

Analytical Review of the Collective Investments Market In The Third Quarter 2008

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1. The Ukrainian Stock Market

The third quarter 2008 witnessed further deepening of the financial crisis that continued affecting the global economy. Whilst during the second quarter those were financial institutions and their clients that were affected most by the crisis, in the third quarter it was already affecting all business entities.

A number of loud bankruptcies and acquisitions, in particular, of US investment banks from the TOP five Lehman Brothers to Merrill Lynch, significantly undermined the trust to the global financial system. Moneys that flowed from the stock markets to the raw material market in the beginning overheated the latter and afterwards caused a decline in the raw materials' prices in the conditions of the global economy's slowing down growth rate. Impairing macroeconomic indices of developed countries, in particular, business activity index decline, growth of inflation and unemployment levels, caused a distrust towards national currencies and significant currency exchange rate fluctuations.

It was only consolidation of the governments of developed countries around overcoming of the said negative processes that allowed to mitigate their consequences to a certain extent and to prevent a collapse in the stock markets. As a result, developed countries' indexes decline over the third quarter (Table 1) could be characterized as moderate. In the meanwhile, decreasing investors' trust toward stock markets caused a serious outflow of capital from the emerging markets, in particular, from the Ukrainian one. During the third quarter 2008, PFTS index dropped by 49,54% and at quarter end comprised 369,47 points, which became one of the worst results among the global indexes.

Table 1. National markets' stock indexes in 2008

Index	As of 01.01.2008	As of 01.07.2008	As of 30.09.2008	Change over 3d quarter 2008	Change YTD
PFTS (Ukraine)	1174,02	732,27	369,47	-49,54%	-68,53%
RTS (Russia)	3158,76	3353,25	1848,66	-44,87%	-41,48%
HANG SENG (China)	27812,65	22102,01	17880,68	-19,10%	-35,71%
WSE WIG (Poland)	55648,53	40489,39	37367,32	-7,71%	-32,85%
DAX (Germany)	8038,6	6315,94	5831,02	-7,68%	-27,46%
S&P 500 (USA)	1468,36	1284,91	1166,36	-9,23%	-20,57%
FTSE 100 (Great Britain)	6456,9	5479,9	4902,45	-10,54%	-24,07%
NIKKEI 225 (Japan)	15307,78	13463,2	11259,86	-16,37%	-26,44%

Such situation in the stock market, which is the main object of investments of non-venture CII funds, conditioned a further decline in the collective investments market both by the volumes of funds under AMC management and the profitability of the CII under their management.

2. Number of AMC and CII

According to UAIB data, in the third quarter 2008, 10 new asset management companies emerged (in the second quarter – 38), and as of 30.09.2008 their number reached 404, whilst the number of registered CII reached 1158 funds. An average number of CIIs per one AMC grew by 0,1 and comprised 2,9 funds (Chart 1).

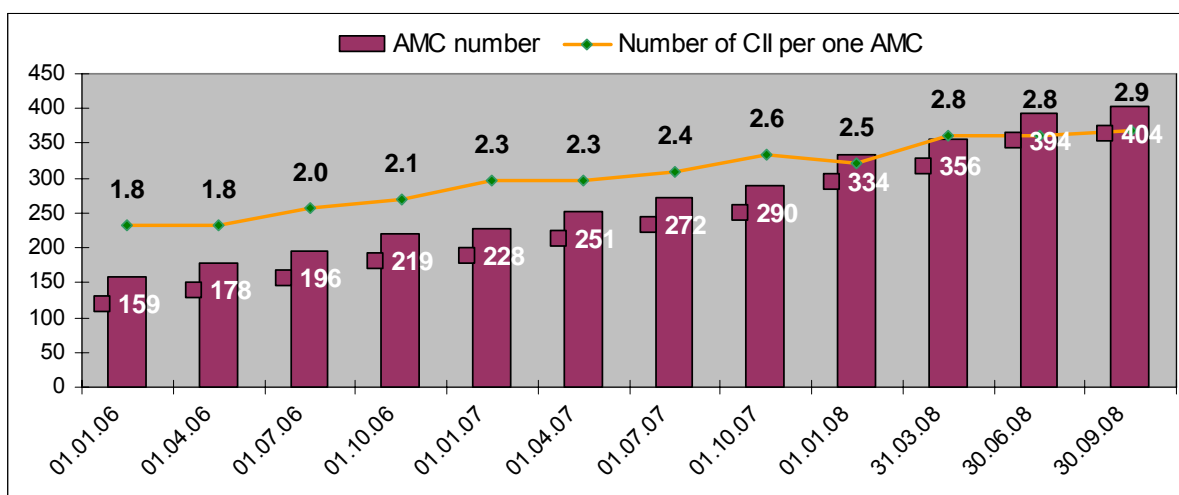


Chart 1. AMC and CII number dynamics per on AMC since 01.01.2007 through 30.09.2008

