

# The Russian Capital Market 2008

## Events and facts



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# Introduction

This report presents the next in a series of reviews of the Russian capital market.

The objective of such reviews, published bi-annually since 2007, is to present a general picture of the Russian securities market and its key components: its instruments, participants, infrastructure, regulatory system and monitoring, as well as to highlight the main events that occurred in the market during this given period.

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

Please note the following key points:

1. In this review we have tried to minimise extensive commentary or evaluation, other than where strictly necessary in order to comprehend fully the data it contains, the dynamics, or the specifics of the Russian capital market;
2. In the majority of cases we have used information pertaining to the end of 2008; however in some cases where this data was not available at the time of writing, we have used facts that relate as close to this date as possible;
3. It is not our intention to demonstrate the growth of the Russian market over a lengthy period prior to 2008. Generally, when using historical data, we will make reference to nothing earlier than 2005;
4. Numerical indicators used in this report are noted in both national and foreign currency. This is due to the peculiarities of trading and the way in which its results are presented;
5. We will often refer to data from a number of different sources in order to demonstrate existing discrepancies in evaluations or accounts.

We would like to thank the MICEX and RTS, the REGION Group of companies, the National League of Management Companies, Standard&Poor's, Ernst&Young, the JSC companies Interfax Business Service, Interfax (SPARK), Finmarket (Rusbonds Project) and CBONDS, and also Offering.ru for their project «IPOs in Russia», the material they provided and their cooperation.

## Main Indicators and Trends for 2008

*In 2008 the Russian securities market was affected by the global financial and economic crisis and the positive dynamics experienced in 2005-2007 were lost to a steep downturn in all sectors of the market. Two stages can be clearly delineated in 2008. The first—January to August, was an evolutionary period during which the market grew by inertia. The second—September to December, saw a hard-hitting financial crisis that led to radical changes on the Russian securities market. As a result of the crisis and the methods employed to stabilise the situation, objective 'pegged' prices were lost and many market indicators took on an anomalous character, not entirely expressive of the fundamental market parameters.*

**Stock market.** The capitalisation of the Russian stock market fell by 72% to 0.37 trillion dollars. The ratio of capitalisation to GDP fell 3.7 times to 26.5%. A high concentration of Russian stock market capitalisation was maintained. Ten of the most capitalised companies accrued a share of 70% capitalisation. In industrial sectors, 57% capitalisation was accrued in oil and gas (production and refining). The domestic exchange transaction turnover of shares in Russian companies in financial terms, discounting repurchase agreements (REPO), decreased by 17% and stood at approximately 12.8 trillion rubles (0.52 trillion dollars) for the year. The share of repurchase transactions in the general exchange stock turnover increased over the year and exceeded 60%. In July—November there was a turnaround in trading activity on foreign markets and, during distinct periods, the number of transactions with depositary receipts of Russian companies on foreign trading platforms was greater than the number of stock transactions on the domestic market.

**Corporate Bonds Market.** The overall volume of corporate bonds in circulation increased by 27% and constituted 1.6 trillion rubles. The number of bond issuers decreased slightly and comprised of 463 companies. In comparison with GDP, the volume of corporate bonds in circulation remains insignificant and constitutes 3.8%. The total on- and off-exchange transaction volume of corporate bonds (excluding repurchase transactions) increased by 6% and constituted 3.9 trillion rubles, in the first three quarters the share of exchange transactions was on average 75%, in the fourth it decreased to 52%. The volume of exchange transactions, discounting repurchase agreements (REPO) fell by 3.5%, amounting to 2.6 trillion rubles. The share of repurchase transactions in the general exchange turnover increased from 78 to 82% in the first three quarters and fell to 53% in the fourth. The volume of initial offerings of corporate bonds constituted 609 billion rubles and these occurred within the period up to August. A new debt instrument appeared on the corporate bonds market—exchange bonds, their volume of offering and turnover insignificant. In the course of the year 10% of company bond issuers committed various violations in servicing their debt, the volume of unfulfilled conditions by default is estimated at 27 billion rubles.

**Derivatives Market.** The market of derivative contracts, whose underlying assets include securities and stock indices, grew overall during the year. Just under 90 types of contracts were offered, moreover the concentration of derivative contract transactions on the stock indices increased. The volume of transactions in monetary terms increased by 44% and amounted to 10.5 trillion rubles, the volume of transactions in the number of contracts grew by 57%, the number of transactions grew by 142% and reached 28.1 million. In the fourth quarter, at the same time as the number of transactions had risen, there was a fall in volume indicators of the derivatives market in comparison with the previous quarters. Also in the fourth quarter, according to all indicators, the options market sharply contracted. The ratio of the volume

of the derivatives market, the underlying assets of which are stocks and stock indices, to the volume of the spot (cash) market (without factoring in repurchase transactions) reached 83%.

**Stock indices.** The main stock indices experienced a slowdown and a serious downtrend. The profitability (APR) by composite indices was minus 71.4% for the RTS Index and for the MICEX index minus 66.5%. All industry and capitalisation indices handled by the stock exchanges showed negative profitability. The greatest drop occurred in the industrial indices (minus 85%). The volatility of the stock indices increased on average three times. An imbalance of analogous stock indices started to appear, as calculated by the various stock exchanges.

**Issuers.** The number of stock and bond issuers on the organised markets fell by 5–7%. Public offerings froze—during the course of the year seven companies placed offerings to the sum of 1.7 billion dollars. On the leading stock exchanges alternative floors were created for the placement and circulation of securities of innovative companies and companies of limited capitalisation. The number of companies floated on these platforms, the volume of offerings and the secondary market volume were insignificant. From figures reported through exchanges of OTC transactions of securities included on the quotation lists, it follows that during the year the volume of OTC transactions did not fall below 25% of the general volume, and at certain times reached 45%.

**Private Investors.** The number of private investors operating on the MICEX stock exchange is growing and has reached 559 thousand; the number of active investors varies from month to month from 62.5 thousand to 90.7 thousand, depending on market conditions.

**Collective Investors.** The number of PIFs (Russian Unit investment funds—henceforward referred to as UIFs) increased insignificantly and comprised of 1020 funds. The increase was caused by growth in the number of closed-end UIFs; the number of opened-end and interval UIFs decreased. The total net asset value of UIFs fell by 136 billion rubles (by 17.5% in respective terms) and constituted 646.0 billion rubles. To a greater extent (65–70%) the net asset value of opened-end and interval UIFs decreased. A negative balance of net raised capital was registered in opened-end UIFs: the outflow amounting to 16.6 billion rubles.

**Foreign investment funds.** As currently estimated, about 2400 foreign funds (from the number of those required to disclose information on their activity) invest into Russian assets (stocks and depository receipts). General growth has been registered in the investment of these funds into Russian assets; the volume of Russian securities is estimated at 76 billion dollars, a quarter of these assets acquired on the Russian exchanges. In global funds (the share of which Russian assets are less than 10%) a drop in the volume of Russian securities was noted. At the same time, the volume of Russian securities increased in specialised funds (the share of Russian assets is more than 75%).

# 1. Instruments

## 1.1. Stocks

Russian legislation requires all stock issues by all joint stock companies (including closed joint stock companies) to be registered. SPARK data as it pertains to stock issuers and issuings is contained in Table 1.

**Table 1** Stock issuers

	2005	2006	2007	2008
Number of Issuers	460 352	471 010	481 372	487 765
<i>Including Open Joint-Stock Companies</i>	62 960	64 431	65 706	66 466
Number of stock issues <sup>1</sup>	463 206	473 881	483 244	490 645

Source: Interfax SPARK

The overwhelming majority of these stocks is absolutely illiquid, and they are not traded in any secondary markets. Only a very small proportion of these stock issuers is traded on the stock exchanges. Table 2 shows collated data on stocks that are offered on Russian stock exchanges.

**Table 2** Organised Stock Markets

	MICEX				RTS			
	2005	2006	2007	2008	2005	2006	2007	2008
Number of stock issuers	163	190	208	231	261	281	302	275
Number of stock issues	256	325	309	309	383	398	413	395
<i>including in the quotation lists (ordinary/preferred shares)</i>	34/16	46/14	71/16	86/15	46/13	63/13	87/16	95/15

Sources: MICEX, RTS.

Thus, as can be seen from Tables 1 and 2, less than 0.5% of all open joint stock companies are represented on the stock exchanges as stock issuers and this indicator has remained practically unchanged over the past few years.

Overall in 2005–2008 the number of public issuers has shown a definite trend toward growth, however qualitative changes did occur in this period. It is worthy of note that the majority of stock issues floated on the organised markets (approximately 70% of the total number in 2007–2008) relates to securities, admitted to trading without the procedure of listing i. e. non-listed stock.

<sup>1</sup> Not including additional issues



In 2005–2006 this statistic was higher, approximately 80%. In 2006–2007 the growth rate in the number of instruments included in the quotation lists of different levels was 30 to 35% annually. In 2008 this indicator was 7–15% at the beginning of the year.

A specific feature of the Russian capital market is the opportunity to conduct organised trade in securities of the same issuer simultaneously on several stock exchanges. Therefore a considerable proportion of issuers are present on both the main Russian stock exchanges and the shares of a number of Russian issuers in the form of depository receipts are also traded on foreign exchanges. According to Standard&Poor's<sup>2</sup>, the number of Russian issuers with stocks listed for trade on RTS, MICEX, NYSE, NASDAQ and which are also LSE-listed S&P EMD Russia index was 309 companies as of December 2006, and 328 as of December 2007. In September 2008 this dropped to 307 companies.

Data on the stock market capitalisation of Russian issuers is shown in Table 3. It should be noted that at present there is no commonly accepted methodology for calculating the stock market capitalisation of Russian issuers, therefore in this overview figures are derived from a number of different sources.

**Table 3** Stock market capitalisation of Russian issuers

Period	unit of measure	2005	2006	2007	2008			
					Q1	Q2	Q3	Q4
MICEX (for stocks traded on the stock market)	billion rubles	7 440	23 338	29 974	26 017	29 305	15 975	9 912
	billion dollars	259	885	1 217	1 106	1 249	633	337
MICEX (general estimate of the stock market)	billion rubles	no data	25 482	32 740	28 971	32 263	18 360	11 017
	billion dollars	no data	966	1 329	1 232	1 375	727	375
RTS (for stocks traded on the stock market)	billion dollars	329	966	1 329	1 232	1 375	727	374
Estimate of S&P <sup>3</sup>	billion dollars	549	1 057	1 503	1 406	1 524	788	no data
GDP	billion rubles	21 625	26 904	33 114				41 540
<b>Capitalisation/GDP<sup>4</sup></b>	<b>%</b>	<b>34.41</b>	<b>94.72</b>	<b>98.87</b>				<b>26.52</b>

Источники: ММВБ, РТС, ФЦС, S&P.

The growth in the stock market capitalisation of Russian issuers seen in the previous few years (2006—175%, 2007 40%) ceased in the first half of 2008, and in the second it began to drop sharply. In general towards the end of 2008, the annual drop in capitalisation was in excess of 950 billion dollars in absolute terms, or 71.9% in relative terms. Correspondingly, the ratio of capitalisation to GDP, which in 2006–2007 was nearing the level of 100%, dropped in 2008 to 26.5%—the level of 2000–2001. It should be noted that while in 2005 the share of stock market capitalisation of Russian issuers traded on foreign trading floors was 40%, from 2006 to 9 months into 2008 this indicator stood at 9–12%. The Russian stock market differs in its high concentration of capitalisation from the point of view of both the issuers, and the industries to which the issuers relate. Table 4 shows a list of the ten most capitalised companies, and Table 5—the change dynamics of the share of the ten most capitalised companies in the period 2006–2008.

2 Emerging Stock Markets Review, S&P, Issues Series 2006-2008.

3 Russian issuers, stocks which were traded on RTS, MICEX, NYSE, NASDAQ and also those on LSE-listed, S&P EMD Russia Index are included in the evaluations.

4 Capitalisation of the domestic stock market is included in the evaluations.

**Table 4** The list of the most capitalised Russian issuers (total for 2008)

Nº	Issuer	Capitalisation (billion dollars)	Stake in total capitalisation (%)
1	OJSC "Gazprom"	86.7	25.7
2	OJSC "NK Rosneft"	36.0	10.7
3	OJSC "Lukoil"	27.7	8.2
4	OJSC "Surgutneftegaz"	21.5	6.4
5	OJSC "Sberbank Russia"	17.1	5.1
6	OJSC "MMC Norilsk Nickel"	12.8	3.8
7	OJSC "Gazprom Neft"	10.0	3.0
8	OJSC "VTB Bank"	7.7	2.3
9	OJSC "Mobile TeleSystems"	7.6	2.2
10	OJSC "Rostelecom"	6.6	1.9
<b>TOTAL</b>		<b>233.6</b>	<b>69.2</b>
<b>General capitalisation</b>		<b>337.4</b>	<b>100.0</b>

Source: MICEX.

**Table 5** Stake of the ten most capitalised issuers in the total capitalisation of the stock market

	2005	2006	2007	2008			
				Q1	Q2	Q3	Q4
TOTAL (%)	77.7	78.5	68.5	66.7	66.4	69.0	69.3
<i>of which OJSC "Gazprom"</i>	–	30.7	27.3	27.0	27.6	28.3	25.7

Calculated from MICEX data.

Over the past few years there has been little significant change in the list of the most capitalised issuers. The end of 2005 saw the public floatation of OJSC "Gazprom" shares, and from the beginning of 2006 this issuer has headed the list of the most capitalised Russian companies. In 2006 OJSC "NK Rosneft" underwent an IPO and became a new issuer on this list, and in 2007, OJSC "VTB Bank" also entered it following with an IPO. In mid 2008 RAO "UES Russia", one of the most capitalised and liquid issuers ceased its activities as a result of the completion of reforms in the electric power industry. Any reduction in the concentration of the capitalisation of issuers in the past few years has been negligible. The growth in the stake of the most capitalised issuers as it appeared in the second half of 2008, in comparison with the end of 2007 and the first half of 2008, does not, in our view, constitute a trend change.

Table 6 shows data on the dynamics of the Russian stock market concentration of capitalisation by industry over the past few years. In this table petrochemicals and mineral fertilizers are categorised as the 'Chemicals industry', pharmaceuticals as 'Other'.

**Table 6** Russian stock market concentration of capitalisation by industry

№	Industry	2006	2007	2008			
				Q1	Q2	Q3	Q4
1	Fuel industry	62.4	50.4	50.9	53.5	56.2	57.0
2	Financial	9.2	11.8	10.2	9.0	9.6	10.1
3	Electric Power	11.9	12.5	11.6	11.0	6.9	8.9
4	Metallurgy	8.1	11.0	12.2	11.5	10.4	9.6
5	Communications	4.1	5.8	5.5	4.7	5.5	5.6
6	Food	1.5	1.3	1.2	1.1	1.5	1.2
7	Construction	0.0	1.3	1.2	1.2	0.6	0.5
8	Mechanical Engineering & Metal Working	0.8	1.1	1.2	1.1	1.0	0.7
9	Transport	0.8	1.2	1.1	0.9	1.0	1.8
10	Trade	0.6	0.7	0.7	0.7	0.9	0.7
11	Mining	0.3	0.7	0.9	1.2	2.6	1.9
12	Chemical	0.2	1.5	2.0	3.0	2.3	1.4
13	Other	0.2	1.0	1.1	1.1	1.6	0.5

Source: MICEX.

Table 6 shows a trend towards a reduced stake of companies functioning in the production and processing of oil and gas in 2007 and there was no further development here. As before, more than half the capitalisation of the Russian stock market is concentrated in the fuel sector. The increase in share of this sector in the total capitalisation evident in the second half of 2008 is not a change in trend either, in our opinion, but a consequence of heightened volatility and a setback in price structuring. A positive trend can be seen in this table from 2007—an increase in the stake of companies in the financial sector. This is linked to the public floatation of two large credit organisations—OJSC “Sberbank Russia” and OJSC “VTB Bank”. However in 2008 this trend did not continue. In the second half of 2008, the electric power companies experienced a discernible downturn in their stake as a result of RAO “UES Russia”’s cessation of activities. The metallurgy sector also saw a decrease in its share of market capitalisation. Otherwise all other industries have not undergone any significant changes in capitalisation in the past few years.

Table 7 shows the characteristic transaction volumes for the stocks of Russian companies on the leading stock exchanges.

**Table 7** Volume of Trading of Russian Stocks

Period	Unit of Measure	2005	2006	2007	2008				2008
		Total	Total	Total	Q1	Q2	Q3	Q4	Total
MICEX <sup>5</sup>	billion rubles	4 025.0	14 859.6	30 927.1	9 570.2	10 249.6	9 521.5	4 363.5	33 704.7
<i>Share of repurchase transactions in the total volume of stock transactions on MICEX</i>	%	18.5	25.6	50.5	58.0	62.4	67.2	65.0	62.8
RTS Classic Market <sup>6</sup>	billion dollars	7.7	16.1	14.6	3.6	3.1	2.44	0.67	9.8
<i>Share of repurchase transactions in the total volume of stock transactions on the RTS Classic Market</i>	%	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
RTS Exchange Market <sup>7</sup>	billion rubles	82.0	27.3	23.5	4.9	7.4	7.35	8.50	28.1
<i>Share of repurchase transactions in the total volume of stock transactions on the RTS Exchange Market</i>	%	0.6	12.0	36.3	48.3	44.6	61.3	20.1	42.2
Stock exchange SPB <sup>8</sup>	billion rubles	936.8	1 205.9	64.2	21.1	18.0	1.92	0.62	41.7
<i>Share of repurchase transactions in the total volume of stock transactions on the s.e. SPB</i>	%	17.5	25.1	64.8	89.9	86.5	36.4	21.6	85.0
Average exchange rate of the US dollar for the period (information)		28.28	27.18	25.57	24.26	23.63	24.24	27.25	24.81
<b>TOTAL (estimated) including repurchase transactions</b>									
	billion rubles	5 260.2	16 530.5	31 386.8	9 682.5	10 349.1	9 589.8	4 390.8	34 012.3
	billion dollars	186.0	608.2	1 233.2	399.1	438.0	395.6	161.1	1 393.8
<b>TOTAL (estimated) including repurchase transactions</b>									
	billion rubles	4 354.1	12 415.6	15 713.0	4 113.1	3 934.7	3 183.8	1 552.2	12 783.8
	billion dollars	151.3	471.5	621.2	169.5	166.5	131.3	57.0	524.4
<b>As estimated by S&amp;P</b>		159.3	514.4	754.5	222.0	214.5	183.0	no data	no data
Turnover differential (annual) <sup>9</sup>	%	45.98	48.81	46.74					140.27
Turnover differential (quarter) <sup>9</sup>	%				13.76	12.11	18.07	15.24	

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

Trading volumes of Russian stocks in 2005–2007 (in monetary terms) sustained growth. Thus, the total volume of trade on the leading trading floors (discounting repurchase transactions) in 2006, in comparison

5 Includes bidding mode, negotiation mode, IPO deals and repurchase transaction deals.

6 Includes market, 'addressed' two-sided transactions and repurchase agreements.

7 Includes market, 'addressed' two-sided transactions and repurchase agreements.

8 Includes market, 'addressed' two-sided transactions and repurchase agreements.

9 In this case seen as the volume ratio—transaction volume (discounting repurchase transactions) for the period (annual, quarter) to capitalisation as of the end of this period.

with 2005, increased almost three-fold. In 2007 the annual growth was less—approximately 30%. In the first half of 2008 growth ceased, but in the second, the quarterly transaction volume began to decline. Correspondingly, according to the totals of 2008, the aggregate volume of trade (excluding repurchase transactions) declined in accordance with the currency of transaction by 16–18%. It is worth noting that monetary terms are used in the comparison of stock transaction volumes, hence the devaluation of traded stocks as a consequence of the sharp fall in listings has played its role in the valuations. The turnover differential of stock exchange trade at the end of 2008 was abnormally high. This resulted from a sharp downturn in capitalisation towards the end of the year.

It is worth pointing out that from the beginning of 2007 the share of stock repurchase transactions changed appreciably. While in 2005 it totaled 17% of the aggregate volume of stock exchange operations on the domestic market, and in 2006—25%, in 2007 this indicator reached a qualitatively different level—50%. In 2008 the share of stock repurchase transactions on the domestic market increased again and exceeded 60%, moreover on some exchanges the volume of such deals rose above 85%, that is to say became predominant. Thus, in the past few years, the domestic stock market has been used increasingly as a financial market guaranteed by securities. The drop in the share of stock repurchase transactions on certain exchanges in the fourth quarter does not signify a change in trend, rather it is a consequence of the loss of faith that trading entities have in each other as a result of the economic turmoil.

Trading stocks is concentrated on a rather limited set of instruments. Table 8 shows the list of issuers whose stocks were traded most actively on MICEX in the first half of 2008<sup>10</sup>.

