

Uzbekistan to withdraw from EurAsEC

Renaissance Capital

Yesterday (12 Nov) Kommersant reported that Uzbekistan President Islam Karimov declared an intention to withdraw from the Eurasian Economic Community (EurAsEC), claiming the organisation is inefficient. At the latest EurAsEC summit in October this year, the leaders announced plans to establish a new customs union which would include only Russia, Belarus and Kazakhstan, which may be the reason the Uzbeks want to withdraw from the organisation.

Relations between Uzbekistan and Russia, and Uzbekistan and Kazakhstan have always been complex. Russia has a monopoly over Uzbek gas purchases, while Kazakhstan rivals Uzbekistan for regional leadership. After the suppression of riots in the Uzbek city of Andijan in May 2005, the EU introduced a ban on visas for Uzbek officials. At the same time, Uzbekistan joined the EurAsEC and agreed to take part in the Caspian gas pipeline project. However, after the recent events in the Caucasus, the EU started to seek alternative sources of energy supplies, and lifted the visa ban urging the Uzbek president to take part in the Nabucco project (gas transfers from Central Asia through Azerbaijan to Europe).

Alliance Bank repays 99% of 2008 outstanding debt

Renaissance Capital

ALLB LI: BUY, target price: \$6.8

Event: According to a press release from Alliance Bank yesterday (11 Nov) the bank has repaid \$181mn in syndicated and bilateral loans maturing in 2008, as follows:

* \$71mn - second tranche of a \$300mn syndicated loan raised in Nov 2006, was repaid on 31 Oct. The lead mandate arrangers were Citibank, ING and Standard Bank.

* \$100mn bilateral loan - raised in Nov 2007 and provided by HSBC with a 370-day maturity, was

CONFERENCE CALL: Frontier markets are a long-term opportunity

Adrian Ciocoi

in London

Capitulation has probably been the best the word to describe the situation in the investment community at the end of October. Those who didn't throw in the towel, are migrating towards companies of high quality, large market caps, strong balance sheets and high trading/liquidity. So why would anyone consider investing in the frontier markets? The former great hockey player Wayne Gretzky put it best: "Skate to where the puck is going, not to where it is."

The above quote sums up the overall belief stated one way or another by most of the 30-plus participants at the recent "Investing in Frontier Markets" conference held in London on November 6 and 7: frontier markets represent a long-term opportunity and may very well be the next major asset class. Currently, of the total assets under management held by the fund managers invested in emerging markets, approximately just 2% is held in frontier markets; that number is expected to increase.

To boldly go

Most of these "frontiers" are actually developing economies but with undeveloped equity markets. Overall, these countries have a population of approximately a billion, an estimated \$2.4 trillion of nominal GDP, and a \$1.7 trillion market cap. The table below shows the main frontier markets split by continent.

Below are some of the pros and cons of investing in the frontier markets:

- The availability of information is scarce and most companies don't even have a website. Larry Speidell of Frontier Market Asset Management suggested that, "the opportunity is inversely proportional to the availability of information";
- There is a lack of good equity analysts to research the companies in Nigeria; Dr. Ayo Salami with Duet Victoire Africa Index said an analyst based in Lagos could earn as much as a London-based equity analyst. Independent equity research providers are filling the gap with local presence on the ground;
- There's a lack of quality management teams, complained Laurent Demey, CIO of Propaco; Andre DeSimone with Kestrel Capital East Africa argued



the companies in Kenya are extremely well managed. One of the conference participants suggested that the current financial crisis might bring some people back to their native countries;

- Some of the frontiers (like Saudi Arabia) have foreign investment restrictions. Nevertheless, a Deutsche Bank or several Gulf Cooperation Council (GCC)-based brokers could allow access to foreign investors through some structured instruments;
- There are high capital gains taxes, yet in some like Kenya there are no capital gains taxes;
- Corruption is still an issue. Laurent Denev, CEO of Propaco, said in order to get access to information, one needs to know those who are connected in the local community because they do business; and avoid those who do business because they are connected;
- Currently, especially in Africa, trading costs are high and settlement is problematic. There are shallow forex markets in the currencies in which the frontiers are dealing with. To address this, some suggested there are many "frontier-based companies" one could access through ADRs or GDRs (see table below). Also indirect plays could be done by investing outright in the stock of global companies like Heineken, Vodafone, Diagio, Barclays, Lafarge, ie. companies that have a strong representation in some of the frontier markets.

Overall, it was agreed that for the medium term, the frontier markets would continue to be decoupled from emerging or developed markets and this low correlation is an appealing feature of such markets.