According to UAIB data, the number of CII that reached compliance with the standards as of the end of the third quarter 2008, reached 780 funds (Table 2). The growth for the quarter comprised 8,9%, and since year beginning – 35,2%. The growth was mainly due to an increase in the number of venture funds that reached compliance with the standards (+43 over quarter, +143 since year beginning), and at quarter end there were already 566 CII (72% of the total number).

Table 2. Dynamics of the number of CII that reached compliance with the standards, by the types of CII in 2008

Date	Total	UIF (SIF)					CIF	
		Open-ended	Interval	Close-end diversified	Close-end non-diversified	Venture	Close-end non-diversified	Venture
01.01.2008	577	14	25	3	15	423	63	34
01.07.2008	716	23	28	3	18	523	80	41
30.09.2008	780	24	34	4	19	566	90	43
Growth over 3d quarter	8,9%	4,3%	21,4%	33,3%	5,6%	8,2%	12,5%	4,9%
Growth YTD	35,2%	71,4%	36,0%	33,3%	26,7%	33,8%	42,9%	26,5%

A growing number of funds that reached compliance with the standards in the conditions of financial crisis could be explained by a considerable time lag between the decision-making on

establishing a fund and reaching the standards by that fund. Slowing down of CII number growth pace should probably be expected over the fourth quarter 2008 through the first quarter 2009.

3. Regional Distribution of AMC's and CIIs

Among the regions, just as before, those were Kyiv and Kyiv Region that led both by the number of AMC's and funds and by the total value of assets under AMC management, where 288 AMC's (Chart 2) and 70% of funds (Chart 3), whose assets comprised 79% of the total asset volume of non-venture funds, were located.

