



Tera Capital Fund

Investor Newsletter August 2012



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	(3.57)	(6.53)	(2.74)
Year-to-date	19.44	17.73	13.48
Trailing 12 months	(15.23)	(23.68)	(19.68)
Since Fund inception (Apr 05)	188.43	172.16	167.36
Anlzd mnthly rtn (since Fund inception)	12.88	11.33	8.64
Annualized Stand. Dev. (since inception)	25.58	38.67	30.91
Sharpe Ratio ²	0.41	0.33	0.20
Trailing 12 m Sharpe	(0.41)	(0.54)	(0.82)

*Weight averaged, all series (currently 9) combined

**RTS: -5.61%, MSCI: -8.17%, ROS (Crédit Suisse): -5.80%

Investment Advisor's Assessment

Russia

➤ **Russian unemployment hit a post-Soviet low** in August of **5.2%**. Andrei Korovkin from the **Russian Academy of Science's Institute of Economic Forecasting** said "This is a historic minimum. The previous record [5.4%] was set in May 2008." According to Igor Polyakov of the **Center for Macroeconomic Analysis and Short-Term Forecasting**, an even lower figure was achieved back in 1993, but at that time **Rosstat** had a number of complications with its methodology. As a result, the figure from last month should be considered the post-Soviet record.

➤ Russia posted a **fiscal surplus equal to 4.7% of GDP** in August and a **1.4% of GDP surplus** for the first eight months of the year.

➤ The **World Travel & Tourism Council** released a study in August which, somewhat surprisingly, showed that the tourism industry contributes more to Russia's GDP than automobile or chemical manufacturing. The **industry's contribution was \$106 B** in 2011, **5.9% of GDP**, compared with 4.8% and 3.3% for automobile car manufacturing and chemicals, respectively.

This percentage is quite high for a European country, said Olivia Ruggles Brise, **Director of Policy and Research** at the Council. The European average is 8%, but manufacturing-focused countries such as Germany, where tourism's GDP share is 4%, have lower numbers. The revenues of Russia's tourism sector are only expected to grow. The study forecasts that **the industry's contribution to GDP will increase by 4% each year over the next decade**, which is faster than the expected growth rate for the whole economy. "There are great tourism opportunities in Russia," Ruggles Brise said.

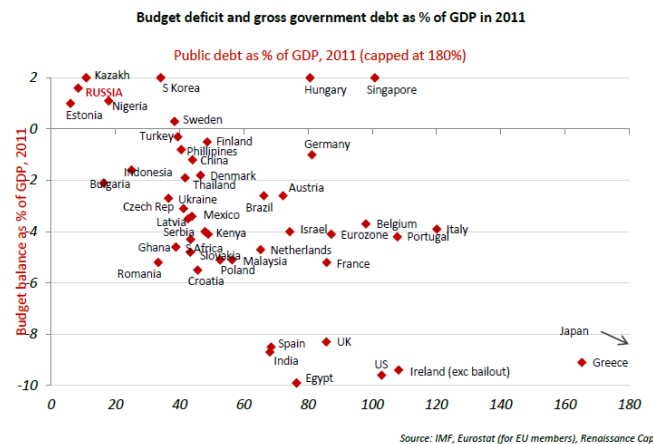
However, there are **still few foreign tourists** in Russia. According to the study, **77% of the tourism sector's revenue in 2011 was from domestic travelers**.

➤ Billionaire investor **Jim Rogers** said he is "ready to invest in Russia" during a roundtable at the APEC summit in Vladivostok. Rogers said that for more than 40 years he has had a negative attitude toward Russia, but that a lot had been done in Russia in recent years. He has not yet disclosed the focus of his investments.

"**Russia needs to tell positive stories about successful investments**," said Karl Johansson, managing partner of **Ernst & Young CIS**, which recently opened an office in Vladivostok. "**There are such examples**," Johansson added. "Things are getting better. Not consistently, but getting better. **The possibilities to grow investments are increasing**."

➤ There are sound reasons for investing in Russia. We illustrate two below, one is the absence of a negative (public debt); the other is a positive (pension fund investments).

First, the **low rate of public debt**. The chart below compares this debt to GDP. You will find Russia in red in the far upper left corner of the chart, with Japan and Greece at the other extreme and Brazil and Austria in the center.

