Overview

While 2016 only saw a modest increase in deal activity, the value of Russian M&A leapt by 46% to USD75.8 billion. Much of this increase was driven by three deals in the oil and gas sector: the sale of a 19.5% stake in Rosneft, the headline deal of the year, the acquisition of significant minority stakes in India’s Essar Oil, and the privatisation of Bashneft. In general, investors started to understand and adjust to the changing outlook for the economy during 2016, and while not expecting a repeat of the previous boom conditions, are becoming more confident that Russia can deliver above average returns over the medium to long-term.

46% up to USD 75.8 billion

3 main deals:
– Rosneft
– India’s Essar Oil
– Bashneft
The outlook for 2017

The number of transactions and the aggregate value of deals will continue to grow and show a strong gain over 2017.

This is because the economy is now moving out of recessionary conditions and the government’s strategy for creating new longer term growth conditions, across a broader number of sectors, is becoming clearer and more credible. While geopolitical concerns are easing, the government does not expect any major change in sanctions during 2017, and will continue to look east for major investments.

And although there is clearly more pragmatism in relations with western nations, it appears that some investors from the region may still be waiting for sanctions relief before making the decision to come to Russia.
We expect to see more deals across a wider range of sectors in 2017, and spread through more regions of the country.

In the past the major M&A deals have been heavily concentrated in energy and extractive industries, and while we expect to see this continue in the future, we also see activity stepping up in sectors linked to the government’s localisation strategy. These include agriculture, food processing and manufacturing. Banking and Insurance are key sectors of the economy which are emerging from recessionary conditions and, with support and pressure from the Central Bank of Russia (CBR), should be more open for changes and restructuring, including foreign investment.

There should also be more interest and activity in sectors associated with the expanding economy and the return to growth of personal and household spending. E-Commerce is one of the fastest growing areas of the economy and is expected to continue to attract investor interest this year. Logistics, warehousing and transport services are an integral part of e-commerce and also a critical to the government’s localisation strategy. Investment activity is also starting to pick up in these areas to support their further development.

The government’s geopolitical diversification policy is also starting to result in higher investment inflows, particularly from Middle Eastern and Asian countries which accounted for over 80% of the USD21.2 billion of inbound M&A announced in 2016. While the involvement of Qatar’s sovereign wealth fund in the Rosneft deal was a clear driver of this, investment from India more than tripled to USD4.3 billion. China has long been expected to be a bigger and more prominent investor in Russia, and while expectations remain high in 2017, these may be tempered by regulations imposed by the State Council to control outbound investments which have seen a sharp fall in Chinese foreign direct investment (FDI) since October 2016. The expansion of China’s ambitious One Belt, One Road programme, much of which transits across Russia, may provide incentives for Chinese investors to look at opportunities in Russia, although so far, many projects have focused on other countries.
2016 marked the first time since our annual review started in 2005, that no Russian acquisitions were announced by US strategic investors, symptomatic of the geopolitical and sanctions concerns of this investor group. And while the proportion of total inbound M&A originating from Europe (67%) remained healthy, the aggregate value of such deals fell to USD1.4 billion (7% of total inbound M&A – well below the long-term average), as the average deal size fell by almost two-thirds to USD64 million, reflecting the cautious nature of investors from the region.

Meanwhile, Russian outbound M&A tripled in value to USD15.3 billion on the back of the Essar Oil deal, which saw Rosneft acquire a 49% stake in the integrated oil and gas company for USD6.3 billion, and United Capital Partners acquire an effective stake of 24.01% worth USD3.1 billion via its interest in a consortium with the international commodity trading firm Trafigura. Elsewhere, Rosneft consolidated its interest in Egypt’s Zohr oil field by acquiring a further 30% stake from Italy’s Eni for USD1.1 billion.

Despite the perceptible increase in optimism in the Russian economy, concerns over geopolitics and sanctions remain a reality. Despite the perceptible increase in optimism in the Russian economy, which, for example, resulted in the RDX Index of Russian foreign listed depository receipts rising by more than 52% in 2016, concerns over geopolitics and sanctions remain a reality which potential investors take into account and add a greater sense of caution to than economic expectations might otherwise warrant. But, as the backdrop remains stable, as is expected, and the economy drifts back to growth in the coming year, and the Administration focuses more on economic priorities for the next Presidential term, the trend in M&A activity is expected to continue growing.

1 Kraft Heinz acquisition of the Ivanovsky Baby Food Production Plant in August 2015, was the last deal announced by a US strategic investor. However, US financial investors, including hedge funds acquired 36% of the 5.2% stake in Moscow Exchange MICEX-RTS, sold by China Investment Corp in February 2016.

2 On 15 October 2016, Trafigura (49%), United Capital Partners Advisory (49%) and Essar (2%) formed a consortium SPV that purchased a 49% stake in Essar Oil Limited for USD6.3 billion.
At the headline level GDP is expected to have contracted by 0.2%, compared to –2.8% in 2015. Below that was a significant divergence between the consumer and construction sectors and those areas of the economy which benefited from the weak ruble and import substitution. In the former category retail sales declined by over 5% last year as consumers continued to be squeezed in real terms and confidence indicators showed widely held concern about the future. Agriculture was one of the best performing sectors, posting a year-on-year increase of 4.8%. The agriculture sector specifically benefited from the lack of imported competition, the weak ruble and the fact that it has been identified as a high priority by the government. It is also a sector that remains in the M&A spotlight of many foreign players.
Although the budget deficit was larger at 3.5% of GDP, it was covered by transfers from the Reserve Fund and with little need to resort to debt financing. Russia’s sovereign external debt to GDP was only 4%, one of the lowest ratios in the world, while total external debt to GDP was an equally comfortable 35%. The cost of debt servicing fell to USD27 billion, from USD60 billion in 2015, and capital outflow totalled only USD15 billion, or one-tenth of the 2014 figure.

