

<https://blog.en.erste-am.com/2015/02/27/become-oil-x-20-rule/>

What has become of the “oil x 20” rule?

Peter Szopo



© Foto: iStock.com

The oil and gas sector is the backbone of the Russian economy. It contributes roughly a quarter to the Russian GDP, and it accounts for almost two thirds of exports. Oil and gas companies represent almost 60% of the market capitalisation of the Moscow stock exchange. It therefore makes sense to analyse the performance of the Russian equity market in connection with the level and development of the oil price. For a long time, the “oil x 20” rule of thumb would suggest that the fair value of the RTS, the Russian equity index, was 20 times the price of crude oil (as measured in US dollar per barrel of Brent). Especially equity strategists – always suckers for simple marketing ploys – would take a liking to this relation.

And it is true – the RTS index has reached or exceeded this threshold of 20x only shortly in the past 15 years: from the beginning of 2006 to the beginning of 2008, i.e. right before the financial crisis. Since then the index has failed to rise to that level again. The new relation between oil and the Russian equity index is significantly lower, i.e. at an average of 15x over the past five years. Even that value has not been reached since 2011. It was only during the most recent rally that the market was able to approach the long-term average again. This is in line with the image that the more conventional valuation techniques are painting: the market PE (price/earnings ratio) of slightly above 6x and the valuation discount of 50% relative to other emerging markets are essentially where the historical average predicts they should be. A lot suggests that the level the index is currently at after the latest rally is roughly where one would expect it to be in view of the current oil price.

Perhaps the rule will be adjusted to “oil x 15” for the Russian market. This does not rule out that the most recent rally may continue, given that the rules of financial markets are sometimes amazingly elastic. However, without the sustainable recovery of the oil price and visible progress in the Ukrainian crisis the upward potential of the Russian equity market from here on out seems limited.

RTS relative to the oil price (Brent, USD per barrel)



Sources: Bloomberg, Erste Asset Management.

Legal disclaimer

This document is an advertisement. All data is sourced from ERSTE-SPARINVEST Kapitalanlagegesellschaft m.b.H., Erste Asset Management GmbH and ERSTE Immobilien Kapitalanlagegesellschaft m.b.H. unless indicated otherwise. Our languages of communication are German and English. The prospectus for UCITS (including any amendments) is published in Amtsblatt zur Wiener Zeitung in accordance with the provisions of the InvFG 2011 in the currently amended version. Information for Investors pursuant to § 21 AIFMG is prepared for the alternative investment funds (AIF) administered by ERSTE-SPARINVEST Kapitalanlagegesellschaft m.b.H., Erste Asset Management GmbH and for ERSTE Immobilien Kapitalanlagegesellschaft m.b.H. pursuant to the provisions of the AIFMG in connection with the InvFG 2011 and regarding ERSTE Immobilien Kapitalanlagegesellschaft m.b.H. published in Amtsblatt zur Wiener Zeitung or at the web site www.ersteimmobilien.at. The fund prospectus, Information for Investors pursuant to § 21 AIFMG and the key investor document/KID can be viewed in their latest versions at the web site www.erste-am.com or www.ersteimmobilien.at or obtained in their latest versions free of charge from the domicile of the management company and the domicile of the custodian bank. The exact date of the most recent publication of the fund prospectus, the languages in which the key investor document/KID is available, and any additional locations where the documents can be obtained can be viewed on the web site www.erste-am.com or www.ersteimmobilien.at. This document serves as additional information for our investors and is based on the knowledge of the staff responsible for preparing it at the time of preparation. Our analyses and conclusions are general in nature and do not take into account the individual needs of our investors in terms of earnings, taxation and risk appetite. Past performance is not a reliable indicator of the future performance of a fund.



Peter Szopo

Peter Szopo has worked as chief equity strategist at the Erste Asset Management since March 2015. Before he already worked as a consultant for equity fund management at Erste Asset Management for Central and Eastern European equity markets. From November 2009 to April 2013, he was head of the research department at Alfa Bank in Moscow.

After his research work at WIFO (Austrian Institute of Economic Research) from 1978 to 1990, he worked as a securities specialist in various management functions at internationally renowned investment banks. During this time he held the position of Head of Research at such institutions as Creditanstalt Investmentbank, UniCredit Bank Austria, Robert Fleming Securities, and at Bank Sal. Oppenheim.

Along with his analysis activities, he worked from 1997 to 2000 at Eastfund Management as the fund manager for Central and Eastern European equity.