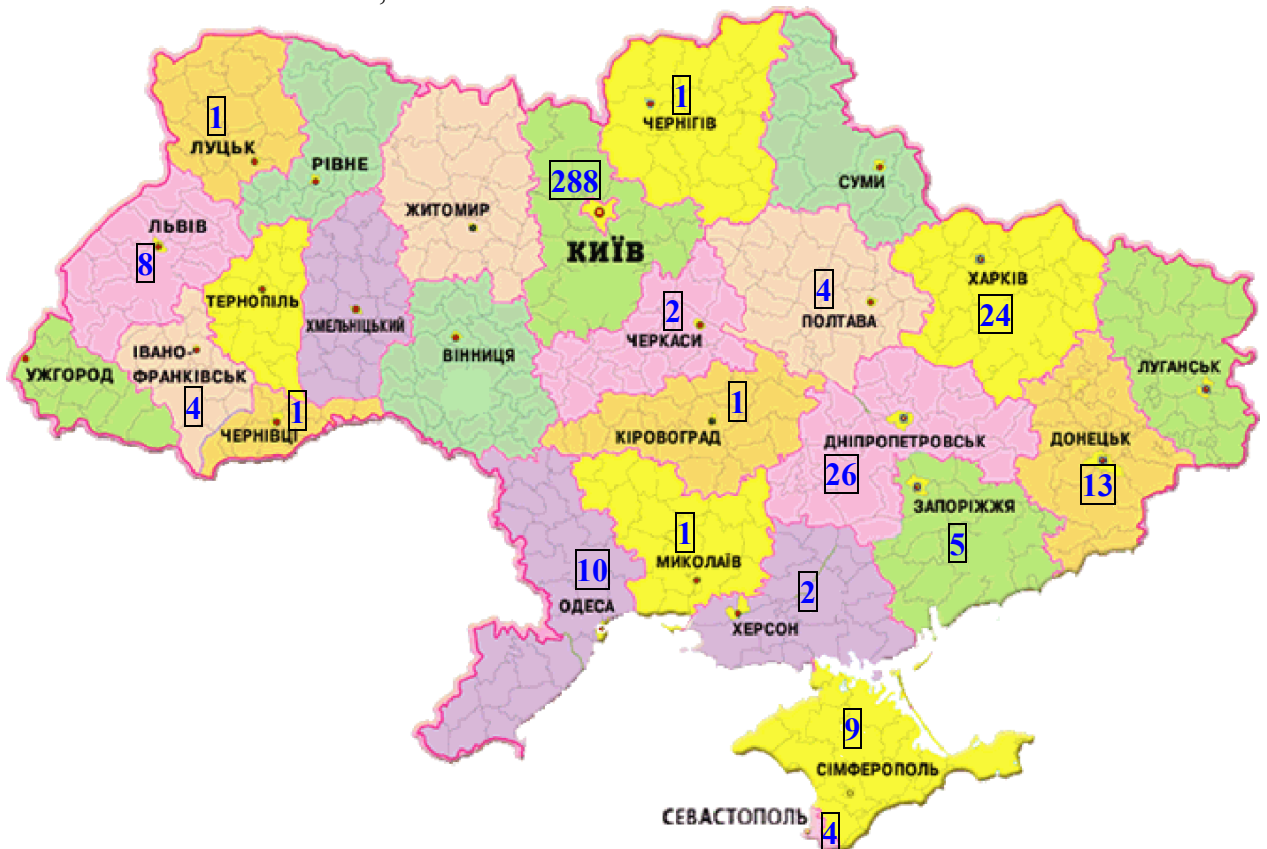


Chart 2. Regional distribution of AMC's as of 30.09.2008

Second place, just as previously, went to Dnipropetrovsk Region (8% of CIIs and 18% of assets), and the third one - to Kharkiv Region (7% of CII and 2% of assets).

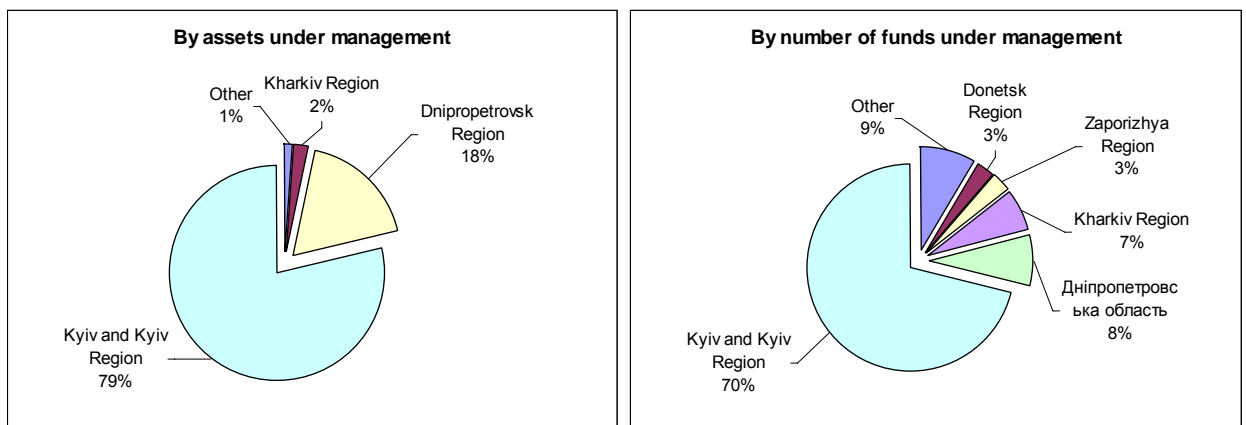


Chart 3. Regional distribution of CII by the number of non-venture funds and the value of non-venture assets under management, as of 30.09.2008.

4. Non-venture CII Asset Value

Against the background of stock market decline, the asset value of non-venture funds somewhat decreased and at quarter end comprised UAH 4669,2 M (-2,5% compared to previous quarter, +16,08% since year beginning) (Chart 4). If in the second quarter the drop of asset value in non-venture CII portfolios was compensated by new close-end funds with significant volumes of assets under management reaching compliance with the standards, in the third one the new funds' asset value was not enough for that. Provided current stock market tendencies in the stock market are preserved in the next quarter, we probably should expect further decline in the asset value of non-venture CII.

