



Tera Capital Fund

Investor Newsletter

July 2012

Altima
asset management

Tera Capital Fund is the only fund of funds in the world which pays no fees other than a success fee

Based on Tera Capital Fund's performance and innovation, in February 2012 the Global Banking & Finance Review announced that Tera won its award as the most innovative fund of funds in Europe for 2011, Tera's second such award

Fund Performance (net of fees)

Returns	Tera* (%)	RTS, MSCI & ROS Avg** (%)	AAM Russia Fund Index ¹ (%)
Monthly	2.12	2.18	1.85
Year-to-date	0.86	(1.57)	(1.76)
Trailing 12 months	(14.97)	(20.17)	(18.91)
Since Fund inception (Apr 05)	159.12	143.94	147.87
Anlzd mnthly rtn (since Fund inception)	10.24	8.61	9.62
Annualized Stand. Dev. (since inception)	26.07	38.88	30.65
Sharpe Ratio ²	0.30	0.26	0.23
Trailing 12 m Sharpe	(0.60)	(0.66)	(0.90)

*Weight averaged, all series (currently 9) combined

**RTS: 1.95%, MSCI: 2.60%, ROS (Crédit Suisse): 2.00%

Investment Advisor's Assessment

Russia

➤After almost 20 years of negotiations, the **Russian Federation joins the World Trade Organization August 22** as its 156th member. Once in the WTO, the Russian government will move to reduce trade barriers on its exports, the Russian Economic Development Ministry immediately announced. The ministry has a "blacklist" of Russia's trade partners which restrict imports from the country and will seek to have unfair constraints removed. The ministry estimates that Russian companies lost \$2 B annually in potential sales as a result of those restrictions, 72 of which



it has specifically identified. It cited steelmakers, chemical producers and agricultural firms as companies which suffer the most from other countries' trade barriers. For instance, Russia and China agreed in May on an MOU based on WTO requirements to align their rules governing farm product safety, with a final agreement expected at the end of 2012. The differences had long prevented Russian grain sales in China, but talks to iron out the hurdle moved ahead quickly after December, when the WTO formally invited Russia to join. **Annual wheat shipments could reach at least 1 million tons.**

In another, more light-hearted example of immediate changes

WTO membership is causing, lovers of high-end imported spirits are in for a treat: tariffs on whiskies, cognacs and other fine spirits are set to fall to make imported products more competitive against local production. (However, the tariff drops come on the heels of **Russian government crackdowns on both drinking and smoking** – both improving the health of its citizens and generating considerable revenue. Russia is the second-biggest tobacco market in the world after China, but an even greater proportion of the population smokes.)

China waited 15 years to join the WTO: joining in 2001 set the stage for a decade that quintupled its exports and propelled its economy from sixth place globally to the world's second-largest.

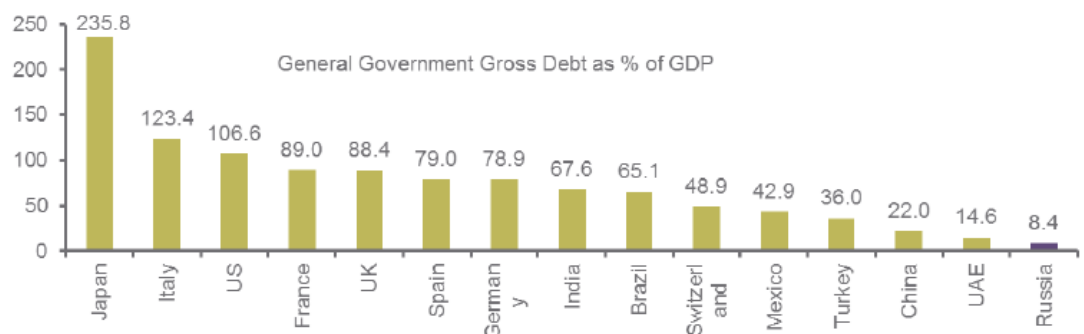
While Russia's commodity-based economy is less well placed to enjoy that kind of spurt, there are still plenty of positives.