The ruble exchange rate was also much less volatile in 2016 than was the case in previous years, which has also contributed to the improving perception of investment in Russia. Partly this was as a result of the rise in the average oil price over 2016. But the stability was also achieved because of effective CBR policy statements and monetary actions.

Improving business confidence has been supported by the actions of the CBR, particularly in reforming the banking and insurance sectors, and success of the Ministry of Finance in managing public finances through the recession. Investors were also greatly encouraged by the evidence that the government is now very focused on creating and improving conditions to boost investment and to create greater sustainable diversification across the economy. The emphasis on creating geopolitical diversification and efforts to ensure no further escalation of the conflict with Ukraine during 2016, also helped improve the attitude towards Russia risk amongst some investors, thereby fostering a greater willingness to look at investment opportunities as the year ended.

“The main message concerning the economy is that it was pulling out of recession in 2016, with some sectors recovering faster than others, and that overall the position was a lot calmer.”

One of the benefits of that effective strategy was to bring headline inflation down to 5.4% at the end of last year, a record for modern day Russia.
2017 Outlook

2017 looks to be a more promising year for investment activity and deal volumes.

The Russian government does not expect any substantive changes in the important sectoral sanctions in 2017, a position supported by analysts and evidenced by the EU’s recent decision to extend restrictive measures until September. It is more likely that the subject will be more closely scrutinized in late 2018. Clearly what happens in eastern Ukraine will have a major impact on sanctions but most analysts expect to see a fresh catalyst for talks only after the EU elections.

But the prospect of sanctions for longer is not expected to delay the recovery in FDI or in M&A deals, with US strategic investors the possible exception.

In general, investors will be encouraged by the fact that the economy avoided the steep decline that many had expected as a result of the sanctions & oil price collapse.

The economy adjusted relatively quickly and calmly to the new situation and is now drifting back to growth in 2017. Also, fears that Russia would run out of money proved unfounded and the country’s balance sheet and its ability to finance the budget expenditures have also greatly improved.

Over the last three years the government has increasingly shifted its main focus from geopolitics to reforming the budget amid deteriorating economic performance, and in doing so, creating conditions to attract more investment spending, together with measures that will lead to greater economic diversification and a higher level of sustainable long-term growth.

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4 UK 35%, US 25%, Europe 20%, Russia 10%, others 10% (http://www.interfax.com/newsinf.asp?id=733249)
The key strategy for boosting growth in the future is the so-called localisation plan that aims to attract more investment into manufacturing and services in Russia to both supply the local market, thus permanently reducing imports, and also to create new sources of exports. The government has already achieved notable success in this effort and prospects for more and bigger deals look promising. Key sectors identified by both foreign and domestic investors, include agriculture, food processing, pharmaceuticals, automotive components manufacturers, general manufacturing and services. The government is expected to reveal measures to improve the attractiveness of such sectors in the coming years and to boost the volume of investment flowing into them.

The key message is that Russia is slowly moving away from being a hydrocarbon based economy and is planning a future based on diversification and prudent economic management.

The key to success for the localisation plan is that Russia maintains competitive economic conditions, principally a competitive ruble exchange rate.

The government has made clear that, and the evidence from 2016 supports this, it intends taking whatever action is required to prevent the exchange rate from rising much beyond sixty rubles against the US dollar. This is a strategy which has also been publicly endorsed by the President.

In January the Finance Ministry announced that it would start to divert surplus oil revenues, i.e. those earned in excess of the assumed USD40 p/bbl oil price used in the three year budget, into rebuilding the Reserve Fund. The effect of this action will be to keep downward pressure on the ruble exchange rate.

Possibly because of the legacy of the last three years of economic turmoil, the government has stated that it intends maintaining tight fiscal discipline, e.g. no increase in budget spending as a result of higher than expected oil revenues, and initiating wide-ranging economic and budget reforms at the start of the next presidential term in 2018. Today the reform plan is being debated and refined with the intention of creating economic conditions which will mean less of the volatility seen over the past fifteen years and replaced with steady and sustainable growth.

While privatisations have failed to meet government targets in recent years, the budget raised in excess of USD17 billion through the sale of stakes in various state owned enterprises during 2016, including Rosneft, Bashneft and Alrosa. In February 2017, the government announced its privatisation plan for 2017-2019, and although some entities have previously been earmarked for sale, the economy ministry is determined to push ahead with the sale of stakes in VTB bank, shipping company Sovcomflot and Novorossiysk Commercial Sea Port by 2019.

While this transition will clearly take time, investors are already starting to respond to that change in emphasis and will increasingly do so as more evidence of that change emerges over the coming years. Interest from foreign investors has been steadily increasing in recent months, and while we expect to see this continue, there is a risk that some deals may not be completed until after the 2018 presidential elections when the direction of fiscal policy for the next Administration is known.
Which sectors are of most interest?