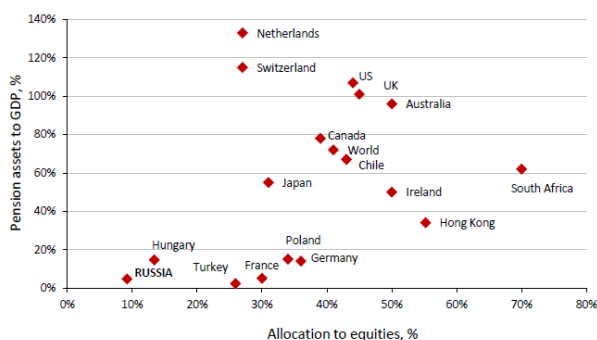


On a more innovative note, Russian **pension funds** are a relatively recent innovation that have been growing rapidly – and they have thus far had almost no exposure to equities. (Russia is located in the extreme lower left of the chart.)

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%

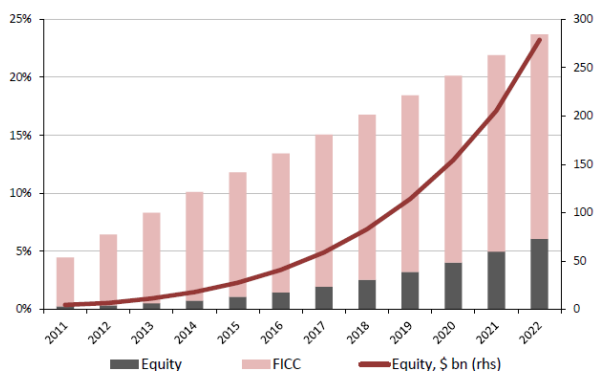
Russia has minimal pension funds and these funds have minimal exposure to equities



Source: UBS, Towers Watson, OECD, FSFM

That is about to change as the funds expand and the regulations governing their investments are updated to allow equity investments. These changes will have a profound and positive impact on Russian stock markets. As you can see below, pensions funds have had virtually no impact on Russia equity markets because of their size. This will begin to change in 2013 and pension funds will have a continued positive influence on Russian equity markets for the foreseeable future.

Russian pension fund assets forecast to grow as % of GDP



Source: UBS, Towers Watson, OECD, FSFM

*FICC = Fixed Income, Currency and Commodities

All of which bodes well for the future of equity investments in Russia.

➤ **Russia extracted oil at a record pace of 10.38 M bpd day** in August, a level not seen since the collapse of the Soviet Union.

➤ Fueled by a growing economy, the **number of households** able to afford **luxury goods** is forecast to **rise to 13 million** by 2025 from 7 million in 2010, according to **Capgemini**.

Those growth prospects are prompting high-end carmakers to expand their presence in the country. **Porsche** plans to **double the number of dealers to 36** over the next six years. **Audi** is adding showrooms as it targets 30,000 car deliveries in 2012, **double its sales** from 2009. **Bayerische Motoren Werke** will add about 20 outlets by 2018, one third more than today.

The 2012 **Moscow International Automobile Salon** was recently held. It had more than double the exhibition space from the last show in 2010.



Russia will surpass **Germany** as **Europe's largest auto market within 18 months**, with sales rising to 3.4 million

vehicles. As more buyers choose upscale cars, total **revenues for automakers will increase 19% to \$75 B** in 2012, outpacing the 10% gain in vehicle sales.

Renault SA, the second-best selling in Russia during 1H 2012, and its alliance partner **Nissan Motor Co.** recently agreed to raise their stake in **Lada's parent, OAO AvtoVAZ to 74.5%** from 25% today. The group is aiming for combined market share of 40% by 2015 from 33% in 2011, though Lada will anchor the lower end of the lineup while more expensive cars will bear the foreign nameplates.

BMW plans to open a new training center for employees and dealers in Russia in 2013 and intends to expand its network of BMW and Mini outlets to 80 from 61 by 2018. The carmaker's **Rolls-Royce brand opened a second**

dealership in Moscow in July, making the Russian capital only the second city, after New York, with more than one Rolls showroom.

"We're continuing to invest in Russia because we believe in the Russian luxury market's future growth potential," said Ian Robertson, head of sales for BMW.

"Russia offers the biggest growth potential for the luxury-car segment worldwide," said Jan-Henrik Lafrentz, **Bentley's** CFO. He expects the brand to **double sales** "in the near future" as it adds showrooms.

Nissan began assembling the Infiniti FX SUV at its St. Petersburg factory, where it also makes the Nissan Murano SUV.