Membership is expected to bring better trade access and more foreign investment to Russia's \$2-trillion economy. The **World Bank estimates that Russia's new status will result in an additional \$162 B in annual economic output, helping to boost Russian household incomes by as much as another 25%.**

Average Russian tariffs will fall by one third. Cheaper imports will leave consumers and companies with more money to spend. Banks and telecoms will be opened to foreign investment. **For instance, tariffs on foreign cars will be cut 50% by 2019.** The first step will take place in August when the tariff for most new cars, including SUVs, will fall from 30% to 25%. They will continue to fall: the tariff for large new cars and SUVs will be reduced 22.5% in 2013 and to 10% in 2019. The tariff for most other new cars will be cut to 15% in 2019.

In addition, Russia is extremely well positioned financially. **Russian Central Bank reserves increased by \$2.6 B to \$510 B.** The country has virtually no debt.

Ed Conroy, a fund manager at **HSBC Global Asset Management**, feels that Russia, like most new WTO entrants, will enjoy increased growth and investment pickup as it dismantles protectionist barriers and shows a clear commitment to free-market policies. "WTO is not a



Source: International Monetary Fund, World Economic Outlook April 2012, www.imf.org

¹ Altima Asset Management created this index of 21 Russia-focused equity funds created on or before May 2005 to provide an appropriate benchmark.

² Risk free rate: 2.5%

magic wand they can wave to create an investment haven, but if you create a less restrictive framework, you automatically create opportunities. Don't expect a revolution but an evolution towards a more open, competitive economy," Conroy said.

The World Bank calculated that the **short-term value of WTO membership to Russia at \$49 B a year or over 3% of gross domestic product at 2010 prices**. That would rise to **\$162 B annually when the longer-term impact on the investment climate** is factored in.

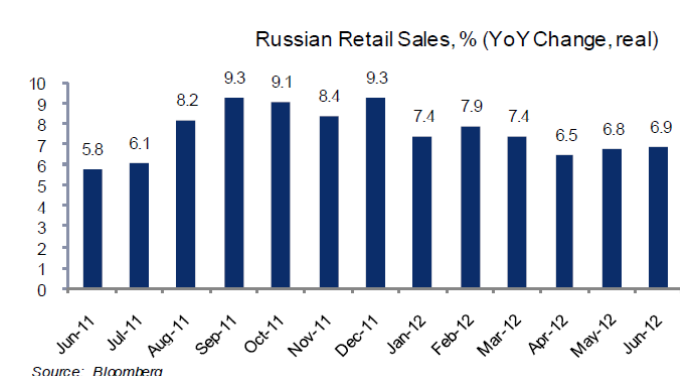
➤ **FDI into Russia rose 8% on the year to \$7.59 B IH of 2012. Capital investment grew 28.9%** to \$3.89 B and other foreign direct investment rose 2.4% to \$713 M. Foreigners invested \$29 B in financial services, \$18.5 B in manufacturing, \$10.4 B in natural resource industries and \$8.7 B in wholesale and retail.

Foreign portfolio investment increased almost fivefold to \$1.19 B. Of this amount, **investment in stocks rose 7.4 times to \$1.1 B**, while investment in bonds was down 3.9% to \$89 M. **Russian investments in foreign economies** totaled \$69.5 B, up 3.4% on the year.

➤ **In July Russian unemployment rate remained at 5.4% for a third month in a row**. In nominal terms, a **number of unemployed decreased by 20k to 4.1 M**.

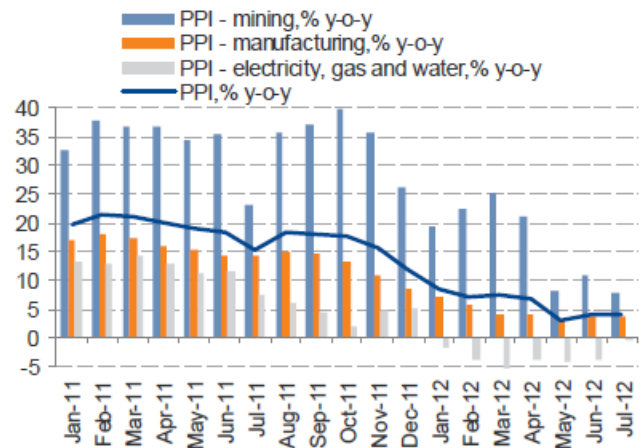


➤ **Real disposable income growth was at 2.2% y-o-y in July**. **Average wages grew by 10.2% y-o-y**, the same rate as in June. **July retail trade turnover grew by 5.1% y-o-y**. **Jan-Jul food sales grew by 4.2% y-o-y** and **non-food goods sales increased by 9.1% y-o-y**.