Historically Russian M&A has been focused on hydrocarbons and the extractive industries, and it is these sectors which have seen the biggest deals in the past. There will continue to be big deals in these sectors but as the government rolls out its reform plans there will be greater incentive and opportunity for deals across the broader economy. One can look at the areas of potential opportunities across the three key categories which are expected to see the greater volume of investor activity in the coming years.

- Oil and Gas
- Banking and insurance
- Agriculture
Oil and Gas

Russia is the world’s largest exporter of oil and gas, and has demonstrated steady production growth.

Annual oil output is now above 11 mbpd*, while gas production increased to 650 bcm**, in 2016 notwithstanding Russian exports to Europe coming under increasing pricing pressure from competitors.

The oil and gas sector has been heavily dominated by internal restructurings in the past and there are more to come. It is expected that further consolidation will take place as the industry looks to become more efficient and globally competitive. Russian majors are expected to sell further equity stakes in domestic upstream assets, with interest likely to continue to come from Asian and Middle Eastern players that are outside the influence of sanctions against Russia. However, some US and European international oil companies (IOCs) are starting to refocus attention towards Russia in anticipation that sanctions may be reconsidered during 2018. BP’s continued expansion of its upstream interests in Russia, via its acquisition of a 49% stake in Yermak Neftegaz for USD300 million in 2016, in the era of international sanctions has not gone unnoticed.

* million barrels per day
** billion cubic metres

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Russia is of interest for IOCs and national oil companies (NOCs) due to its relatively low (on a global basis) technical risks, CAPEX and OPEX costs, and price of assets.

As a consequence of the drastic cuts in exploration spending triggered by the fall in oil prices from mid-2014, 2016 was the worst year for exploration discoveries that the industry had experienced in the last 70 years.

The renewed interest in Russian upstream assets stems from the opportunities to quickly replace reserves and production through acquisitions or partnerships.

Meanwhile, Russian companies continue to look for acquisition and expansion opportunities internationally, especially across North Africa, the Middle East, and including Iran, where Rosneft, Gazprom Neft and LUKOIL have shown interest. These regions offer Russian companies even lower CAPEX and OPEX than experienced domestically, material reserves and production, acceptable political relationships and manageable security risks. Russian companies are focusing on such regions to help diversify portfolio risk and establish medium to long-term growth opportunities.

The oil field services (OFS) industry is seeing increasing demand for services and equipment companies to substitute those impacted by sanctions. Russian OFS players, similar to those globally, continue to suffer from lower volumes and pricing, which could potentially lead to joint ventures with foreign strategic players or see them sell minority equity stakes to improve debt positions and finance future development or acquisition of more competitive specialised service providers.

Asian investors have been very active in Russian oil and gas projects in recent years, such as the Yamal LNG project, with future investments likely as the Presidents of Russia and China continue to affirm their support for further cooperation. In addition to the interest expressed by Pertamina, Petrovietnam may consider further expansion in Russia through its existing partnership with Zarubezhneft, while PETRONAS can be expected to remain interested in opportunities that play to its corporate strategy and core strengths. Qatar Investment Authority’s acquisition of a minority stake in Rosneft opens up the possibility of future joint investments between the two companies, and perhaps even broader Middle East interest in the Russian oil and gas sector. Finally, India has made clear its intention to investment into Russia, having established substantial positions in both the West and East Siberian oil fields operated by Rosneft.
Banking and insurance

While reforms imposed by the Central Bank of Russia (CBR) to increase capital requirements and withdraw licences have significantly improved the health and perception of the sector, this has yet to translate into increased M&A activity.

The aggregate value of transactions almost halved in 2016 to USD 1.1 bn, on fewer deals than the prior year.

Although generally an issue across the market, we continue to see sizeable price expectation gaps between buyers and sellers in the banking and insurance sector – buyers are typically seeking a substantial discount to net asset value to compensate for legacy risks, while sellers push hard to maximise the price, with some prepared to sit-it-out in the expectation of valuations improving as the economy and exchange rate continue to recover.

During 2016, the CBR realised the transfer of several banks via the Deposit Insurance Agency (DIA) which was tasked with rehabilitating financial institutions placed into administration. These included the transfer of Bank Sovetsky to Russian investment and commercial bank, Tatfondbank, and CB Poidem to Sovcombank, which focuses on retail and corporate banking. Such transfers are specifically excluded from our database as they result from the regulatory activities of the CBR, rather than the strategic objectives of free market participants. Furthermore, changes in Russian legislation expected to be implemented in 2017 will remove the need for banks placed under administration to be transferred in this way.

Banking and insurance deal value and volume, 2010–2016


Deal value, USDbn Number of deals

3.3 9.6 14.9 5.5 3.8 2.1 1.1

Source: KPMG analysis
Banking and insurance

Several factors were at play in the insurance sector. Driven by further consolidation, Otkritie Life was acquired by Rosgosstrakh Life for USD21.5 million, which itself was subsequently acquired by Redvans, the insurance holding company owned by Alkhas Sanguliya, for USD161 million, due to capital constraints. BIN Group and VSK consolidated their insurance businesses (estimated deal value available only for BIN Group’s acquisition of share in VSK Insurance house – USD102 million), and several supplementary acquisitions such as VTB Insurance acquiring the medical insurer Rosno-MS from Allianz, and Sogaz Insurance Group’s acquisition of a 75% stake in Zhaso Insurance.