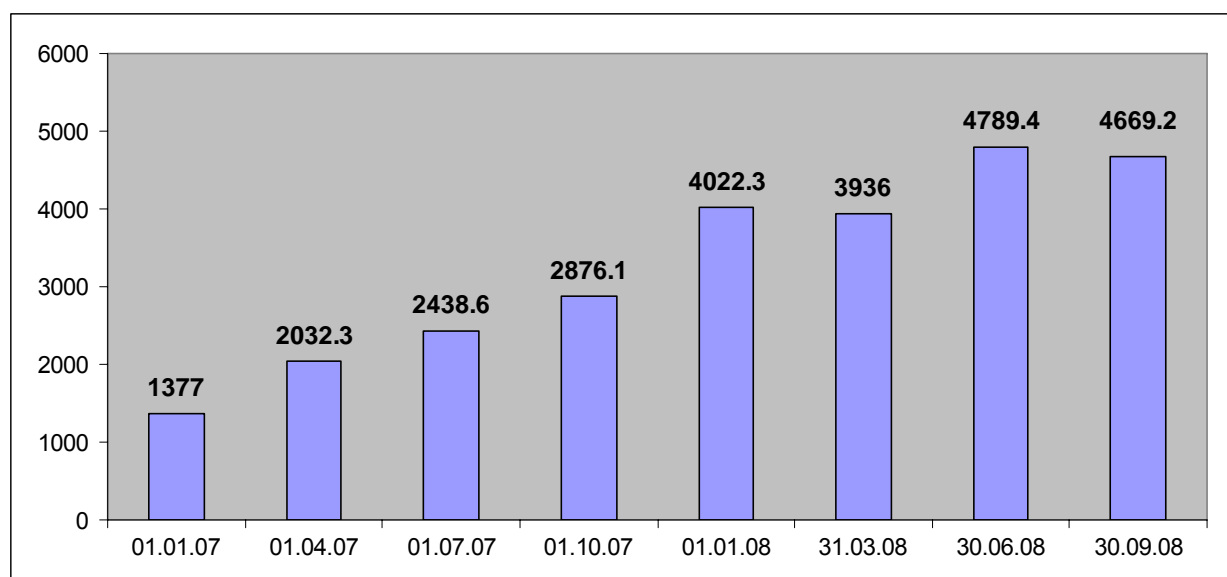


Chart 4. Non-venture CII asset value dynamics in 2007-2008, UAH M

In the third quarter, non-venture funds of all types were relatively evenly losing asset value. Compared to the previous quarter, a considerable slowing down in the rate of value decrease of the least liquid open-end CII, which decreased by 3,52% (-24,36% since year beginning) and at quarter end comprised UAH 427,2 M (Table 3), was observed. Taking into account the loss of their portfolio's value, that could be explained by appearance of new funds with a considerable asset value.

Table 3. Non-venture CII assets under management dynamics in 2008, by the types of funds

Types of Funds	AuM as of 01.01.2008, UAH M	AuM as of 01.07.2008, UAH M	AuM as of 30.09.2008, UAH M	Change over 3d quarter 2008	Change YTD
Open-ended	564,8	442,8	427,2	-3,52%	-24,36%
Interval	294,1	263,6	258	-2,12%	-12,27%
Close-end	3163,4	4083	3984	-2,42%	25,94%
Total	4022,3	4789,4	4669,2	-2,51%	16,08%

Due to the evenness of non-venture CII asset value changes by the types of funds, their proportion by asset value did not change (Chart 5). Just as previously, the greatest share – 85% – was comprised by close-end funds.

