

<https://blog.en.erste-am.com/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.

Sources: Bloomberg, Erste Asset Management.

Legal disclaimer

This document is an advertisement. Unless indicated otherwise, source: Erste Asset Management GmbH. The language of communication of the sales offices is German and the languages of communication of the Management Company also include English.

The prospectus for UCITS funds (including any amendments) is prepared and published in accordance with the provisions of the InvFG 2011 as amended. Information for Investors pursuant to § 21 AIFMG is prepared for the alternative investment funds (AIF) administered by Erste Asset Management GmbH pursuant to the provisions of the AIFMG in conjunction with the InvFG 2011.

The currently valid versions of the prospectus, the Information for Investors pursuant to § 21 AIFMG, and the key information document can be found on the website www.erste-am.com under “Mandatory publications” and can be obtained free of charge by interested investors at the offices of the Management Company and at the offices of the depositary bank. The exact date of the most recent publication of the prospectus, the languages in which the key information document is available, and any other locations where the documents can be obtained are indicated on the website www.erste-am.com. A summary of the investor rights is available in German and English on the website www.erste-am.com/investor-rights and can also be obtained from the Management Company.

The Management Company can decide to suspend the provisions it has taken for the sale of unit certificates in other countries in accordance with the regulatory requirements.

Note: You are about to purchase a product that may be difficult to understand. We recommend that you read the indicated fund documents before making an investment decision. In addition to the locations listed above, you can obtain these documents free of charge at the offices of the referring Sparkassen bank and the offices of Erste Bank der oesterreichischen Sparkassen AG. You can also access these documents electronically at www.erste-am.com.

N.B.: The performance scenarios listed in the key information document are based on a calculation method that is specified in an EU regulation. The future market development cannot be accurately predicted. The depicted performance scenarios merely present potential earnings, but are based on the earnings in the recent past. The actual earnings may be lower than indicated. Our analyses and conclusions are general in nature and do not take into account the individual characteristics of our investors in terms of earnings, taxation, experience and knowledge, investment objective, financial position, capacity for loss, and risk tolerance.

Please note: Past performance is not a reliable indicator of the future performance of a fund. Investments in securities entail risks in addition to the opportunities presented here. The value of units and their earnings can rise and fall. Changes in exchange rates can also have a positive or negative effect on the value of an investment. For this reason, you may receive less than your originally invested amount when you redeem your units. Persons who are interested in purchasing units in investment funds are advised to read the current fund prospectus(es) and the Information for Investors pursuant to § 21 AIFMG, especially the risk notices they contain, before making an investment decision. If the fund currency is different than the investor's home currency, changes in the relevant exchange rate can positively or negatively influence the value of the investment and the amount of the costs associated with the fund in the home currency.

We are not permitted to directly or indirectly offer, sell, transfer, or deliver this financial product to natural or legal persons whose place of residence or domicile is located in a country where this is legally prohibited. In this case, we may not provide any product information, either.

Please consult the corresponding information in the fund prospectus and the Information for Investors pursuant to § 21 AIFMG for restrictions on the sale of the fund to American or Russian citizens.

It is expressly noted that this communication does not provide any investment recommendations, but only expresses our current market assessment. Thus, this communication is not a substitute for investment advice, does not take into account the legal regulations aimed at promoting the independence of financial analyses, and is not subject to a prohibition on trading following the distribution of financial analyses.

This document does not represent a sales activity of the Management Company and therefore may not be construed as an offer for the purchase or sale of financial or investment instruments.

Erste Asset Management GmbH is affiliated with the referring Sparkassen banks and Erste Bank.

Please also read the "Information about us and our securities services" published by your bank.

Subject to misprints and errors.



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.