➤ **PPI decreased by 1.1% in July** after dropping 0.9% in June and 2.3% in May; the July price decrease was largely driven by a 14.4% decline in oil prices.

Producer prices



Source: Bloomberg

➤ **Industrial output rose 3.4% in July** from a year earlier, much stronger than a 1.9% increase in June. **Manufacturing output rose 5.7% in July** (3.4% in June) and was the main driver of growth in industrial production.

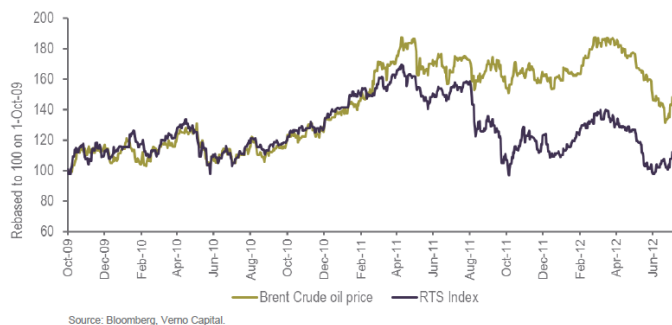
➤ **Russia's equity market has become a true paradox**. Despite a quite strong economic recovery, the potential for positive reform momentum, and a relatively insulated domestic economy, the Russian equity market continues to react to international risk. **Between the end of February and the end of Q2, the RTS Index went from the best performing large market YTD to the worst performing**. Equities are trading at **forward-looking P/Es nearly as low as any since Putin came to power in 2000**. The **discount to emerging market peers is at its largest in a decade**.

Country	Index	Dividend Yield	Forward P/E	5Y USD CDS
USA	MXUS	2.1%	13.3	47.5*
India	MXIN	1.5%	13.0	n. a.
Australia	MXAU	5.1%	11.9	70.0
South Africa	MXZA	3.5%	11.6	141.8
UK	MXGB	4.1%	10.4	64.0
Brazil	MXBR	4.4%	10.1	142.8
Turkey	MXTR	2.1%	10.0	201.7
Poland	MXPL	5.2%	9.7	180.1
China	MXCN	3.1%	8.9	115.8
Hungary	MXHU	3.4%	8.5	490.0
Russia	MXRU	3.8%	4.7	192.0

*EUR for USA CDS

Source: Bloomberg, July 23, 2012.

Further, in the last 12 months, the **close correlation between oil prices and Russian equities has been dramatically broken**. Russian markets have room for a 40% increase if the correlation is to be re-established. Our contention, of course, is that the correlation was always overdone, but we did not expect such curious timing for the de-correlation to take place, nor for it to be so abrupt.



➤ Russia became the **world's largest diamond producer** in terms of volume last year, turning out 35 million carats at a value of \$2.7 B and an average price of \$76.12 per carat – up 11% on the year.

➤ The Russian Federal Air Transportation Agency is predicting a **15% increase in air travel in Russia in 2012** compared with 2011 to more than 70 million people.

➤ **Sales of new cars and light commercial vehicles** in Russia were at 255,560 for the month of July, **up 14% y-o-y**, and to 1,669,455 for the first seven months of 2012.

➤ Russia's **Federal Anti-Monopoly Service** ordered a new tender for Moscow's \$300 M tram contract, which will allow more foreign bidders to participate. **Bombardier** and **Siemens** are the potential contenders that didn't make it into the previous tender. The city began taking bids to supply 120 high-speed trams from two companies, including **Alstom's** Russian JV with **Transmashholding**, in early August but FAS voided the bidding.

➤ Russia, the world's **third-biggest wheat exporter** last season, **sold 1.8 million metric tons of the grain abroad in July**, more than double the prior month's shipments, the second-highest monthly total ever after the record amount shipped in July 2011. Russia should be able to **export 10 million to 12 million tons of all grains** in the current season begun July 1. Wheat exports were 21.3 million tons in the 2011-12. **Shipments are set to fall to 11 million tons** in the current period after drought affected fields across Russia.