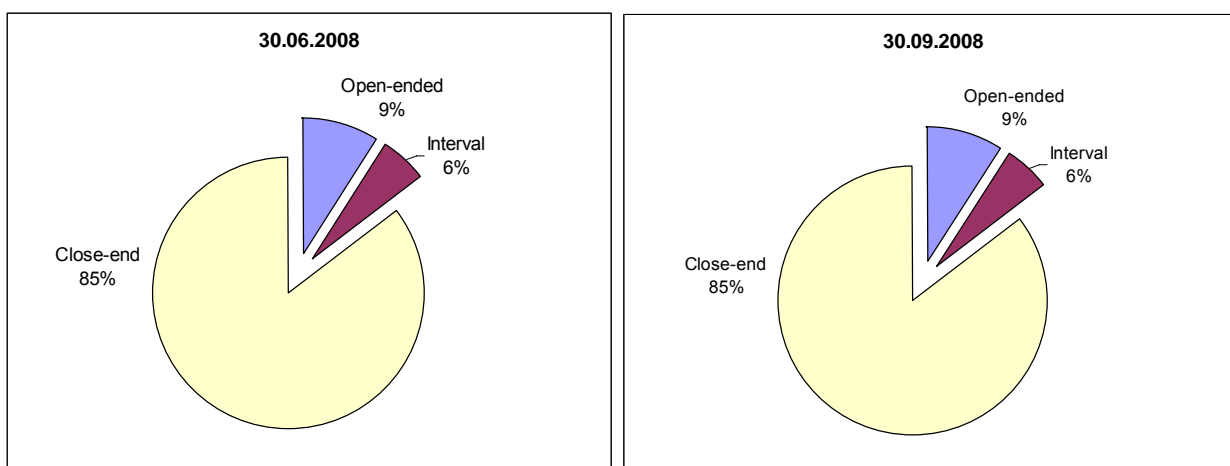


Chart. 5. Non-venture CII asset value distribution in 2008, by the types of funds

Total value of the *net assets* of non-venture funds also dropped from UAH 4160,3M at quarter beginning to UAH 4153,8M (-0,16%) – at the end (Table 4). That happened owing to open-end (-0,98%) and interval (-2,64%) CII, whilst the NAV of close-end CII increased. The stake of close-end CII liabilities within their asset value dropped from 15% at quarter beginning to 8,9% at the end, which was probably due to the settlements for the assets provided in the previous quarter.

Table 4. Non-venture CII net asset value dynamics in 2008, by the types of funds

Types of Funds	NAV as of 01.01.2008, UAH M	NAV as of 01.07.2008, UAH M	NAV as of 30.09.2008, UAH M	Change over 3d quarter 2008	Change YTD
Open-end	555,4	427,8	423,6	-0,98%	-23,73%
Interval	283,4	260,9	254	-2,64%	-10,37%
Close-end	2781,3	3471,6	3476,2	0,13%	24,98%
Total	3620,1	4160,3	4153,8	-0,16%	14,74%

5. Non-venture CII Asset Structure

Just as in the previous periods, the asset structure of open-end and interval funds was fairly similar. The stake of cash and bank deposits within an aggregate portfolio of those types of funds comprised 20,1% and 24,57% accordingly, and of securities – 72,67% and 67,51%. The structure of an aggregate portfolio of close-end CII was less liquid. The stake of cash and bank deposits comprised 9,13%, and the stake of securities – 65,45%.

The key changes within the structure of non-venture CII assets over the quarter consisted in a decrease of the stake of shares and an increase of the stake of bonds within the structure of the aggregate portfolios of open-end and interval CII. In the former, the stake of shares went down by 15 p. p. and the stake of bonds went up by 11,7 p. p., whilst in the latter the stake of shares went down by 12,9 p. p. and the stake of bonds went up by 4,8 p. p. Such changes could, on one hand, be explained by depreciation of shares and, on the other – by the attempts of managers to get rid of such assets, satisfying the requirements to portfolio diversification via purchases of bonds.

Characteristically, the said tendency was considerably less observable in close-end funds, the stake of shares in the portfolios of which decreased by 4 p. p. only. Taking into account the requirements to the evaluation of shares of non-diversified close-end funds, we could assume

that the shares (of unquoted companies) contained in close-end funds' portfolios had not been overpriced.

