

Early Investor Vostok Nafta Closing Russian Equity Portfolio

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Commodities investor Vostok Nafta Investments has a local portfolio spanning oil and gas, agriculture, forestry and other sectors.

Sweden's Vostok Nafta, one of the first foreign investors to buy into Russia after the fall of the Soviet Union, will sell all of its shares because of increasing competition and falling returns.

The veteran of 14 years of trading in commodity stocks said that it has already exited from almost all of its portfolio of Russian listed holdings — which included oil giant TNK-BP, diamond miner Alrosa and power company Inter RAO — because of increasing competition and falling returns.

While the Stockholm-listed fund manager that has a net asset value of \$495.39 million maintained it was not abandoning Russia, industry insiders suggested it was capitulating due to exhaustion.

Investors in Russian shares face strong headwinds in the current climate as international macroeconomic uncertainty depresses local markets. Despite buoyant oil prices, the MICEX Index has risen only 3.6 percent since the beginning of the year.

"We have felt that even though there remains potential upside in our portfolio of Russian-listed holdings, the risk reward ratio ... has deteriorated," Vostok Nafta's managing director, Per Brilioth, said in a report published on the company's website.

"Demand is still there but the increased number of sources of capital has led to returns coming down."

While Vostok Nafta's focus in Russia had always been commodity stocks, including particularly large holdings in gas giant Gazprom in 2008, it will now move exclusively into private equity.

The core of its existing private equity holdings are stakes in agriculture firm Black Earth Farming, Internet trading platform Avito, online credit card provider Tinkoff Credit Systems and Siberian forestry outfit RusForest.

But Brilioth told The Moscow Times on Thursday that the decision was linked to internal strategy and that Vostok Nafta would be prepared to return to investing in Russian shares if conditions changed.

"I wouldn't read too much into the timing of the decision ... our focus on Russia is unchanged," he said by telephone.

The stock sell-off since the start of the year has generated a cash pile of about \$242 million for Vostok Nafta, which it intends to distribute to shareholders via a mandatory share redemption program likely to be approved by a special general meeting on Aug. 29.

At one point, Vostok Nafta was rare in its ability to generate profits from Moscow-traded equity, Brilioth added, but this is no longer the case. "There are a bunch of people doing Russia," he said. "We can do it, but can we do it better?"

Some Russian fund managers concurred that it was the prospect of more mundane work that was deterring Vostok Nafta.

"There are very specific reasons for why they are doing this," said a partner at an equity investment fund with over \$1 billion under management in Russia and Eastern Europe, who requested anonymity to speak freely.

"Vostok Nafta has been very successful and very lucky ... [they] don't want to fight hard and struggle."

Others pointed to the adverse macroeconomic conditions, particularly the uncertain situation in Europe, and the negative international perception of the Russian investment climate.

"This is not the first foreign investor in Russia that has Russia fatigue," said Bruce Bower, a partner at Verno Capital in Moscow. "Unfortunately, there is a significant amount of skepticism ... a lot of people roll their eyes when you start talking about Russian reform."

Despite its long history, Vostok Nafta is a relatively small player among the foreign funds that provide capital to a domestic market that lacks homegrown institutional investors.

And, while Vostok Nafta's Brilioth denied that his company's decision was likely to be followed by others suffering from the competition, some industry players disagreed.

"Things right now are not as they were 5 or 10 years ago ... markets are becoming more mature," said a director at a Russian fund with \$3.5 billion under management, who requested anonymity to speak freely.

"You cannot rule anything out in these conditions."

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