The expansion in Russia marks a **sharp contrast to the European Union**, where **car sales are expected to decline 7%** in 2012 to the **lowest level since 1995**, according to the auto-industry association **ACEA**. This makes a strong presence in Russia even more critical for high-end carmakers to remain competitive.

"Russia is starting to close the gap for us to Germany and the U.K. volume-wise," said Doug Speck, sales chief for **Volvo Car Corp.** "We've taken the **forecast for Russia up three times this year**" and are now targeting sales of more than 20,000 cars there, **at least 18% more than 2011**.

Volvo's sales surged 50% in Russia through June 2012, compared with an 8.2% slump in western Europe.

➤President Vladimir Putin hosted an **Asia-Pacific Economic Cooperation** summit in Vladivostok and announced that the talks would take into account "new realities such as **Russia's accession to the World Trade Organization**. Membership in the WTO gives us the ability to participate more broadly in setting the global trade rules – an issue that has been a focus of attention for APEC in the past," Putin wrote in an article for The Wall Street Journal's Asian edition. "Russia will use its membership in the World Trade Organization to help shape global rules to address a crisis in world trade", Putin wrote.

"The **very principle of free trade is undergoing a crisis**. We regularly observe recurrences of protectionism and veiled trade wars instead of lifting barriers," Putin wrote, adding, "it is imperative that we develop common approaches."

"We suggest that the dialogue in Vladivostok focus on **freeing up trade and investment flows to stimulate economic growth**," Putin said.

Russia spent more than \$20 B on roads, bridges and renovations for the summit.

➤Russian retailers sold **9.4 M cell phones** in Q2 2012, **7.2% more** than in Q2 2011. In monetary terms, **mobile phone sales were up 17%** at \$1.3 B. The average cell phone price was up 9% at \$150. Smartphones accounted for 27% of all cell phones sold in Q2. **Smartphone sales increased 60%** to 2.5 M devices. In monetary terms, they amounted to \$900 M in the period, also a **60% increase** y-o-y. **Samsung** increased its market share to 41.4% in the period from 26.4% in 2011, while **Nokia's** share fell to 22.4% from 46%.

➤The country's **top ten insurance companies** took in **\$7 B in revenue** from premiums in 1H 2012, not

including mandatory medical insurance, which accounted for 58% of all premiums collected in the period.

Company News

➤**Lenovo plans to sell 24.6 M of its products in Russia** and other CIS countries in 2014 for **\$14 B**, Lenovo's senior vice president and president for the EMEA region, Gianfranco Lanci, said. **Lenovo's business in Russia grew by 96.7%** in the last financial year and it intends to invest in its Russian business, including in personnel and marketing, Lanci said.

➤After delaying a sale due to volatile financial markets, the **Russian Central Bank** used the market rally prompted by stimulus measures in the US and Europe to cut its 57.58% stake in **Sberbank** through a placement of shares in Moscow and GDRs in London. The majority of the stake will be listed on the London Stock Exchange, Sberbank's first listing in compliance with the United Kingdom's **Financial Services Authority**.

Sberbank president German Gref announced the state-owned bank's **successful sale of a \$5.2 B stake** to domestic and international investors.



The deal leaves the Russian Central Bank with **50% plus one share** of the Sberbank, Russia's largest lender, and will help reinvigorate Russia's ambitious privatization program.

"If they believe in us, they believe in Russia," Gref told reporters at Sberbank headquarters. "With this deal, **Sberbank has opened the**

gates for privatization in this country."

The final price for the new shares was 93 rubles (\$3.04), two rubles above the minimum set for the placement and a 4.1% discount to the last closing price – a remarkable achievement for any transaction and even more remarkable considering the size of this one. The books for the deal were covered on the first day and were **twice oversubscribed**.

Russian Central Bank Deputy Chairman Alexei Ulyukayev proudly announced that this is "one of the three largest placements in modern Russian history. It is important as a **model of a high-quality privatization deal.**"

The deal involved 1.7 billion common shares sold to buyers, including 300 institutional investors. Funds controlled by George Soros were



some of the biggest participants; there were 10 bids for \$100 M or more of the stock. Gref stated that "A large proportion [of the buyers] had never invested in us or in Russia in general. It was an international exam that we passed."

President Putin stated that "For every **\$100 invested in Sberbank 10 years ago**, today the majority shareholder, **the Central Bank, received \$3,700**," Putin said. "That's a very good yield."