**Table 8** The list of issuers, the shares of which were most actively traded on MICEX  
(based on the 2008 results)

Nº	Issuer	Share in total turnover (%)
1	OJSC “Gazprom”	27.8
2	OJSC “Sberbank Russia”	26.4
3	RJSC “MMC Norilsk Nickel”	12.6
4	RJSC “UES of Russia”	5.3
5	OJSC “Lukoil”	5.0
6	OJSC “Surgutneftegaz”	4.6
7	OJSC “Rostelecom”	4.3
8	OJSC “NK Rosneft”	2.9
9	OJSC “VTB Bank”	2.5
10	OJSC “Tatneft”	1.2
<b>Total</b>		<b>92.6</b>

Source: MICEX.

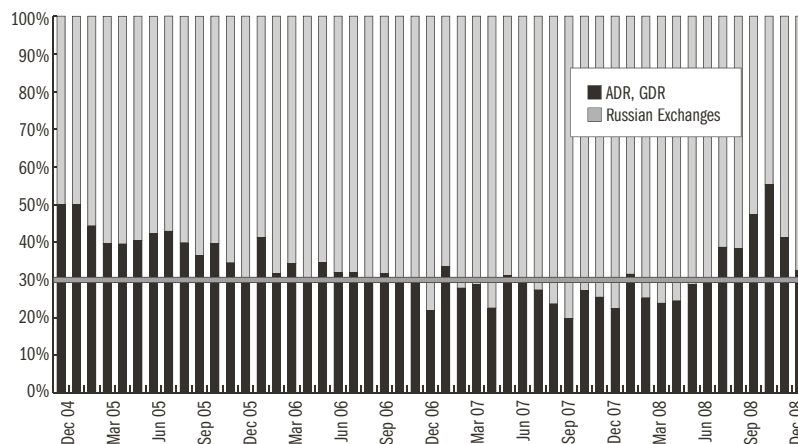
The concentration of turnover shows a very insignificant downtrend (the share of top ten most liquid issuers was 96.6% at the end of 2006 and 94.8% at the end of 2007<sup>11</sup>). In recent years there has been little change on the list of most liquid issuers: in 2006, OJSC “NK Rosneft” entered the list after an IPO, and in 2007, OJSC “VTB Bank”.

An important issue for the Russian capital market is the correlation between domestic and foreign trading floors in the general structure of Russian stock turnover.

<sup>10</sup> Including repurchase transactions.

<sup>11</sup> According to MICEX Data

**Figure 1** The trading volume of stocks and depository receipts of Russian companies, whose depository receipts are traded on foreign exchanges



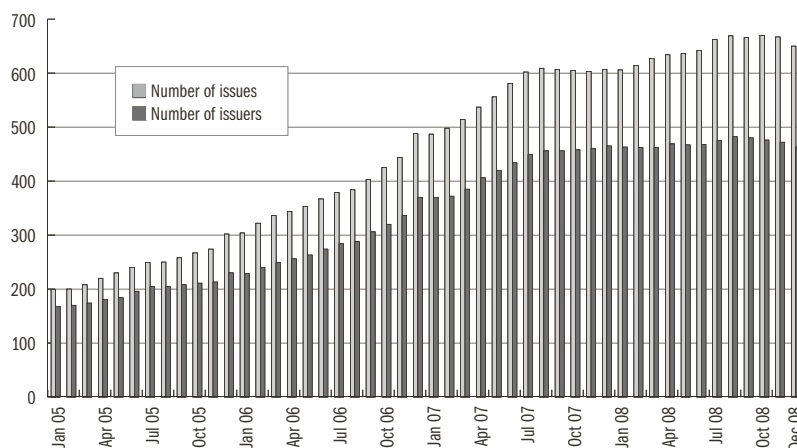
Source: MICEX.

At the end of the 1990s foreign trade in depository receipts far exceeded that of domestic trade. However at the end of 2004 (see fig. 1) domestic exchanges restored parity with foreign ones and in 2005–2007 established a ratio of on average 70:30%, with mild fluctuation in either direction. In the second half of 2008 (July—November) the existing balance was rocked, and for separate periods the volume of trade on foreign markets exceeded the volume of trade on the domestic market. Towards the end of 2008, the ratio of 70:30 was restored in favour of the domestic exchanges.

## 1.2. Corporate bonds

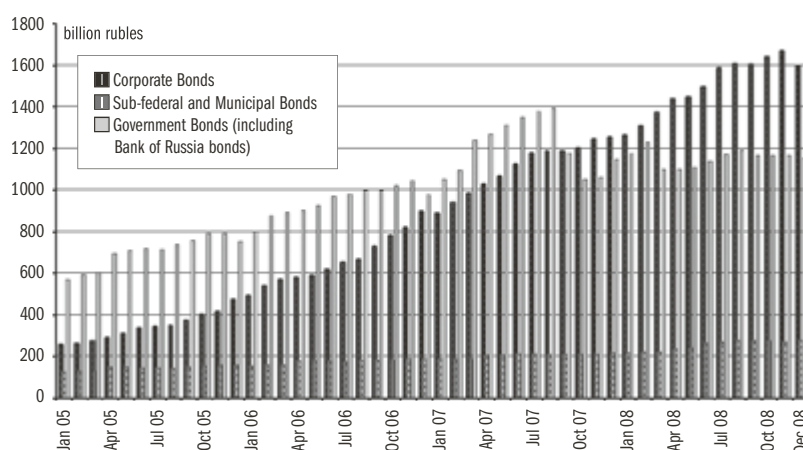
Unlike many other national bond markets, the Russian domestic corporate bonds market developed from the very outset predominantly as an exchange market. Development of the corporate bonds market over the past few years is characterised by an increasing number of issuers, issues and growth in trading volumes.

However, as is evident from figure 2, from July 2007 the temp of growth in the number of bond issues and issuers slowed sharply (in 2005 these indicators showed 52.7 and 36.3%; in 2006—61.6 and 60.9%, in 2007—24.4 and 25.7%). According to the agency CBONDS, at the end of 2008, there were 650 corporate bond issues in circulation on the domestic market (7% more than at the end of 2007). At the same time, the number of bond issuers for the year fell slightly—from 465 to 463 companies.

**Figure 2** The number of corporate issuers and issues on the domestic debt instruments market

Source: CBONDS.

According to the agency CBONDS, the total volume of Russian corporate bonds in circulation (see fig. 3), as of the end of 2008, constituted 1,596.67 billion dollars at par—an increase in comparison with 2007 of 27%. In comparison with 2005–2006, such rates of growth must be considered insignificant (in 2005 the annual growth was 88.3%, in 2006—87.4%, but in 2007 it fell to 39.2%).

**Figure 3** The volume of the domestic debt market (at par)

Source: CBONDS.

In general, in comparison with GDP, the volume of corporate bonds in circulation remains insignificant (2005—2.3%, 2006—3.4%, 2007—3.8%, 2008—3.8%).

It is necessary to note (see fig. 2 and 3), that October—November 2008 saw the beginning of a downturn in the number of issuers, issues and the general volume of corporate bonds in circulation.

In 2008 a whole series of bond issuing companies found themselves unable to fulfill their obligations on time and to the full amount. According to CBONDS, over the year payment breaches were committed in up to 54 issues of 49 issuers. Default occurred on 37 corporate bond issues of 33 issuers, the

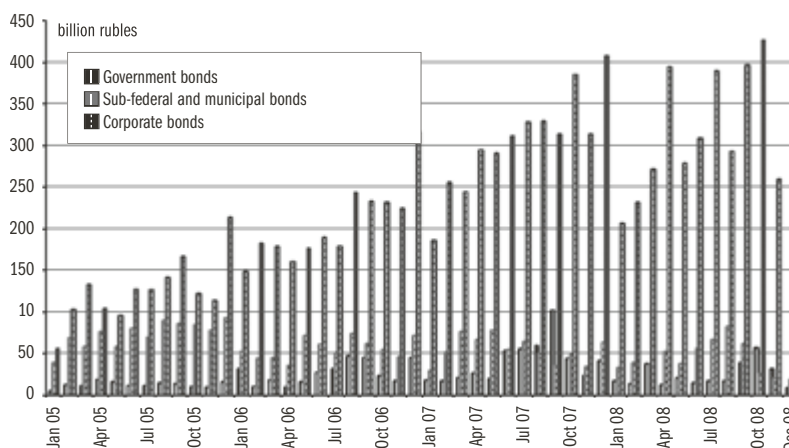
aggregate sum being in excess of 27 billion rubles<sup>12</sup>. Thus, up to 10% of corporate bond issuers committed various breaches in servicing their debt. This is a new phenomenon, which in previous years has not been witnessed to such a degree: in 2002–2007, also according to CBONDS, 10 cases were recorded of non-fulfillment of obligation regarding corporate bonds.

It should be noted that in September 2007, the volume of corporate bonds exceeded the volume of government bonds, including Bank of Russia bonds, and from then onwards this chasm has grown steadily. It is of note that in the total volume of corporate bonds in circulation, the stake of the financial sector is constantly increasing<sup>13</sup>. At the end of 2005 it was 20.7%, in 2006—26.3%, in 2007 it reached 32.4% and in 2008—41.1%. Thus financial companies, first and foremost credit organisations, in greater and greater numbers are using the debt market for additional debt financing.

The number of primary offerings of corporate bonds in 2008 is estimated<sup>14</sup> at 609.8 billion rubles, moreover the bulk of initial placements came about in the period up to August, with peaks in March and July, then the placements stopped. In 2007 the volume of primary offerings of corporate bonds at its height was 484 billion rubles, in 2006—470 billion. In the volume of primary offerings in 2008, according to experts, the share of so-called “technical” placements which were actioned in the first instance by large Russian banks is significant. Excluding them, the volume of initial placements in 2008 remains at the level of 2006–2007, and is estimated at 470 billion rubles.

The secondary market<sup>15</sup> (such as exchange and off-exchange) of corporate bonds has grown constantly in volume over the past few years (see fig 4). However, the turnover has differed greatly from month to month during the year. Thus in the last few years, seasonal factors have become apparent: activity is at its height in December and a fall occurs at the beginning of the year. In this way 2008 has not differed from previous periods, with the exception of a sharp upswing of turnover in April and October.

**Figure 4** Total volume of trade on the domestic debt market (monthly)



Source: CBONDS.

The total volume of corporate bond transactions (including exchange bonds) on the secondary market in 2005–2008 is presented in Table 9.

12 In nominal terms, excluding from consideration those volumes by which bond issuers could restructure debt.

13 CBONDS evaluation.

14 Evaluation by REGION Group of companies.

15 Here and henceforth the volume estimates of the secondary market are of all bond types; if it is not stated in particular otherwise, this does not include repurchase transactions.



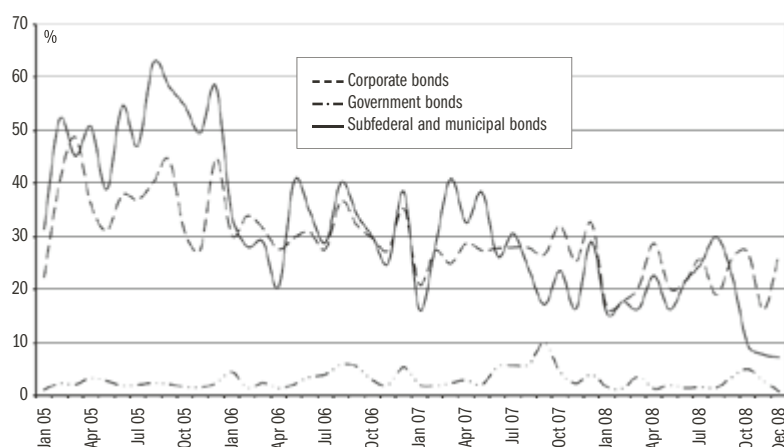
**Table 9** Volume of corporate bond transactions

Period	Unit of Measure	2005	2006	2007	2008				2008
		Total	Total	Total	Q1	Q2	Q3	Q4	Total
Total turnover	Billion rubles	1514.3	2437.5	3669.5	711.8	984.4	1080.6	1112.8	3889.5
Share of exchange transactions in total turnover	%	60.31	72.19	73.92	70.39	77.68	72.23	52.70	67.71

Source: CBONDS.

As shown by Table 9, the volume of corporate bond transactions is steadily rising: the total turnover for 2006 rose by 61% exceeding the results of 2005. 2007 shows the volume of transactions rose by 51%. In 2008 a slowdown in the temp of growth was witnessed: the volume of transactions in 2008 indicated a rise of only 6% more than in 2007. Interestingly, the share of exchange transactions in the total turnover grew constantly and mid 2008 it had reached 78%. However in the second half of 2008 the trend changed dramatically—the fourth quarter sees that the share of exchange transactions with corporate bonds rose little above 50% of the total turnover.

The corporate bonds market is distinguished by a relatively high liquidity (see fig 5).

**Figure 5** Turnover index for various segments of the domestic debt market

Source: CBONDS.

The corporate bond turnover<sup>16</sup> index is subject to significant changes, including seasonal changes. From 2005–2008 its median value was permanently decreasing: from 37% in 2005 to 21% in 2008.

Corporate bonds are traded on the exchanges MICEX and RTS. Table 10 contains summary data on corporate bonds (including exchange bonds) circulated on the Russian stock exchanges, and Table 11—data on the volume of bonds traded on MICEX<sup>17</sup>.

<sup>16</sup> Here meant as the ratio of trading volume per month to the volume of corporate bonds in circulation at par each month.

<sup>17</sup> Data on RTS bond trading is shown in this table, but not in table 16, as volumes are relatively small (in 2005, the total transaction volume on the RTS Classic and Exchange markets of corporate, subfederal and municipal bonds including market and 'addresses' two-sided deals amounted to 0.15 billion rubles, in 2006—8.24 billion rubles, in 2007—1.23 billion rubles, and in 2008—6.21 billion rubles).

**Table 10** The organised corporate bonds market

	MICEX				RTS			
	2005	2006	2007	2008	2005	2006	2007	2008
Number of bond issuers	202	316	445	455	4	77	79	74
Number of bond issues	250	414	577	622	4	118	120	108
<i>Included on the quotation lists (issuers/issues)</i>	46/62	69/98	149/207	198/280	1/1	0/0	0/0	2/2

Source: MICEX, RTS.

**Table 11** Trading volumes of corporate bonds on MICEX<sup>18</sup>

Period	Unit of Measure	2005	2006	2007	2008				2008	
		Total	Total	Total	Q1	Q2	Q3	Q4	Total	
Corporate bonds	without REPO	900.4	1801.3	2700.5	500.7	763.0	775.7	564.8	2604.1	
	with REPO	1249.7	3665.1	9374.4	2268.57	3450.7	4433.2	1196.3	11348.8	
Share of REPO transactions in the total volume of corporate bond transactions		%	27.95	50.85	71.19	77.93	77.89	82.50	52.79	77.05

Note: REPO—Repurchase Transactions.

Source: MICEX.

Therefore, as follows from Figure 2 and Table 10, at the present time approximately 95% of all corporate bond issues are offered on the organised market. Additionally, despite the constant growth of the absolute volumes of corporate bond exchange transactions, the rate of growth is decreasing. Thus, while in 2006 the figures doubled in comparison to 2005, (excluding any repurchase agreements), 2007 showed growth of 50%. In 2008, the volume of corporate bond exchange transactions (excluding any repurchase agreements), dropped by 3.5%. The trend that appeared in the last few years demonstrated a sharp increase in the volume of repurchase transactions in the total secondary turnover of corporate bonds. Thus, over the 2 years from 2005 to 2007 this indicator increased 2.5 times and exceeded 70%. In 2008 the trend continued, but in the third quarter the share of repurchase transactions reached 82%. Thus, the organised corporate bonds market, like the stock market, is increasingly used as a money market backed by securities. The fall in the share of repurchase agreements in the fourth quarter of 2008 to 52% is unusual and does not signify a change in market trend. It is a consequence of the financial crisis as it has become apparent in the large numbers of unexecuted deals and the appearance of mutual distrust amongst market participants.

A notable characteristic of the corporate bonds market, and an advantage over the stock market, is the low concentration of its trading volumes. Table 12 contains data on ten issues of bonds, exchange deals with the highest transaction volumes in 2008<sup>19</sup>.

18 Bidding and negotiation mode are included. Initial offerings are not included.

19 Including repurchase agreements.

**Table 12** List of corporate bonds issues that were traded most actively on MICEX (2008)

Nº	Security	Issuer	Share in the total turnover (%)
1	BankMosk-2	OJSC "Bank of Moscow"	4.58
2	RZhD-08obl	OJSC "Russian Railways"	1.91
3	SudostrB-2	LLC "Sudostroitelny Bank"	1.60
4	RZhD-06obl	OJSC "Russian Railways"	1.42
5	FGC UES-02	OJSC "FGC UES"	1.39
6	VTB - 5 ob	OJSC "VTB Bank"	1.37
7	Hydro O GK-1	OJSC "UK HydroOGK"	1.36
8	VTB - 6 ob	OJSC "VTB Bank"	1.23
9	IKS5Fin01	LLC "IKS 5 FINANS"	1.20
10	StrTrGaz03	OJSC "StroyTransGaz"	1.17
<b>TOTAL</b>			<b>17.22</b>

*Calculated according to MICEX data.*

Therefore, the secondary bonds market is much less concentrated on particular instruments, than the stock market. It should be noted that the concentration of corporate bond transactions has a downward tendency: according to the results of the first quarter of 2007, the share of the top 10 most actively traded corporate bonds in the total turnover was 26.1%, and in 2007–20.1%. We should also emphasize that the list of the most liquid corporate bonds is subject to significant changes. Thus, of the 10 issuers listed in Table 11, only 3 were present in a similar list for 2007.

In March 2008, a pilot offering of exchange bonds was placed on the MICEX stock exchange. To issue exchange bonds, it is not necessary to register the issue with the government, nor 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 series of requirements that include:

- the shares of the exchange bonds issuer must be included on the exchange's quotation lists;
- the issuer must have been in business for at least 3 years and must have properly ratified annual financial statements for at least 2 complete fiscal years;
- the date of maturity on the exchange bonds cannot exceed one year after the offering date.

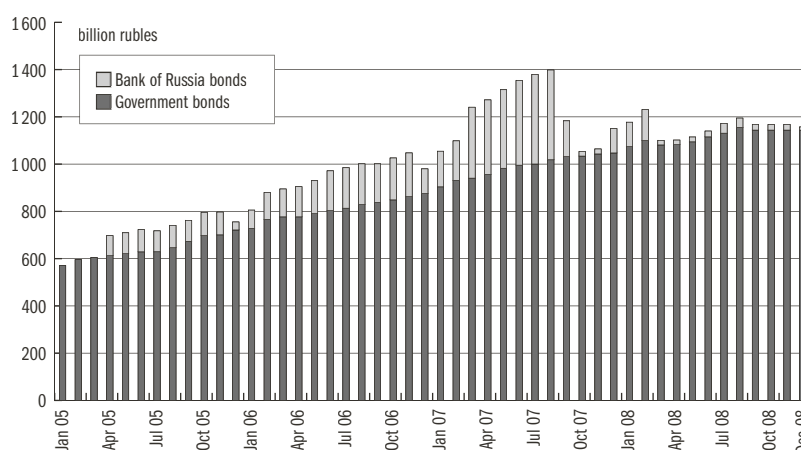
During the year 66 issues of the exchange bonds of eight issuers were registered on MICEX, the total volume of which constituted 159 billion rubles. Initial offerings were carried out with 15 issues of eight issuers to the total sum of 14 billion rubles<sup>20</sup>. Secondary circulation of exchange bonds (including repurchase agreements) came to 106.7 billion rubles, the total volume of trade in corporate bonds was less than 1%.

<sup>20</sup> MICEX data.

### 1.3. Government, sub-federal and municipal bonds and bonds of the Bank of Russia

The first Russian Federation government bonds were issued in 1991. Rapid development of the domestic government bonds (GKO, i. e. Russian Government Treasury Bills and OFZ, i. e. Federal Loan Bonds) exchange market took place between 1993 and 1998, but was interrupted by a default that occurred on 17 August 1998. Since then this market has 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, are not formally government securities, even though they are on the same reliability level. They are short-term securities and are used by commercial banks for liquidity management; other investors are not permitted to buy them. The volume of the government bonds market has been increasing over the past few years (see Fig. 6).

**Figure 6** The volume of the domestic government debt market (at par)



Source: CBONDS.

According to the agency CBONDS, the volume of government bonds circulating on the domestic market at the end of 2008 amounted to 1 144.02 billion rbl. at par, an increase compared to 2007 of 9.2% (for comparison: in 2006, the increase was 21.4%, in 2007—19.6%). At the same time, the volume of the secondary market and the liquidity of government bonds is small compared to those of the corporate bonds market (see Figures 4 and 5). The government securities market is organised at MICEX. Table 13 contains data on the turnover of the government bond market.