Although inbound M&A into the sector remains depressed, the acquisition of a 5.2% stake in Moscow Exchange MICEX-RTS by UK, US and European investors, almost half of which were hedge funds, for USD135 million, was the largest inbound acquisition since 2014. With foreign strategic investors still absent from the sector, this transaction at least implies that financial investors have confidence in the prospects of broader Russian financial services sector. As in other sectors, we continued to see interest from foreign investors considering entry into the market, and should this finally translate in 2017 into the first sizeable acquisition by a foreign strategic investor for many years, it could provide an important catalyst for further deals of this type in Russia going forward.

The need to create new sales channels and revenue streams has been behind the trend of the largest private banks such as BIN Group, Moscow Credit Bank (MKB) and Promsvyaz to create financial supermarkets. As part of this trend a number of banks have embarked on a strategy of expanding into investment banking and brokerage operations. For example, MKB acquired Savings and Loan Services (SKS) Bank from Igor Kim specifically to build its platform brokerage operations. We expect to see further acquisitions of non-banking financial intermediaries, brokerage and asset management companies during 2017.

Following the merger of Orient Express Bank and Uniastrum Bank earlier this year, and several acquisitions by Sovcombank during 2016, it will be interesting to see whether these, and other players, seek to participate further in the consolidation of the Russian banking sector during the remainder of 2017.

While there were only a handful of Russian M&A deals in the much talked about Fintech and InsurTech sectors during 2016, we expect this to continue to be a growing trend into 2017 and beyond.

Banks will look for further opportunities to acquire payment processing companies, payday lenders and other digital finance businesses, while insurers will explore opportunities to deliver improved customer experience, increase the efficiency of claims handling, and reduce customer churn.

Overall, we believe that the fundamentals remain strong for Russian M&A in the banking and insurance sector during 2017 and beyond.

In domestic banking, M&A will be driven by the requirement for additional capital, the need to develop revenue streams from new business segments and to deliver further cost optimisation through increased economies of scale. The ongoing geopolitical situation will continue to see state owned Russian banks being encouraged to exit the Ukrainian market. And we expect to see continued consolidation of the insurance sector driven by horizontal integration with banks to realise synergies, increased competition amongst the larger players and further tightening of regulation by the CBR.

The largest deal involving a Russian bank during 2016 was the acquisition of Ukrsotsbank, from the Italian banking group, UniCredit, by Alfa Group for USD323 million, enabling the Russian holding to create a leading player in Ukraine’s retail and corporate banking market. Other outbound deals included the acquisition of Royal Bank of Scotland in Kazakhstan and Marfin Bank in Serbia by Igor Kim, the owner of Expobank.

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Agriculture

Russia’s drive to increase self-sufficiency, the ban on western food imports and localisation strategy, have provided a welcome boost to the country’s agriculture sector.

A combination of high yields and competitive production costs helped Russia to become the world’s leading exporter of wheat for the first time in 2016.

The growth potential of the sector saw the number of deals increase by almost \( \frac{2}{3} \) as domestic and foreign investors announced USD1.5bn of Russian M&A in 2016, continuing the previous year’s growth trend.

The fishing segment saw the largest deal in the agriculture sector during 2016, as Vitaly Orlov took control of Norebo Holding, through the acquisition of a 33% stake from his business partner Magnus Roth. Elsewhere in the segment, Gleb Frank exited his stake in the fish farming and distribution company, Russian Aquaculture, which in turn sold its distribution business, Russian Fish Company, to a group of local investors.

In April 2016, RusAgro Group, the vertically integrated agriculture holding, returned to the capital markets via a secondary public offering (SPO) on the Moscow Exchange that raised USD250 million to fund existing investment projects, modernise production facilities and potential acquisitions. In addition to stakes purchased by the group’s controlling shareholder and CEO, investors from the US and Europe were also reported to have participated in the offering.
While some regions enjoyed modest increases in the market value of land during 2016, there was no notable overall trend for the price of agricultural assets. AFK Sistema announced several deals during the year that will see it acquire 100,000 hectares of agricultural land, increasing its total land bank to around 235,000 hectares, in addition to its acquisition of the vegetable producer Agrokombinat Yuzhny and the Progress cattle breeding plant. M&A generally proved to be more attractive in 2016 than compared to green-field projects in the agriculture sector, given the background of investor concerns regarding the stability of future state subsidies to the sector. In this regard, many companies delivering projects with marginally low profitability have already, or will suffer from greater risks of delays in receiving government funding, and as a consequence, lower returns on investment. Although Asian investors were absent from M&A in the sector during 2016, Abu Dhabi’s Mubadala Development Co, together with the Russian Direct Investment Fund, announced two deals. In June, they agreed to acquire an undisclosed stake in the rice and packaged cereals producer AFG National for USD137 million, followed in November by plans to co-invest USD158 million for significant but not controlling stakes in vegetable oil and fat producer, EFKO Group. The only other inbound deal in the sector saw Norway’s central bank acquire an additional 1.14% stake in Cherkizovo Group. It remains to be seen whether some of the largest Russian agricultural holdings may yet become potential targets of such investors given comparatively low asset valuations in US dollar terms, and potential to earn high margins, particularly from crops. It is likely that we will continue to see more acquisitions of smaller farm holdings (i.e. those with land banks of 10-20 thousand hectares) by larger agricultural holdings seeking to expand production. We also anticipate seeing a number of stressed and distressed agricultural businesses come to the market, potentially at more attractive valuations. Falling pork and poultry prices, compounded by rising feed and veterinary costs, have put smaller producers at an increasing commercial disadvantage to their larger, and vertically integrated competitors. This could lead to consolidation of good quality but financially distressed assets in 2017. RusAgro announced in November 2016 that it would construct three pig breeding complexes in the Tambov region, and recently indicated investment could be USD210 million with annual production capacity of 85 thousand tonnes of live weight, perhaps indicating that it, at least, sees this as a temporary market situation.

