treaties, a company registered in one country and receiving income from sources located in two countries (Russia and the other signatory country) pays taxes only in one of these countries: either in Russia, using a discounted rate, or in the other country that signed the agreement, also on a discounted rate.

The RF Ministry of Finance has published a list of the offshore zones³⁵, the registration in which does not entitle the companies to transfer non-taxable dividends to Russia as provided for in the subsection 3 of section 284 of the Tax Code of the Russian Federation. 41 offshore zone is included in the list.

Table 33. Taxation of securities transactions.

Income	Tax rate, for a resident, %	Tax rate, for a non-resident, %
Individuals		
Dividends on stocks of Russian companies	9	15
Interest on bonds with a mortgage backing issued before January 1, 2007	9	30
Other income from securities and operations with them	13	30
Legal entities		
Dividends from daughter companies, provided that certain conditions are met (the share of more than 50% in capital, ownership for at least one year etc.; if the company is a foreign one it should not be located in an offshore zone)	0	Not applicable
Dividends from Russian and foreign organizations	9	15
Interest on state and municipal bonds, interest on mortgage-backed bonds issued after January 1, 2007, interest on the income of the founders of trust management for mortgage backing received upon purchasing the mortgage participation certificates issued by the mortgage backing management after January 1st, 2007	15	15
Interest on municipal bonds with term at least 3 years long, issued before January 1, 2007, as well as interest on mortgage-backed bonds issued before January 1, 2007, and interest on the income of the founders of trust management for mortgage backing received upon purchasing the mortgage participation certificates issued by the mortgage backing management before January 1st, 2007	9	9
Other income from securities and operations with them	24	24

Source: Tax Code.

The Russian system of capital market regulation was formed simultaneously with the formation of the market itself and has played a positive role in its development, in many aspects. This system generally follows the norms of international capital market regulations and meets the world development trends of regulation in this area; it has, however, some national specifics. The most important specific feature is a complicated distribution of regulatory and supervising authorities in the area of financial markets between several departments. At present a significant part of the corresponding functions in the area of capital market as such has actually passed to a single state body, the Federal Financial Markets Service; however, certain powers still remain with the Central Bank and to a lesser degree with the Ministry of Finance.

3.1. The Federal Financial Markets Service of the Russian Federation

The Federal Financial Markets Service (FFMS) is at present the principal State regulating authority on the Russian capital market. Its status is similar to that of a ministry, as it reports directly to the Government of the Russian Federation and performs both regulating and supervising functions.

³⁵ The Ministry of Finances Order of November 13, 2007, No.108n "On approval of the list of the states and territories providing tax shelter and/or allowing non-disclosure of information for financial operations (offshore zones)".

The FFMS activities are defined by the Law “On securities market” and by the Regulation on FFMS approved by the Decree of the Government of the Russian Federation of June 30, 2004, No. 317. According to this Regulation, the FFMS is a federal executive authority performing adoption of normative legal acts, controlling and supervising the financial markets, except for insurance, banking and auditing activities.

The FFMS regulates the activities of all the principal subjects of the capital market: issuers, professional participants, collective investment institutions and, in some cases, the investors, too. The FFMS has functional independence; it does not coordinate its actions with other bodies. Nevertheless, being an executive body it reports to the Government of the Russian Federation that has a right to suspend or cancel any act of the FFMS.

Concerning **issuers**, the FFMS has authority to approve the standards of securities issuing, securities registration procedures and reports on results of issue, as well as prospects of securities (except for State and municipal securities). The FFMS also checks the issuers, and issues instructions to them in case of any violations; it can suspend issue of securities if required and file a lawsuit for the securities issue to be declared invalid. The FFMS also determines the order of the admission to IPO and circulation of the Russian issuers' securities outside the territory of the Russian Federation.

Concerning **professional securities market participants**, FFMS approves requirements to the rules of conducting professional activities with securities, approves norms of sufficiency of internal funds, grants licenses for professional activities in capital market, registers some internal documents of professional participants. It also carries out checks of professional participants and issues instructions to them if required; it can prohibit or restrict particular transactions at the securities market, and has right to suspend or cancel licenses of violators.