➤Russia's second largest bank, **VTB**, immediately announced that it was hoping to complete a privatization of at least \$2 B, probably by in the spring of 2013. Under current plans approved by the Kremlin, the government must sell 25.2% of its majority stake in VTB by 2014.

"The **Sberbank SPO will open a window of opportunity for Russian companies** to follow," said Alexander Morozov, chief economist at **HSBC** in Moscow.

➤Sberbank posted an **eight-month net profit of \$7.41 B, a 6% increase** from the same period in 2011 under Russian accounting standards, boosted by strong net interest income. **Net interest income was up 26.2% y-o-y**, with corporate lending up 1.2% and retail lending up 3.3% in August month-on-month.

➤US billionaire investor **Jim Rogers** has become a consultant at **VTB Capital**, the investment banking arm of VTB to assist in attracting agriculture investments. Rogers co-founded the **Quantum Fund** with George Soros.

➤According to a plan confirmed by Prime Minister Dmitry Medvedev in June 2012, in addition to the 7.58% stake in Sberbank and 25.2% of VTB, by the end of 2013 Russia must sell 50% of shipping giant **Sovkomflot** and 25% of **Russian Railways**.

➤Russian Railways has entered into exclusive negotiations to buy **PSA Peugeot-Citroen's GEFCO** logistics holding, after the French carmaker identified the rail monopoly's bid as the most attractive.

The acquisition would be a significant boon to the Russian rail monopoly in its long-term goal of building an **overland cargo route from China to Europe**.



Russian Railways submitted a **\$1 B bid for a 75% stake** in GEFCO, outbidding other suitors.

GEFCO, which ships Peugeot and Citroen cars around the world, is one of the struggling French carmaker's **only profitable divisions**. PSA is selling the stake in an effort to alleviate growing debt.

PSA Peugeot-Citroen would receive a special dividend of **\$130 M** from GEFCO as part of the deal, which is subject to approval by competition regulators in both countries. Discussions are still underway about whether to sell 75% or 51% of the company.

Russian Railways said the acquisition would benefit it and the Russian economy as a whole by decreasing production costs "thanks to **world-class state-of-the-art logistic technologies**" and an increase in "the effectiveness of using existing infrastructure through the optimization of transportation."

But the most prized goal seems to be using the company to build the Russian Railways' long-planned "**Eurasian land bridge**," an overland cargo route between east Asia and Europe.

"The acquisition of GEFCO would help Russian Railways to promote the attractiveness of transit cargo flows along the Europe-Asia transcontinental route," the company said. "Russian Railways has recently undertaken a significant amount of work to be in a position to offer competitive transportation services along this route."

The "next logical step" would be developing a sales network for transcontinental transportation services via an international logistics company, the company added.

One industry professional described the acquisition as part of a "serious play" on the part of Russian Railways to become the dominant provider on the route.

"We're going to see a shift in power in **China-to-Europe logistics**, which has previously been dominated by **Deutsche Bahn**," said Alexander Rogan, CEO of **AJR Logistics**.

Russian Railways has also made offers for Poland's **PKP Cargo**, the second-largest rail freight operator in Europe after Deutsche Bahn, and has expressed interest in cargo operators in Bulgaria, Slovakia and Greece.

Yakunin has frequently expressed an interest in developing a Eurasian land bridge and has even expressed support for building a **rail tunnel beneath the Bering Strait to Alaska**.

While the overland rail route is much quicker, even the longest trains cannot compete with the sea route on either price or volume, meaning the route would likely have to focus on high-value goods customers are keen to get to market quickly.

Rogan said many in the industry believed **China is seeking to boost overland links to Europe** in case territorial disputes in the East China Sea threaten the security of sea routes.

➤**AFK Sistema's net profit under US GAAP rose 22.8% y-o-y to \$407.8 M** in Q2 2012.

➤Moscow's **Sheremetyevo International Airport** handled **17.4 M passengers in January-August, 17.1% more** than in the same period in 2011.

➤Grocery retailer **Magnit raised its full-year 2012 sales guidance to 30-32% from 30%** and said growth was expected to **slow down to 25-27%** in 2013. Magnit has more than 5,700 stores and said its capital expenditure program would total \$1.6 to \$1.7 B this year and \$1.6 to \$1.8 B in 2013.

➤**Volvo Group will invest \$118.6 M in a new facility for the production of taxi cabs** at a plant in Kaluga.

