

Investment Commentary

From the Investment Desk
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From Russia With Love

I summarize key findings of my week-long research trip to Moscow last week. Views came from companies that represent stockbroking, oil & gas, gold mining, property development, telecom, steel manufacturing & retail/ hypermarket.

- ❑ Company representatives present upbeat prospects, domestically & internationally. Companies boost profits via higher value-add activities & acquisitions. The extraction companies expressed confidence in supply of Russian mines/ fields & robust demand. The steel manufacturer mines its iron ore where supply could last 100y. Russia's 17m km² fertile land mass is rich in natural resources.
- ❑ Connections to former Soviet satellite countries facilitate business expansion beyond Russia. Central Asia is booming.
- ❑ The greasy & gassy wealth has boosted Russia's confidence as a rising superpower, both economically & politically. Europe imports 40% of its natural gas from Russia.
- ❑ Moscow is the most expensive city on earth, thanks to oil & gas, inflation & "shortage" of real estate. Residential apartments go for US\$2,000 to US\$10,000 per m². Four-star Aerostar Hotel charged S\$420 per night, believed to be foreigner's rate. You can't get a visa without booking accommodation first.
- ❑ While the city look rich (in history & ornate buildings), average monthly salary ranges from US\$300 to US\$700. Middle class represents 17% of Russia's dwindling population of 147m; domestic consumption is an attractive theme. A minority (7%) earns US\$4,000-7,000/ month. The 861y-old city of 10m people spread over 1,000 km² attracts 3m foreign workers & students, including guest workers from Central Asia.
- ❑ Credit & customer service are lacking, but we expect lending to pick up. Banks charge housing loan rates ranging from 18-30% for 5y loans. A near-complete apartment block

close to the future Russian mega mall was sold out, all paid with cash. Real estate prices could crash, but impact could be low due to low borrowings.

- ❑ As a function of real estate, most things are generally expensive. On the flip side beer & bread are pretty affordable (both S\$1-plus) and subway/ train rides (RUB90). Moscow runs the world's largest subway network, with subway trains that pass, each minute, its >165 stations over 265km track. Inside each station looks like a museum, other than functioning as bomb shelters.
- ❑ Traffic is a nightmare despite 6- to 12-lane highway: airport-hotel ride took 4 hours, instead of one. Russia is Europe's largest car population (29m). Gasoline goes for RUB 25 (US\$1) per liter.
- ❑ **Russian equities are even cheaper** than beer & bread, where 2009 PE & PB ratios have been pummeled to 6x & 1.5x respectively. Russian Trading System, (1,282; 80% commodities), which plunged by 50% since peak in May, or -14% in August. Foreigners sold US\$15b of Russian equities in reaction to TNK-BP tussle, government action against certain Russian mining conglomerates & Russia's intrusion in Georgia. The rich sold heavily to meet margin calls. This is despite US\$9b to support the rouble & US\$10b injected into the banking system to alleviate credit shortage.
- ❑ The stockbroker suggests spiraling inflation & crude oil <US\$80 as being damaging to Russian equities. Catalysts that trigger equities recovery next year: commodity rebound, blow up in Middle East, tax cuts/ government reform & time. The oil & gas company said that tax cuts could bump up its earnings in 2009; Russia has been building its foreign reserves from energy revenue. Like this title from a James Bond movie, time will tell when Russia will be another hit among investors.

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