At the conference, there were several case studies presented on the stock markets in frontier markets. Dr. Ayo Salami, CIO of the Duet Victoria Africa index Fund, a veteran investor in the Sub-Saharan African (SSA) region, said the change in Africa over the past 10 years has been dramatic. "In the past, there were many companies trading in single P/Es but none above \$1m per day. Now the situation reversed, and there are larger companies available to invest in but some P/Es are in double digits."

repaid on 5 Nov.

* \$10mn - partial repayment of the third tranche of the \$300mn syndicated loan mentioned above was made on 10 Nov.

As a result, Alliance has repaid 99% of its \$1.022bn in foreign liabilities maturing in 2008, leaving just \$12mn to be repaid in 2008.

Action: Neutral for the bank, in our view.

FAO warns of fisheries crisis in Central Asia bne

Production by fisheries in Central Asia and the Caucasus has dropped dramatically in the years after the breakup of the Soviet Union, a new report from the UN Food and Agriculture Organization (FAO). The region's fishing and aquaculture sectors are now in a state of crisis, the report warns.

The greatest collapse in production was seen in Georgia and Kyrgyzstan, where annual inland fisheries and aquaculture output fell by 98% between 1989 and 2006. In Tajikistan a drop of 94% was recorded, and in Azerbaijan 92%.

Armenia saw a reduction in fisheries output of 81%, and in Kazakhstan, Turkmenistan and Uzbekistan the decrease was between 60% and 72%.

"As a result, fish consumption in the entire region is down -- to less than 1 kilogramme per capita per year -- and fish and fisheries products have largely disappeared from the population's diet," the FAO says.

Causes of the drop in production include overfishing and poor management; dramatic cuts to investment in research and production facilities; decreased spending on maintenance of fleets and hatcheries; weak management of water bodies and other ecological problems, including pollution of rivers; and, a lack of investment in modern processing and marketing facilities and equipment.

Dr. Salami is an advocate for indexing the stocks currently in the SSA rather than actively manage a portfolio, given there are only approximately 40 companies in the "over \$1bn market cap" universe (mostly companies located in Nigeria and Kenya, and predominantly banks), which draw most of the attention anyway. "So why pay a higher fee for an active portfolio manager that has approximately the same options to invest in?"

The following table presents the number of companies with market caps above \$1bn that operate in the frontier markets in each of the five continents.

The Frontier Markets

Africa	Central & East Europe	Middle East	Asia	America
Algeria	Bulgaria	Bahrain	Bangladesh	Argentina
Botswana	Croatia	Iran	Cambodia	Belize
Egypt	Cyprus	Jordan	Kazakhstan	Colombia
Ghana	Estonia	Kuwait	Maldives	Cuba
Ivory Coast	Georgia	Lebanon	Pakistan	Ecuador
Kenya	Latvia	Oman	Philippines	Jamaica
Mauritius	Lithuania	Qatar	Sri Lanka	Panama
Morocco	Romania	Saudi Arabia	Vietnam	Paraguay
Mozambique	Serbia	UAE		Peru
Namibia	Slovakia			Trinidad-Tobago
Nigeria	Slovenia			Uruguay
Tanzania	Ukraine			Venezuela
Tunisia				

Frontier Markets Eligible through ADRs, GDRs or H shares

Bangladesh	Ghana	Namibia	Ukraine
Cambodia	Jamaica	Panama	Zimbabwe
Cote d'Ivoire	Kazakhstan	Qatar	
Cyprus	Kenya	Slovenia	
Ecuador	Lebanon	SriLanca	
Estonia	Lithuania	Trinidad&Tobago	
Georgia	Mauritius	Tunisia	

Source: Seminar Investing in Frontier Markets Nov 2008

Companies in the frontier markets with market caps above \$1bn

Africa	Central & East Europe	Middle East	Asia	America
37	14	268	47	29

Source: Seminar Investing in Frontier Markets Nov 2008

Comparative returns and volatility

	Frontier	Emerging	Developed
Total return	392.1%	225.8%	121.9%
Return per annum	13.3%	9.7%	6.5%
Volatility (*)	11.5%	23.8%	13.9%

Source: PDML, Bloomberg, S&P, MSCI Barra. Indices used are the S&P/IFCG Frontier Markets Composite, S&P/IFCI Composite and the MSCI World Index. Data are total returns in USD. Period is 31.12.95 to 31.08.08.

Performance of the frontier markets

In the 12 years from January 1996 to August 2008, the frontier markets outperformed both the emerging and developed countries, and exhibited lower volatility. Dan Broby of Danfunds mentioned that since 1995, there has been at least one African-based equity market among the top-10 best performing markets in the world; in 2007, Zambia returned 127% (in dollar equivalent), Malawi 114%, Cote D'Ivoire 105% and Nigeria 90%, and in 2006 Malawi returned 129%. **bne**

Adrian Ciocoi is Head of Research "Emerging Europe & Beyond" at Riedel Research Group