Looking ahead, we expect to see an increase in M&A by foreign investors in 2017, and particularly those from Asia and the Middle East, building on the general trend seen over the last few years.

Although three greenhouse farming deals were announced in 2016 we do not anticipate any significant activity in the segment this year.

Provided there continues to be timely state support in the form of subsidies, the segment is expected to continue growing as new green-field projects come into use. However, in November 2016 RusAgro decided to cease its greenhouse project announced earlier that year, due to its high sensitivity to government support, which RusAgro expected to be insufficient in coming years to guarantee a reasonable pay-back period. With the ban on EU dairy products extended until the end of 2017, Russia’s milk production segment could continue to attract investors. During 2016, Vietnam’s TH Group started work on the first phase of its USD2.7 billion multi-year project to develop modern dairy complexes in the Moscow region, and Russian Direct Investment Fund, together with Charoen Pokphand Group (Thailand), and Banner Infant Dairy Products Company (China), signed an agreement to construct a USD1 billion dairy complex in the nearby Ryazan region. And while long payback periods appear to deter the majority of Russian investors, we may see foreign investors entering the market through M&A and additional green field projects in 2017.

Methodology

KPMG Russian M&A database
This report is based on the KPMG Russian M&A database which includes transactions where either the target (inbound) or acquirer (outbound) or both (domestic) are Russian. All data is based on transactions completed between 1st January and 31st December 2016, or announced during this period but pending at 31st December 2016. Historical data may differ from earlier versions of this report as the KPMG Russian M&A database is updated retrospectively for lapsed deals and information subsequently made public.

Data includes transactions valued in excess of USD5 million, as well as transactions with undisclosed deal values where the target’s turnover exceeds USD 10 million. Deal values are based on company press releases as well as market estimates disclosed in the public domain.

The KPMG Russian M&A database has been complied over a number of years based on information included in the Mergemarket M&A deals database and EMIS DealWatch database, together with KPMG desktop research of other sources.

Allocation of deals to industry sectors may involve using our judgment and is therefore subjective. We have not extensively verified all data within the KPMG Russian M&A database, and cannot be held responsible for its accuracy or completeness. Analysis of different databases and information sources may yield deviating results from those presented in this report.

Macro trends and medium term forecasts
Information presented in this report on macro trends and medium term forecasts are based on data from Macro-Advisory Ltd., an independent macroeconomic and political strategy firm specialising in the Eurasia region, including Russia and the CIS.

Appetite and capacity for M&A
Our analysis of forward-looking appetite and capacity for Russian M&A is based on the principles of KPMG’s M&A Predictor, a tool which tracks important indicators 12 months forward. The rise or fall of forward P/E (price/earnings) ratios offers a good guide to the overall market confidence, while net debt to EBITDA (earnings before interest, tax, depreciation and amortisation) ratios helps gauge the capacity of companies to fund future deals.

Our analysis is based on 42 Russian companies for 2016, all the raw data within the Russian M&A review was sourced from S&P Capital IQ as at April 2017. The financial services and property sectors are excluded from our analysis, as net debt/EBITDA ratios are not concerned relevant in these industries. Where possible, earnings and EBITDA data is on a pre-exceptional basis.
Appendices

1. Macro trends and medium term forecasts
2. Appetite and capacity for M&A
3. Cross-border M&A highlights
4. Sector highlights
# Macro trends and medium term forecasts

## Appendix 1

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<td>63,800</td>
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<td>–10.0%</td>
<td>–1.0%</td>
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<td>1.2%</td>
<td>3.5%</td>
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<td>3.0%</td>
<td>4.0%</td>
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<td>Real disposable income, % YoY</td>
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<td>4.8%</td>
<td>–1.0%</td>
<td>–6.5%</td>
<td>–5.9%</td>
<td>1.0%</td>
<td>2.0%</td>
<td>3.0%</td>
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<td>5.3%</td>
<td>5.6%</td>
<td>5.3%</td>
<td>5.5%</td>
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</tr>
<tr>
<td>Budget, balance % of GDP</td>
<td>—</td>
<td>–0.5%</td>
<td>–0.5%</td>
<td>–2.4%</td>
<td>–3.5%</td>
<td>–2.3%</td>
<td>–1.5%</td>
<td>—</td>
</tr>
<tr>
<td>Current account, % GDP</td>
<td>3.7%</td>
<td>1.6%</td>
<td>3.0%</td>
<td>5.3%</td>
<td>1.7%</td>
<td>1.9%</td>
<td>1.9%</td>
<td>2.0%</td>
</tr>
<tr>
<td>RUB/USD, year-end</td>
<td>30.8</td>
<td>32.9</td>
<td>61.4</td>
<td>73.5</td>
<td>61.3</td>
<td>62.0</td>
<td>64.0</td>
<td>66.0</td>
</tr>
<tr>
<td>RUB/USD, average</td>
<td>31.1</td>
<td>31.9</td>
<td>38.6</td>
<td>62.0</td>
<td>67.0</td>
<td>59.0</td>
<td>63.0</td>
<td>64.0</td>
</tr>
<tr>
<td>Urals, USDp/bbl, average</td>
<td>110</td>
<td>108</td>
<td>100</td>
<td>54</td>
<td>45</td>
<td>54</td>
<td>65</td>
<td>75</td>
</tr>
</tbody>
</table>

Source: State Statistics Agency, Central Bank, Macro-Advisory estimates
Appetite and capacity for M&A

The capacity of Russia’s largest listed companies for M&A improved significantly during 2016, and while appetite for deals also continued to grow, the rate of growth was slightly below 2015.