Concerning **collective investment institutions** the FFMS licenses activities of private pension funds, equity investment funds, management companies and specialized depositories. It registers rules of investment fund management and rules of mortgage backing management, rules for private pension funds, and documents of specialized depositories. The FFMS also approves requirements to the structure of assets of joint-stock and unit investment funds, defines standards of disclosing information and forms of reporting for PPF; conducts checks of these organizations and issues instructions to them.

The FFMS also regulates admission of securities to public offering, their circulation, quotation and listing, takes measures to stop unfair advertising in the capital market, publishes methodology materials and recommendations on the matters in its competency. It has right to file lawsuits and take claims to the court and arbitration court. An important function of the FFMS is its right to review cases of administrative violations within its area of competence, and to take measures established by administrative legislation.

It should be noted that that the FFMS competence has a number of essential exemptions concerning financial organizations: for them, the FFMS can neither establish measures of prudential nature nor regulate issue of their securities. The authority of the FFMS does not extend to the matters of issue and circulation of the state and municipal securities.

3.2. The Central Bank of the Russian Federation

The Central Bank is not an executive power authority and carries out its activity on the basis of the special law “On the Central bank of the Russian Federation (Bank of Russia)”. Its authority on regulation of commercial banks are defined by the law “On banks and banking activities”. Being an organization responsible for the organization of monetary circulation and stability of the banking system in Russia, the Bank of Russia has a number of powers affecting to some extent the capital market and its participants.

For example, the Bank of Russia works together with the Government of the Russian Federation to develop and implement a consistent state monetary and credit policy that affects many factors of capital market. Effecting its monetary and credit policy, it acts as an issuer of its own bonds and carries out open market transactions with state securities and its own bonds, being a large player in this market.

As a banking system regulator, the Bank of Russia defines specifics for the procedures of securities issue for financial organizations, and registers issues of these securities. Further on, it supervises the banking activity of financial organizations and bank groups, including their activity as investors in the capital market. Concerning the activity of financial organizations as professional securities market participants, the Bank of Russia, in fact, defines the procedures for some operations (for example, trust of securities, procedures for depositary registration etc.). It also carries out “indirect regulation” of the capital market by participation in the capital of infrastructural organizations of capital market (for example, MICEX).

The Bank of Russia also defines procedures for banking operations, for accounting and reporting of the banking system of the Russian Federation.

Thus, even though the Bank of Russia's powers over capital market participants directly affect only the financial organizations operating in this market, its overall influence on the financial market is significant. Because of these powers, the Bank of Russia is the second in importance among the State regulators of the capital market.

3.3. The Ministry of Finance of the Russian Federation

According to the Regulation on the Ministry of finance (approved by the Decree of the Government of the Russian Federation from 30.06.04 No 329), it performs a number of functions related to the securities market and its participants. First of all, the Ministry of Finance approves terms of issue and circulation of federal state securities, makes decisions on particular issues of these securities, and reports on the results of their issue. At the same time, the Ministry of Finance is itself an issuer of the federal state securities.

Further, it acts as a regulating authority for the state securities of subfederal level and municipal securities; it performs the official registration of the terms of issue and circulations of these securities, approves standards of disclosing information on these securities.

Besides, the Ministry of Finance remains a regulator in the area of pension savings investments for financing the savings part of labor pension, as well as a regulator for insurance companies including their financial investments in securities (supervising functions in relation to insurance companies are exercised by Federal Insurance Supervision Service that reports to the Ministry of Finance). The Ministry of Finance also approves the normative legislative acts concerning accounting procedures and financial statements.

3.4. Other State bodies

Law enforcement system in the capital market also includes tax authorities, financial control and monitoring bodies, the antimonopoly authority, judiciary system and law enforcement agencies. However the detailed analysis of their functions and tasks is out of scope for the present review.

3.5. Self-regulatory organizations

System of the securities market regulation includes, beside State bodies, the Self-Regulatory Organizations (SROs). They are created by professional securities market participants to provide an environment for their professional activities, compliance with the standards of professional ethics in the capital market, protection of investors' and other clients' interests, as well as establishment of the rules and standards of trading in securities ensuring efficiency of the capital market activities. SROs may be established by management companies as well.