**Table 13** Transaction volumes of government bonds

Period	Unit of Measure	2005	2006	2007	2008				2008
		Total	Total	Total	Q1	Q2	Q3	Q4	Total
Turnover	billion rubles	166.2	335.0	491.5	71.6	51.7	75.7	99.1	298.1

Source: CBONDS.

Analysis of Tables 9 and 13 show that despite the comparability of the volumes of offerings at par, the turnover of government securities in comparison to corporate bonds is one order of magnitude lower, consequently, much less an indicator of turnover.

Interest in the government bond market is falling. While growth in the volume of transactions in 2006 was 101%, in 2007 it dropped two-fold to 46.7%. In 2008 a decline in turnover of 40% was observed compared with 2007. It should be noted that there is an irregularity of transaction volumes in government bonds from quarter to quarter in 2008. Thus, while the turnover in the first and third quarters did not differ significantly, an anomaly presents itself when examining the small transaction volume in the second quarter and the sharp increase in turnover in the fourth. This irregularity would seem to be a consequence of the financial crisis.

The volume of Bank of Russia bond issues in 2005–2006, with the exception of a normal December slump, grew at a fast rate; for 2006 the volume rose by 35.2%. However, in 2007–2008 the tide turned dramatically (see Fig. 6). According to CBONDS, as of the beginning of 2008, the total volume of circulating Bank of Russia bonds was 102.9 billion rubles, in February—131 billion, but then towards the end of the year it fell sharply to 12.9 billion rubles.

Bonds subject to the Russian Federation (sub-federal) and municipal bonds are issued in lesser volumes than government or corporate bonds and there are no particular tendencies towards change to speak of (see Fig. 3). According to the agency CBONDS, the volume of sub-federal and municipal bonds circulating on the domestic market as of the end of 2008 amounted to 277.1 billion rbl. at par, a 26% increase compared to the same period of 2007 (for comparison, in 2006 the increase was 18%, and in 2007, 16.%.)

The total transaction volume of sub-federal and municipal bonds for 2005–2008 is shown in Table 14.

**Table 14** The volume of sub-federal and municipal bond transactions

Period	Unit of Measure	2005	2006	2007	2008				2008
		Total	Total	Total	Q1	Q2	Q3	Q4	Total
Total turnover	billion rubles	890.1	682.8	663.5	110.1	149.2	213.1	66.7	539.1
Share of exchange transactions in total turnover	%	70.0	79.9	83.2	86.1	92.3	90.0	58.8	86.1

Source: CBONDS.

Therefore, from Table 14 we can see that the total sub-federal and municipal bond transaction volume is decreasing from one year to the next. In 2006 it dropped 23%, in 2007—3%. In 2008 the fall in turnover amounted to 19%. One should note the sharp fall in the share of exchange transactions in the total turnover that occurred in the fourth quarter.

Exchange trading of sub-federal and municipal bonds takes place on MICEX and RTS. Table 15 contains summary data on sub-federal and municipal bonds offered on Russian stock exchanges, and Table 16 on trading volumes of these bonds on MICEX.

**Table 15** The organised market for sub-federal and municipal bonds

	MICEX				RTS			
	2005	2006	2007	2008	2005	2006	2007	2008
Number of bond issuers	41	50	59	45	2	14	16	10
Number of bond issues	90	105	116	116	16	35	30	21
Included on the quotation lists (issuers/issues)	22/53	22/49	27/49	27/53	1/1	0/0	0/0	0/0

Sources: MICEX, RTS.

As can be seen from Table 14, the tendency towards growth in the number of issuers of sub-federal and municipal bonds on the stock exchanges as observed in 2005–2007 about-turned and in 2008 this number had fallen by 20%.

**Table 16** Trading volumes of sub-federal and municipal bonds on MICEX<sup>21</sup>

Period	Unit of Measure	2005	2006	2007	2008				2008	
		Total	Total	Total	Q1	Q2	Q3	Q4	Total	
Sub-federal bonds	without REPO	billion	556.7	520.1	496.8	87.0	98.6	178.5	35.0	399.1
	with REPO	rubles	773.2	1301.9	2478.2	537.7	707.1	1042.7	287.8	2575.4
Share of REPO transactions in the total volume of sub-federal bond transactions		%	28.00	60.05	79.95	83.82	86.05	82.88	87.84	84.50
Municipal bonds	without REPO	billion	24.0	24.0	28.3	4.5	3.4	3.5	1.7	13.1
	with REPO	rubles	35.03	41.33	84.6	16.33	13.30	18.30	14.70	62.6
Share of REPO transactions in the total volume of sub-federal bond transactions		%	31.52	42.05	66.54	72.22	74.60	80.87	88.44	79.06

Note: REPO—Repurchase Transactions

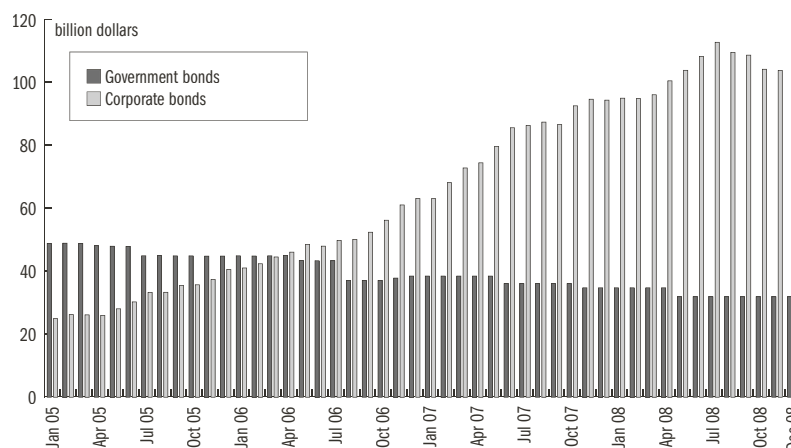
Source: MICEX

Despite the small volumes in circulation, these bonds differ generally by their relatively high liquidity. As a comparative analysis of Tables 9,13, 14 and 16 will demonstrate, notwithstanding the essentially small issue volumes of sub-federal and municipal bonds in 2005–2008, significantly lower than corporate bonds, they show a turnover exceeding that of government securities. The turnover indices for sub-federal and municipal bonds (see fig. 5) are not dissimilar in their values and trends to those of corporate bonds. Also in the past few years the share of repurchase transactions (see Table 16) in the total exchange turnover of sub-federal and municipal bonds has changed considerably: in comparison with 2005, it has on average increased 2.5–3 times, sometimes exceeding 85%. Excluding repurchase agreements, the volumes of exchange transactions of these bonds have shrunk. 2008 saw a reduction in the numbers of exchange transactions with sub-federal bonds of 20%, and in municipal—more than 50%. Thus, the sub-federal and municipal bonds sector, like the stock and corporate bonds markets, is increasingly becoming a money market underwritten by securities.

## 1.4. Eurobonds

Along with ruble bonds, the Russian Federation, subjects of the RF and Russian companies attract capital for their development by way of issuing Eurobonds on foreign markets. Figure 7 contains data showing Eurobond market volumes in various sectors.

<sup>21</sup> Includes bidding and negotiation mode. Initial offerings are not included.

**Figure 7** Eurobond market volumes

Source: CBONDS.

According to CBONDS, the total number of Eurobond issues at the end of 2008 was 137.02 billion dollars, in which 31.9 billion dollars were sovereign (government) Eurobonds, and 103.77 billion dollars—corporate Eurobonds. With this in mind, the volume of Eurobonds issued by subjects of the RF can be considered insignificant, for a continued period has remained on a level a little over 1 billion dollars. It is of note that the volume of corporate Eurobonds first exceeded that of sovereign Eurobonds in March-April 2006.

Sovereign and corporate Eurobonds have demonstrated a fluctuating tendency over the past few years. While the volume of sovereign Eurobonds has had a constant downward trend of about 10% a year, the volume of corporate Eurobonds has exhibited continued growth: in 2005—of 73%, 2006—55%, 2007—49%. In 2008 the rise in the volume of corporate Eurobonds constituted 10% overall, but in the second half of the year this was replaced by a downward trend.

If we were to compare the volume of corporate borrowing on the domestic and foreign markets with the help of debt market instruments, then in 2006–2008 the ratio of domestic to foreign borrowing was on average 35 to 65% and nothing significant has happened to alter this.

## 1.5. Bills of Exchange/Promissory Notes\*

Bills of Exchange/Promissory notes, like securities, were exceptionally popular in Russia in the mid 1990s. They filled a dual role: firstly, that of a money substitute, used for settling accounts between businesses and organisations, and also for paying tax in the case of very low monetisation in the Russian economy. Secondly they are substitute bonds, used for debt financing, an alternative to bank credit. From the end of the 1990s, as instruments of finance these became increasingly ousted by bonds, which were taken to be a more “civilised”, reliable and liquid instrument. However the bill market by its sheer size continues to be one of the most significant elements of the domestic debt market. Thus, by the figures and evaluations of the “Region” Group of companies, at the beginning of 2005 the share of the bill market was 25% of the whole debt market, towards the end of 2007 it had decreased to 16%. In 2008, this ratio didn’t change. Table 17 shows estimates of the volumes of bill issues in circulation and the volumes of bill transactions on the secondary market.

\* translator’s note—there is no differentiation in the Russian language between these two concepts.

**Table 17** Volume and turnover of the bill market in circulation (billion rubles)

Period	2005	2006	2007	2008
<b>Volume of bills in circulation</b>				
	350-370	500	580	570
<b>Average daily turnover of the secondary bill market</b>				
	7-8	10-12	no data	16

Source: "REGION" Group of Companies.

As shown by Table 17, after a spell of active growth in 2006, when in a year the bill market volume increased by 35%, 2007 saw a slowdown in the rate of growth. The volume of the bill market fell slightly in 2008. Activity on the secondary bill market shown in Table 18 was characteristic for the first half of the year. According to the "Region" group, from mid September there were practically no deals on the secondary bill market.

## 1.6. Investment units

The secondary organised market for investment units was solidly grounded by the end of 2007 and has an upward tendency.

Exchange trading of investment units takes place on the stock exchanges MICEX and RTS. Table 18 contains summary data on investment units offered on the Russian stock exchanges, and Table 19—data on exchange trading volumes of investment units.

**Table 18** The organised investment units exchange market

	MICEX				RTS			
	2005	2006	2007	2008	2005	2006	2007	2008
Number of management companies	33	48	88	99	6	10	15	23
Number of UIFs	69	114	219	306	18	22	38	49
<i>Included on the quotation lists (management company/UIFs)</i>	3/4	4/4	20/30	25/43	1/1	3/3	6/7	8/11

Sources: MICEX, RTS.

**Table 19** Investment unit transaction volume on the capital markets

Period	Unit of Measure	2005	2006	2007	2008				2008
		Total	Total	Total	Q1	Q2	Q3	Q4	Total
MICEX	million dollars	43.8	186.0	790.0	248.0	382.0	174.0	146.0	950.0
RTS	million dollars	1.7	30.9	27.9	0.7	2.2	0.8	0.3	4.0
TOTAL	million dollars	45.5	216.9	817.9	248.7	384.2	174.8	146.3	954.0

Source: MICEX, RTS, National League of Management Companies (\*Abbreviation of the Russian often seen in translation and used on their own website: NLU).



The number of UIFs admitted to circulation on the stock exchanges has grown considerably over the past few years (in 2006 growth exceeded 60%, in 2007—over 90%). In 2008 the growth was less, about 40% towards the beginning of the year. By and large, at the present time around 30% of all functioning UIFs are offered on the stock exchanges. Exchange turnovers of investment units grew very fast from 2005–2007: in 2006 they increased by 4.7 times, 3.7 in 2007. In 2008 the growth in exchange transaction volumes of UIFs was 16%. Thus comparing to previous years, the rate of growth in exchange transaction volumes of UIFs fell sharply, the general depreciation of assets in unit investment funds playing its role in this. Although certainly not all UIF investment units are distinguished by their high liquidity, the concentration of transactions with investment units is very high: in 2007, the share of the top ten most liquid UIFs accounted for more than 80% of the total turnover of investment units, in 2008 this dropped to 71%.

## 1.7. Futures and options on securities and stock indices

At the present time fixed-term instruments, whose underlying assets are securities and stock indices, are concentrated on the derivatives market RTS FORTS. Besides these fixed-term instruments, gold, currency, oil and other contracts are also traded on FORTS, however the relative trading volume of these contracts is not significant and, depending on the type of volume indicator, constitutes no more than 4–7%, although this share is growing.

The instrument base of the derivatives market is becoming increasingly complex. In 2006, FORTS offered 18 types of derivatives contracts (12 futures and 6 options), the underlying asset of which are securities and stocks indices. By the end of 2007, their number increased to 53 (36 futures and 17 options), and in 2008 this reached 88 (38 futures and 50 options). Thus, the number of types of derivative contracts based on securities and stocks indices has been growing over the past few years (this increase was 194% in 2007, and 66% in 2008). A notable characteristic is that while in 2006–2007 the ratio of futures to options was on average, 65 to 35%, the options share increased in 2008: 43 to 57%.

In mid 2007 the stock exchange MICEX introduced its first stock asset derivative contract—futures on the MICEX index. The transaction volumes for this instrument, however, remain low: trade volume at the end of 2007 was 1.76 billion rubles, in 2008—0.86 billion.

Tables 20 and 21 summarise FORTS data on fixed-term instruments linked to stock assets for 2005–2008.

**Table 20** Summary of FORTS trading for securities and stock indices contracts

Period	2005	2006	2007	2008				2008
	Total	Total	Total	Q1	Q2	Q3	Q4	Total
<b>Futures Contracts</b>								
Trade volumes, billion rubles	607.8	2397.1	6052.4	2553.8	2710.9	2648.5	900.3	8813.6
<i>Incl. on index</i>	119.8	752.0	3587.1	2048.3	2199.1	2260.9	771.8	7280.1
<i>Incl. on stocks</i>	471.0	1569.6	2389.2	501.8	510.9	387.5	128.4	1528.6
<i>Incl. on bonds</i>	9.0	13.7	29.3	3.7	0.9	0.0	0.1	4.8
Trade volumes, million contracts	46.0	78.9	114.6	41.9	44.9	49.7	36.9	173.3
<i>Incl. on index</i>	2.3	9.0	34.7	20.7	20.5	26.4	20.3	87.9
<i>Incl. on stocks</i>	42.6	66.3	75.5	20.8	24.3	23.3	16.6	85.0
<i>Incl. on bonds</i>	0.8	1.3	2.8	0.4	0.1	0.0	0.0	0.5
No. of transactions, million pcs	1.8	4.9	11.3	5.3	5.5	7.0	9.6	27.4
<i>Incl. on index</i>	0.1	0.7	4.3	2.9	3.1	4.5	6.5	17.1
<i>Incl. on stocks</i>	1.7	4.1	7.0	2.4	2.4	2.5	3.1	10.3
<i>Incl. on bonds</i>	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Options contracts</b>								
Trade volumes, billion rubles	79.3	311.4	1300.2	513.9	605.5	546.3	74.2	1739.9
<i>Incl. on index</i>	2.6	84.3	758.7	341.2	312.6	363.3	50.0	1067.1
<i>Incl. on stocks</i>	76.6	226.9	541.4	172.7	292.9	183.0	24.2	672.7
<i>Incl. on bonds</i>	–	–	–	–	–	–	–	–
Trade volumes, million contracts	7.3	10.7	25.0	10.9	17.3	14.1	3.0	45.2
<i>Incl. on index</i>	0.0	1.0	7.1	3.4	3.0	4.1	1.0	11.4
<i>Incl. on bonds</i>	7.2	9.7	17.8	7.5	14.3	10.0	2.0	33.8
<i>Incl. on bonds</i>	–	–	–	–	–	–	–	–
No. of transactions, million pcs	0.1	0.2	0.3	0.1	0.2	0.3	0.1	0.7
<i>Incl. on index</i>	0.0	0.0	0.1	0.1	0.1	0.2	0.1	0.5
<i>Incl. on bonds</i>	0.1	0.1	0.2	0.1	0.1	0.1	0.0	0.2
<i>Incl. on bonds</i>	–	–	–	–	–	–	–	–
<b>Total</b>								
Trade volumes, billion rubles	687.1	2708.5	7352.6	3067.7	3316.4	3194.8	974.5	10553.5
Trade volumes, million contracts	53.3	89.6	139.6	52.7	62.2	63.7	39.9	218.5
No. of transactions, million pcs	1.9	5.0	11.6	5.4	5.7	7.3	9.7	28.1

Source: RTS.

As follows from Table 20, the derivatives market FORTS experienced a period of spasmodic growth in 2006: the total transaction volume in monetary terms increased almost fourfold, the number of contracts by

68% and the number of transactions grew by 164%. In 2007 the growth continued: the trading volume of fixed-term instruments in monetary terms increased by 170%, and the number of contracts by 56%, the number of concluded transactions increased by 130%. In 2008 the growth in trading volume increased to a lesser extent: in monetary terms by 44%, the number of contracts—by 56%, and growth in the number of transactions remained the same—142%. The ratio of trading volume of futures and options stayed at the level of 2005–2007: futures accounted for over 80% of trading volume and 97% of deals.

It should be noted that in the fourth quarter of 2008 there was a fall in the volume indicators for the derivatives market: the trading volume in monetary terms dropped in comparison with the previous quarter by 70%, the number of contracts by 37%. At the same time the number of transactions increased by 32%.

It is also a characteristic that in the fourth quarter the situation with options altered sharply: in comparison with the previous quarters the trading volume in monetary terms, the number of contracts and also the number of transactions fell sharply. The drop constituted 65–85% depending on the type of indicator. In all likelihood this is a reaction to increasing market volatility, when investors are painstakingly evaluating acceptable options premiums.

Interest towards fixed-term contracts is growing constantly on the stock indices. While in 2005 the trading volume of these contracts was 18% in monetary terms, in 2007 this indicator rose to 60%. In 2008 the trading volume of contracts on the stock indices became definitive and reached 80% of the total volume of the FORTS derivatives market, whereas the turnover of contracts for stocks fell sharply (a drop of around 30%) and more still for bonds (a fall of around 80%).

If we compare the market volumes of fixed-term contracts, the underlying assets of which are stocks and stock indices, and the volumes of the stocks spot market, excluding repurchase agreements (see Table 7), then their ratio is growing steadily: in 2005 it was 15.4%, in 2006—21.2%, in 2007—46.3%, and in 2008 it reached 82.8%.

On the derivatives market the volume of open positions and their distribution amongst various instruments (see Table 21) has changed significantly. This Table contains data on the average volume of open positions—the mathematical mean of daily open positions for the period.

**Table 21** Open Positions on the derivatives market FORTS for securities and exchange indices contracts

Period	2005	2006	2007	2008			
				Q1	Q2	Q3	Q4
<b>Futures Contracts</b>							
Average volume of open positions, billion rubles	11.5	34.6	74.7	57.2	60.7	59.8	10.9
<i>Incl. on index</i>	0.6	7.9	33.5	26.9	28.6	32.2	5.8
<i>Incl. on stocks</i>	9.5	20.9	38.9	29.6	31.7	27.6	5.1
<i>Incl. on bonds</i>	0.7	1.6	2.3	0.6	0.5	0.1	0.0
Average volume of open positions, million contracts	1.0	1.2	1.9	1.9	2.2	2.3	0.9
<i>Incl. on index</i>	0.0	0.1	0.3	0.3	0.3	0.4	0.2
<i>Incl. on stocks</i>	0.9	0.9	1.3	1.5	1.8	1.9	0.8
<i>Incl. on bonds</i>	0.1	0.1	0.2	0.1	0.0	0.0	0.0
<b>Options contracts</b>							
Average volume of open positions, billion rubles	6.5	30.0	117.3	154.6	207.9	183.8	47.5
<i>Incl. on index</i>	0.2	9.0	71.7	103.0	122.0	126.2	38.3
<i>Incl. on stocks</i>	6.3	20.9	45.5	51.6	86.0	57.6	9.3
<i>Incl. on bonds</i>	–	–	–	–	–	–	–
Average volume of open positions, million contracts	0.6	1.0	2.3	3.1	5.3	4.6	1.1
<i>Incl. on index</i>	0.6	0.9	0.7	1.0	1.3	1.4	0.6
<i>Incl. on stocks</i>	0.0	0.1	1.6	2.1	4.0	3.2	0.5
<i>Incl. on bonds</i>	–	–	–	–	–	–	–
<b>Total</b>							
Average volume of open positions, billion rubles	18.0	64.6	191.9	211.8	268.6	243.7	58.4
Average volume of open positions a year, million contracts	1.6	2.2	4.2	5.0	7.5	6.8	2.0

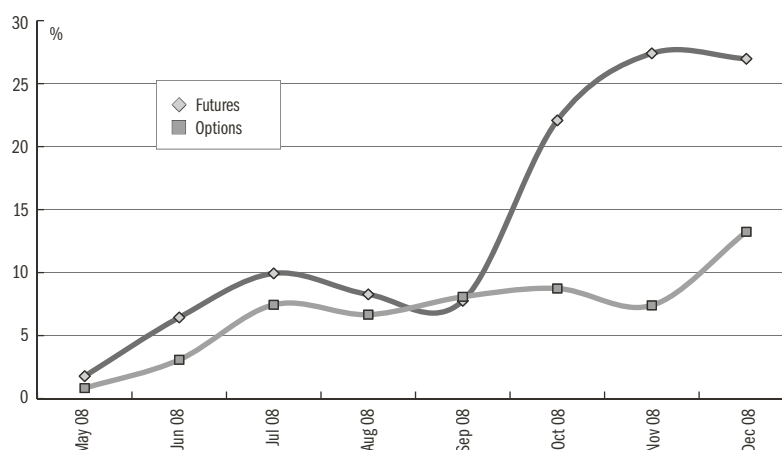
Source: RTS.