Market capitalisations substantially improved after several years of decline, demonstrating a 51% increase compared to the previous year.

Forward P/E ratios, a measure of appetite, increased by an average of 35%, continuing the positive trend observed in the previous year.

Net debt to EBITDA, a measure of capacity, is forecast to improve by an average of 21% by the end of 2017, returning to 2013 levels, with only Transport and Infrastructure demonstrating a negative outlook.
Appendix 3

Inbound M&A deal volume by region (2016 vs. 2015)

- Europe: 25% (2016) vs. 7% (2015)
- North America: 56% (2016) vs. 45% (2015)
- CIS: 8% (2016) vs. 7% (2015)
- Asia-Pacific: 7% (2016) vs. 6% (2015)
- MEA: 26% (2016) vs. 11% (2015)
- Other regions: 6% (2016) vs. 4% (2015)

Source: KPMG analysis

Inbound M&A deal value by region, USDbn (2016 vs. 2015)

- Europe: 5% (2016) vs. 3% (2015)
- North America: 20% (2016) vs. 17% (2015)
- CIS: 4% (2016) vs. 27% (2015)
- MEA: 6% (2016) vs. 12% (2015)
- Other regions: 4% (2016) vs. 12% (2015)

Source: KPMG analysis

Outbound deal value by target’s region, USDbn (2016 vs. 2015)

- Europe: 16% (2016) vs. 14% (2015)
- North America: 5% (2016) vs. 9% (2015)
- CIS: 7% (2016) vs. 9% (2015)
- Asia-Pacific: 7% (2016) vs. 12% (2015)
- MEA: 3% (2016) vs. 17% (2015)
- Other regions: 2% (2016) vs. 4% (2015)

Source: KPMG analysis

Outbound deal number by target’s region, (2016 vs. 2015)

- Europe: 15% (2016) vs. 17% (2015)
- North America: 7% (2016) vs. 15% (2015)
- CIS: 21% (2016) vs. 48% (2015)
- Asia-Pacific: 4% (2016) vs. 17% (2015)
- MEA: 4% (2016) vs. 67% (2015)
- Other regions: 8% (2016) vs. 7% (2015)

Source: KPMG analysis
Appendix 4

Sector highlights
Oil and gas

Largest oil and gas sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rosneft Oil Company</td>
<td>A Consortium led by Qatar Investment Authority</td>
<td>Rosneftegaz</td>
<td>19.5%</td>
<td>11,270</td>
</tr>
<tr>
<td>Essar Oil Limited</td>
<td>Rosneft Oil Company</td>
<td>Essar Group</td>
<td>49.0%</td>
<td>6,328</td>
</tr>
<tr>
<td>Bashneft ANK</td>
<td>Rosneft Oil Company</td>
<td>The Federal Agency for State Property Management</td>
<td>50.1%</td>
<td>5,299</td>
</tr>
<tr>
<td>Bashneft ANK</td>
<td>Rosneft Oil Company</td>
<td>Minority Shareholders</td>
<td>31.2%</td>
<td>3,112</td>
</tr>
<tr>
<td>Essar Oil Limited</td>
<td>United Capital Partners Advisory</td>
<td>Essar Group</td>
<td>24.0%</td>
<td>3,101</td>
</tr>
</tbody>
</table>

Metals and mining

Largest metals and mining sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Polyus Gold</td>
<td>Polyus Gold</td>
<td>Polyus Gold International; Minority Shareholders</td>
<td>31.8%</td>
<td>3,735</td>
</tr>
<tr>
<td>Arkhangelsk-geoldobycha</td>
<td>Otkritie Holding</td>
<td>Lukoil</td>
<td>100.0%</td>
<td>1,450</td>
</tr>
<tr>
<td>Alrosa Co</td>
<td>Russian Direct Investment Fund (RDIF); Institutional and private investors</td>
<td>Government of the Russian Federation</td>
<td>10.9%</td>
<td>813</td>
</tr>
<tr>
<td>Elgaugol, Elga-Óroga, Mecheltrans-East</td>
<td>Gazprombank</td>
<td>Mechel</td>
<td>49.0%</td>
<td>536</td>
</tr>
<tr>
<td>Polymetal International</td>
<td>ICT Group (2.98%), not disclosed (3.1%)</td>
<td>Jiri Smejc; PPF Group NV</td>
<td>6.1%</td>
<td>326</td>
</tr>
</tbody>
</table>
## Real estate and construction

### Largest real estate and construction sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Morton Group</td>
<td>PIK Group</td>
<td>Alexander Ruchyov</td>
<td>100.0%</td>
<td>2,235</td>
</tr>
<tr>
<td>Lafarge-Holcim Ltd</td>
<td>Sberbank</td>
<td>Eurocement Holding AG</td>
<td>6.1%</td>
<td>1,530</td>
</tr>
<tr>
<td>Eurasia Tower</td>
<td>VTB Bank</td>
<td>Suleiman Kerimov</td>
<td>99.6%</td>
<td>713</td>
</tr>
<tr>
<td>Evolution Tower</td>
<td>Transneft</td>
<td>Snegiri Development</td>
<td>100.0%</td>
<td>350</td>
</tr>
<tr>
<td>President Plaza</td>
<td>Sberbank</td>
<td>Ruslan Baisarov</td>
<td>100.0%</td>
<td>303</td>
</tr>
</tbody>
</table>

