



# Midlincoln Fund Atlas

April 2018  
Fund Research

Bloomberg: RUSE:RM

Focus: Russia

Asset Class: Equity

Type of fund: UCITS ETF

Underlying Index:  
RTS Index

Domiciliation: Luxembourg

Registration Body: CSSF

Fund Administrator: Edmond de Rothschild

Custodian:  
Edmond de Rothschild

Management Company: Fuchs Asset Management

Investment Manager:  
Da Vinci Capital Mgmt.

Index Owner: S&P

Replication: Physical

ETF Components:  
All 46 stocks of RTS Index

Listing: Irish Stock Exchange

Admission to trading:  
LSE, Moex

NAV Currency: USD

NAV Frequency: Daily

Dividend Distribution: Annual

TER %: 0.65

Auditor:  
KPMG

## ITI Funds RTS Equity ETF -

### The Optimal Way to access Russian equity markets

ITI Funds is a European ETF provider specializing in Emerging Markets.

The first 2 UCITS ETFs provide exposure to Russian equity and fixed income markets.

These 2 exchange funds (ETFs) were successfully launched on the London Stock Exchange (LSE) to growing International investor demand, and on the Moscow (Moex) Exchange for local investors

The ITI Funds RTS Equity ETF offers the most diversified, liquid and efficient physical exposure to Russian financial markets.

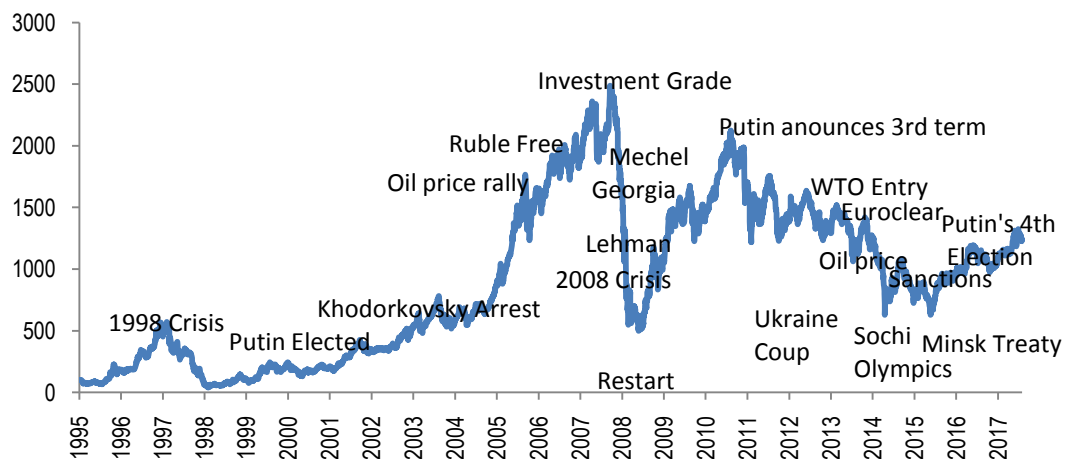
The ETF physically replicates the free-float, cap-weighted RTS Index (46 equities), and which is Russia's oldest and most widely used equity index for securities traded on the Moscow Exchange.

### ITI Funds RTS Equity ETF

#### Key Benefits:

- Diversified exposure to Russian equity markets
- Physical replication to 46 largest and most liquid Russian equities
- Low cost access to local Russian securities Vs peers or Active Managers
- USD/RUB denominated
- Local / Euroclear settlement
- Listing on the Moscow (MOEX) and London Stock Exchange (ISE) which offers global liquidity