SROs are created as nonprofit organizations. They establish rules, obligatory for their members, for conducting professional activities in the capital market, and standards of trading in securities. They also control compliance with these rules. Membership in a SRO is voluntary.

At present five organizations of professional securities market participants and collective investment institutions, have SRO status in Russia³⁶:

- The National Association of Securities Market Participants (NAUFOR) includes brokers, dealers, trust managers and depositaries. The total number of its members is 413 organizations. NAUFOR has headquarters in Moscow and branches in 14 regions of the country;
- The professional association of registrars, transfer agents and depositaries (PARTAD) comprises 97 depositaries and registrars.
- The National Equity Association (NFA) includes organizations that hold licenses to conduct broker, dealer, depositary activities and trust management of securities; most of these are credit institutions. NFA has more than 246 member organizations.
- National League of Management Companies of Russia (NLMC) includes 80 organizations;
- Noncommercial partnership of professional securities market participants of the Ural region (PUFRUR) – the only SRO, for now, whose headquarters are located outside Moscow (in Ekaterinburg). Its members are 24 professional securities market participants from the Ural region.

It should be noted that rather often professional securities market participants are members of several SROs simultaneously. Therefore it is impossible to evaluate precisely the general involvement of professional market community into self-regulating activities. Nevertheless, under our estimations approximately 30%–35% of the total number of professional securities market participants are members of at least one self-regulating organization; the highest level of participation in SRO is among registrars – over 70%.

It is necessary to note that over the last years the member base of leading SROs has stabilized and the membership in the self regulating organizations has actually become a standard of professional work among large professional securities market participants.

³⁶ According to FFMS data and SRO web-sites, as of the end of 1H08.

4. Principal events of January-June 2008

January	
09.01.08	The first business day at Russian stock market started against the background of the quotations tumbling down at US and Asian stock exchanges.
21.01.08	Quotations tumbling down at US and Asian stock exchanges (6% on the average). MICEX and RTS indices dropped 5.8%, some stocks quotations by 10%, and trades were suspended for some instruments.
24.01.08	RTS and MICEX Indices grew by 5.2% – 5.8%.
25.01.08	An extraordinary shareholders meeting of the CJSC "DCC" made a decision to increase the registered capital.
February	
01.02.08	The order of the FFMS of October 23, 2007, No. 07-105/pz-n "On approval of the Provision on qualification of foreign financial instruments as securities" came into effect.
07.02.08	A misrepresenting notification was published at the FFMS web-site, in the "Mergers and Acquisitions" section. The publication affected the quotations of the stocks of the issuer mentioned in the notification. FFMS announced that an official investigation was started to find out whether a price manipulation occurred.
11.02.08	At the FORTS derivative market, the length of the intermediate clearing session is shortened from 5 to 3 minutes.
13.02.08	State Duma has given preliminary approval to the "On stock exchanges and organized trade" law.
22.02.08	The FFMS Order of December 25, 2007 No. 07-112/pz-n "On amendments for the norms of internal funds sufficiency specification for professional securities market participants" came into effect. The amendments provide for decreasing the norms of internal funds sufficiency if the professional responsibility is insured and there is a petition from a self-regulating organization.
28.02.08	FFMS published the results of the official investigation on the misrepresenting notification that was published at the FFMS web-site, in the "Mergers and Acquisitions" section. The publication was found to be a technical error. No price manipulation was found.
March	
01.03.08	The order of the FFMS of November 13, 2007, No. 07-108/pz-n "On approval of the procedures for auditing the organizations the regulations and control of which is entrusted to FFMS", came into effect.
02.03.08	The Presidential elections in Russian Federation were held. The results of the election did not affect Russian capital market.
18.03.08	The technology of obligations fulfillment for securities transactions by simple clearing was launched at MICEX.
20.03.08	At RTS, upon NAUFOR's initiative, the trade of OJSC "RichBrokerService" was suspended for reasons that the consequences may violate the stockholders' rights.
24.03.08	At Saint Petersburg Stock exchange, upon the initiative of the trade participants, the trade of OJSC "RichBrokerService" was suspended (since the beginning of the trade, February 12, the quotations grew 100%).
25.03.08	Pilot offering of exchange bonds of OJSC "RBK Information systems" started at MICEX.