Thus, while in 2005 futures made up 64% of the total volume of open positions, the volume of open positions with futures subsequently began to decrease: 2006–54%, 2007–38%. In 2008 the volume of open positions with futures dropped to 18%, consequently options contracts make up more than 80% of open positions on the derivatives market FORTS. Thus, for the last few years options strategies have become more utilized in market risk management.

In the fourth quarter, in comparison with the previous quarters, the volume of open positions dropped sharply. Futures contracts decreased more than fivefold, options—approximately fourfold. Therefore, in the then current conditions of steeply growing market volatility, investors preferred to close previously open positions.

The volume ratio of open positions to the volume of futures and options transactions shows significant discrepancies. Whilst the ratio for futures (according to data for 2005–2008) spans from 1 to 5%, the options ratio in 2007 decreased quarterly from 55% in the first quarter to 16% in the fourth. In 2008 there was a contrary trend—this ratio grew from 30% in the first quarter to 64% in the fourth.

In May 2008 evening trading sessions were introduced on FORTS (for more information see section 2.3b). Figure 8 shows a graph of relative volumes of trade of these evening sessions.

**Figure 8** Trading volumes for the evening sessions on the derivatives market FORTS (monthly)

Source: RTS.

The share of transactions per 24 hours that took place during the evening sessions stands out by its great variability; nevertheless on separate days it exceeded half of the total trading volume. In general the mean trading volumes of the evening sessions is 10.9% for futures, for options—5.6%. We can note that from the date the evening sessions were introduced to the end of 2008, there has been a trend toward growth in the trading share of evening sessions. This mode can therefore be said to have a following amongst investors.

## 1.8. Stock Indices

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

Traditionally, however, the most quoted indices are those put together by RTS and MICEX.

The RTS Index has been calculated since 1995. It is a consolidated index currently based on 50 stocks of the most capitalised and liquid issuers. The list of stocks for indices calculation is revised once every three months. Besides the main RTS Index, the RTS Stock Exchange has calculated RTS-2, an index of “second tier” company stocks since 2003. Since 2005–2007 industry indices have also been calculated:

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

The prices of securities as calculated for the RTS indices are given in US dollars.

The MICEX Index has been calculated since 1997 and is a consolidated index currently based on 30 issuers’ stocks that represent the main sectors of the economy. The index basket is updated twice a year.

The MICEX stock exchange also began calculating industry and capitalisation indices in 2005–2007:

1. MICEX O&G—oil and gas stock index
2. MICEX PWR—electric power stock index
3. MICEX TLC—telecommunication stock index
4. MICEX M&M—metallurgical and mining stock index
5. MICEX MNF—mechanical engineering stock index
6. MICEX LC—large cap stock index
7. MICEX MC—mid cap stock index
8. MICEX SC—small cap stock index

The MICEX Stock Exchange added another industry index in September 2008, the MICEX FNL—a financial-banking stock index.

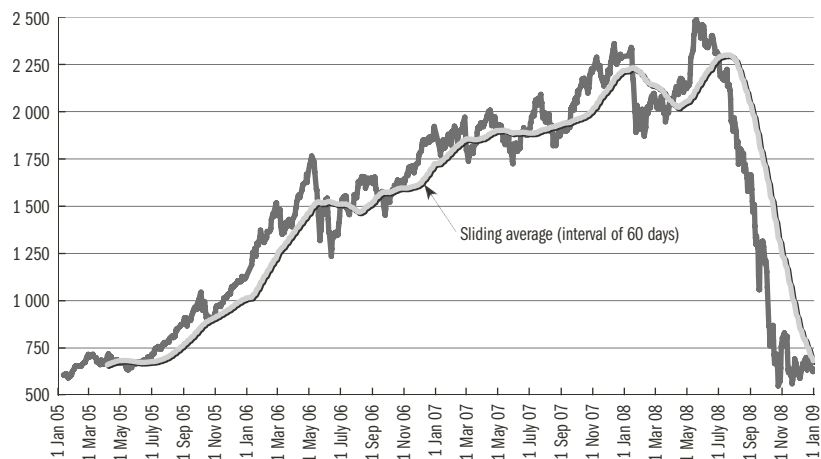
The prices of securities as calculated for the MICEX indices are given in Russian rubles.

Among the industry indices maintained by various stock exchanges, a clear parity base for calculation (concurrence 75–80%) can be observed for oil and gas industry indices (RTSog, MICEX O&G), telecoms (RTStl, MICEX TLC), power (RTSeu, MICEX PWR), metallurgy and mining (RTSmm, MICEX M&M), and also the financial-banking industry (RTSfn, MICEX FNL). The RTSin and MICEX MNF indices demonstrate somewhat lesser conformity.

Figures 9, 10 and 11 show graphs of the RTS, MICEX and RTS-2 indices.

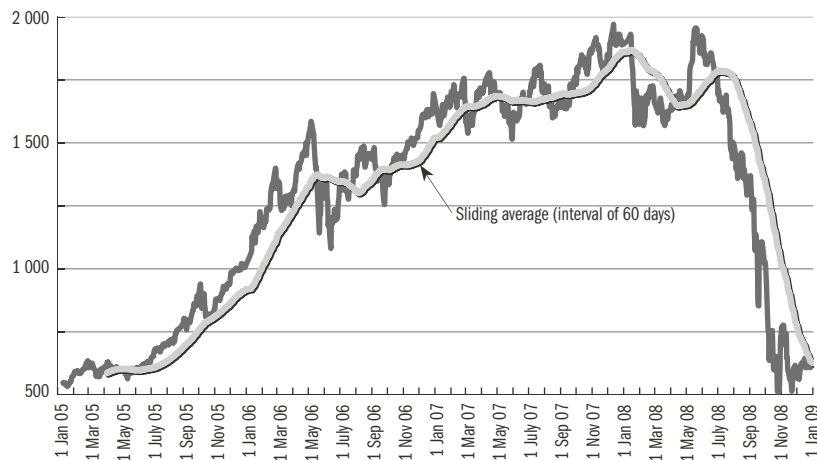
Table 22<sup>22</sup> shows profitability data on the RTS and MICEX indices over the past few years.

**Figure 9** RTS Index

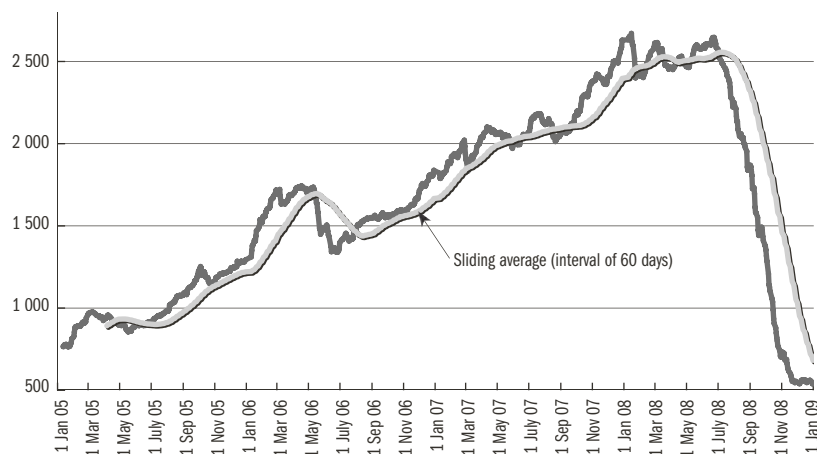


Source: RTS.

22 Profitability was calculated at intervals from the last day of trading of the previous year to the last day of trading of the period to be evaluated on the basis of 365 days.

**Figure 10** MICEX Index

Source: MICEX.

**Figure 11** RTS-2 Index

Source: RTS.

As follows from these graphs, the consolidated indices RTS and MICEX generally show very similar behaviour. The significant growth of these indices, which began in 2005, started slowing down in 2007. In the first half of 2008, they went through two phases of a diametrically opposed behaviour. The first—a fall for 7 consecutive trading days from 15 January to 23 January (the RTS Index dropped by 19.2%, and the MICEX Index—18.7%). Then, on 24 January, the steepest increase in the period in question occurred (the RTS Index rose by 5.2% and the MICEX by 5.8%).

The second phase was one of growth. The RTS Index demonstrated constant growth for 11 trading days in a row, from 4 May to 19 May, resulting in a 17.2% rise. For MICEX this phase was shorter, from 6 May to 14 May, with 12.8% growth. On 19 May the consolidated stock indices achieved historic maximums (RTS—2487.92; MICEX—1956.14).

Between these two phases, there was a sustained lateral trend of high volatility. The first half of 2008 ended on a downturn for composite indices.

In the second half of the year the fall in the consolidated stock indices continued and became a steep drop. The indices achieved maximum value on 24 October (RTS—549.43, MICEX—513.62). Thus the maximum and minimum values of the composite stock indices differ fourfold.

**Table 22** Stock indices profitability (% per annum)

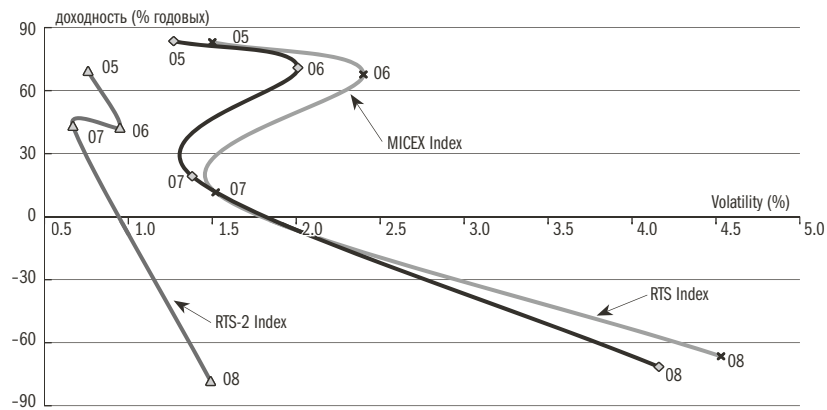
	2005	2006	2007	2008
<b>Composite indices</b>				
RTS Index	83.52	70.94	19.23	- 71.48
MICEX index	83.08	67.69	11.57	- 66.47
RTS2 Index	69.32	42.27	43.17	- 78.29
<b>Industry indices</b>				
Oil and Gas industry				
<i>RTSog</i>	86.78	50.80	1.05	- 65.76
<i>MICEX O&amp;G</i>	91.95	47.95	-3.57	- 58.42
Telecoms				
<i>RTStl</i>	40.78	81.47	28.13	- 72.74
<i>MICEX TLC</i>	39.10	65.98	14.56	- 75.55
Metallurgy and mining				
<i>RTSmm</i>	53.18	52.42	54.00	- 74.50
<i>MICEX M&amp;M</i>	74.60	51.69	42.61	- 71.96
Electric Power				
<i>RTSeu</i>			31.96	- 80.33
<i>MICEX PWR</i>	38.68	134.51	7.87	- 73.72
Industry				
<i>RTSin</i>	40.50	73.76	66.83	- 84.30
<i>MICEX MNF</i>	28.90	69.62	60.57	- 85.72
Consumer goods				
<i>RTScr</i>	92.51	51.24	29.31	- 79.54
Finances				
<i>RTSfn</i>			14.30	- 78.37
<i>MICEX MNF</i>				- 67.32
<b>Capitalisation indices</b>				
MICEX LC			9.89	- 66.47
MICEX MC			15.64	- 71.69
MICEX SC			29.17	- 76.09

Calculated from RTS and MICEX data .

While in 2007, despite an evident slowdown, the majority of indices (as seen in Table 22) nevertheless showed a positive profitability; in 2008 all the indices analysed experienced a sharp fall. The composite indices dropped by 66–78% annually. Amongst sector indices, industry was most badly hit with up to an 85% drop per annum.

Russian stock indices are characterised by high volatility. In 2008 this volatility grew still more. The maximum fall of the composite stock indices in a single day was on 6 October and was 18–19%. The maximum growth in a single day was recorded on 19 September and amounted to 24–28%. Figure 12 demonstrates the behaviour of the composite indices on a “profitability-volatility” plane.



**Figure 12** Profitability and volatility of composite stock indices profitability (% per annum)

Calculated from MICEX and RTS data.

As Figure 12 demonstrates, the behaviour of the indices in 2008 was anomalous—in sharply growing volatility a deep drop in profitability occurred. This is evidently a consequence of the financial crisis.

## 2. Institutional Structure

### 2.1. Issuers

In Russia there are no precise statistics relating to issuers of securities. Any joint stock company is an issuer as it floats stocks at the moment it is founded (and is required to register them). A limited liability company, and, in some cases, a non-profit organisation can also be an issuer of bonds. Data from SPARK and RusBonds relating to issuers of securities is presented in Table 23. Composite data on the number of issuers on organised markets is displayed in Table 24.

**Table 23** Issuers of Securities

	2005	2006	2007	2008
Number of issuers of shares and bonds	460 431	471 158	481 591	487 996
<i>Of those JSCs</i>	62 960	64 431	65 706	66 466
Number of issues of shares and bonds	463 670	474 484	483 962	491 415

Source: Interfax (Database SPARK, RusBonds).

**Table 24** Issuers on the organised stock market

	MICEX				RTS			
	2005	2006	2007	2008	2005	2006	2007	2008
Number of issuers (of stocks and bonds)	385	539	670	632	262	332	354	329
<i>included on the quotation lists</i>	93	127	229	255	46	64	88	92

Source: MICEX, RTS.

According to estimates, the stocks of approximately 40 issuers also circulate as depository receipts on foreign stock exchanges.

Therefore, only around 1% of all stocks and bonds issuers are represented on the organised markets. On the whole, as Table 24 shows, the number of issuers on the organised market in 2005–2007 grew steadily, however in 2008 the trend changed and the number of issuers represented on the exchanges dropped by 5–7%.

#### Public offerings

The floatation of most stocks currently traded on the Russian stock exchanges came about as a result of the privatisation process in the 1990s. The first public offering of Russian stocks abroad was in 1996, and on the Russian exchanges—in 2002.

In 2006–2007 the volumes of public offerings of Russian companies increased dramatically (see Table 26). At this time Russia occupied a leading position globally for the total volume of placements, as

well as for the capital volumes raised by a single company. It is necessary, however, to point out, that such growth was caused, not as a result of a massive insurgence of new companies onto the market, but due to the large scale stock placements of several companies, mainly those in which the government played a role or which were supported by the government. Amongst the biggest public offerings at that time were the so-called “People’s IPOs” OJSC “NK Rosneft” (10.4 billion dollars), OJSC “Sberbank” (8.8 billion dollars) and OJSC “VTB Bank” (7.9 billion dollars).

In 2008 on a backdrop of liquidity deficit and world financial market dynamics that were hard to predict, IPOs of Russian companies as good as stopped. Many companies which had previously announced their plans to float their shares, cancelled, deferred the plan to a much later date or turned instead to private offerings.

**Table 25** Russian IPOs

Period	2005	2006	2007	2008
Volume of offerings (billion dollars)	4.55	17.98	23.6	1.7
Incl. on the domestic market (%)	6	36	44	no data
Number of companies	13	24	25	7

Sources: *Offering.ru/IPO in Russia project, Alpha Bank, Ernst&Young, The PBN Company.*

It should be noted that one of the companies that performed an IPO in 2007, stated in October 2008 its intention to remove its shares from public circulation on Russian exchanges.

In 2007–2008 alternative trading platforms were created on MICEX and RTS for the release of securities of innovational companies and companies of small capitalisation onto the open market. The number of issuers and trading volumes on these platforms is negligible.

Also in 2007–2008 a regulatory-legislative framework was created to facilitate the placement and circulation of foreign issuers’ securities on Russian trading platforms. However there were no such placements.

## 2.2. Investors

By investors we mean any individuals or institutions that invest funds in securities with a view to making a profit. Official systematised data on the structure and quantitative characteristics of the Russian capital market investor base does not yet exist, however, recently securities market professionals, self-regulatory organisations and research groups have begun work on listing and studying Russian investors.

### a) Public

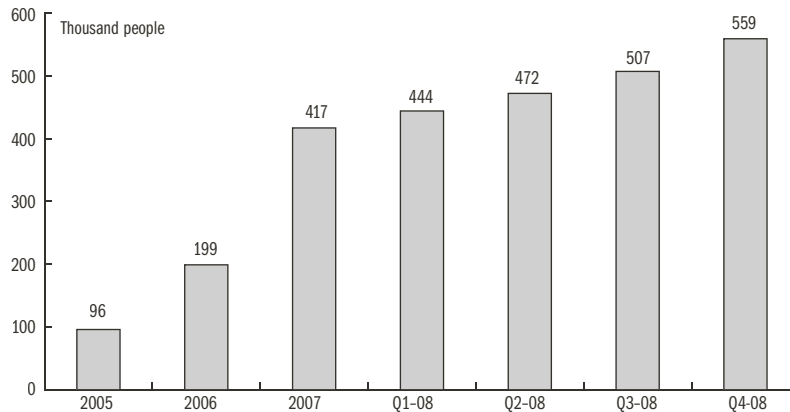
Here, the term public includes “market investors”—individuals who have deliberately decided to work independently on the capital market and who periodically use the services of brokers or trust managers, or individuals who have acquired units in UIFs. Such investors differ from those individuals who acquired stocks as a result of voucher privatisation, or from shareholders of voucher investment funds or mutual (unit) fund shareholders who emerged as a result of the conversion of voucher investment funds. Such investors are not included in this category.

There are no complete and reliable statistics regarding the number of the individuals who operate on the Russian securities market. It is possible to create the following far from complete picture by compiling data from various disparate sources.

Since 2005 MICEX has been regularly publishing data on the number and format of their trading clients, including individuals (hereafter referred to as “MICEX clients”). It should be noted that in mid 2007 MICEX changed the way they list clients in favour of a more exact method that takes into account individual identifying attributes (unique clients).

Figure 13 shows data on the number of clients—individuals working on MICEX, calculated using MICEX’s new methods and commencing from 2005.

**Figure 13** Russian public investment on the securities market (MICEX clients)

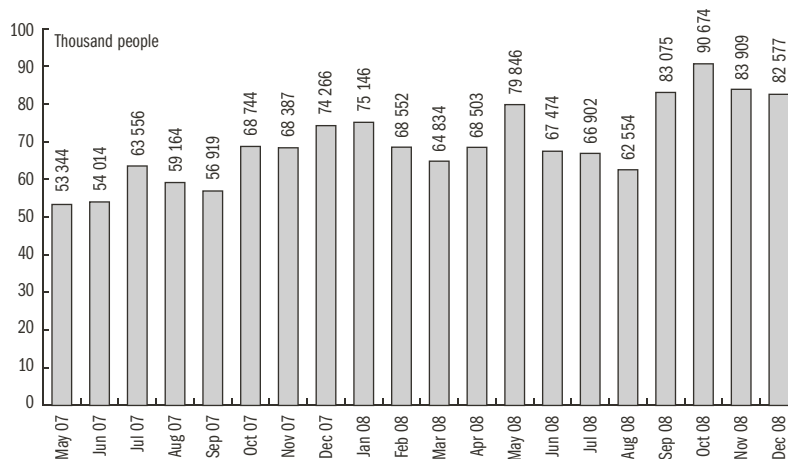


Source: MICEX.

In 2006 growth in the number of MICEX ‘individual’ clients constituted 108%. The calculated growth for 2007 was similar—109%, however if we exclude individuals who were involved in the IPO of OJSC “VTB Bank”, then the growth was approximately 60%. Starting from the third quarter of 2007, the growth rate of MICEX individual clients dropped to 5–7% quarterly. At the end of 2008 the increase constituted 34%. Thus, despite the severely worsening market conditions, it would seem that the public is not losing interest in the capital market.