### Market share
- Total value: USD 8.3bn
- Domestic: +28.5%
- Inbound: +9.8%
- Outbound: +94.0%
- Volume: USD 102 deals
- Market share: 11.0%

## Consumer markets

### Largest consumer markets sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>M.Video</td>
<td>Safmar Financial &amp; Investment Group</td>
<td>Alexander Tynkovan; Mikhail Tynkovan; Pavel Breev</td>
<td>57.7%</td>
<td>1,206</td>
</tr>
<tr>
<td>Eldorado</td>
<td>Safmar Financial &amp; Investment Group</td>
<td>PPF Group N.V.; Emma Capital</td>
<td>100.0%</td>
<td>347</td>
</tr>
<tr>
<td>Arc International SA</td>
<td>A consortium led by Russian Direct Investment Fund and CDC International Capital</td>
<td>Not disclosed</td>
<td>n/d</td>
<td>281</td>
</tr>
<tr>
<td>Pharmacy Chain 36.6</td>
<td>Existing shareholders; Rossium; Baring Vostok Capital Partners; Undisclosed</td>
<td>Not disclosed</td>
<td>58.1%</td>
<td>250</td>
</tr>
<tr>
<td>Danone Russia</td>
<td>Danone SA</td>
<td>Unimilk</td>
<td>40.0%</td>
<td>250</td>
</tr>
</tbody>
</table>

### Market share
- Total value: USD 3.5bn
- Domestic: +199.1%
- Inbound: +122.4%
- Outbound: +36%
- Volume: USD 36 deals
- Market share: 4.7%
### Largest communications and media sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Sistema Shyam TeleServices Limited</td>
<td>AFK Sistema</td>
<td>Government of the Russian Federation</td>
<td>17.1%</td>
<td>777</td>
</tr>
<tr>
<td>2 VimpelCom Ltd</td>
<td>Undisclosed private and institutional investors</td>
<td>Telenor Group</td>
<td>9.3%</td>
<td>574</td>
</tr>
<tr>
<td>3 National Media Group</td>
<td>Gazprom-Media</td>
<td>Not disclosed</td>
<td>7.5%</td>
<td>163</td>
</tr>
<tr>
<td>4 Mobile TeleSystems</td>
<td>Not disclosed</td>
<td>Sistema JSFC</td>
<td>1.5%</td>
<td>124</td>
</tr>
<tr>
<td>5 European Media Group</td>
<td>Andrei Bokarev; Andrei Kozitsyn; Igor Kudryashkin</td>
<td>Not disclosed</td>
<td>75.0%</td>
<td>112</td>
</tr>
</tbody>
</table>
## Largest transport and infrastructure sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Wagon Company</td>
<td>Not disclosed</td>
<td>ICT Group</td>
<td>24.9%</td>
<td>334</td>
</tr>
<tr>
<td>Vozdushnye Vorota Severnoi Stolitys (VVSS)</td>
<td>Qatar Investment Authority</td>
<td>Fraport AG</td>
<td>25.0%</td>
<td>266</td>
</tr>
<tr>
<td>Primorsk International Shipping</td>
<td>SCF Tankers Ltd.</td>
<td>Not disclosed</td>
<td>n/d</td>
<td>215</td>
</tr>
<tr>
<td>Murmansk Commercial Seaport</td>
<td>Siberian Coal Energy Co (SUEK)</td>
<td>EuroChem</td>
<td>36.2%</td>
<td>143</td>
</tr>
<tr>
<td>Khrabrovo Airport; Mineralnye Vody International Airport</td>
<td>Novaport</td>
<td>Government of Stavropol Krai; Aeroinvest</td>
<td>100.0%</td>
<td>118</td>
</tr>
</tbody>
</table>

### Total value

- **USD**: 1.9bn
- **Volume**: 39 deals
- **Market share**: 2.5%

### Changes

- **Domestic**
  - Total value: -84.5%
  - Volume: -7.9%
- **Inbound**
  - Volume: +124.0%
  - Value: -15.2%

#### Transport and infrastructure market share

- **Domestic**: 2.5%
- **Inbound**: —

## Largest power and utilities sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Irkutskenergo</td>
<td>EuroSibEnergo Plc</td>
<td>INTER RAO UES</td>
<td>40.3%</td>
<td>1,062</td>
</tr>
<tr>
<td>Inter RAO UES</td>
<td>Alor Group; Blagosostoyanie</td>
<td>United Capital Partners</td>
<td>8.7%</td>
<td>494</td>
</tr>
<tr>
<td>Leningrad Regional Managing Electric Grid Company (37.55% stake); USK (50% stake)</td>
<td>Vadim Serdyukov</td>
<td>Not disclosed</td>
<td>37.55%; 50.0%</td>
<td>64</td>
</tr>
<tr>
<td>Power Retail Company of Bashkortostan</td>
<td>INTER RAO UES</td>
<td>RusHydro OAO</td>
<td>100.0%</td>
<td>64</td>
</tr>
<tr>
<td>Krasnoyarskaya GES</td>
<td>EuroSibEnergo</td>
<td>Not disclosed</td>
<td>10.0%</td>
<td>49</td>
</tr>
</tbody>
</table>