➤**Rosneft's** board of directors said it had approved a decision to nearly **double a planned dividend payout for 2011** after President Putin effectively ordered an increase in dividends at the state-owned giant.

The world's top holder of oil reserves said that the board approved an additional dividend of 4.08 rubles (\$0.13) per share, bringing the total 2011 payout to 7.53 rubles per share.

➤**Uralkali**, the world's second-largest potash producer by capacity, reported a **6% increase in 1H 2012 net profit y-o-y** due to rising potash prices. Uralkali said net profit rose to \$842 M for the period. **Revenue was \$2.23 B, up 13%**; EBITDA rose 33% to \$1.40 B. Its EBITDA margin reached a **half-year record of 74%**.

➤**APM Terminals**, the ports arm of Denmark's **A.P. Moller-Maersk**, announced that it would **buy a 37.5% stake in Global Ports** from Russian transportation group **N-Trans**. The deal is the **largest foreign direct investment in Russia's transportation sector**. APM Terminals will run the company on an equal basis with N-Trans, each owning 37.5% with 25% being listed in London. The acquisition will raise Global Ports' share capital to \$2.3 B; the acquired stake is worth roughly \$860 M.

➤**UTair Group increased passenger transport by 34.5% y-o-y** to 5.6 M people in January-August 2012.

➤Italy's **Itaco Precast** announced it will invest up to **\$1 B to build factories for construction of prefabricated**



houses in Russia, Alexander Braverman, head of the **Fund for Promoting Housing Construction**. Currently, the company is building a \$140-M factory in Saratov on land purchased from the Fund.

➤ **Takeda Pharmaceutical**, Japan's largest pharmaceuticals manufacturer, **completed construction of a \$96 M** manufacturing facility in Yaroslavl. The company plans to **outgrow rivals** in the Russian market.

"It anchors us firmly as one of the leading pharmaceutical companies in Russia," said Frank Morich, who is responsible for all Takeda sales outside Japan.

Takeda bet on emerging markets when it bought Swiss-based **Nycomed** for some \$13 B in 2011; the company is now the seventh-largest drug maker in Russia by sales.

IMS Health expects the **Russian drug market to grow 11% annually between 2012 and 2016**. Takeda plans to outstrip that, with **annual growth of 15%** over the same period.

➤ The head of **ExxonMobil**, Rex Tillerson, with **Rosneft** CEO Igor Sechin, held up a partnership with Rosneft as a model for the rest of the world at the APEC summit Russia hosted recently. He was the first foreign CEO to greet Putin before the Vladivostok summit.

In April 2012, ExxonMobil and Rosneft unveiled an offshore exploration partnership that could **invest up to \$500 B** in developing Russia's vast energy reserves in the Arctic and Black seas. Under the deal Exxon and Rosneft will seek to develop three fields in the Arctic with recoverable hydrocarbon reserves estimated at **85 B barrels of oil-equivalent**. Tillerson said seismic studies at the Arctic **Kara Sea oil exploration project** with Rosneft were ahead of schedule and he expected **drilling to commence in 2014-15**. He also said ExxonMobil and Rosneft would work in "challenging circumstances" to meet the growing global energy demand, which he expects to grow by 30% by 2040.

➤ France's **Antoine Grumbach et Associés** won a tender to prepare a plan for the development of Moscow's recently annexed territories, which will triple the size of Moscow city, while US based **Urban Design Associates** will design a government compound there.

➤ **Rostelecom's Q2 net profit rose 3% y-o-y** to \$274 M.

➤ **Polyus Gold** reported net profit of \$426 M in 1H 2012, **more than double y-o-y**, due to increased sales volumes and higher gold price.

➤ Thierry Chiche, head of **Michelin**, Russia and CIS, announced that Michelin will **invest \$44 M** in 2012 in the **development of its tire factory** in Davydovo in the Moscow region, as well as a logistics base in Russia and the CIS. The money will be used to expand the size range of tires produced at the Davydovo factory.

Between 2000 and 2011, **Michelin invested a total of \$200 M** in the development of its business in Russia and the CIS.

The factory in Davydovo has been operating since 2004; its production capacity is 2 M tires a year.

➤ **Renault** is also expanding its Russian business. **Avtoframos**, the automaker's plant in Moscow, plans to **increase its production capacity in 2012 by 17% to 180,000 vehicles**, Renault chief in Russia Bruno Anselén announced.