An important characteristic of the private investor base is the number of so-called active investors, that is those who make at least one deal per month on the stock exchange. Figure 14 shows the data available on active investors on MICEX.

**Figure 14** The number of active clients on the MICEX stock exchange



Source: MICEX.

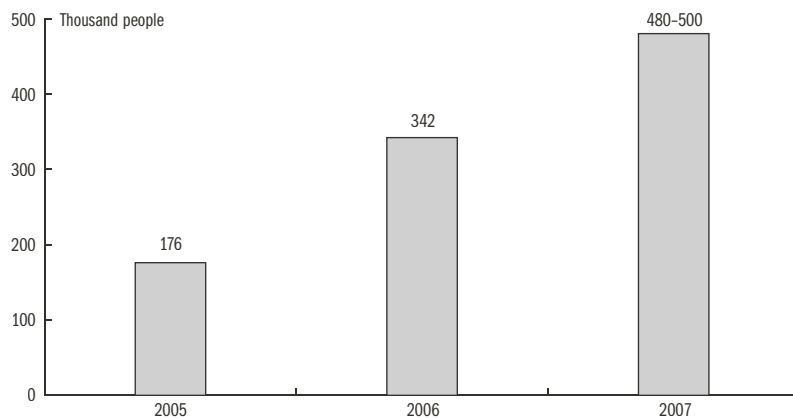
Therefore, as follows from Figures 13 and 14, active individual investors account for 13–14% of MICEX’s unique client base. It is remarkable that the number of active MICEX clients is very close to the difference between the total number of MICEX client accounts and the number of its unique clients. This difference corresponds to the segment of client base that, for example, use the services of more than one broker.

Between May 2007 (when data on the number of active clients began to be published) and the end of 2007, the number of active clients rose by 40%. At the same time, there was a lull in activity in August—September, which can be explained both by the holiday period and by the adverse conditions on the securities market.

In 2008 no long-term trend for change in the number of active clients was noted. The median value stabilised at 72 thousand people. In January, May and October there were growth spurts that coincided with positive and negative market trends.

The National League of Management Companies has been professionally estimating the number of accounts of “market” UIF stockholders (see Figure 15) with non-zero accounts, since 2002.

**Figure 15** Russian public investment in the securities market (UIF customers)



Source: NLU (National League of Management Companies).

According to these estimates, the growth in the number of the UIF stockholders constituted 94% in 2006, and around 40% in 2007.

There is no data for the number of “market” shareholders available for 2008.

In 2006–2007 a new extensive group of private investors appeared—private individuals who participated in the so-called “People’s IPO” of OJSC “NK Rosneft”, OJSC “Sberbank” and OJSC “VTB Bank”. According to the mass media and to data supplied by the issuing companies, the total number of such individuals was approximately 115 thousand for the Rosneft offering, 30 thousand for the OJSC “Sberbank” offering and 131 thousand for the OJSC “VTB Bank” offering.

### b) Investment funds

From a legal perspective, unit investment funds are asset portfolios without the incorporation of a legal corporate body. Table 26 shows summarised data on the dynamics of change in the numbers of UIFs in the past four years.

**Table 26** Number of Unit investment funds<sup>23</sup>

Type of UIF	Period			2008			
	2005	2006	2007	Q1	Q2	Q3	Q4
Opened-end	201	299	455	487	486	486	450
Interval	59	86	95	101	101	100	94
Closed-end	121	234	398	466	468	481	476
<i>Of which—real estate</i>	73	152	269	335	336	351	350
<b>TOTAL</b>	<b>381</b>	<b>619</b>	<b>948</b>	<b>1054</b>	<b>1055</b>	<b>1067</b>	<b>1020</b>

Source: NLU (National League of Management Companies)

By the end of 2007 there were 948 functioning UIFs in Russia, 53.2% more than in the beginning of the year. Considering that in 2006 growth in the number of UIFs was 60.7%, it is necessary to note that in 2007 this growth rate decreased somewhat. In the first half of 2008 the number of UIFs hardly changed. This does not signify the consequence of any market trends, however. Rather, in 2008 some amendments to the law “Investment funds” were introduced, but the necessary legislative enforcements were delayed, thus also delaying the registration of new funds. In the second half of the year the number of UIFs tended to drop, so, for the fourth quarter the number of opened-end funds had fallen by 7%. In general for 2008 the total increase in the number of funds amounted to 7.5%, explained by the growing number of closed-end funds.

Table 27 contains summary data on the change dynamics of the net asset value of UIFs over the past four years.

**Table 27** Net asset value of UIFs (billion rubles)<sup>24</sup>

Type of UIF	Period			2008			
	2005	2006	2007	Q1	Q2	Q3	Q4
Opened-end	30.8	91.1	134.8	124.2	118.5	81.1	47.1
Interval	38.7	59.6	43.8	38.6	39.3	28.1	13.2
Closed-end	163.4	268.1	604.2	634.1	684.6	676.9	585.7
<i>Of which—real estate</i>	24.9	69.0	189.9	223.1	251.8	266.7	261.3
<b>TOTAL</b>	<b>233.0</b>	<b>418.8</b>	<b>782.8</b>	<b>797.0</b>	<b>842.5</b>	<b>786.1</b>	<b>646.0</b>
Net asset value/GDP (%)	1.08	1.56	2.37				1.55

Source: Federal State Statistic Service (FSSS), NLU (National League of Management Companies).

The net asset value of UIFs as of the end of 2007 was 782.8 billion rbl.—an increase of 87% on the beginning of the year. In 2006, growth constituted 80%. Towards the end of 2008 the net asset value of UIFs fell by 136 billion dollars in absolute terms, or by 17.5% relative to the beginning of the year. Thus for the first time in several years a considerable devaluation of UIF asset value was observed. Opened-end and interval funds were the most affected (a fall of 65–70%). For closed-end funds there was a less tangible drop—about 3%. That said, the asset value of real estate funds rose by 38% that year.

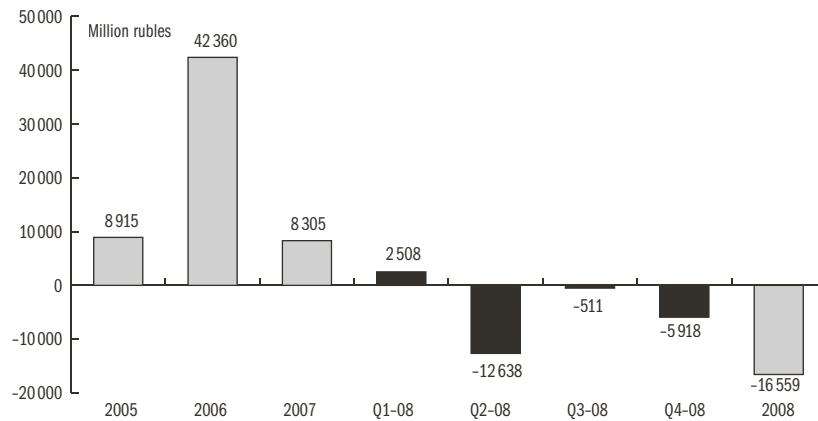
Overall in comparison with GDP the net asset value of UIFs over the past few years has been, and remains insignificant (1–2.4%). If one takes into account only opened-end and interval UIFs, then the ratio of net asset value to GDP will be less—0.15–0.55%.

<sup>23</sup> Only completely formulated funds are included in the statistics.

<sup>24</sup> Only completely formulated funds are included in the statistics.

Besides the net asset value, an important characteristic of UIFs is the volume of net capital invested into the funds. The most telling statistics are for opened-end UIFs, where applications for unit issues and redemptions are accepted daily. Figure 16 shows statistics on net raised capital in opened-end UIFs.

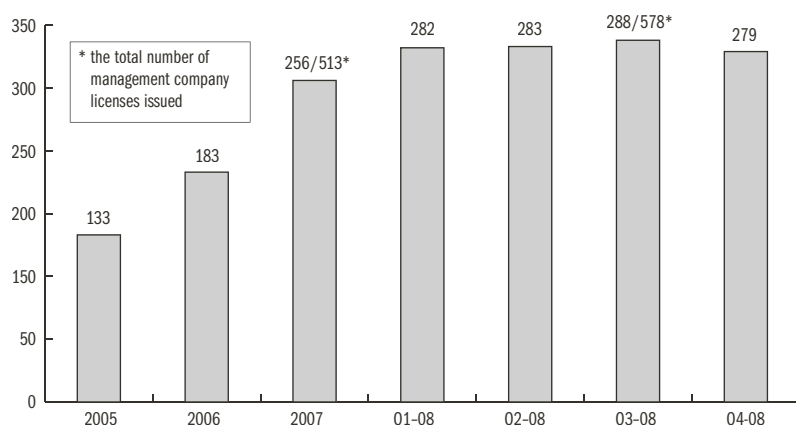
**Figure 16** Volume of net raised capital in opened-end UIFs.



Source: NLU (National League of Management Companies).

As is evident from Figure 16, 2006 set the record for net funds raised over the last four years—the volume of net capital raised amounted to 42.4 billion rubles. In 2007 there was a significant cash inflow in the first quarter and an outflow in fourth; summarily over the year the volume of the net raised capital amounted to only one fifth of the previous year, 8.3 billion rubles. In the first half of 2008 there was a characteristic cash inflow in January and a steady outflow in February to June; in May, at a time of market uptrend, outflow (evidently a result of official financial accounting) was very significant. In the second half of the year a considerable outflow of capital (approximately 6 billion rubles) was seen in the fourth quarter. As a result, the balance of invested capital into opened-end UIFs was negative—minus 16.6 billion rubles. So, the overall net asset value of opened-end UIFs depreciated by 87.7 billion rubles, about 20% accounted for by investors withdrawing funds.

A key element in the structure of a UIF is its management company. Figure 17 depicts composite data on the number of management companies working with UIFs over the last four years.

**Figure 17** The number of the management companies working with UIFs

Source: The Federal Financial Markets Service (FFMS), National League of Management Companies (NLU)

In 2006 the number of management companies controlling UIFs increased by 36.6%, and in 2007 by 39.9%. The growth statistics of 2006–2007 were remarkable against changes in the other spheres of professional activity on the securities market and demonstrated the great interest towards collective investments of the period. In the first half of 2008 the growth in the numbers of management companies controlling UIFs ceased, and towards the end of the year this figure dropped. This is most likely linked to the suspension of new UIF registration and to manifestations of the economic crisis on the financial markets. Approximately half of the organisations that have management company licenses are involved in managing UIFs. The rest concentrate solely on managing private pension fund assets and on other projects. There are also companies that are not active in the market at all.

### c) Bank-managed mutual funds

Bank-managed mutual funds (BMMF) are an investment product that credit organisations offer based on instructions issued by the Bank of Russia<sup>25</sup>. A BMMF is acknowledged as a property portfolio that consists of property given to trust management by various entities, as well as the property acquired by the trust manager in the course of exercising the trust management. BMMFs are viewed legally similarly to UIFs, however participation in them is not assured by a security and the level of protection of the participants' interests is lower. The investor, by investing into BMMFs, receives a so-called Participation Certificate, which is not a security. Requirements as to the composition and structure of BMMF assets are less restrictive than they are for UIFs. According to existing information, around 30 credit organisations are involved in BMMF management. Statistics for the number of funds and their net asset values for the past four years are shown in Table 28<sup>26</sup>.

25 Central Bank instruction of 02.07.97 "The procedure for conducting trust management transactions and the book-keeping of these operations by credit organisations of the Russian Federation".

26 Data on BMMFs for 2005-2008 were revised by investfunds.ru in connection with the introduction of a more detailed method used to collect information.



**Table 28** Bank-managed mutual funds

Period	2005	2006	2007	2008			
				Q1	Q2	Q3	Q4
Number of funds	173,0	239,0	273,0	272,0	289,0	293,0	291,0
of which—ruble funds	120,0	170,0	201,0	200,0	211,0	216,0	215,0
of which—foreign currency funds	53,0	69,0	73,0	72,0	78,0	77,0	76,0
Net asset value (billion rubles)	7,9	17,1	21,1	18,1	17,0	9,8	7,5

Source: *investfunds.ru*.

As is clear from Table 28, BMMFs stand below UIFs both in terms of the number of funds, just as in regard to their total net asset value. While in 2006 there was growth in BMMFs (their number increased by 38%, and their net asset value by 118%), in 2007 growth was highly insignificant (14 and 23% respectively). In 2008 growth in the number of BMMFs came to a halt (an increase of 7%), and their net asset values dropped from the beginning of the year by 13.6 billion rubles (around 65%). Summarised data on the number of BMMF investors is not disclosed, though some experts estimate it at 30,000 (for 2006–2007).

#### d) Private (non-state) pension funds (PPF)

According to the FFMS<sup>27</sup>, at the end of 2007, 253 organisations held valid private pension fund licenses, of which 126 funds were eligible to work in mandatory pension insurance. Towards the end of 2008 the number of valid private pension fund licenses fell to 241, and the number of funds with eligibility regarding mandatory pension insurance increased to 136. Information on private pension fund assets linked to the private pension surety (pension reserves) and to mandatory pension insurance (pension savings) is presented in Table 29.

**Table 29** Investment resources for private pension funds (billion rubles)

Period	2005	2006	2007	2008			
				Q1	Q2	Q3	Q4
Pension reserves	277,34	405,18	472,89	485,06	502,47	506,74	no data
Pensions savings	2,01	9,96	26,76	42,56	43,07	39,92	no data
<b>Total</b>	279,35	415,14	499,65	527,62	545,54	546,66	no data
Investment Resources PPF/GDP (%)	1,29	1,54	1,51				no data

Source: *www.investfunds.ru*.

As shown in Table 29, while in 2006 PPF pension reserves grew 1.5 times, in 2007 they increased only slightly, by 16.7%. Pension savings had spurts of growth in 2006, increasing fivefold, and in 2007 they increased 2.7 times. In the first half of 2008, compared to the same period of 2007, the growth of pension reserves and pension savings amounted to 16.5% and 116% respectively. Figures for the end of 2008 were not available at the time of writing this review, but it is of note that growth of pension reserves practically stopped in the third quarter, and the volume of pension savings, for the first time since the pension reform, fell by 7.3%.

Overall in comparison with GDP the volume of PPF investment resources was and remains insignificant (1.3–1.5%). The management of PPF investment resources can be undertaken by the fund independently, just as it can be passed to an investment company to be managed. In the past few years a practice has come about whereby the conditions of the agreement with management companies regarding the

managing of PPF investment resources make provision for a certain revenue to be received from the investment. At a time of a steep drop in the securities market in 2008, losses in the management of PPF investment resources were incurred in a whole series of cases. One management company was sued for the return of the total capital given to their management and for compensation for losses in its investment.

### e) Investment of pension savings capital

Insured persons, that is employees for whom employers make pension contributions to the Pension Fund of Russia and who have an employment pension savings pot, may transfer their pension savings into a PPF or entrust it to a management company—either private or state-owned. The first tender amongst private management companies for the right to participate in the investment of pension savings was held in 2004 and commanded great interest from both the professional community and the interested public. As a result 55 companies became eligible to manage pension savings capital. That said, in the years that followed private companies lost interest in the project.

However in 2008 four more management companies went through the tender process and became eligible to manage the employment pensions savings pot. Thus towards the end of 2008 the Pension Fund of Russia signed contracts with 59 companies for the trust management of pension savings capital. The role of state management company has, up to now, been filled by the OJSC State Corporation “Bank of Development and Foreign Trade” (“Vnesheconombank”)

As a state management company, “Vnesheconombank” has the right to invest pension savings only into state securities. Private management companies have a much wider range of investment opportunities.

Figures on the size of pension savings transferred into PPFs are shown in Table 29. Table 30 gives information regarding the net asset value of the pension savings capital entrusted to “Vnesheconombank” and to private management companies.

**Table 30** Value of net assets into which Pension savings capital is invested (billion rubles)

Period	2005	2006	2007	2008			
				Q1	Q2	Q3	Q4
“Vnesheconombank”	176.3	267.1	362.9	348.7	353.7	350.1	343.1
Private management companies	5.6	9.4	12.2	12.1	12.3	10.5	7.1
<b>TOTAL</b>	<b>181.9</b>	<b>276.4</b>	<b>375.1</b>	<b>360.7</b>	<b>366.0</b>	<b>360.6</b>	<b>350.2</b>
Investment resources (%) Management companies/GDP	0.8	1.0	1.1				0.8

Source: VEB (“Vnesheconombank”), Pension Fund of Russia, [www.investfunds.ru](http://www.investfunds.ru).

As seen in Table 30, the overwhelming majority (about 97%) of the volume of the insured persons’ pension savings capital that was surrendered to trust management was entrusted to “Vnesheconombank”. In 2006–2007 there was an increase in the capital looked after by the state management company (in 2006 the growth constituted 51.5%, in 2007—35.9%). In 2008, however, for the first time since the pension reform and despite a very conservative investment policy, there was a drop in the net asset value of pension savings capital under “Vnesheconombank” management, a drop of 19.8 billion rubles in absolute estimation, or of 5.5%.

The net asset value of pensions savings entrusted to private management companies also fell towards the end of the year. In absolute terms this fall amounted to 1.7 billion rubles, or in relative terms—42%.

This fall may be linked to the redistribution of pension savings towards PPFs and to the negative investment results of their management.

Overall in comparison with GDP, the volume of the investment resources linked with the investment of the employment pensions’ savings pot and managed by state and private management companies has remained insignificant over the past few years (0.8–1%).

### f) Commercial banks

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

Summary data on the volumes of various types of securities held by credit organisations as assets over the last three and a half years are shown in Table 31<sup>28</sup>.

**Table 31** Securities in the assets of credit organisations (billion rubles)

Period	2005	2006	2007	2008			
				Q1	Q2	Q3	Q4
Securities* (TOTAL)	1400.1	1745.4	2250.6	2252.5	2347.5	2195.0	2365.2
<i>Of which</i>							
Debt instruments*	998.0	1251.4	1541.4	1563.9	1608.6	1577.2	1760.3
Equity securities*	127.1	185.0	316.3	285.5	290.9	209.3	193.4
Portfolio of controlling shares in daughter and affiliate JSCs	64.9	79.8	141.9	144.6	176.9	195.3	212.0
Discounted bills of exchange	210.1	229.2	251.1	258.5	271.1	213.2	199.5
Securities with repurchase agreements	139.3	215.9	304.1	–	–	–	–

\* Until 1.02.08 excluding securities with repurchase agreements

Source: Bank of Russia

In 2006–2007 the volume of securities in the assets of credit organisations had, on average, increased by 25% a year, however in 2008 growth ceased and constituted only 5%. In relative terms, the share of securities (discounting repurchase transactions) in the assets of credit organisations over the last few years has had a downward trend: in 2005 it was 14%, in 2006—12%, in 2007—11%. During the course of 2008 this downward trend continued from 10% in the first quarter to 8% in the fourth.

Debt securities in the collective securities portfolio of credit organisations constitute on average 68%–71%. The downward trend that appeared in 2007—first half of 2008, about-turned in the second half of the year. The share of stocks (discounting shares of daughter and affiliate organisations) amounted to on average 9–14% and had an inverse trend—it grew from 2005 to 2007, but in 2008 it began to steadily fall. The share of bills of exchange in 2005–2008 dropped steadily from 15 to 8%.

### g) Foreign investment funds

The Russian capital market is always attractive to foreign investment funds. According to “Interfax Business Service”, 1200 foreign funds openly invested in Russian stocks and depository receipts in 2005. In 2006–2007 their number grew on average by 25% a year (2006—1520 funds, 2007—1942 funds). In 2008, despite the economic crisis, the growth rate remained the same and towards the end of the year the number of foreign investment funds had risen to 2406 funds.

The volume of investments into Russian securities (both as local stocks and as depository receipts) is experiencing constant growth. In 2005 it amounted to 22.8 billion dollars, in 2006—49.5 billion (growth of 117%), and in 2007—73.4 billion (growth of 48%). In 2008 the volume of investment into Russian securities rose insignificantly (a rise of 4%) and reached 76.4 billion dollars.

Around 60% of Russian assets are concentrated in foreign funds, either in Great Britain or in the USA.

At the same time, the relative share of Russian assets in foreign funds is small—on average accounting for 3.3% of the aggregate fund portfolio. The number of Russian specialised funds (where the share of Russian assets is more than 75%) is not high, 25 to 30. By the end of 2008 they had accumulated around 8.7 billion dollars, that is 19% more than the previous year. There are far more global funds where the share of Russian assets does not exceed 10%. By the end of 2008 such funds numbered more than

<sup>28</sup> Includes securities acquired on the domestic and foreign markets.

1900, and the aggregate volume of Russian assets in them amounted to 29.1 billion dollars—23% less than in the previous year. So while specialised funds, oriented first and foremost towards Russia, saw a growth in Russian assets, global funds, on the contrary, saw their reduction.

