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Smart, successful investors in the Baltic States, Russia, Ukraine and other CIS countries are no different than smart, successful investors in the United States and western Europe. Savvy investors in the countries of the former Soviet Union know how to balance risk and return, but above all, they take the long-term view. Without adequate perspective, the ebbs and flows of stock prices, analysts' forecasts and global developments can cause the inexperienced investor in the region to swing from "irrational exuberance" to "irrational depression."

It is true that the Russian economy is growing faster than most others around the globe, posting a 5.3 percent growth rate in 2001 and a

The Dangers of Market Manic Depression

An Opinion Editorial by Ruben Vardanyan,
President of Troika Dialog

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The Future of Investing in Ukraine and Moldova

An Interview in Izvestiya with Natalie Jaresko,
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Dasha, the Newest Addition to PBN's
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predicted 3.8 percent growth rate this year. The U.S Government finally designated Russia a "market economy" for the first time in June 2002, a status also recently achieved by Kazakhstan. The Russian Trading System index is up 25 percent for the year.

Other countries in the region are also experiencing strong growth. For example, Latvia's GDP grew by 7.6 percent last year and Ukraine's grew 9 percent. Kazakhstan saw a double digit rise in GDP – up 13.2 percent in 2001.

These results have led many foreign investors, including those that abandoned the market after Russia's 1998 ruble devaluation, to again consider putting their money back into the region. BP's decision to increase its stake to 25 percent in the Russian oil company SIDANCO is another important indicator of growing confidence in Russia's long-term economic prospects. The PBN Company is proud to serve as strategic consultant both to BP and to SIDANCO.

But long-time players in these markets caution newcomers not to step foot into the region without a realistic evaluation of the risks and a prudent, long-term perspective. The fact is that most of the economies remain in flux – with all the associated opportunities and dangers.

This edition of **Access PBN** highlights sage advice from two other clients of The PBN Company – Ruben Vardanyan, president of Troika Dialog of Moscow and Natalie Jaresko, president of the Western NIS Enterprise Fund (WNISEF) in Chicago.

First is an opinion editorial authored by Mr. Vardanyan for The Moscow Times. In it, he encourages foreign investment in Russia, but warns against "unqualified optimism." Troika is the largest investment bank and brokerage in Moscow, and recently led a consortium that purchased a 49 percent stake in Rossgostrakh, Russia's largest insurance company. Mr. Vardanyan is also General Director of Rossgostrakh.

Second is an interview with WNISEF President Natalie Jaresko that appeared in the Russian newspaper Izvestiya on investment opportunities in Ukraine and Moldova. WNISEF, based in Chicago, is the largest foreign venture fund in Ukraine and Moldova with a shareholder capital of \$150 million.

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The Dangers of Market Manic Depression

By Ruben Vardanyan, Reprinted with permission from The Moscow Times

Westerners frequently comment that Russians oscillate between extremes. They say the Russian character mirrors the country's dramatic changes in seasons and climate. Few can disagree that the moods of Russian people can change in a flash from exuberance to depression.

Perhaps Westerners have now taken on this very Russian character trait that they find so different from their own. What else can explain today's infectious optimism in the West about the Russian economy? Has it really been so long since the markets and pundits in New York and London were calling Russia economically irrelevant, or worse?

Make no mistake, Russia is far better off today than in 1998 or even one year ago. Once crippled by government default and ruble devaluation, the feel-good factor is back. Thanks to prudent economic and fiscal policies, Russia has joined China as a Cinderella story on the world economic stage.

But does Russia's progress justify the unqualified exuberance of Western investors and politicians recently witnessed at the widely attended Russian Economic Forum in London and the World Russian Forum in Washington? Rational exuberance may be fitting. On the other hand, what Alfa Bank president Pyotr Aven has aptly termed

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Ruben Vardanyan is general director of the Rosgosstrakh insurance company and CEO of the Troika Group of Companies, Russia's top investment company

unbridled euphoria, will lead to false expectations, lost investment and serious damage to Russia's reputation.

Tax, pension and land reforms together with serious attention to corporate governance are laying foundations for sustainable economic growth. But fundamental problems persist -- the dysfunctional banking system, gargantuan government bureaucracy and a demographic crisis of alarming proportion. As President Vladimir Putin recently pointed out in his state of the nation address, while the Russian economy is growing faster than most others around the globe, that growth is neither stable enough nor robust enough to compete effectively in the world economy.