Anselén said that Renault had initially planned to increase Avtoframos' capacity to 175,000 automobiles, but because of **high demand for the Duster SUV** the French company decided to change its work schedule to

increase its output. During 1H 2012, the plant already increased vehicle output 21% to more than 81,000.

➤ **McDonald's broke ground on a new hotel for families of patients at the Republic Children's Clinical Hospital** in Kazan. **Ronald McDonald House** is a "home away from home" for families whose children are undergoing long-term care at the hospital. McDonald's charity program has supported construction of 317 such mini-hotels in 31 countries; this is the first in Russia.

➤ McDonald's also announced that it has served more than **2 billion fast-food meals** and opened more than 300 locations in Russia. McDonald's has now committed to opening its **first restaurants east of the Ural Mountains**.

It is actively looking into opening restaurants in Novosibirsk, Barnaul, Tomsk and Novokuznetsk. In addition, McDonald's will open its first location in Krasnoyarsk at the end of 2013 or the beginning of 2014. Since it entered the Russian market in January 1990 with its restaurant near Moscow's Pushkin Square, **McDonald's has grown to about 30,000 employees** throughout European Russia. It is also expanding its network of domestic suppliers that manufacture foodstuffs which are delivered to its restaurants.

McDonald's Russia president Khamzat Khasbulatov said expanding in Siberia and even the Urals posed logistical problems. "We have to consider the possibilities for obtaining real estate that makes it possible for us to create a chain, so that the logistics and logistics management will be effective," he said.

The Siberian locations will get their food items from the logistics center in Kazan, which is midway between Moscow and the Urals. Later, they will receive items through Yekaterinburg.

➤ **Auchan** has **invested over \$1.56 B** in the development of its business in Russia over the ten years of its operations in the country, the company's president Vianney Mulliez stated at a recent news conference.

Over the course of that decade, Auchan has **paid more than \$1.4 B rubles in taxes and social benefits**. Auchan currently has **52 stores** in Russia, including 36 classic Auchan hypermarkets, 14 Auchan City hypermarkets and two Nasha Raduga stores.

The French retailer plans to **expand its chain to 150 hypermarkets by 2015 to 2017**. It will open **seven new stores by the end of 2012**, including hypermarkets in Samara, Tyumen, Volgograd and St. Petersburg, as well as two Nasha Raduga stores in Kostroma and Yaroslavl.

➤ **Volkswagen** announced that it **will invest \$1.25 B in Russia by 2018**, initially expanding by building an engine plant in Kaluga.

➤ **M.Video** posted a **58% jump in 1H earnings** on rising sales and announced it may pay a special dividend to shareholders in December. The company is Russia's only listed home appliances retailer and is benefiting from consumer purchases of new flat-screen TVs and vacuum cleaners. **1H net profit rose to \$37.5 M on net revenue, which increased 26%**. The revenue gain was driven by the addition of **16 new stores**, a 16% rise in

like-for-like sales and a **71% increase in Internet sales.**

➤ **Three red double-decker buses** began operating around the Kremlin in August, as Moscow became the last European capital to introduce the tourist vehicles that are a familiar sight for holidaymakers across the world.

Spain's **City Sightseeing** invested about **\$3 M** to start the service in 2012 in Russia, President Enrique Ybarra said.

The three buses unveiled at a demonstration tour for guests and reporters cost about \$200,000 each. After a period doing tours in Stockholm and Copenhagen, they were refitted in Germany before being shipped to Russia in early 2012.

During a test period that will last until New Year's, they will run on a 9-kilometer circuit taking in **St. Basil's Cathedral**, Bolotnaya Ploshchad, **Christ the Savior Cathedral**, the

Bolshoi Theater and Lubyanskaya Ploshchad.

Passengers can hop on and off the buses, which currently offer commentary in English and

Russian, as many times as they like. Adult tickets cost RUR 600 per day. The 18 stops along the route will be marked with special signs. St. Petersburg, Sochi and Minsk are destinations to be added in the near future.



Fund Awards



**Most Innovative Funds of Funds
(for innovation and performance)**



**No. 3 ranked fund of funds in
the world, February 2012**



**No. 2 ranked fund of funds in
the world for 2010**



**No 1 ranked fund of funds
in the world for 2005**



**Most Innovative Funds of
Funds (for innovation and performance)**



**No. 4 ranked fund of funds in
the world, YTD 2012**



**No 8 ranked fund of funds in
the world for 2009**

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