According to data available, over the past few years there has been a steady increase in the volume of net raised capital by foreign funds investing in Russian assets<sup>29</sup>. In 2006—0.9 billion dollars and in 2007—1.2 billion dollars. In 2008 this trend continued, despite the economic crisis, and according to the same evaluations, the volume of net investment remained positive and amounted to around 2.0 billion dollars. That said, there was a significant inflow in May and outflow in July-August.

Overall the volume ratio of foreign fund investment into Russian assets, made through Russian and foreign exchanges is estimated at 25 to 75%. Apart from foreign investment funds that disclose information regarding their activities, foreign hedge funds are also interested in Russian assets. Hedge funds are far less transparent; hence it is not possible to estimate their investment.

### 2.3. Professional participants of the securities market

Composite, systematised and detailed data regarding professional participants of the Russian securities market has not been published. According to the FFMS<sup>30</sup>, the total number of professional securities market participants involved in various forms of activity based on the appropriate licenses amounted to 1711 organisations at the end of 2006. According to our estimates, around 40% of these are credit organisations.

There is no data available regarding the total number of professional securities market participants for 2007 or 2008.

#### a) Brokers, dealers, trust managers

Russian legislation regulates three kinds of intermediary activities on the capital market—brokerage, dealing and the management of securities. The definitions of these various activities are more or less the same as those of the developed markets, with the following provisions:

- Brokerage as such does not presuppose the registration of clients' rights on securities; therefore brokers wishing to do so must get a separate license for depository activity;
- Dealing is recognised only in buy/sell transactions of securities that are accompanied by a public declaration of the purchase and/or sale prices; therefore companies and members of the public who regularly conduct operations involving securities, even including those who publically offer to buy or sell securities who do not, however, declare the prices, are exempt from regulation.
- The trust management of securities formally differs from that of UIFs and private pension funds; a fact expressed by the existence of two separate licenses for these similar types of activity.

Information on the number of valid professional intermediary licenses is presented in Table 32.

**Table 32** Professional Intermediary licenses

Type of activity	2005	2006	2007	2008
Broker	1379	1433	1445	1475
Dealer	1398	1394	1422	1470
Securities Trust Manager	1022	1100	1169	1286

Source: FFMS Russia

<sup>29</sup> "Alpha Bank" evaluations.

<sup>30</sup> FFMS annual report, 2006.

As is clear from Table 32, over the last four years numbers of professional market intermediaries have been generally stable and with a tendency towards growth. We would point out that we are discussing namely the number of issued licenses and not the number of organisations working in the securities market. The majority of professional capital market intermediaries have three-four licenses (brokering, dealing, depository, and securities' management).

In 2008 the FFMS purged the market of organisations which had licenses to practice professionally on the capital market, but which did not exercise this right and which did not present financial reports, however this did not affect growth in numbers of valid licenses. Neither have the stricter requirements regarding own capital of professional securities market participants, introduced at the beginning of 2008, had an effect on the list of professional securities market intermediaries, nor has it led to a reduction in their number, or to mergers and acquisitions. In addition, in the second half of 2008, at the peak of the economic crisis, a string of organisations—professional financial market players underwent a change in their controlling stakeholders (ownership).

It is interesting that in 2008 the number of licenses issued for the trust management of securities increased by 117, or by 10% in comparison to the previous year. This stands trust management apart from the other types of activity. In the context of the drop in the growth rate of management companies as described above (see Figure 17), this could be seen as a reaction to the temporary limitations imposed on UIF registration, since there was still demand for trust management services.

#### b) Trade and settlement infrastructure

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

- the organisation of capital market trading (including stock exchanges);
- clearing;
- depository functions as settlement depositories.

Additionally, nonbanking credit organisations that conduct settlement operations also form part of this infrastructure.

According to FFMS data, as of the end of 2008 there were 9 organisations in Russia with trading or stock exchange licenses. 13 organisations have clearing house licenses, two of which received them in 2007 and 2 more in 2008.

Two leading infrastructural centres were essentially formed as a result of market competition and external integration processes—the groups MICEX and RTS. These today form the organised market for securities and securities derivatives in Russia.

**The MICEX Group** is an integrated trade and settlement infrastructure that includes:

- CJSC “Moscow Interbank Currency Exchange”;
- CJSC “MICEX Stock Exchange”;
- Noncommercial partnership “National Depository Centre”;
- Nonbanking credit organisation “MICEX Settlement House” (CJSC);
- CJSC Joint Stock Commercial Bank “National Clearing Centre”.

In June 2008, within the framework of the MICEX Group, a specialised company was formed—CJSC “MICEX–Information Technologies”. The primary function of this new enterprise was to develop and support technical and software solutions that would link traders to the trading system MICEX.

The MICEX Group supports several trading modes:

- Government securities market
- Main trading mode
- Negotiations mode
- Repurchase agreements mode

A trading mechanism on **the government and municipal securities market** (organised by CJSC “Moscow Interbank Currency Exchange” forms the basis for an “order driven market”—a market of competitive bids in which a deal is done automatically in the case a crossover in offsetting bids. Transactions are carried out on the principle of “delivery versus payment” with 100% preliminary deposit of assets. Deals are executed on the day they are concluded (T+0).

**On the MICEX capital market** (trading organiser—CJSC “MICEX Stock Exchange”) a trading mechanism again forms the basis for an “order driven market” principle “delivery versus payment” with 100% pre-deposition of assets and the execution of deals on the day of their conclusion (T+0).

**In negotiations mode** traders are able to quote securities by entering “non-addressed” orders (an invitation for a firm offer to all market participants) and to conclude deals on a bilateral (not anonymous) basis, using counter addressed bids (an offer to conclude a deal from one trader to the address of another). If this occurs, the traders, on the conclusion of the deal, define the date for its obligations to be fulfilled that ranges from the current day of trading (T+0) to 30 calendar days post transaction completion (T+30). This trading mode allows the participants to conclude their deals either with complete collateral control or without.

**Repurchase agreement mode** allows for deals to be concluded with the date of execution being any day, beginning from the day after the transaction is concluded to a date selected for its execution inclusively. The date of execution of the second part of the repurchase transaction is the date, defined as T+x+k, where T+x is an appropriate date for the execution of the first part of the repurchase transaction, and k—the term of the repurchase agreement (k meaning from 0 to 180 calendar days, x—from 0 to 2 settlement days).

The clearing of MICEX Stock Exchange transactions is carried out by CJSC MICEX. Settlement of a trader’s net liabilities on executed deals is effected on the basis of settlement documents from CJSC MICEX as a clearing centre, in “MICEX Settlement House” (a settlement house for monetary assets), and in NP “NDC” (a settlement depository for securities).

In March 2008 an additional service was introduced that allowed deals to be concluded or obligations to be fulfilled on an earlier deal subject to simple clearing, with the settlement made on the “delivery versus payment” principle during the course of the working day and not at its end.

Also in 2008 the MICEX stock exchange brought in technology for buffering bids that allows bids to be collected during the course of a particular period of time (up to 30 days). Use of this technology facilitates operations in which an issuer repurchases its own shares and/or by the creation of a bid log directly through the trading system. In March a shares repurchase was conducted by one Russian issuer using this technology.

In 2007 the MICEX stock exchange formed a Sector of Innovative and Growing Companies (IGC). The closed-end UIF of particularly risky (venture) investments “FINAM—Information Technology” was the first issuer in this sector. This fund specialises in the acquisition of assets in various areas of IT. The fund raised 500 million rubles from its initial offering in June 2007. As of the end of 2007 the volume of deals with UIFs on the MICEX stock exchange constituted 565 million rubles, by the end of 2008—274 million rubles. Also in June 2007, simultaneously in the IGC sector of MICEX and on RTS START an additional issue of stocks was floated by the company OJSC “Armada”, which specialises in IT technology. This raised 29.7 million rubles. At the end of 2007 this issuer’s stock transaction volume on MICEX constituted 20.2 million rubles, by the end of 2008—737 million rubles. In July 2008 in the IGC sector of MICEX, OJSC “O2TV” that specialises in television broadcasting did an IPO. The volume of the offering amounted to 10 million dollars. By the end of 2008 the stock transaction volume of this issuer on the MICEX stock exchange was 4.6 million rubles.

In August 2008 a new sector—MICEX Discovery was created on the MICEX stock exchange as part of the main market exchange, with a special procedure for the admission of stocks to trading and special criteria for the selection of companies. The stocks included in this sector are admitted to trade on the exchange’s initiative, which to reduce the risks for investors, uses a multilevel system for the selection of companies and an institute for information sponsorship. The stocks of 40 Russian companies were included in this sector during the course of the year. At the end of 2008 the stock transaction volume of these issuers on the MICEX stock exchange reached 311 million rubles.

August 2008 saw the completion of an obligatory regulatory framework on the MICEX stock exchange for the circulation of a new equity instrument—Russian depository receipts (RDRs) on the Russian securities market. A new edition of Listing Rules was brought into effect. Up to the end of 2008 no RDRs had been placed.



The collated trading results for non-government securities on the MICEX stock exchange for 2005–2008 are listed in Table 33<sup>31</sup> in both rubles and in foreign currency.

**Table 33** Trading total for the MICEX stock exchange

Period	Unit of Measure	2005	2006	2007	2008				2008
		Total	Total	Total	Q1	Q2	Q3	Q4	Total
Trade volume	billion dollars	226	755	1708.9	516	618	629	222	1986
Trade volume	billion rubles	6400	20380	43500	12523	14650	15153	6033	48359

Source: MICEX

As follows from Table 33, 2006 and 2007 experienced furious growth in the exchange turnovers on the MICEX stock exchange (the annual growth in rubles was 218% and 113% respectively. With this in mind the growth of 2008 (11%) looks slight. The sharp fall (more than twofold) in the exchange turnovers in the fourth quarter begs note.

In 2008 there was a sharp increase in the number and volume of unexecuted deals on the MICEX stock exchange. Largely these are linked to unfulfilled repurchase transactions. According to the information provided by the exchange, 1442 cases of unfulfilled deals were recorded during the year—a sum of 38.8 billion rubles. The peak in transaction breaches occurred in September-October (1354 breaches, the sum of unexecuted deals—36.1 billion rubles).

The situation regarding unexecuted repurchase agreements erupted particularly around 17<sup>th</sup> September 2008. At this time the Bank of Russia and MICEX had had to take extraordinary measures to “resolve” the defaults. The situation that arose with nonfulfillment of repurchase agreements exacerbated the crisis on the capital market.

From the 1<sup>st</sup> October the MICEX stock exchange resumed its evening trading sessions until 19:00.

**The RTS Group** is an integrated trade and settlement infrastructure that includes:

- Noncommercial partnership—Stock exchange “Russian Trading System”;
- OJSC Stock exchange “Russian Trading System”;
- Noncommercial partnership—Stock exchange “Saint Petersburg”;
- CJSC “RTS Clearing Centre”;
- Nonbanking credit organisation NCB “RTS Settlement Chamber”
- CJSC “Depository and Clearing Company”.

The RTS Group supports several trading modes:

- Exchange market
- Classic market
- FORTS Derivatives market

Trading is organised by OJSC “RTS” stock exchange. The NP Stock exchange “Saint Petersburg” trades the stocks of OJSC “Gazprom”.

**The RTS Exchange market** works on the following principles: an anonymous bids auction (order-driven market), 100% preliminary deposit of assets; the settlement method is “delivery versus payment” on a T+0 basis, the quotations and settlements are made in rubles. The clearing centre used is NP “SE RTS”, the settlement depository is CJSC “DCC”, and the settlement credit organisation is “RTS Settlement Chamber”.

In the framework of the **RTS classic market** two trading models are used:

- The classic market with nonanonymous trade presumes the conclusion of deals is based on non-anonymous quotations (“quote-driven market”), there is no preliminary deposit of assets; the quotations are in US dollars and it is possible to choose the settlement date (from T+0 to T+30), the method

31 Deals with stocks, corporate, sub-federal and municipal bonds and investment units are calculated, including repurchase transactions.

of settlement (“delivery versus payment” or free delivery), the currency of settlement (rubles or foreign currency). Neither a clearing centre nor a settlement depository are used. Monetary settlements in “delivery versus payment” mode are effected through the “RTS Settlement Chamber” or J. P Morgan Chase Bank, and the settlements in free delivery mode are effected through any bank.

- The Classic market with anonymous trade presumes an anonymous bids auction (order-driven market), partial preliminary deposit of assets; the method of settlement is “delivery versus payment” on a T+4 basis; the quotations and settlements are in US dollars. The clearing centre used is NP “SE RTS”, the settlement depository is CJSC “DCC”, the settlement credit organisation—NCB “RTS Settlement Chamber” or J. P Morgan Chase Bank.

In September 2007, “central counterpart in transactions” technology was launched onto the stock market, where NP “SE RTS” functions as a counterpart to all transactions. In June 2008, netting technology for stock market settlements in “central counterpart” trading mode was introduced.

In May 2008 the Board of Directors of RTS made the decision to transfer the clearing of securities from NP “SE RTS” to OJSC “RTS Clearing Centre”, effective as from 1<sup>st</sup> September 2008.

**The FORTS derivative market** is based on an anonymous bids auction (order-driven market). Settlements and delivery are effected on the expiration date of the circulation of the contract. Quotations and settlements are made in rubles. The clearing centre is OJSC “RTS Clearing Centre”, the settlement depository is CJSC “DCC”, and the settlement credit organisation is NCB “RTS Settlement Chamber”. Since September 2007, the FORTS market has been using intermediate clearing (14:00–14:03).

Evening trading sessions were introduced onto the FORTS derivative market in May 2008. The main session ends at 17:45, after which there is a clearing session. Evening sessions continue from 18:00 to 23:50; settlements for the session’s transactions are effected at 14:00 the following day.

Within RTS there is an indicative quotations system RTS Board, which is based upon the following principles: the display of indicative quotations on the securities not admitted to trade on the RTS stock exchange; no preliminary deposit of securities or monetary capital is 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 (rubles or foreign currency). Neither a clearing centre nor a settlement depository are used. Monetary settlements in “delivery versus payment” mode are effected through NCB “RTS Settlement Chamber” or J. P Morgan Chase Bank, and settlements in free delivery mode are effected through any bank.

In 2008 in the RTS Group a new project—RTS Global was launched, designed to display indicative quotations on foreign securities concluded in off-exchange deals, and also to settle deals in CJSC “DCC”. At the end of 2008 there were 51 securities admitted into this sector, however they were left practically untraded.

In 2007 a special segment—RTS START was created within the RTS Group for the entry of small cap companies onto the open market. The first issuer represented on RTS START was JSC “BB” Kommunar”, then in the course of the year four more issuers appeared on the platform—OJSC “Armada”, JSC “Kosogorsky Metallurgical Plant”, JSC “SIGMA” and JSC “Neftekamsk Automobile”. In 2007 the stock trading volumes of these issuers was very small.

The most liquid issuers at the end of the year were OJSC “Armada” and OJSC “Neftekamsk Automobile” (the trading volumes 4.0 million dollars and 2.7 million respectively); the least liquid was OJSC “SIGMA” (five transactions with an overall volume of 20 thousand dollars). In November 2007, the main and additional issues of OJSC “Armada” shares circulating on RTS were transferred to quotation list “B” with a subsequent exclusion from RTS START. In May 2008 one issuer made it onto RTS START—OJSC “Electrozink”. The total transaction volume in this segment as of the end of 2008 was very small—around 4 million rubles.

In 2008 calculation technology was launched onto RTS with the use of a “central counterpart”. Deals in this mode at present are conducted with the securities of two issuers. CJSC “RTS Clearing Centre” acts as central counterpart. Again in 2008 FIX was created on the RTS to manage of bids in the trading system in electronic trading mode (anonymous classics).



Summary results for RTS Group trading on different markets in 2005–2008 are shown in Table 34<sup>32</sup>.

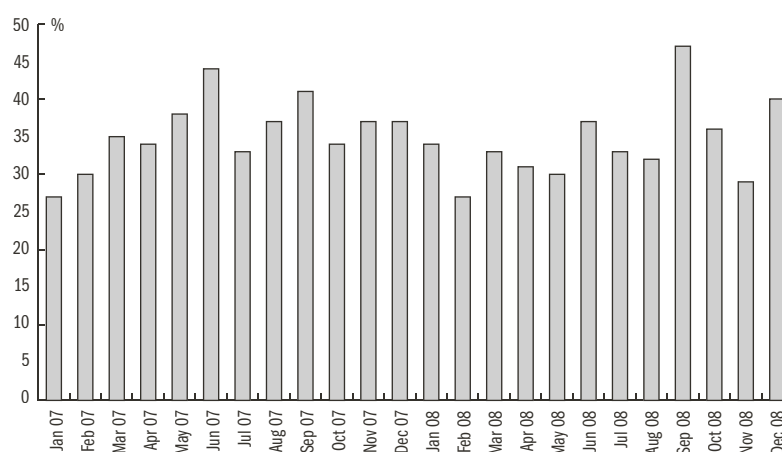
**Table 34** Results for RTS trading

Period	Unit of Measure	2005	2006	2007	2008				2008
		Total	Total	Total	Q1	Q2	Q3	Q4	Total
<b>Classic Market RTS</b>									
Trading volume	billion dollars	7.7	16.1	14.6	3.6	3.1	2.4	0.7	9.8
<b>Exchange market RTS</b>									
Trading volume	billion rubles	82.0	27.3	23.5	4.9	7.4	7.4	8.5	28.1
<b>Exchange market SE "Saint Petersburg"</b>									
Trading volume	billion rubles	936.8	1205.9	71.2	21.1	18.0	1.9	0.6	41.7
<b>Derivatives market FORTS</b>									
Trading volume	billion rubles	687.1	2708.5	7531.2	3195.7	3453.7	3408.1	1100.2	11157.7
<b>RTS Board</b>									
Trading volume	million dollars	309.1	544.8	751.9	199.1	141.2	81.7	14.5	436.4

Source: RTS

In compliance with the Disclosure of Information ruling,<sup>33</sup> stock exchanges collect information regarding over-the-counter (off-exchange) transactions with securities included on the stock exchanges' quotation lists, provided that the execution of their obligations provides for the transfer of ownership of these securities. Figure 18 shows a graph illustrating the share of reported off-exchange deals in the aggregate volume of exchange transactions (excluding repurchase agreements) and the reported off-exchange deals conducted (reported) through the MICEX stock exchange and RTS.

**Figure 18** Share of off-exchange (over-the-counter) transactions



Source: MICEX

<sup>32</sup> Deals with stocks, corporate, sub-federal and municipal bonds and investment units are calculated, including repurchase transactions; for the derivatives market FORTS—futures and options transactions.

<sup>33</sup> The FFMS dictate of 22 June 2006 No. 0667/pz-n "Ratification of the regulation regarding disclosure of information on concluded transactions".

In 2007 around 8.5 trillion rubles of off-exchange transactions were recorded, in 2008—6.5 trillion rubles. On average, the share of reported off-exchange transactions constituted 34–35% of the total transaction volume, and certain months can be noted (for example June 2007 and September 2008) when this indicator was in the region of 45%. From the date the collation of this information on over-the-counter deals began, the indicator did not sink below 25%.

The suspension and cessation of exchange trading on both the stock exchanges MICEX and RTS were negative features of the stock market from mid September to the end of 2008. The general rules regarding the suspension of trading, in force at the end of 2008, were statutory according to the Regulation for Organised Trading on the Capital Market, as laid down by the FFMS dictate of 9<sup>th</sup> October 2007 № 07-102/pz-n. In accordance with these regulations, exchanges must suspend trading for one hour in the case of a rise or fall in the value at opening of the technical index of more than 12% in comparison to the value of closure of the index of the previous day; a rise or fall of the technical index of more than 8% in comparison with the value of opening of the index of the present day. Besides this, it is laid down in the Regulation that exchanges suspend trading to the end of the working day (in the absence of a FFMS Russia dictate on earlier resumption of trading), if the value of opening of the technical index is 15% higher or lower than the last closing value, or the current value of the index is 10% higher or lower than the value of opening of the present day.

However, from 30<sup>th</sup> October 2008, a FFMS directive laid down a narrower corridor for price movement on the exchanges. Trading had to be suspended in the case of fluctuation in the technical index of more than 10% in comparison with the level at closure, or more than 5% compared to the level of opening. From 7<sup>th</sup> October the limitations regarding fluctuations of the technical index became stricter still: by FFMS stipulation exchange trading of securities ceases for an hour if the technical index were to deviate more than 5% from the level at closing, and to the following day if the deviation were more than 10%. From 14<sup>th</sup> October 2008 the values by which the index could fluctuate before suspending exchange trading were introduced and remained in force until the end of the year: trading is suspended for an hour in the case of a fall of the technical index of more than 5% or growth of more than 10%, and until the end of the next working day if the index falls more than 10% or grows more than 20%.