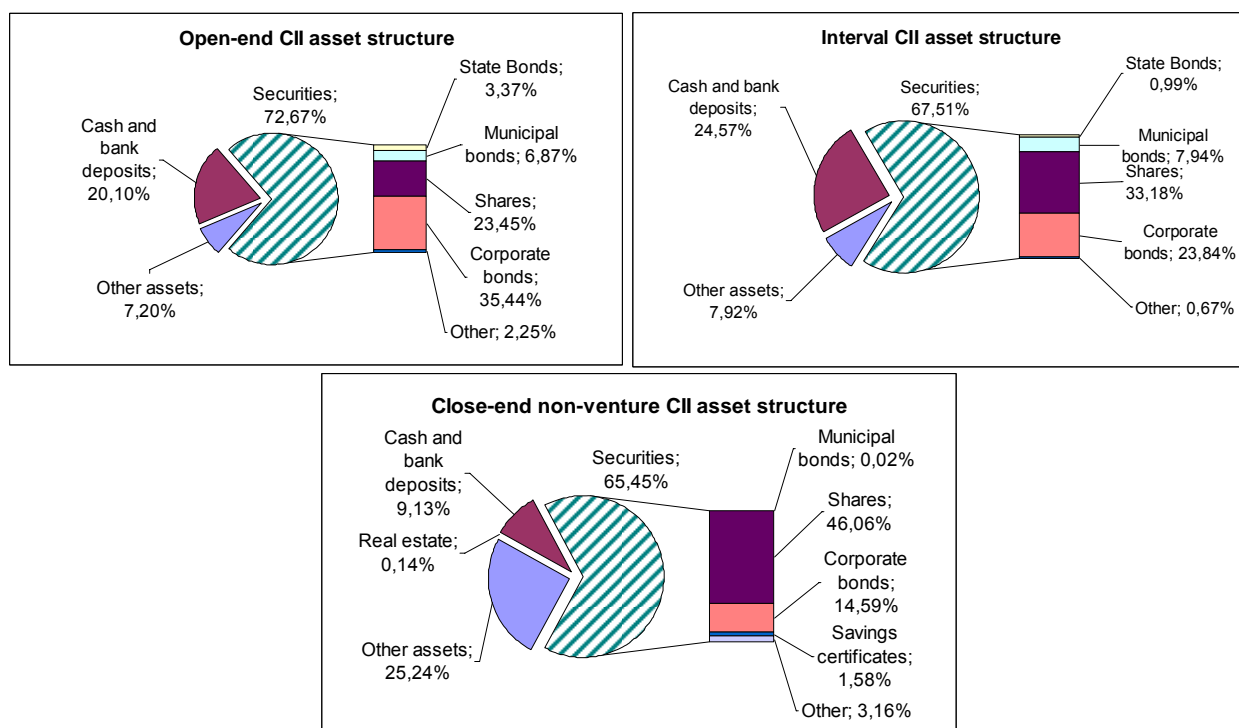


Chart 6. Non-venture CII asset structure in different types of funds as of 30.09.2008

Let us review the structure of consolidated CII securities portfolio by investment industries. As it can be seen from Chart 7, as of 30.09.2008, the key sectors into which the funds of non-venture CII had been invested were industry (25% +3 p. p.) and consumer goods (20% +3 p. p.). Compared to quarter beginning, the greatest decrease was observed in raw materials sector (13%, -7 p. p.), which, probably, was due to a drastic fall in the demand for raw materials.

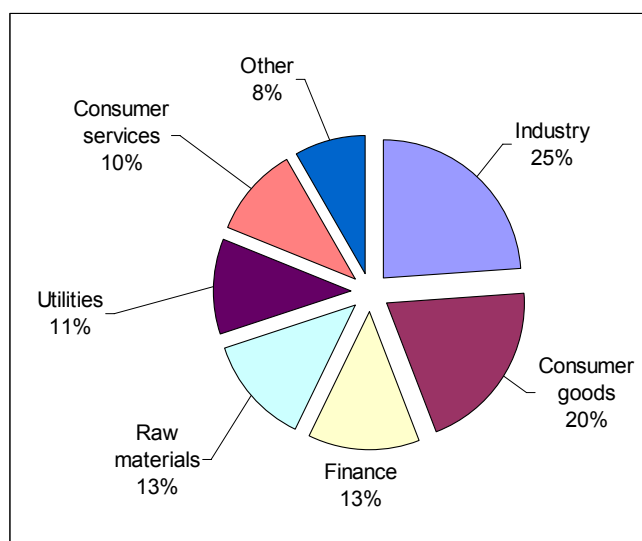


Chart 7. Consolidated non-venture CII securities portfolio structure as of 30.09.2008¹, by investment industries

The most popular by the presence in non-venture CII portfolios remained the blue chips of the Ukrainian stock market, the first top ten of which, with exception of *Lutsky Automobile*

¹ According to PFTS industry classification.

Works (LUAZ) and *Poltava GOK* (PGZK), are PFTS index components (Table 5). Just as at quarter beginning, the leaders were the shares of *Azovstal Metallurgical Works* (AZST), which were present in the portfolios of 90 funds (82 at quarter beginning).

Compared to quarter beginning², JSCB *Ukrsotsbank* (USCB) entered the top ten, and shares of *Donbasenergo* (DOEN) left the top ten.