### RTS Index



Source: Midlincoln Research

## The RTS Equity Index...

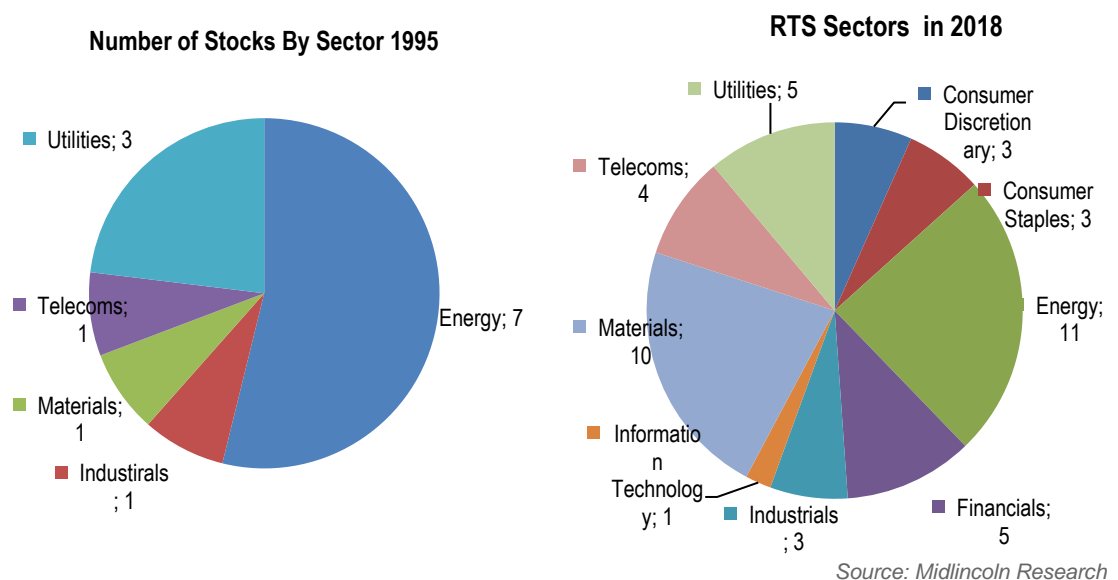
ITI Funds selected to replicate the RTS Index as:

- It is the longest standing Index in the Russian Equity Market
- RTS is the broadest benchmark diversified across 13 industries
- The Index is composed of the 46 most liquid/ largest capitalized companies in Russia
- The index timely reflects on capital markets activity on the Russian markets and includes almost all sizeable Russian IPOs while the peers don't
- Free float information, liquidity assessment, and corporate actions have been far timelier and transparent
- RTS Index includes local shares whereas other Russian benchmarks include GDRs and ADRs that frequently trade with premium to locals

## Investment Summary

The Russian market is ideal for index ETF. It has been anything but unexciting since its inception. For most of the years since inception, it makes the ranks of being the best equity market globally. RTS index is full of value names trading on low multiples and offering chunky dividends. Yet it is offering exposure to Russian growth sectors in infrastructure, consumer, financials and IT. For most of the times RTS index is driven by flows. Well diversified ETF will be a robust tool to follow Russian politics, oil price, emerging market risk or related flow trades.

## How RTS Index Changed From inception



RTS Index is even more important domestically. Its RUB mirror Moex Index is a benchmark for all Russian pension managers while they are regulated to make their stock selection within the universe of the RTS – Moex Index stocks. In the future - ITI Funds RTS ETF will also likely be a key instrument available for Russian pension investment portfolios.

## Passive vs. Active Funds.

For a long time, Russian investment managers avoided passive products favouring actively managed products. Whilst this attitude is still prevalent in Russia, passive products globally keep attracting the biggest

While the idea of beta generation is attractive for investors even on a global scale, passive products globally keep attracting the biggest inflows. Supporting the argument that passive products have a variety of advantages in any market and even more so in Russia.

Very often active products are not diversified at all and focus on a few high conviction long-term top picks where the investment horizon is 3 years or 5. The price of an error with stock picking is quite expensive. Poor diversification of the funds poses significant risk for investors. Whereas broad market ETF products offer optimal diversification inherent into index construction.

ETF shares are easily transferable from a broker to broker while this option is not always suitable for active products. With ETFs investors get daily or real-time liquidity in the majority of the products. Fund redemptions are allowed instantly. While actively managed products for the most part offer only annual liquidity at most quarterly and rarely monthly. Investors should notify managers in a special time window about the upcoming redemption and then wait for a while for the funds to arrive and frequently pay additional redemption fees.