➤ According to the **World Health Organization's Global Adults Tobacco Survey**, 39% of Russian adults (22% of women and 60% of men) are habitual smokers, compared with 28% in China. **Tobacco-related diseases annually take the lives of 350,000 to 400,000 Russians.**

The alcohol problem is even worse. The World Health Organization estimates that **one in five men in the Russian Federation dies due to alcohol-related causes** (and three-fourths of the 12,000 murders in Russia in 2010 were committed under the influence of alcohol). **Health experts have welcomed recent Russian government moves to limit advertising and make both alcohol and tobacco more expensive.**

The authorities' latest temperance campaign started in 2010, when the government introduced **minimum pricing for vodka** and **banned sales of strong alcohol at night**. No sale of any drink stronger than 0.5% is allowed between 11 p.m. and 8 a.m. the next day except in restaurants and bars. Also, **sales of alcohol were banned in stores close to schools, markets, sports and health facilities and other high-risk locations.**

And last month President Putin signed a decree "to create conditions to reduce the consumption of alcohol,

including beer," **outlawing advertising of alcohol on the Internet and in print media**. Separately, **advertising of spirits has been banned everywhere** – including on billboards or television – except at the point of sale.

As a result of WTO accession, tariffs on imported beer will be set at €0.6/l, dropping to €0.018/l by 2018. Wine tariffs will be 20%, reducing to 12.5% by 2016, and tariffs on spirits will be set at €2/l, dropping to €1.4 to €1.5/l by 2015.

Tackling the nation's drinking problem has been a headache for generations of Russian leaders, and was periodically cracked down on with varying success by both tsarist and Soviet governments.

The last Soviet anti-drinking drive launched by **Mikhail Gorbachov** in 1985 managed to **boost male life expectancy by two years** through drastic increases in alcoholic beverage prices, strict limits on sales hours, and prosecuting drunkenness. A 2009 study published in U.K. medical journal **The Lancet** credited the move **with saving up to a million lives.**

But Gorbachev's program was also blamed for decimating national viniculture and boosting production of and dependency on sometimes-dangerous home-brews. Facing increasing unpopularity and a problematic fall in revenues from sales, enforcement was quietly eased from 1987.

The government claims the latest temperance campaign has already begun to pay off. In December last year, then-Deputy Prime Minister Viktor Zubkov announced that **consumption of pure alcohol per person per year over 2011 had dropped from 18 liters to 15**, largely because of the nighttime sales ban.

That's a success, but still leaves a large hill to climb. For comparison, **when Gorbachev launched his anti-drinking campaign in 1985, consumption was at 10.5 liters per person** (not counting illegal home brew).

WHO's benchmark is that consumption above 8 liters per capita begins to have an adverse impact on the health of a country.

Magnit, Russia's largest retail chain, said it had halted alcohol sales at 255 stores since July 1 because of their proximity to schools and other restricted locations and had to temporarily suspend sales at another 144 stores while they obtained long-term leases, which are now mandatory for premises selling alcohol. The company said the changes would have no material impact on 2012 revenue.

The **Russian Health Ministry** believes smoking accounts for another 23% of male deaths, meaning **alcohol and tobacco combined kill almost half of all Russian men**. A draft law on tobacco developed by the ministry and currently being agreed with other ministries would not only ban all tobacco advertising, but also forbid open displays of cigarettes in shops and introduce a Western-style ban on smoking in public places.

The Russian Finance Ministry last year said it was considering hiking excise taxes to \$94 per 1,000 cigarettes by 2015 as part of plans that would seek to **add \$66.9 B to the federal budget over three years.**

Such increases could see the **price of a packet of cigarettes jump almost five times from today's average of \$1 per pack to \$5 by 2018**. International health bodies have praised the bill, which has the "total support" of the WHO and is on par with global standards.

Company News

➤ **VimpelCom posted an 83% increase in Q2 net profit** as subscriber numbers grew across its markets. Net profit totaled \$488 M, up from a pro forma \$267 M a year ago. Revenue fell 4% due to dollar appreciation against its main operating currencies, the euro and ruble to \$5.7 B. EBITDA increased 2% to \$2.48 B.

VimpelCom, in which Norway's **Telenor** has a 39.5% voting stake, generates 40% of its revenues in Russia, while Europe and North America is its second-biggest business unit, with a combined 30% share in total sales.

➤ **Mobile TeleSystems boosted its revenue by 9.7% y-o-y** to \$2 B in Q2 2012. In 1H 2012, revenue grew 12.2% y-o-y.