Of course, many in the business and financial community have deliberately and justifiably talked up Russia's prospects to persuade the outside world it is a place worthy of investment. Amid global economic slowdown and sluggish performance in both the United States and Western Europe, Russia's growth rates, 5.3 percent in 2001 and probably 4 percent this year, make Russia look like an attractive bet.

I, too, am one of the most forceful advocates of new foreign and domestic investment in Russia. But investment decisions must be based on facts, prudence and an objective view of the economic risks and opportunities.

Well-run companies understand that it is essential to manage expectations of the markets and to deliver performance in line with their own predictions. Overperformance can destabilize share prices as much as underperformance. Markets are interested in whether companies can sustain growth over the long-term. Russia must and will be judged by these same criteria.

Increased political stability, the adoption of progressive economic and tax legislation, a raft of plans to reform the civil service, the natural monopolies and the banking sector, and the country's eager pursuit of WTO membership are all highly encouraging. Putin has stabilized relations with Western countries, evidenced by the decision to ally Russia with the United States in the war against terrorism and the extraordinary upgrading of Russia's relations with NATO.

But the facts are the facts, and we must face up to them. Real exchange rate appreciation has eroded the effects of devaluation in 1998, and increased quantities of imports are returning to the Russian

market. For the economy to grow, industry must increase labor productivity and efficiency levels -- factors that have been Russia's Achilles' heel for centuries.

The backbone of any successful modern economy is small and medium enterprises. Their number is growing, but they are still painfully under-represented. Small businesses need relief from the stranglehold of state bureaucracy as proposed by Putin, as well as access to finance and credit from the domestic banking system.

We also have to face the fact that foreign investment is a highly competitive process. Russia has no right to assume that foreign investment will happen simply because of the country's huge market potential and low tax rates. For major multinational manufacturers, Russia is just one of many markets.

On the plus side, more Russian capital is being repatriated from abroad, a sure sign of increased business confidence. The recent publication of a corporate governance code is a significant step forward in establishing a modern business culture in Russia and in attracting and protecting investors.

However, the economy as a whole remains far too reliant on oil and gas exports, which represent about 40 percent of total exports and 15 percent of gross domestic product. Their proportion has diminished, but the country's overall economic performance and foreign debt repayment schedule is hostage to high commodity prices. Russia exports little other than raw materials, weapons and vodka.

Growing numbers of the Russian business elite share my determination to be able to conduct business in Russia according to international norms. While we see the obstacles on the horizon, we also see that Russia has no choice but to make a quantum leap toward full integration into the global economy.

A year and a half ago, there was talk in the United States about the possibility of a vacuum in the heart of Eurasia, "a world without Russia." Today, with the growth of the economy and after the turning point of Sept. 11 and the just-concluded Russia-U.S. summit, the situation has again radically changed.

Russia is unquestionably moving in the right direction, and we can justifiably feel confident and optimistic about the future. But despite the country's significant progress, we must recognize that we are only a

small way down the road of economic transformation. We cannot afford to be economical with the truth; otherwise, these achievements will be for naught.

If Russia can build an infrastructure for lasting economic growth, the better able the country will be to withstand the sudden and extreme changes in the perceptions of this great country held by Russians and foreigners alike.

For additional information: <http://www.troika.ru/>

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The Future of Investing in Ukraine and Moldova

An Interview in Izvestiya with Natalie Jaresko, President of the Western NIS Enterprise Fund

Natalie Jaresko, President and CEO of the Western NIS Enterprise Fund (WNISEF) based in Chicago, recently shared her thoughts on investment opportunities in Ukraine and Moldova with Izvestiya journalist Svetlana Lokotkova. WNISEF is the largest foreign venture company in Ukraine and Moldova with \$150 million of shareholder capital, and controlling stakes in some of Ukraine's most promising confectionery and construction companies. Below is a translated reprint of her June interview with Izvestiya.

Izvestiya: *Your fund has been working in Ukraine since 1995. Did you go there by chance or were you trying to secure an advance stake in the most promising industries?*

Jaresko: Before investing in Ukrainian and Moldovan enterprises we thoroughly studied similar companies in the Central and Eastern Europe. As a result, we worked out a strategy only to buy stakes exceeding 25% and amounting to not less than \$1 million and not more than \$10 million. The area of our interests includes small and medium –sized Ukrainian companies concentrated mostly in food processing and agriculture, construction materials production, consumer goods trading and telecommunications.