ETFs rooted by domestic Russian management companies until recently were mostly nonexistent. Few existing international ETFs such as iShares MSCI Russia ETF, Van Eck RSX Russia and Lyxor Dow Jones Russia ETF are mostly fueled by international money and were not available to Russian domestic investors and as such they were perceived as exotic and an artificial way to invest into Russia where domestic investors always been a force behind liquidity on Moscow Exchange. These ETFs prefer GDRs/ADRs (that are frequently trading with a premium) to locals and the indexes they track contain additional hidden costs inherent into rebalancing procedures.

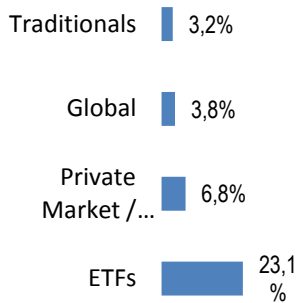
## RTS ETFs vs. RTS Index Futures

The prolonged absence of the liquid domestic broad market ETF on Russian market has skewed investors in Russia towards using RTS index futures instead. RTS future is one of the most liquid domestic market instruments – accounting at times for a half of daily liquidity on Moscow Exchange – they will be losing market share to ITI RTS ETF in the near future.

Futures are convenient because they also offer minimal size entree, they offer diversification and they are suitable for robots. But RTS futures require diligent management approach and investors can lose income if they miss a rollover date. Because of that, they are not suitable for long-term investors. They are paper contracts and are not backed up by any real assets. RTS Index futures do not offer a dividend yield. For the most of the time, RTS futures trade in backwardation even to the price RTS price index and this has further depressed investors' returns.

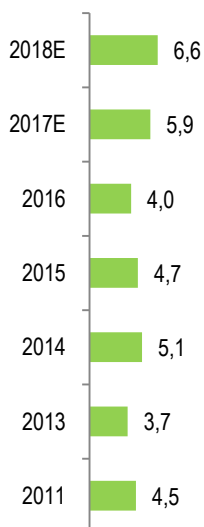
There are further limitations. Futures are like 10xRTS product the leverage is an inherent part of the product. It is not possible to use the credit against future elsewhere on the market. While

### Industry Trends Inflows 2017 Annualized



Source: Morgan Stanley

### RTS Index Historic Dividend Yield



Source: Midlincoln Research

RTS ETF is euroclearable UCITS instrument and will be backed by REPO with Moscow Exchange NKC bank and funds could be used elsewhere. RTS ETF will have tax advantages for investors based in countries with no double tax treaty.

## ITI Funds RTS Index ETF vs. current peers

- **The ITI Funds RTS Equity ETF:**
- **Offers superior diversification across all 46 stocks in the RTS Index**
- **Invests in the underlying local shares as opposed to synthetic ADRs /GDRs**
- **Total Expense Ratio (TER) is 0.65bps, lower than average charges of + 0.90bps**

ITI RTS ETF uses physical replication. However, Lyxor DJ Russia ETF uses synthetic index tracking and contains index return swaps while holding unrelated to Russia stocks on the balance sheets as collateral, increasing unnecessary swap counterparty risks. Investing into synthetic ETF is really like investing into a basket of futures issued by a swap provider. The balance sheet of the swap provider is key to the sustainability of returns. ETF fund manager's ability to roll over the swap at all times replicating index performance is another headache. We recommend switching out of Lyxor into physically replicated ETFs. This idea coincides with the ETF fund flow YTD – out of synthetic ETFs into physically replicated.

## 12 Month Fund Flow

Fund	12 m Flow USD mn
iShares MSCI Russia ADR/GDR	152.19
HSBC MSCI Russia Capped	147.9
iShares MSCI Russia Capped ETF	40.09
db x-trackers MSCI Russia Capped	39.6
Direxion Daily Russia Bull 3x S	21.47
Source RDX UCITS ETF	-25.72
LYXOR ETF RUSSIA Dow Jones Russia	-85.53
Market Vectors Russia	-755.51

ITI Funds RTS ETF is targeting minimal levels of tracking error while other ETFs can't match index performance well.

## RTS Index dissected

RTS index is free float weighted, capped index containing stocks trading on Moscow exchange with stock selections criteria based on the liquidity of free float, size of the market cap and size of free float. Candidate inclusion/exclusion stocks are added to the respective index waiting lists a quarter ahead of the rebalancing minimizing rebalancing costs. Moex RTS Index board is the body making the rebalancing decisions.