Table 5. Most popular securities – by presence within non-venture CII portfolios as of 30.09.2008

№	Security type	Category	Issuer	Number of CII that have respective securities in their portfolios
1	Shares	Common registered	<i>Azovstal Metallurgical Works</i>	90
2	Shares	Common registered	<i>Mariupol Heavy Engineering Works</i>	76
3	Shares	Common registered	<i>Ukrnafta</i>	75
4	Shares	Common registered	State Energy Generating Company <i>Tsentrenergo</i>	73
5	Shares	Common registered	<i>Yenakyivsky Metallurgical Works</i>	73
6	Shares	Common registered	<i>MOTOR SICH</i>	71
7	Shares	Common registered	<i>Poltavsky GOK (Ore-Enrichment Works)</i>	69
8	Shares	Common registered	<i>Lutsky Automobile Works</i>	64
9	Shares	Common registered	JSCB <i>Ukrsotsbank</i>	63
10	Shares	Common registered	<i>Zakhidenergo</i>	63

Just as at quarter beginning, the leaders by an aggregate value in CII portfolio at 30.09.2008 were assets not represented in Table 5. In other words, within CII assets the greatest by volume are the securities purchased by big blocks by a small number of CII, for instance, by one CII. Compared to previous quarter, an aggregate value of securities included into the top ten hardly changed. Shares of *Rivneenergoatom* (third place, UAH 71,2M) and *Promtitan* (fourth place, UAH 66,7M) became the new positions in the top ten (Table 6).

Due to market price drop, the number of most liquid shares in CII portfolios decreased considerably, whilst the number of CII that owned those shares expanded. None of the securities from the top ten leaders by the presence in CII portfolios appeared in the top ten leaders by aggregate value within CII portfolios. For instance, despite the number of CII holding *Azovstal* shares in their portfolios during the quarter increased by 8 funds, an aggregate value of those securities in non-venture CII portfolios decreased more than twice – from UAH 47,4M to UAH 20,49M.

² See: «Analytical Review of the Collective Investments Market in the Second Quarter 2008», http://www.uaib.com.ua/files/articles/444/24_4.pdf

Table 6. Most popular securities – by aggregate value in CII portfolios as of 30.09.2008

№	Security type	Category	Issuer	Value of securities purchased by CII, UAH
1	Corporate bonds	Non-interest bearing, registered	<i>Vyrobnychy Viector</i>	85 365 597,67
2	Shares	Common registered	<i>"Leninska Kuznia" Plant</i>	78 898 095,09
3	Shares	Common registered	<i>Rivnenerhoprom</i>	71 186 700,00
4	Shares	Common registered	<i>Promtitan</i>	66 675 000,00
5	Shares	Common registered	<i>Darnytsky ZBK Works</i>	65 658 632,85
6	Shares	Common registered	<i>Ukravtoresurs</i>	65 409 749,00
7	Corporate bonds	Interest bearing, registered	<i>Yug-Stieкло</i>	60 000 000,00
8	Shares	Common registered	OJSC "Beer&non-alcohol complex "Radomyshl"	58 899 970,04
9	Corporate bonds	Interest bearing, registered	<i>Ukrainian Automobile Holding</i>	44 565 566,22
10	Shares	Common registered	<i>Donetsky Rudoremontny Zavod</i>	44 071 260,14

6. Non-venture CII Rate of Return

The stock market decline continuing in the third quarter 2008, resulted in even greater than in the second quarter decrease of CII rate of return. At quarter end, only close-end non-venture CII demonstrated on average smaller losses than in the previous quarter (-3,5%) (Chart 8). As analysis of the changes in the aggregate portfolio of those funds for the quarter demonstrated, their comparatively high rate of return was due to the fact that a considerable portion of their assets had not been overpriced.

