

No More Russian Roulette

Stability, Growth

Make for a Market

Set to Climb Higher

By ANDREW LANGLEY from THE WALL STREET JOURNAL

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MOSCOW -- A robust economy, an increasingly clear political landscape and promises of hefty state spending make Russian stocks an attractive bet to at least maintain this year's pace through 2008, market participants say.

But any slowdown in the global economy could put a damper on that performance.



OAQ Gazprom, with connected Chairman Dmitri Medvedev, could be a top performer in 2008. Here, a company pipeline project

"Russia should fare better relative to other emerging markets due to its strong exposure to very high oil prices, huge foreign reserves, double surplus [in both trade and current-account balances], political stability and strong domestic demand," said Credit Suisse analyst Vladimir Savov, who expects the RTS index to advance to 2600 by the end of 2008.

The country's benchmark RTS index has risen more than 19% to 2264.95 since the end of 2006. This year, the dollar-denominated index has lagged well behind the emerging markets of

Brazil, India and China -- known collectively as the BRIC group of economies. But investors believe that is set to change in 2008.

"We favor Russia over the other three BRIC countries and will look to increase our exposure next year," said Michael Konstantinov, who manages Allianz RCM's \$600 million BRIC Stars Fund in London.

Russian shares look attractive based on valuations, he said. The market is at 11 times next year's prospective earnings, compared with 17 times for China and 20 times for India.

The reasons behind the market's relatively modest performance this year include a massive pipeline of initial public offerings, rising costs in the oil sector that dented earnings at energy companies as well as political tensions, most notably over who would succeed Vladimir Putin as president in March.

With the issue of Mr. Putin's successor now largely settled, many investors and brokerage firms are predicting a more lucrative 12 months ahead. Lofty crude prices, they say, should continue to bolster the economy, and the government will begin spending some of its windfall oil revenue.

Investment watchers now expect foreign investors to allocate more cash to Russia-focused funds, rather than to the other BRIC countries, all of which have proved more popular destinations for institutional money throughout most of 2007.

Indeed, this trend has already begun, according to global data published by Emerging Portfolio Fund Research, of the U.S., which notes net inflows into Russian funds over the past three months and a particularly big jump this month.

"There's been a sigh of relief [among foreign investors]. In the medium term, there will be more of the same economically under Putin and it's working," said Ed Conroy, an assistant investment manager on the global emerging-markets equity team at Aberdeen Asset Management.

The focus now, the investment watchers say, will switch away from politics and toward Russia's economy, which is notching annual growth in excess of 7% thanks to high global prices for the likes of metals and crude oil.

Gas monopoly OAO [Gazprom](#) should be a top performer as its current chairman, Putin protégé Dmitri Medvedev, becomes president and could give the company favorable treatment, such as desired tariff increases and access to gas and oil projects.

Companies that don't rely on exports and that benefit from the strengthening ruble, such as state-owned bank OAO Sberbank, should also fare well, said Roland Nash, chief strategist at investment bank Renaissance Capital in Moscow. He sees the RTS soaring to 3000.

Many agree most headwinds in 2008 will likely come from abroad.

"I don't expect astonishing returns -- around 15% to 20% -- but next year will also be much more volatile due to the worsening global backdrop," said Alexander Golovtsov, head of investment research at UralSib Asset Management, which manages \$4 billion in both equities and fixed income.

There is also a risk that a drop in oil prices could be a drag on Russia's prospects. But Mark Atherton, London-based head of emerging markets at Aviva PLC's Morley Fund Management, which manages \$20.8 billion in emerging markets funds, said even if oil dropped to \$65 a barrel from its current perch above \$90 a barrel, it wouldn't immediately end Russia's growth story.