### Sector Weights

	Weight
Energy	47.4%
Financials	19.8%
Materials	16.4%
Staples	4.7%
Telecoms	4.7%
Utilities	3.0%
IT	1.4%
Industrials	1.3%
Cons. Disc.	0.9%

### Industry Weights

	Sub Industry	Weight %
Integrated Oil & Gas		36.4%
Diversified Banks		17.8%
Oil & Gas Exploration & Prodi		9.5%
Diversified Metals & Mining		6.2%
Food Retail		4.5%
Wireless Telecommunication S		4.1%
Steel		4.0%
Precious Metals & Minerals		3.3%
Electric Utilities		2.7%
Financial Exchanges & Data		1.8%
Internet Software & Services		1.4%
Gold		1.1%
Oil & Gas Storage & Transport		1.0%
Aluminum		0.9%
Fertilizers & Agricultural Che		0.9%
Airlines		0.8%
Integrated Telecommunication S		0.6%
Homebuilding		0.4%
Oil, Gas & Coal		0.3%
(nyct o)		0.3%
Banking		0.3%
Utilities		0.3%
Oil & Gas Equipment & Servic		0.3%
Transportation & Logistics		0.3%
Construction Machinery & Hex		0.3%
Distributors - Consumer Staple		0.2%
Computer & Electronics Retail		0.2%