The FFMS also stopped exchange trading three times in September-October 2008 with its own special mandates.

Following a consultation with the professional securities market community on 13<sup>th</sup> October 2008 FFMS Russia accepted changes to the Regulation for Organised Trading on the Capital Market in accordance with which the following rules were introduced after the document came into force: exchange transactions must be suspended for an hour (but not later than 16:00) should fluctuations of 15% occur on the share index in comparison with the last value calculated during the main trading session of the previous trading day, and to the end of the working day (if another period of time is not specified by the FFMS) if there are fluctuations of 25% of the stock index compared with the last indicator of the said index calculated during the main trading session of the previous trading day. If trade is suspended for an hour, a further suspension will be imposed only if grounds arise for ceasing trade until the next day. The given rules were more effective—they tied trading suspensions to the main indices and not to the technical indices, the calculation of which was not entirely clear to market traders, and also widened the corridor of exchange price movement, which was preferable to the market volatility that arose at the end of 2008. As of 31<sup>st</sup> December 2008 new rules had not come into force and those set down by the FFMS directive of 14<sup>th</sup> October 2008 continued to hold.

From 18<sup>th</sup> September 2008 the FFMS banned “short sales” and also marginal deals. On the 23<sup>rd</sup> September the FFMS redetermined the directive, overall affirming the bans and adding other unsecured deals to the embargo. On the 26<sup>th</sup> September, after consultation with professional members the FFMS allowed the execution of “short sales” and other unbacked transactions, limiting the threshold margin level 1:1. On 30<sup>th</sup> September the FFMS again brought in a ban on “short sales” which at the very end of 2008 still held. The FFMS bans extended to all securities traded on the organised market.

Discussion on the effectiveness of the measures taken by the FFMS has indicated polar opinions. The excessiveness of the demands to stop trading has incurred criticism, as has the extreme nature and length of time that the ban was in place on “short sales”. According to the professional community, the

given measures limited the liquidity of the Russian capital market, leading to part of the operations being redirected towards foreign markets, and they could provoke “grey” schemes aimed at circumventing the established rules.

The operations of Vnesheconombank proved yet another feature of Russian capital market performance at the end of 2008, with their acquisition of four large issuers by means of share capital allocated by the government, a fact that influenced the direction of the market indices and which also caused multi-valued estimations.

### c) Registration system

On the Russian capital market there are two alternative ways in which to register rights on securities, both carrying the same legal weight: via personal accounts in the stock registering system and by depo accounts in a depository. Registrars, depositaries and also issuers who independently keep registers of their shareholders together constitute the record keeping system of the capital market.

Registration and depository activity is subject to licensing. The Registrar is a professional participant of the securities market who keeps the stock register i. e. the ownership register of securities. This involves the collecting, inputting, processing, saving and presenting of the data that makes up the stock registration system. The registrar works on the basis of an agreement with the issuer: individuals opening an account in the register do not sign an agreement with the registrar. An issuer with no more than 50 shareholders is allowed to keep an independent register or to contract this out to a registrar. If the number of shareholders exceeds 50, the issuer is obliged to entrust the stock register to a registrar, although the issuer will still be responsible for it.

A Depository is responsible for registering and certifying rights on securities, registering and certifying the transfer of securities, and also for the custody of securities (if issued in document form). They do their job on the basis of an agreement with an owner of securities or with an individual who has other rights with regard to securities (a depository agreement).

Russia has adopted the generally accepted global practice of dividing depositories into settlement and custodial. Settlement depositories are those that make securities’ settlements on the results of clearing and that conduct all operations in the depo accounts of capital market participants for the execution of deals made through trading organisers. All other depositories are custodial depositories.

Information on the number of valid registrar and depository licenses are presented in Table 35.

**Table 35** Registrar and Depository licenses

	Period	2005	2006	2007	2008
<b>Type</b>					
Registrar		82	73	66	59
Depository		743	831	787	789

Source: FFMS of Russia

Therefore, as follows from Table 35, while the number of depository licenses over the last few years has been subject to increases and decreases; the number of registrars has a pronounced downtrend.

### 3. Legislation and regulation

In the Russian Federation regulatory legislation for the capital market is laid down by several laws “The Securities market”, “The Protection of rights and legal interests of investors on the securities market” and “Mortgage securities” which define the general rules in place on the securities market, and by sub-legislative normative acts (predominantly Russian Federal Government decrees and FFMS Russia dictates) that set out special codes of practice. Individual institutions are regulated by special laws: “Investment Funds”, “Private pension funds” “Capital investment for financing employment pension savings”, “The savings and mortgage system for military housing” in conjunction with a significant amount of sub-legislative regulation.

In December 2007 amendments were made to the Federal law “Investment Funds” and to other legislative acts of the Russian Federation<sup>34</sup>. One of the main amendments was the introduction of the concept “qualified investor” into the legislation and the differentiation of the circle of operations that can be performed for qualified and unqualified investors. New requirements regarding accountability were also brought in by law, represented in FMMS Russia by incorporated investment funds, management companies and specialised depositories, and regarding the rules governing trust management of unit investment funds. Changes to the law predicated a large number of changes to sub-legislative normative acts. The most important of these—changes to the standard regulations covering unit investment funds, were brought in only in autumn 2008. In September, October and December 2008, the Russian Government made changes to the standard regulations imposed on the trust management of closed-end, opened-end and interval unit investment funds.<sup>35</sup>

In 2008 in order to enforce these changes FFMS Russia ratified the Licensing Procedure for investment funds, investment fund management, unit investment fund management and private pension fund management, for specialised depositories of investment funds, unit investment funds and private pension funds; for private pension funds with pension security and pension insurance<sup>36</sup> and also the Regulation on annual reports and quarterly financial reporting of a private pension fund.<sup>37</sup> In May 2008, in accordance with these amendments to the legislation, FFMS Russia ratified the procedure for acknowledging corporate bodies and individuals as qualified investors, set the requirements to which these entities must conform to be acknowledged as qualified investors, and the procedure for entering onto the register the entities accepted as qualified investors.<sup>38</sup>

34 Federal law of 06.12.07 № 334-F3 “Making changes to the Federal law—“Investment Funds” and individual legislative acts of the Russian Federation”.

35 RF Government Decree of 01.09.08 № 651 “Making changes to the Standard rules of trust management of closed-end unit investment funds”.  
RF Government Decree of 27.10.08 № 790 “Making changes to the Standard rules of trust management of opened-end unit investment funds”.  
RF Government Decree of 24.12.08 № 1005 “Making changes to the Standard rules of trust management of interval unit investment funds”.

36 FFMS Dictate of 07.02.08 № 08-4/pz-n “Licensing for investment funds, investment fund management, unit investment fund and private pension fund management; for specialised depositories of investment funds, unit investment funds and private pension funds; for private pension funds with pension security and pension insurance”.

37 FFMS Dictate of 30.08.07 № 07-92/pz-n “Ratification of the Regulation on annual reports and quarterly financial reporting of private pension funds and instructions how to complete them.”

38 FFMS Dictate of 18.03.08 № 08-12/pz-n “Ratification of the Regulation on the acknowledgment of individuals as qualified investors”.

The Regulation on the qualification of foreign financial instruments as securities came into force from 1<sup>st</sup> February 2008 and was ratified by FFMS Russia.<sup>39</sup> In this Regulation the procedure for the qualification of foreign financial instruments as securities subject to the code implications for the qualification of financial instruments—CFI (Classification of Financial Instruments) is defined, and also the procedure for the registration of foreign financial instruments by Russian depositories for Russian investors.

In order to stimulate pension savings and to raise the level of collateral in the people's pension, amendments were made in April and June 2008 to the Federal law "Private pension funds", which came into force from January 2009. Thus, in accordance with the said amendments and the Federal law "Additional insurance contributions to the savings pot of employment pensions and government support in establishing pensions savings", which came into force in 2008, provision was made for 10 years of government support in the creation of pensions savings, commencing the year following that when payment of the additional insurance contributions would be made (year end thereof). The size of the contribution for the co-financing of pension savings is determined from the sum of additional insurance contributions to the employment pension savings pot paid for the last calendar year, but cannot constitute more than 12000 rubles a year. The size of the contribution is calculated by the Pension Fund of Russia, and the contributions themselves are transferred to private pensions funds.

In the first half of 2008, FFMS Russia ratified a new Regulation on the auditing of organisations; the monitoring and supervision of which is assigned to FFMS Russia,<sup>40</sup> in accordance with which authorised employees of corresponding self-regulated organisations are brought in to carry out planned field checks on organisations which are members of the self-regulatory bodies of professional capital market participants or of self-regulatory managing bodies.

In May 2008 an FFMS dictate "Ratification of the regulation on the procedure of registering the owners of Russian depository receipts" came into force, written in line with the amendments to the Federal law "The Securities Market" regarding issue characteristics and the circulation of Russian depository receipts that were brought into effect in 2007.

At the end of 2007 FFMS Russia issued a dictate on "The required procedures for registering ownership of securities by the issuers of those securities"<sup>41</sup> laying down that on the securities issuer's staff there must be at least one employee who is certified as a financial markets specialist qualified to keep the stock ownership records. However this was nullified by a Supreme Court decision of 16<sup>th</sup> May 2008. Later the FFMS revoked these requirements<sup>42</sup> with the dictate of 14<sup>th</sup> August 2008.

In the second half of 2008 changes were made to the Standards of issuing securities and the registration of securities prospectuses as pertains to widening the check list of documents necessary for government registration of total issue records (additional issue) of securities, and also new rules were set out for the issuing of securities when restructuring corporate bodies.

In November 2008 a federal law was passed as one of the measures imposed to stabilise the financial market, which gave the Bank of Russia the right to become a trader on the stock exchange and (or) a participant in any other organised trading on the capital market. In accordance with these changes, the Bank of Russia can execute buy-sell operations of bonds and stocks of commercial organisations by a decision of its board of directors. Prior to this, the Bank of Russia only performed similar operations with treasury bills of exchange, government bonds and other government securities and Bank of Russia bonds.

At the end of 2008, by FFMS Russia dictate, licensing requirements for professional activity on the capital market were tightened, laid down in the Procedure for licensing various professional activities

39 FFMS Dictate of 23.10.07 № 07-105/pz-n "Ratification of the Regulation on the qualification of foreign financial instruments as securities".

40 FFMS Russia dictate of 13.11.07 № 07-108/pz-n "Ratification of the Regulation on the auditing of organisations, the monitoring and supervising of which is assigned to Federal Financial Markets Service."

41 FFMS Russia dictate of 07.12.07 № 07-113/pz-n "The required procedures for registering ownership of securities by the issuers of those securities."

42 FFMS Russia dictate of 14.08.08 № 08-33/pz-n "The Revocation of the FFMS Russia dictate of 27 December 2007 № 07-113/pz-n "Required procedures for registering ownership of securities by the issuers of those securities" and the FFMS Russia dictate of 27 March 2008 № 08-16/pz-n "Amending the FFMS Russia dictate of 27.12.2007 № 07-113/pz-n "Required procedures for registering ownership of securities by the issuers of those securities".

on the securities market. Therefore, it is now necessary to present FFMS Russia with full information on the structure of ownership, that is of the person or group of persons who either directly or indirectly owns or own five or more percent of the equity capital of the licensee, and stand alone subdivisions, situated outside of the location of the license holder, can be created only as representative offices or filials.

At the end of December 2008 changes were made to the federal laws “Banks and Banking activity” and “Joint stock companies” as they pertain to regulating the procedure for restructuring credit organisations, the procedure for notifying interested parties about the restructuring of credit organisations and the specifics of the restructuring of credit organisations in the form of mergers, affiliations and reorganisations.

Also in December 2008 amendments were made to federal laws regarding the Civil Code of the Russian Federation, in particular the rules on collateral and the rights of creditors in the restructuring of corporate bodies were extended. In accordance with these said amendments, in the case of the existing laws, the requirements of the charge holder can be satisfied by the transfer of the collateral to the ownership of the charge holder; the law can make provision for the records and/or the registration of collateral agreements and of collateral by the act of law concerning separate objects of personal property. In addition a new procedure was laid down for the foreclosure of encumbered assets.

### Taxation of the capital market

The Russian Federation belongs in the category of countries that has a traditional taxation system.

Table 36 lists the main taxes and rates in place in 2008 as applied to profit (the income of organisations whose activities are subject to taxation in the Russian Federation as pertaining to trading securities and to the income of individuals from securities or the trading of them).

**Table 36** Main taxes and rates

Income	Tax Rates For Residents %	Tax Rates For Non-residents %
<b>Individuals</b>		
Dividends on Russian stocks	9	15
Interest on bonds with a mortgage backing issued before 1 January 2007	9	30
Other income from securities and operations with them	13	30
<b>Corporate Bodies</b>		
Dividends from daughter companies, provided that certain conditions are met (a share in capital of more than 50%, ownership for at least one year etc.; if the company is foreign it should not be located in an offshore zone)	0	Not applicable
Dividends from Russian and foreign organisations	9	15
Dividends from government and municipal securities, interest on bonds with mortgage backing issued after 1 January 2007, and on the founding shareholder's income for the trust management of mortgage backing, received on the acquisition of mortgage participation certificates issued by the mortgage backing management after 1 January 2007	15	15
Interest on municipal securities with a term of no less than 3 years, issued before 1 January 2007, as well as interest on mortgage-backed bonds issued before 1 January 2007, and on the the founding shareholder's income for the trust management of mortgage backing, received on the acquisition of mortgage participation certificates issued by the mortgage backing management before 1 January 2007	9	9
Other income from securities and operations with them	24	24

The Russian Federation has signed international agreements on the elimination of dual taxation with 74 countries. In accordance with these agreements, companies registered in one country, receiving an income from sources in two countries (Russia and the country with whom the treaty is signed), will pay tax at a reduced rate in only one of these countries: in Russia or in the other signatory country.

The Ministry of Finance of the Russian Federation has published a list of offshore zones.<sup>43</sup> Companies registered in these zones are not allowed to transfer non-taxable dividends to Russia, as covered in point 3 of section 284 of the Russian Federation Tax Code. 41 offshore zones are included on this list.

The Russian system to regulate the capital market was established in parallel with the founding of the actual market itself and in many ways has played a positive role in its development. This system generally incorporates international experience of regulating the financial markets and follows the global tendency regarding the continued development of regulation in this area, however it does boast a range of national specifics. The most important of these is the complicated division of regulatory and supervisory authorities between several institutions in the financial markets. At present a significant proportion of the relevant financial market functions falls to one government body—The Federal Financial Markets Service, however certain powers remain with the Central Bank and 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 main governmental regulatory body of the Russian capital market. Its status is similar to that of a ministry, as it reports directly to the RF Government and carries both regulatory and monitoring-supervisory authority.

FFMS functions are regulated by the law “The securities market” and by the Regulation on the FFMS, ratified by the RF Government decree of 30.06.04 № 317. According to this regulation the FFMS is deemed a federal executive body that fulfills its functions by way of normative legal acts and the monitoring and supervising the financial markets, with the exception of insurance, bank and auditing.

The FFMS regulates all the main capital market entities: issuers, professional participants, collective investment institutions, and also, to a certain degree, investors. The FFMS has a functional independence in that it does not coordinate its activities with any other authority. However as an executive body it does report to the RF Government which has the right to suspend its activities or to revoke any FFMS legislative decisions.

With regard to issuers, the FFMS has the authority to ratify the standards of securities issuing, sanction the procedure for the government registration of securities and reports on its issue results, registration of securities and reports on its issue results, and also approve securities prospectuses (with the exception of government and municipal securities). The FFMS also monitors issuers and in the case of breaches issues them with directives, and if necessary can suspend the issuing of securities and file for the securities issue to be declared invalid. The FFMS also determines the procedure for initial offerings and for the circulation of Russian stocks outside the Russian Federation.

Regarding professional securities market participants, the FFMS ratifies the requirements set out by the rules of professional securities trading, approves standard practice in relation to the sufficiency of own funds, grants licenses for professional activity on the capital market and registers certain internal documents of professional participants. It also verifies and monitors market professionals and can issue them with directives if required, prohibit or restrict particular operations on the securities market, and it also has the right to suspend or annul the licenses of those in breach.

Concerning collective investment institutions, the FFMS licenses the activities of private pension funds, equity investment funds, management companies and specialised depositories. It registers the rules of unit investment fund trust management and mortgage backing trust management, the rules on private pension funds and the documents of specialised depositories. The FFMS also ratifies the requirements of the asset structure of joint-stock and unit investment funds, determines the standards of the disclosure of information and the forms of reporting for PPFs and monitors these entities and issues them with directives.

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<sup>43</sup> Ministry of Finance Dictate of 13.11.07 №108n “Ratification of the list of states and territories that provide a privileged tax regime and/or which do not provide for the disclosure of information regarding financial operations (offshore zones)”.



The FFMS also regulates the admission of securities to public offerings, to circulation, to quotation and listing, takes measures to stop unscrupulous advertising on the securities market, publishes methodology materials and recommendations on in its competency. It has the right if necessary to go to court or arbitration with suits or claims. An important function of the FFMS is its right to review cases of administrative violation within its area of competence, and to take responsible measures as laid down by administrative legislation.

It should be noted that there are a number of essential exemptions to the FFMS's competency relating to credit organisations: here the FFMS can neither impose measures of prudence, nor regulate the issuing of their securities. FFMS authority also does not extend to the issue and circulation of government and municipal securities.

### 3.2. The Central Bank of the Russian Federation

The Central Bank is not an executive body and fulfills its function on the basis of a special law "The Central Bank of the Russian Federation (Bank of Russia)". Its authority in the regulation of commercial banks is also determined by the law "Banks and banking activity". As an organisation responsible for monetary circulation and the stability of the banking system in Russia, the Bank of Russia has a range of powers that to a greater or lesser extent affect the capital market and its participants.

Thus the Bank of Russia in cooperation with the Russian government develops and implements an integrated state monetary and credit policy that influences many aspects of the capital market. In order to effect its monetary and credit policy, it acts as an issuer of its own bonds and performs open market transactions with government securities and its own bonds and is a big player on this market.

As a banking regulator, the Bank of Russia determines the specifics for the securities issuings of credit organisations, and registers issues of these securities. It performs banking checks on credit organisations and banking groups, including on their involvement in the capital market as investors. As regards credit organisations as professional securities market participants, the Bank of Russia effectively determines the rules for performing particular operations (for example, the trust management of securities, the rules for depository registration etc.). It also carries out the "indirect regulation" of the securities market by playing a part in the capital of the infrastructure of the securities market (for example, MICEX).

The Bank of Russia also establishes the regulations that apply to banking operations and the procedures for the accounting and reporting of the banking system of the Russian Federation.

Thus, although the regulatory powers of the Bank of Russia with regard to the capital market and its participants affects directly only the credit organisations operating on this market, its overall influence on the market itself is significant. Using the aforementioned authority, the Bank of Russia, in essence, is the second most important state regulator of the capital market.

### 3.3. The Ministry of Finance of the Russian Federation

According to the Regulation on the Ministry of Finance (ratified by a Decree of the RF Government of 30.06.04 No 329), the Ministry performs a number of functions related to the securities market and its participants. Firstly, the Ministry of Finance approves the terms of issue and circulation of federal government securities, approves decisions on particular issuings of these securities, and also reports on the results of these issues. At the same time, the Ministry of Finance is itself an issuer of federal government securities.

The Ministry of Finance acts as a regulatory body in relation to government securities—subfederal and municipal; it performs the official registration of the terms of issue and circulation of these securities and approves the standards relevant to information disclosure on these securities.

In addition, the Ministry of Finance remains a regulator of pension savings investments for the financing of the employment pension savings pot, as well as being regulator of insurance companies where, amongst other things, this pertains to their investments in securities (the supervision of insurance



companies is exercised by the Federal Insurance Supervision Service that reports to the Ministry of Finance). The Ministry of Finance also passes normative legislative acts on accounting procedures and the writing of financial statements.

### 3.4. Other State bodies

The system of law enforcement on the securities market also includes the tax authorities, financial control and monitoring bodies, the antimonopoly authority, the judiciary system and law enforcement agencies. However a detailed analysis of their functions and objectives is beyond the remit of this review.

### 3.5. Self-regulatory organisations

The system that regulates the securities market includes a number of government bodies and self-regulatory organisations (SROs). They are set up by professional market participants with the aim of providing the terms of their professional activity, compliance with the standards of professional ethics in the securities market, protection of the interests of investors and other clients of professional market participants, and also to establish the rules and standards for trading securities in order to ensure the efficiency of capital market activity. SROs may also be set up by management companies.

SROs are nonprofit organisations. They lay down rules, mandatory for their members, for professional activity on the securities market, and the standards of trading in securities. They also ensure compliance with these rules. Membership in a SRO is voluntary.