Izvestiya: *What is the total turnover of the Ukrainian enterprises under your control?*

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Natalie Jaresko is President and Chief Executive Officer of the Western NIS Enterprise Fund, the largest foreign venture fund investing in Ukraine and Moldova.

Jaresko: The total revenues of our companies is \$232 million, \$142 million of this is from Ukraine and \$90 million from Moldova.

Izvestiya: *Do you feel competition from Russian investors? If so, In which sectors?*

Jaresko: There are many venture capital funds in Ukraine – American, Russian, Greek and Dutch. They compete with each other to some extent. If we do not take into account strategic industries like heavy machine building, metallurgy, electric energy, in which we do not invest due to the limitations I mentioned, Russian funds are represented mostly in food processing. The investors are large industrial corporations like LUKoil and SibAl that seek business diversification. In addition, Russian industry investors like Wimm-Bill-Dann and Planeta Management that are not venture funds, but strategic investors, are very active in these sectors.

Izvestiya: *What are Ukraine's most promising industries for investments at present, in your opinion?*

Jaresko: Of the ones I've mentioned, construction materials production is expected to grow most rapidly, so , the related companies will be the most attractive to investors. In addition, the Ukrainian energy companies are in the process of privatization, so they are definitely of great interest to foreign venture funds. It's a safe bet that land reform will lead to the re-division of Ukrainian land so we expect investment flows into food processing and agriculture.

Izvestiya: *What are the main investment and political risks in Ukraine?*

Jaresko: The main business risk is the same as everywhere – reliability of business partners. Many Ukrainian companies still violate contracts and agreements and are ignorant of corporate governance standards and shareholders' rights. Macroeconomic risk is characteristic of all emerging markets. Another risk is the purchasing power of the population, which has to be increased to develop production, otherwise people won't be able to buy goods. As far as political risks are concerned, the results of the recent elections in Ukraine have boosted investor confidence. The current situation in the country is the most stable we have had over the past seven years both from the political and economic standpoint.

For additional information: <http://www.wnisef.org/>



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News from PBN

TREASURY NOTE. Myron Wasyluk, Senior Vice President and Managing Director of The PBN Company's Kyiv office, recently gave a briefing on intellectual property issues to a delegation of visiting U.S. Treasury officials led by Secretary Paul O'Neill. The delegation attended a breakfast meeting of the American Chamber of Commerce in Ukraine. Myron is a member of the Board of Directors of AmCham.

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ON CENTER STAGE. Myron also recently delivered a presentation to the Ukrainian Foreign Investment Advisory Council of Ukraine on ways to improve that country's foreign investment climate.

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ALSO ON STAGE IN UKRAINE. Oksana Monastyrskya, PBN's Senior Account Manager in Ukraine, offered insights on "Effective Communications as a Mechanism for Attracting Investment" at the 7th Annual Forum on Capital Markets in Ukraine.

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AND NOT TO BE UPSTAGED. The Chairman of the PBN Board of Directors, Peter G. Kelly, addressed the International Business Council of the Metro Hartford Regional Economic Alliance on "Doing Business Internationally: Have the Rules Changed?" with Russia as a case study. [See a copy of Peter's speech.](#)

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Dasha Necarsulmer is the latest addition to PBN's Moscow office

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ON BOARD. Tom Thomson, The PBN Company's Senior Vice President, was invited and agreed to serve on the Board of Directors of the U.S.-Baltic Foundation, a Washington, DC-based foundation that supports democratic and free market reforms in Estonia, Latvia and Lithuania.

Email Tom: tom.thomson@pbnco.com

BETS WHO? It's Radu Betsiu, who recently moved from our Moldova office to join our Moscow staff, where he is serving as an account manager.

Email Radu: radu.betsiu@pbnco.com

A NEW ADDITION TO THE PBN FAMILY. Please welcome the latest addition to the PBN family, Dasha Necarsulmer, a Jack Russel Terrier. Originally from Bend, Oregon, Dasha is now based in the Moscow office, with responsibilities for acting cute, being spoiled and learning how to bark in Russian.

Email Dasha: dasha.necarsulmer@pbnco.com

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