Ticker	Company	Sector	Free float%	Restricting coefficient	Weight	Market Cap \$mln	Est Div Yield 2018	Est PE 2018	EV/EBITDA 18	Est ROE 18	Est P/E 18
GAZP RM	Gazprom	Energy	46%	92.0%	15.00%	57989.6	5.9	4.1	6.8	6.8	0.3
SBER RM	Sberbank of Russia	Financials	48%	49.0%	14.00%	102075.4	4.3	7.7	-	23.3	1.8
LKOH RM	LUKOIL	Energy	46%	92.0%	14.00%	56123.1	5.5	7.1	7.2	11.6	0.8
GMKN RM	MMC Norilsk Nickel	Materials	38%	92.0%	6.00%	31581.5	7.8	13.0	10.8	60.5	7.8
NVTK RM	Novatek	Energy	27%	92.0%	5.00%	39256.5	2.0	13.9	14.4	23.4	3.0
ROSN RM	Rosneft Oil Co	Energy	11%	100.0%	4.00%	60687.7	3.3	10.5	10.4	8.1	0.9
TATN RM	Tatneft	Energy	32%	100.0%	4.00%	23033.1	6.0	10.6	8.8	17.5	1.7
MTSS RM	Mobile TeleSystems	Telecoms	48%	100.0%	3.00%	10875.1	8.5	10.0	8.5	45.2	5.0
VTBR RM	VTB Bank	Financials	39%	100.0%	3.00%	10896.2	2.1	7.9	-	7.3	0.6
SNGS RM	Surgutneftegas	Energy	25%	100.0%	3.00%	17957.2	2.2	4.6	-	6.2	0.3
MGNT RM	Magnit	Staples	66%	100.0%	3.00%	7714.4	4.5	12.5	8.8	15.8	1.6
ALRS RM	Alrosa	Materials	34%	100.0%	2.00%	11265.0	6.7	7.8	6.9	28.6	2.0
CHMF RM	Severstal	Materials	20%	100.0%	2.00%	14048.7	9.1	8.8	7.3	44.8	3.7
YNDX RM	Yandex NV	IT	95%	25.0%	2.00%	13737.4	0.0	39.1	32.8	22.6	7.0
SNGSP RM	Surgutneftegas pref.	Energy	73%	100.0%	2.00%	4017.4	5.2	5.4	-	6.0	0.4
HYDR RM	RusHydro	Utilities	25%	100.0%	1.00%	5817.6	6.8	6.2	6.1	7.4	0.5
IRAO RM	Inter RAO UES	Utilities	29%	100.0%	1.00%	6921.1	3.8	6.0	5.4	12.1	0.9
MFON RM	MegaFon	Telecoms	21%	100.0%	1.00%	5964.2	7.2	12.8	10.2	20.3	2.7
RTKM RM	Rostelecom	Telecoms	32%	100.0%	1.00%	3007.8	7.9	10.8	9.0	6.2	0.6
MAGN RM	Magnitogorsk Steel	Materials	16%	100.0%	1.00%	9014.7	7.9	8.8	6.8	19.4	1.7
NLMK RM	Novolipetsk Steel	Materials	16%	100.0%	1.00%	16285.6	8.0	10.3	8.5	24.2	2.4
PHOR RM	PhosAgro	Materials	25%	100.0%	1.00%	5699.0	4.7	11.1	9.0	42.0	2.9
POLY RM	Polymer	Materials	37%	100.0%	1.00%	4805.6	3.9	12.0	11.7	35.2	3.8
RUAL RM	Rusal	Materials	16%	100.0%	1.00%	10570.2	3.2	7.9	11.5	34.0	2.4
PLZL RM	Polyus	Materials	16%	100.0%	1.00%	10658.2	5.6	10.0	8.0	138.9	8.5
AFLT RM	Aeroflot	Industrials	45%	100.0%	1.00%	2704.9	9.1	5.7	4.7	43.1	2.7
MOEX RM	Moex	Financials	58%	100.0%	1.00%	4470.6	6.4	12.2	-	16.3	2.1
SBERP RM	Sberbank of Russia pref.	Financials	100%	49.0%	1.00%	3739.0	5.8	6.2	-	23.5	1.4
TATNP RM	Tatneft	Energy	100%	100.0%	1.00%	23018.8	7.7	7.5	8.8	17.5	1.2
TRNFP RM	Transneft	Energy	32%	100.0%	1.00%	4960.3	4.3	5.8	2.2	12.0	0.7
FIVE RM	X5 Retail Group NV	Staples	41%	50.0%	1.00%	9945.0	1.0	16.3	11.9	23.4	3.5
FEES RM	Federal Grid	Utilities	18%	100.0%	0.00%	3969.3	8.0	3.1	5.1	7.7	0.3
RSTI RM	ROSSETI	Utilities	11%	100.0%	0.00%	2992.2	1.5	1.8	5.0	4.7	-
UPRO RM	Unipro	Utilities	16%	100.0%	0.00%	3006.3	8.9	6.3	7.1	24.5	1.5
AFKS RM	Sistema FC	Telecoms	36%	100.0%	0.00%	2119.3	12.1	15.2	7.2	-26.7	0.9
MTLR RM	Mechel	Materials	50%	100.0%	0.00%	1085.0	0.0	4.7	-	-	-
UWGN RM	United Wagon Co	Industrials	26%	100.0%	0.00%	1621.2	-	-	-	-	-
NMTP RM	Norosiisk Sea Port	Industrials	15%	100.0%	0.00%	2814.4	2.7	7.0	7.5	57.3	5.0
CBOM RM	Credit Bank of Moscow	Financials	22%	100.0%	0.00%	2249.8	-	6.0	-	16.1	0.9
SFIN RM	Safmar	Financials	29%	100.0%	0.00%	1456.2	-	-	-	-	-
TRMK RM	TMK	Energy	30%	100.0%	0.00%	1474.2	2.1	13.0	11.3	11.8	2.1
RNFT RM	Rusneft	Energy	20%	100.0%	0.00%	3148.6	-	20.5	22.5	23.1	4.1
AGRO RM	Ros Agro	Staples	21%	100.0%	0.00%	1394.2	5.1	9.7	11.8	9.4	0.8
MVID RM	M.Video	Cons. Disc.	27%	100.0%	0.00%	1400.5	4.1	12.9	10.0	33.4	3.6
PIKK RM	PIK Group	Cons. Disc.	18%	100.0%	0.00%	3687.9	1.0	22.7	12.8	15.9	3.3
DSKY RM	Detsky Mir	Cons. Disc.	34%	100.0%	0.00%	1178.8	6.5	13.7	10.2	-229.9	-
Weighted Averages							5.1	8.8	6.8	20.8	2.0

Source: Moex

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