April

- 08.04.08 The General Prosecutor's office published on its web-site the information about violations in activities of FFMS regional branch in Ural federal district.
- 09.04.08 The State Duma of the RF inquired with FFMS about the measures taken for development and approval of the new standard UIF regulations related to the amendments to the "On investment funds" coming into effect.
- 11.04.08 State Duma passed in the second reading the law on voluntary additional pension savings of the individuals.
- 22.04.08 It is announced that FFMS is auditing the companies that promise unreasonably high incomes to the investors and look like pyramid investment schemes. Seven such companies were identified in North-West federal district. The number of victims in the whole country is estimated at 100,000 people.
- 25.04.08 The Federal State and Social Fund for protection of investors' and shareholders' rights held a tender for the fund asset management. Three management companies were declared as winners. The fund's assets are estimated at 2 billion roubles.

May

- 08.05.08 V.V.Putin made a speech at the RF State Duma session and was appointed the Chairman of the RF Government. He announced that one of the major regional financial centers of the world will be created in Russia. He also mentioned possible lowering of tax burden for the oil industry. The quotations of oil and gas industry stocks grew by 5-6%.
- 13.05.08 FFMS registered an additional issue of CJSC "DCC" stocks for the amount of 800 million roubles.
- 14.05.08 Chairman of the Government of the Russian Federation announced the taxation changes for the oil and gas industry. The quotations of some oil and gas industry stocks grew by more than 10%. The capitalization of Russian capital market grew by more than 40 billion dollars.
- 16.05.08 The RF Supreme Court invalidated the section of FFMS order that obliges the companies maintaining the shareholders' register without a registrar to perform this activity only with the help of a certified specialist.
- 22.05.08 RTS Board of Directors made a decision to transfer the securities clearing from NP "SE RTS" to OJSC "RTS Clearing Center" effective on September 1, 2008.
- 23.05.08 The order of the FFMS of March 18, 2008, No. 08-09/pz-n "On approval of the Provision on the procedure for maintaining the register of owners of Russian depository receipts" came into effect.
The order of the FFMS of March 18, 2008, No. 08-12/pz-n "On approval of the Regulation on procedure for becoming a qualified investor" came into effect.
- 26.05.08 Night trade session was introduced at FORTS derivative market.

June

- 07.06.08 At the 12th Saint-Petersburg Economy Forum, the President of the RF suggested creating a major regional financial centers of the world in Russia.
- 05.06.08 State Duma passed in a first reading the law on restricting the administrative responsibility for the financial market participants.
FFMS issued an Order of June 05, 2008, No. 08-24/pz-n "On amendments for Provision on the procedure of issuing a permission for issue and/or circulation of emission securities outside the RF" (effective from July 25, 2008). The maximum number of stocks that can be offered or circulated abroad is changed from 35 to 30%; for strategic issuers the limit is 25%, and for the issuers that perform geological prospecting and/or mining for mineral resources, 5%.
- 06.06.08 The last day of trade for stocks of RJSC "UES of Russia" at stock exchanges.

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- 17.06.08 The RF Ministry of Interior announced that since the beginning of the year seven pyramid investment schemes were stopped. The total damage from their activities exceeded 32 billion roubles.
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- 16.06.08 The results of the open tender for trust managers of temporarily uninvolved assets of a state corporation, the Fund of assistance to reform of housing maintenance and utilities infrastructure. Two banks and ten management companies were declared winners. The total amount of assets transferred for trust management is estimated at 100 billion roubles.
-
- 20.06.08 At MICEX, the stocks of OJSC "Mosenergo" were suspended in trade because the quotations grew more than 15%.
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- 24.06.08 FFMS published at its regional websites a list of 16 companies and one USA citizen whose activities exhibit the symptoms of a pyramid investment scheme.
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- 26.06.08 The first session of the Community council of the capital market participants under FFMS of Russia was held.
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- 27.06.08 A specialized company, CJSC "MICEX – Information technologies" was founded within MICEX Group.
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- 30.06.08 The new RTS documents revisions came into effect, introducing netting technology for stock market settlements in the mode of "central counterparty for transactions".
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