➤ **VEB Leasing**, a subsidiary of state lender VEB, has concluded a **\$1.26 B deal** to finance **Aeroflot's** acquisition of four **Boeing 777-300ER** airliners, the world's largest twin-engine jets, adding to its current fleet of eight Boeing 767-300ER aircraft. The aircraft will be supplied from January to April 2013. The acquisition is part of an Aeroflot agreement to buy six Boeing 777-300ER aircraft and eight Boeing 200ER planes that was concluded in March 2011.

Aeroflot will use the new aircraft to operate flights in the peak traffic period during the **2014 Winter Olympics in Sochi**. The Boeing contract will also help Aeroflot in its future negotiations with **Airbus**, giving the airline more leverage in talks.

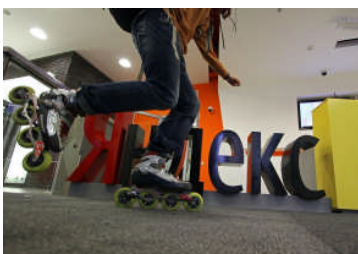
➤ Magnit announced that its July sales grew 32% y-o-y to \$1.20 B, the same pace as in June. **The company opened 115 outlets in July**, bringing its **total number of stores to 5,837**. Magnit is targeting 30% sales growth in 2012.

➤ **VTB Capital** and Sofia-based **Corporate Commercial Bank** reached an agreement with the creditors of **Vivacom**, Bulgaria's second-biggest telecommunications company in terms of clients, to buy the company for €130 M and pay debts of €588 M. Vivacom creditors, which include **Deutsche Bank, UBS, UniCredit** and **Royal Bank of Scotland** have agreed to write off 64% of the company's €1.6 B debt

➤ **Mail.ru** announced it would pay shareholders a special dividend of \$3.80 per share, or a total of **\$795 M**.

➤ Internet search engine **Yandex** beat forecasts with a **64% rise in Q2 adjusted net profit**, boosted by higher online advertising revenues and lower costs.

Net profit, excluding share-based compensation expenses, **totalled \$65 M**.



Revenues were \$310 M, driven by continued growth of the online advertising market and strong search market share. According to **LiveInternet**, **Yandex's share of Russia's search market**

averaged 60.4% in Q2, ahead of **Google** and **Mail.Ru**.

Yandex, which raised \$1.4 B in an oversubscribed IPO in New York in May 2011, said its profitability was supported by lower costs as a percentage of revenues compared with those of a year ago, when costs rose due to the IPO.

In Q2 2012, Yandex' selling, general and administrative expenses were up 11% y-o-y but decreased as a percentage of revenues from 20.8% to 15.5% in comparison with the same period of 2011. **Adjusted EBITDA rose 60%**; adjusted EBITDA margin rose from 42.1% a year ago to 45%.

➤ Software developer and IT services company **IBS Group generated close to \$820 M in revenue** for FY 2012, a 24% increase over 2011, as Russian businesses added IT infrastructure and clients worldwide demanded tailored software. **Consolidated EBITDA rose 55% y-o-y** to about \$80 M. It also decreased its debt from \$58 M to about \$43 M.



Revenue for IT services rose 22%, while software development sales went up 37%, partly because of sales growth among current customers in the








financial services, transport and automotive, aviation and telecom industries, the company said in a presentation to reporters.

IBS has about 8,300 employees, who are located here and in Ukraine, Romania, Poland, Germany and the United States.

➤ **Surgutneftegaz** posted a net profit of \$3.15 B in 1H 2012, up 30% from the same period last year.

➤ **E.ON Russia**, a subsidiary of Germany's **E.ON**, **increased its sales revenue by 14% y-o-y to \$1.095 B in 1H 2012.**

Fund Awards

 Most Innovative Funds of Funds (for innovation and performance)  EUREKAHEDGE Hedge Fund Databases No. 3 ranked fund of funds in the world, February 2012	 Most Innovative Funds of Funds (for innovation and performance)  EUREKAHEDGE Hedge Fund Databases No. 4 ranked fund of funds in the world, YTD 2012
 EUREKAHEDGE Hedge Fund Databases No. 2 ranked fund of funds in the world for 2010	 EUREKAHEDGE Hedge Fund Databases No 8 ranked fund of funds in the world for 2009
 EUREKAHEDGE Hedge Fund Databases No 1 ranked fund of funds in the world for 2005	

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