At the present time five organisations in Russia have the SRO status of professional securities market participants and collective investment institutions.<sup>44</sup>

- The National Association of Securities Market Participants (Russian abbreviation: NAUFOR) includes brokers, dealers, trust managers and depositaries. It has 391 organisations as members. NAUFOR has its central office in Moscow and branches in 14 regions of the country;
- The Professional Association of Registrars, Transfer Agents and Depositaries (PARTAD) comprises of 97 depositaries and registrars.
- The National Securities Market Association (NSMA—Russian abbreviation NFA) includes companies that hold broker, dealer, depository and trust management licenses for securities; most of these are credit institutions. The NSMA has more than 246 member organisations.
- The National League of Management Companies (NLMC—Russian abbreviation NLU) includes 82 organisations and unites UIF and PPF management companies.
- Noncommercial Partnership of Professional Securities Market Participants of the Ural region (Russian abbreviation PUFRUR) is the only current SRO whose headquarters are located outside Moscow (in Ekaterinburg). It has 24 members—professional securities market participants from the Ural region.

It should be noted that professional securities market participants are quite often members of several SROs. It is therefore not possible to evaluate precisely the general involvement of the professional market community in self-regulatory structures. Nevertheless, by our estimations, approximately 30%—35% of the total number of professional securities market participants are members of at least one self-regulatory organisation; the highest level of participation in an SRO is amongst registrars—over 70%.

One should point out that over the past few years the membership base of leading SROs has stabilised, and that among large professional participant companies of the securities market, membership in self-regulatory organisations has effectively become standard professional practice.

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44 Data from FMMS Russia and from SRO websites as of the end of 2008.

## 4. Main Events Calendar for 2008

<b>January</b>	
09.01.08	The first day of trading on the Russian stock market in 2008 is overshadowed by the on-going fall in on quotations on the US and Asian stock exchanges (continued from year-end 2007)
21.01.08	Fall in quotations on the US and Asian stock exchanges (average 6%). MICEX and RTS indices drop 5.8%, particular stock quotations by 10%; trade is suspended for certain instruments.
24.01.08	RTS and MICEX indices rise by 5.2%—5.8%.
25.01.08	At an extraordinary shareholders general meeting of the CJSC “DCC”, the decision is made to increase equity capital.
<b>February</b>	
01.02.08	The FFMS dictate of 23.10.07 No. 07-105/pz-n “Ratification of the regulation on the qualification of foreign financial instruments as securities” comes into effect.
07.02.08	Misleading information was put on the FFMS website page “Mergers and Displacement” that affected the quotations of the stock issuers it mentioned. The FFMS announces its intention to officially investigate whether this disclosure was an attempt at price manipulation.
11.02.08	The duration of intermediate clearing sessions is reduced from 5 minutes to 3 minutes on the FORTS derivatives market.
13.02.08	The State Duma of the Russian Federation gives preliminary approval to the legislative draft “Exchanges and organised trading”.
22.02.08	The FFMS dictate of 25.12.07 No. 07-112/pz-n “Making amendments to the regulations on the sufficiency of internal capital for professional securities market participants” comes into effect. The amendments make provision to relax the sufficiency ruling in the case of existing professional indemnity and an accompanying petition from a self-regulatory organisation.
28.02.08	The FFMS publishes the results of the official investigation into the incorrect information that had been placed on its website page “Mergers and Displacement”. The finding was that of a technical error and no price manipulation was ascertained.
<b>March</b>	
01.03.08	The FFMS Dictate of 13.11.07 No. 07-108/pz-n “Ratification of the regulation on the auditing of organisations, the monitoring and supervising of which is assigned to Federal Financial Markets Service.” comes into effect.
02.03.08	RF Presidential elections are held. The election results are not seen to affect the results of the Russian stock market.
18.03.08	Technology for the discharge of obligations in securities transactions through simple clearing is launched on MICEX.
20.03.08	NAUFOR calls for a suspension in the trading of OJSC “RichBrokerService” shares on the RTS, on the grounds that continued trading could violate stockholders’ rights.
24.03.08	Trading of OJSC “RichBrokerService” shares is suspended on the Saint Petersburg Stock exchange on the initiative of trading participants (since trading began on 12 February the quotations had risen 100%).
25.03.08	A pilot offering of the exchange bonds of OJSC “RBK Information systems” takes place on the MICEX stock exchange.

#### April

- 08.04.08 The General Prosecutor's office publishes information on its website regarding violations that occurred in the regional branch of the FFMS in the Ural Federal District.
- 09.04.08 The RF State Duma questions the FFMS measures for drawing up and ratifying new rules of standard practice regarding UIFs, in connection with amendments to the law "Investment funds" that were due to come into effect.
- 22.04.08 FFMS declares its intention to audit companies promising investors unreasonably high returns and which appear to be pyramid investment schemes. Seven such companies were identified in the North-West Federal District. The number of victims of these schemes is estimated at 100,000 countrywide.
- 25.04.08 The Federal State and Social Fund for the Protection of Investor and Shareholders Rights held a tender for the fund's asset management. Three management companies won the tender. The fund's assets are estimated at 2 billion rubles.

#### May

- 08.05.08 Vladimir Putin is confirmed as Prime Minister of the Russian Federation (translator's note: in Russian politics this position is known as 'Government Chairman'). Before the RF State Duma V. Putin announces a plan to create a major global financial centre in Russia and touches upon a proposal to lower the oil industry's tax burden. Oil and gas industry stock quotations rise by 5–6%.
- 13.05.08 The FFMS registers an additional issue of CJSC "DCC" stocks amounting to 800 million rubles.
- 14.05.08 The Russian Prime Minister announces changes in the taxation of the oil and gas industry. The quotations of various oil and gas industry stocks grow by more than 10%. An increase in the capitalisation of the Russian capital market exceeds 40 billion dollars.
- 16.05.08 The RF Supreme Court revokes the section in an FFMS dictate that obliges companies to employ a certified specialist to keep their shareholders' register and to cease doing so without the services of this qualified registrar.
- 22.05.08 The Board of Directors of RTS decides to transfer the clearing of securities from NP "SE RTS" to the OJSC "RTS Clearing Centre", effective as of 1 September 2008.
- 23.05.08 The FFMS dictate of 18.03.08 No. 08-09/pz-n "Ratification of the regulation on the procedure for keeping an ownership register for Russian depository receipts" comes into effect.
- 23.05.08 The FFMS dictate 18.03.08 № 08-12/pz-n "Ratification of the Regulation on the procedure for acknowledging individuals as qualified investors" comes into effect.
- 26.05.08 An evening trading session is introduced on the RTS FORTS derivative market.

#### June

- 07.06.08 At the XII Saint Petersburg International Economy Forum, the President of the RF voices the idea to turn Russia into one of the world's major regional financial centres.
- 05.06.08 The RF State Duma passes on first reading a draft to increase administrative responsibility for violations of legislation on the financial market.
- 06.06.08 Last day of trading for RJSC "UES of Russia" stocks on the stock exchanges.
- 16.06.08 The results of the open tender for the trust management of the temporarily unencumbered assets of the state corporation the Cooperative Fund for the Reform of Housing and Public Utilities is announced. Two banks and ten management companies win the tender. The total asset volume transferred to trust management is estimated at 100 billion rubles.
- 17.06.08 The RF Ministry of Interior announces the closure of seven pyramid investment schemes since the beginning of the year. Total damages resulting from their activity exceed 32 billion rubles.
- 20.06.08 OJSC "Mosenergo" stock trading is suspended on MICEX due to increased quotations of more than 15%.
- 24.06.08 On its regional websites the FFMS publishes a list of 16 companies and one US citizen whose activities appear to suggest a pyramid investment scheme.

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26.06.08	The first session of the Community Council of Capital Market Participants affiliated to the FFMS Russia is held.
27.06.08	A specialised company, CJSC “MICEX–Information technologies” is founded within the MICEX Group.
30.06.08	New edited versions of RTS documents introducing netting technology for trading modes with a central counterpart comes into effect.

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#### July

01.07.08	Trading of OJSC RAU “UES Russia” securities ceases due to the restructuring of the company as an affiliation of OJSC Federal Grid Company “United Energy Systems of Russia” (FGC “UES Russia”).
01.07.08	FFMS decides to acknowledge manipulation on the securities market as it relates to a group of individuals.
03.07.08	Technical failure on the RTS.
03.07.08	FFMS revokes the professional securities market participant license of a company offering investors their trust management services with a guaranteed rate of return.
16.07.08	Trading begins of OJSC “FGC UES” stocks—a company that emerged as a result of the reform in the electric power industry.
24.07.08	RF Prime Minister clearly makes known his issues with OJSC “Mechel”. The company’s ADR quotation falls by 38%.
25.07.08	The FFMS dictate of 05.06.08 № 08-24/pz-n “Making amendments to the Regulation on the procedure of authorising the placement of securities within the boundaries of the Russian Federation” comes into force. The number of stocks placed (in circulation) within the boundaries of the RF is reduced from 35 to 30%. For strategic industry sectors this cannot exceed 25%, and for companies involved in the geological study of mineral resources and/or the prospecting and extraction of mineral deposits—5%.
25.07.08	The FFMS dictate of 05.06.08 № 08-24/pz-n “Making amendments to the Regulation on the procedure of authorising the placement and/or circulation of issued securities within the boundaries of the Russian Federation” comes into effect.
28.07.08	The RF Ministry of Finance clarifies the taxation on Russian depository receipts (Ref. № 03-03-05/83).
30.07.08	Technical failure on the RTS.

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#### August

08.08.08	A Memorandum of Understanding is signed between the FFMS and the Commission for securities regulation of the People’s Republic of China.
08.08.08	Armed Russia—Georgia conflict begins.
12.08.08	The FFMS dictate of 01.07.08 № 08-102/pz “Ratification of the Regulation on the procedure of officially reviewing the applications of citizens and organisations” comes into force.
14.08.08	The FFMS publishes the results of the tender for management companies for the management of pension savings capital. 5 companies are chosen.
20.08.08	The FFMS revokes professional securities market participant licenses for repeated failure to present financial reports during the course of the year.
20.08.08	The FFMS revokes the professional securities market participant license of a company which proposed to its “People’s IPO” clients the transfer to the company the trust management of their acquired stocks under terms of a guaranteed percentage return.
26.08.08	The RF President’s edict on the declaration of independence of South Ossetia and Abkhazia is made public. The Russian stock indices fall on average by 6%.
29.08.08	The Investigation Commission of the RF Procurator’s Office announces the arrest of a director of a PPF for attempting to bribe an FFMS employee.

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<b>September</b>	
01.09.08	Georgia breaks off diplomatic relations with Russia.
01.09.08	The RF Government ratifies rules of standard practice for the trust management of closed-end UIFs.
09.09.08	A meeting of the Community Council of Participants of the Financial Market affiliated to the FFMS is held to discuss the "development strategy of the RF financial market to 2020".
09.09.08	FFMS revokes the professional securities market participant licenses of 20 companies for the repeated failure to present financial reports during the year.
10.09.08	The RF President has a meeting with the heads of the FFMS.
11.09.08	The RF President holds a meeting about building an international financial centre in Russia.
13.09.08	The American investment fund Lehman Brothers Holding Inc. declares bankruptcy.
16.09.08	The bank "KIT Finance" announces its inability to settle up with its counteragents.
16.09.08	RTS launches RTS Global.
16.09.08	Trading on the MICEX and the RTS stock exchanges is suspended.
17.09.08	FFMS suspends trade on the Russian stock exchanges from 12:10 until corresponding instruction.
17.09.08	Trading in repurchase transactions and negotiations mode recommences for the evening session on MICEX.
18.09.08	The RF President holds a meeting about minimising the negative effects of the financial crisis on the economy.
18.09.08	A meeting is held in the Central Bank of Russia with professional participants of the securities market and credit organisations.
18.09.08	The FFMS suspends "short sales" and the completion of marginal deals.
18.09.08	Trading time in repurchase transaction mode on the MICEX stock exchange is prolonged until 22:30.
19.09.08	The FFMS revives trading on the Russian stock exchanges.
19.09.08	The FFMS consults with professional members about the crisis situation on the financial market.
19.09.08	Trading is suspended on RTS.
23.09.08	The FFMS authorises professional participants to accept and carry out instructions on the sale of securities previously acquired within the framework of marginal deals and concluded before 17 September, which had been prohibited by a previous directive.
23.09.08	The FFMS puts a new ban on concluding "short sales" and other unbacked transactions.
24.09.08	Technical failure on the MICEX stock exchange.
26.09.08	The FFMS authorises the execution of "short sales" and other unbacked deals and revokes its ban on the execution of marginal deals with the restriction of a margin limit one to one.
29.09.08	The Chamber of Representatives of the US Congress rejects the legislative draft on the country's support of the financial market (so-called "G. Paulson's plan"). Capitalisation of the US financial market falls by 1.2 trillion dollars in a day and a serious drop is experienced in the European and Asian markets.
29.09.08	K. N. Korischenko is named MICEX President; A. I. Potemkin leaves this position.
30.09.08	The FFMS suspends trading on the Russian stock exchanges until 12:30.
30.09.08	The FFMS makes the procedure for suspending trade on the stock exchanges more rigorous.
30.09.08	The FFMS bans the execution of "short sales".
30.09.08	The FFMS authorises the stock exchanges to lengthen the main trading session to 19.00.

<b>October</b>	
01.10.08	The federal law of 30.04.2008 n 56-fn "Additional insurance contributions to the employment pensions savings pot and government support for the creation of pensions savings" comes into force.
01.10.08	End of trading is moved to 19:00 on the MICEX stock exchange.
03.10.08	Trading is suspended on RTS.
03.10.08	The FFMS dictate of 14.08.08 N° 08-33/pz-n "Revocation of the FFMS dictate of 27.12.07 N° 07-113/pz-n" comes into effect, by which the standard on mandatory employment of a financial market specialist to keep the ownership register for securities is rescinded.
06.10.08	Most dramatic fall in the global financial indices of recent years. The Russian stock indices drop by 18–19%, prices on Russian assets on the LSE drop by 30–50%.
06.10.08	Trading is suspended on the MICEX and RTS stock exchanges.
06.10.08	FIX protocol for the management of bids in the trading system is implemented on RTS.
07.10.08	The RF President holds a meeting about minimising the negative influence of the crisis on the economy.
07.10.08	The FFMS suspends trading on the Russian stock exchanges until 13:00.
07.10.08	The FFMS amends the procedure for the cessation and resumption of trading on the stock exchanges.
08.10.08	Trading on the RTS is suspended.
09.10.08	Trading on the MICEX and RTS stock exchanges is suspended.
13.10.08	The Pension Fund of Russia prolonged agreements on the trust management of pensions savings for a further 5 year period.
13.10.08	Trading on the MICEX and RTS stock exchanges is suspended.
13.10.08	Trading on the MICEX stock exchange is suspended.
13.10.08	The legislative package on stabilising the Russian financial market, including the law of 13.10.08 N° 173-FZ "Additional measures to support the RF financial system" come into effect.
14.10.08	MICEX Discovery is launched on the MICEX stock exchange.
14.10.08	The FFMS introduces a new procedure on the suspension and resumption of trade on the stock exchanges.
15.10.08	Trading on the MICEX and RTS stock exchanges is suspended.
16.10.08	The RF President holds a meeting about minimising the negative influence of the financial crisis on the economy.
16.10.08	Trading on the MICEX and RTS stock exchanges is suspended.
17.10.08	Technical failure on the MICEX stock exchange.
20.10.08	A Council for the Development of the Financial Market is created under the jurisdiction of the RF President and headed by the First Deputy Prime Minister of the Russian Federation.
21.10.08	RF Government decree of 15.10.08 N° 766 "Making amendments to the Russian Federation Government decree of 19.01.08 N° 18 "Procedure for managing the capital of National Welfare Fund" come into effect, allowing "Vnesheconombank" to invest 175 billion rubles in Russian securities.
23.10.08	Trading on the MICEX stock exchange is suspended.
24.10.08	Trading on the RTS is suspended until the end of the day or to an FFMS instruction.
24.10.08	Trading on the MICEX stock exchange is suspended until 28 October.
28.10.08	The President of the Russian Federation signs amendments to the laws "The Central Bank of Russia" and "The securities market", which allow the Bank of Russia to conduct open market buy-sell operations in securities.
28.10.08	The FFMS dictate of 20.05.08 "08-19/pz-n "Ratification of the Regulation on the composition and structure of shareholder and UIF assets" comes into force.
28.10.08	The RF government ratifies the rules of standard practice regarding the trust management of opened-end UIFs.
28.10.08	Trading on the RTS is resumed in normal mode.



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- 30.10.08 The directors of “Vnesheconombank” state their intention to invest daily from designated capital of the National Welfare Fund 5 billion rubles to support the financial market.
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- 30.10.08 Trading on the MICEX and RTS stock exchanges is suspended.
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- 30.10.08 The FFMS management announces its intention to consider the possible refusal of professional securities market participant licenses.
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#### November

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- 01.11.08 NAUFOR sends a proposal to the Council under the RF President for the development of the financial market.
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- 05.11.08 The RF President makes an address to the Federal Assembly of the RF, in which it is deemed necessary to pass a legislative package that will form the basis for the creation of a leading global financial centre in Russia.
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- 06.11.08 Trading on the MICEX and RTS stock exchanges is suspended.
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- 06.11.08 Trading on the RTS is suspended.
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- 07.11.08 The “Plan of action to rectify the situation in the financial sector and in various sectors of the economy” is ratified by the RF Prime Minister.
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- 10.11.08 Technology for the conclusion of deals with OJSC “Sberbank Russia” stocks with settlements on the fourth day via a central counterpart is launched onto the RTS.
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- 10.11.08 Technical failure on the RTS.
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- 11.11.08 Trading on the MICEX stock exchange is suspended.
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- 11.11.08 Trading on the RTS is suspended.
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- 12.11.08 Trading on the RTS is suspended.
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- 12.11.08 Significant drop in the US share indices in the light of the US Ministry of Finance’s refusal to buy back the illiquid mortgage assets of banks.
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- 13.11.08 Trading on the MICEX and RTS stock exchanges is suspended.
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- 13.11.08 NAUFOR discusses the FFMS draft regulation on the procedure of calculating own assets and prepares a proposal to rescind the FFMS regulation.
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- 14–15.11.08 An anti-crisis summit takes place in Washington with the heads of “G20” countries.
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- 17.11.08 The “Long-term socio-economic development strategy of the Russian Federation to 2020” is ratified by the RF Government Order № 1662-r.
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- 17.11.08 Trading on the MICEX and RTS stock exchanges is suspended.
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- 18.11.08 Trading on the MICEX and RTS stock exchanges is suspended.
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- 18.11.08 Technical failure on the RTS.
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- 19.11.08 Trading on the MICEX stock exchange is suspended.
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- 19.11.08 A Memorandum of Understanding is signed between the FFMS and the Commission for securities and exchange operations of Cyprus.
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- 19.11.08 An informal meeting of members of the NAUFOR Board of Directors with the head of the FFMS is held to discuss the current problems on the securities market caused by the financial crisis and also the measures taken by the FFMS.
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- 20.11.08 Trading on the MICEX and RTS stock exchanges is suspended.
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- 24.11.08 Trading on the MICEX stock exchange is suspended.
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- 28.11.08 Amendments to the FFMS dictate of 06.03.07 № 07-21/pz-n “Procedure of licensing various types of professional activity on the securities market” come into effect, in particular the disclosure of information on the structure of ownership of the licensee.
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<b>December</b>	
02.12.08	Trading on the RTS is suspended.
05.12.08	A Memorandum of Understanding is signed between the FFMS and the Commission for securities and exchanges of India.
08.12.08	The ratings agency Standard&Poors drops the sovereign rating of the RF by one level with a “negative” prognosis.
10.12.08	The FFMS registers amendments in the rules of trade on MICEX, which allows the Bank of Russia to become an exchange trader.
12.12.08	Trading on the MICEX and RTS stock exchanges is suspended.
15.12.08	Moody’s ratings agency drops the sovereign rating of the RF.
16.12.08	NAUFOR asks the FFMS to revoke the ban on executing unsecured deals and “short sales”.
23.12.08	The RF Ministry of Internal Affairs talks publically about the growing number of “investment pyramids”, 28 such organisations were precluded from trading; overall damages constituted 400 billion rubles and the number of injured parties—400 thousand people. The biggest “pyramid” caused damages of 18 billion rubles and the number of injured parties—250 thousand people.
24.12.08	The RF Government ratifies the rules of standard practice regarding the trust management of interval UIFs.
29.12.08	The RF Prime Minister states that the situation in the country’s financial sector will stabilise in the III–IV quarters of 2009.
29.12.08	“The strategy for the development of the financial market of the Russian Federation to 2020” is ratified by the RF Government Order № 2043-r.
31.12.08	MICEX announces it is being sued, a positive outcome from which could significantly influence the financial situation.