### Total value

- **USD**: 1.8bn
- **Volume**: 13 deals
- **Market share**: 2.4%

### Changes

- **Domestic**
  - Total value: +144.8%
  - Volume: +143.9%
- **Inbound**
  - Volume: —
  - Value: -133.3%
### Innovations and technology

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mail.ru Group Limited</td>
<td>MegaFon</td>
<td>USM Holdings Limited</td>
<td>15.2%</td>
<td>740</td>
</tr>
<tr>
<td>Uber Technologies Inc</td>
<td>LetterOne Group</td>
<td>Not disclosed</td>
<td>n/d</td>
<td>200</td>
</tr>
<tr>
<td>Mikron</td>
<td>RusNano</td>
<td>Mikron</td>
<td>8.4%</td>
<td>171</td>
</tr>
<tr>
<td>A consortium led by Elbrus Capital</td>
<td>Mail.ru Group Limited</td>
<td>Not disclosed</td>
<td>100.0%</td>
<td>131</td>
</tr>
<tr>
<td>Luxoft</td>
<td>Not disclosed</td>
<td>IBS Group</td>
<td>4.0%</td>
<td>89</td>
</tr>
</tbody>
</table>

**Domestic**
- Total value: USD1.7bn (+90.4%)
- Volume: 48 deals (+29.7%)

**Inbound**
- Total value: USD0.01bn (-55.6%)
- Volume: 48 deals (-60.4%)

**Outbound**
- Total value: USD0.3bn (+64.0%)
- Volume: 48 deals (+29.7%)

**Market share**
- 2.3%

### Agriculture

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>Norebo Holding</td>
<td>Vitaly Orlov</td>
<td>Magnus Roth</td>
<td>33.0%</td>
<td>330</td>
</tr>
<tr>
<td>RusAgro Group</td>
<td>Vadim Moshkovich; Maxim Basov; Institutional and private investors</td>
<td>RusAgro Group</td>
<td>12.2%</td>
<td>250</td>
</tr>
<tr>
<td>Efko Group</td>
<td>Mubadala Development Co, Russian Direct Investment Fund (RDIF) and other investors</td>
<td>Not disclosed</td>
<td>n/d</td>
<td>158</td>
</tr>
<tr>
<td>AFG National</td>
<td>Mubadala Development Co, Russian Direct Investment Fund (RDIF) and other investors</td>
<td>Not disclosed</td>
<td>n/d</td>
<td>137</td>
</tr>
<tr>
<td>Eurodon</td>
<td>Vnesheconombank (VEB)</td>
<td>A1 Investment Co</td>
<td>40.0%</td>
<td>89</td>
</tr>
</tbody>
</table>

**Domestic**
- Total value: USD1.5bn (+63.4%)
- Volume: 48 deals (+29.7%)

**Inbound**
- Total value: USD0.3bn (+64.0%)
- Volume: 48 deals (+29.7%)

**Outbound**
- Total value: USD0.3bn (+64.0%)
- Volume: 48 deals (+29.7%)

**Market share**
- 2.0%

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Russian M&A Overview 2016
### Largest banking and insurance sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Ukrsotsbank</td>
<td>Alfa Group Consortium</td>
<td>UniCredit SpA</td>
<td>99.8%</td>
<td>323</td>
</tr>
<tr>
<td>2 Rosgosstrakh-Life</td>
<td>Redvans</td>
<td>Rosgosstrakh</td>
<td>100.0%</td>
<td>161</td>
</tr>
<tr>
<td>3 Moscow Exchange MICEX-RTS</td>
<td>Not disclosed</td>
<td>China Investment Corp</td>
<td>5.2%</td>
<td>135</td>
</tr>
<tr>
<td>4 VSK Insurance House</td>
<td>B&amp;N Bank Joint Stock Company</td>
<td>Not disclosed</td>
<td>49.0%</td>
<td>102</td>
</tr>
<tr>
<td>5 Dalnevostochny Bank</td>
<td>Region Asset Management</td>
<td>Russian Regional Development Bank</td>
<td>70.4%</td>
<td>69</td>
</tr>
</tbody>
</table>

### Largest healthcare and pharmaceuticals sector deals in 2016

<table>
<thead>
<tr>
<th>Target</th>
<th>Acquirer</th>
<th>Vendor</th>
<th>% acquired</th>
<th>Value USDm</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 OTCPharm</td>
<td>Pharmstandard</td>
<td>Not disclosed</td>
<td>3.0%</td>
<td>125</td>
</tr>
<tr>
<td>2 Pharmstandard</td>
<td>Augment Investments</td>
<td>Not disclosed</td>
<td>12.0%</td>
<td>72</td>
</tr>
<tr>
<td>3 Unfinished plant for processing of blood products in Kirov</td>
<td>Kedrion Biopharma</td>
<td>Rostec</td>
<td>JV</td>
<td>61</td>
</tr>
<tr>
<td>4 Biosintez</td>
<td>Sun Pharmaceutical Industries Limited</td>
<td>Not disclosed</td>
<td>85.1%</td>
<td>60</td>
</tr>
<tr>
<td>5 TransMedics, Inc.</td>
<td>Pharmstandard International SA; Fayer-weather Fund</td>
<td>TransMedics, Inc.</td>
<td>n/d</td>
<td>51</td>
</tr>
</tbody>
</table>
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