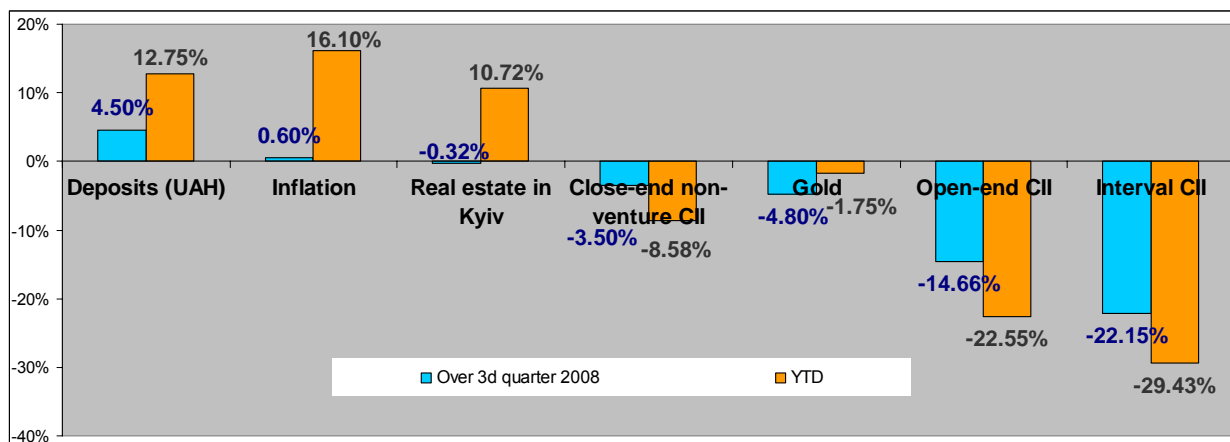


Chart 8. Average rate of return of different types of CIIs, gold, deposits, and inflation rate in 2008³

³ The inflation rate provided is based on the State Statistics Committee data. The rate of return on real estate is calculated based on Kyiv real estate value index (Source: <http://www.domik.net/mod/main/indexes/>)

Interval funds continued demonstrating the poorest results (-22,15% for the quarter and -29,43% since year beginning). Those results were mainly due to the operations of the “old” interval funds – successors of privatization funds, whose portfolios had been formed at certificate auctions and could not boast high quality. Second place by losses belonged to open-end CII (-14,66% for the quarter and -22,55% since year beginning). Required of such funds daily redemption of certificates demands from them maximally objective revaluation of assets, which makes those funds the most reliable indicator of the collective investments market situation. Their efficiency is somewhat reduced by currently existing requirements to open-end funds’ diversification and their being most vulnerable to capital outflow.

For the first time, negative rate of return was demonstrated by investments into real estate (-0,32% for the quarter). With dollar stabilization and raw materials’ market decline in the background, gold also started losing its positions (-4,8% for the quarter and -1,75% since year beginning).

In the third quarter, the most profitable financial instrument was a national currency deposit, the rates on which somewhat increased in the conditions of liquidity crisis (+4,5% for the quarter and +12,75% since year beginning) and considerably exceeded quarterly inflation rate (0,6%). However, low value of the last indicator was rather of seasonal nature. For instance, for the period since year beginning inflation exceeded the rate of return on national currency deposits by 3,35%.

7. Non-venture CII Certificates Distribution

In the first quarter 2008, the share of the main investors of non-venture CII – legal entities – non-residents continues to grow. At 30.09.2008, it comprised 77,96% of the total NAV (59,66% – at quarter beginning). That growth occurred primarily due to an increase of the share of those investors’ funds in close-end CII from 68,36% of NAV at quarter beginning to 91,71% – at the end. Such increase was in the first turn due to entering the market by new close-end funds with considerable NAV, and to the stake of legal entities – residents among investors.

The second place was held by natural persons– residents, whose investments went down from 30,12% of the total NAV of non-venture CII at quarter beginning to 14,4% – at quarter end. The greatest share of such investments– 93,79% – could be found in interval funds. The third place went to legal entities – non-residents (7,59% of the total NAV of non-venture CII (9,74% – at quarter beginning), that were investing mainly into open-end CII (67,63% of those funds’ NAV).

**Table 7. Non-venture CII certificates distribution by the ownership
as of 30.09.2008, % of NAV**

Types of Funds	Legal entities- residents	Legal entities non-residents	Natural persons - residents	Natural persons non-residents
Open-end	9,85%	67,63%	22,10%	0,42%
Interval	5,71%	0,49%	93,79%	0,01%
Close-end	91,71%	0,80%	7,48%	0,00%
Total	77,96%	7,59%	14,40%	0,04%

8. Resume

The third quarter 2008 was characterized by the further stock market crisis development, which was affecting the economy. Unlike during the previous quarter, national stock market decline obtained economic grounding, although the majority of experts agree that the price level that had formed thereat was greatly understated.

The collective investment market also incurred losses, but demonstrated a certain stability as to the volumes of investments attracted, which gave evidence that it preserved its growth potential. CII demonstrated their ability to minimize their participants' losses, although strict legislative limitations, in particular as regards diversification, coupled with the inability of the government to take anti-crisis measures promptly, did not allow them to avoid losses.

Provided such measures are implemented immediately and internal economic situation stabilizes, quick positive response of the stock market could be expected, which would unlock the potential of the collective investments market.