

Where's the money? The money is there, where it has always been!

EXPERT, OCTOBER 2016

Andrey Yakunin: "Our funds have open limits, and at the moment we are looking for three to four interesting new projects. Our target investment volume remains unchanged at USD 5-15 million, with a preferred share in a company between 25% and 49%."

In his interview with "Expert North-West", Andrey Yakunin, VIYM founder and managing partner, talks about the impact of the economic crisis and the sanctions on the investment potential of Russian business. He also discusses the industries in which his funds operate and addresses the difficulties of running a business when you are related to a politically exposed person.

- Andrey, your company invests in projects and businesses that operate in different sectors in Russia and abroad. Above all, you are interested in development, consumer goods and hotel business. How have these sectors changed over the past two years of crisis and sanctions? Have any changes occurred in the projects in which you invested?

- We are trying to develop two platforms. The first one concerns the hospitality industry and other related aspects of the real estate sector, such as serviced apartments. Likewise, we are developing other options of integrating hotel services with private residential properties.

The second one concerns specialised production, food production and recycling, manufacturing of personal hygiene products, medical services, and so on. Classic examples of our investments in these particular industries are "Syktyvkar Tissue Group" (a producer of sanitary-hygienic goods), "Agro-Alliance" (a leader in Russia's packed-cereal market), which we divested last year, and a chain of medical clinics called "Family Doctor". All of these companies are affected in different ways by changes in macroeconomic indicators.

So, for example, the medical clinic chain "Family Doctor" has changed the investment strategy by slowing down its regional expansion programme and focusing on expanding within Moscow, where the market is still far from saturation, and where people's purchasing power and the activity of insurance companies are much higher. Despite the overall industry recession, in April 2016 the company opened its seventh clinic in Moscow and is now offering more than 50 different medical services. On top of that, the company's client base exceeded the 300 thousand mark by the end of the first half of 2016.

At the same time, we have a reversed situation with regard to "Syktyvkar Tissue Group". The economic recession has led to an increase in the use of paper sanitary-hygienic items across the regions of Russia. In view of that, the company is strengthening its regional market presence by increasing the number of distribution centres, expanding its range of products and ramping-up its production capacity to 85 thousand tonnes per year. This was made possible by our RUB 3 billion investment into the company's production facilities.

As for real estate, our company is no different from others. It is no secret that access to debt financing is key to the implementation of these projects. Given an austere monetary policy (which ultimately leads to a decrease in available project funding) and high interest rates, it becomes rather difficult to carry out new projects. On the other hand, this situation offers scope for mergers and acquisitions, which rarely happened beforehand. Above all, we are now seeing new projects entering the market, led by investors who have previously only built hotels as noncore assets. We believe that, given a certain stagnation in the launch of new projects (by which I mean the projects that were preparing to open), the possibility of market consolidation is an interesting one. It is possible that during this period we might see a

development of key market players, which will take the dominant market positions. This particularly applies to brand hotels.

With regards to the consumer sector, we all know what happened to the economic growth rate and we understand that the devaluation of the rouble has had a direct impact on people's purchasing power. Thus, the situation we are seeing with regards to this sector is not much different from the one that other market players are seeing. We are seeing consumers who are changing their consumption patterns, we are seeing a substitution of premium segments for mid-market and sometimes for lower mid-market. We are also witnessing instances of both deferred demand and deferred purchases.

- What projects would you potentially be interested in in Saint-Petersburg and in the North-West?

- Our target investment volume remains unchanged at USD 5-15 million with a preferred share in a company between 25% and 49%. Assuming that the current EBITDA multiplier is 6.0, the companies with USD 10 million EBITDA are a "sweet spot", and we would be interested in working with them. We sometimes consider "big tickets", and if they are of interest to us we try to make package offers together with some of our industry colleagues.

Our funds have open limits, and at the moment we are looking for three to four interesting new projects. For example, right now we are considering a food production and recycling company. The agricultural sector was of interest to us even before sanctions were imposed (eg. "Agro-Alliance), but now the sector and the companies which operate in it are expanding at a higher rate than before, restrictions on competition were introduced.

Furthermore, we are still very much interested in the construction market. There is one company that is of particular interest to us, as well as to some of our competitors. I would also like to highlight the fact that many Private Equity funds did not fully use their capital in the previous cycle, meaning that companies have an opportunity to attract this capital for their development programmes. As such, we find ourselves in a situation where the market players are fighting amongst themselves for prospective companies. If a company owner understands macroeconomics and knows the multipliers that we work with, then he should be well-placed to take advantage of the extremely favourable conditions for attracting private capital – conditions that were hard to even imagine three to five years ago.

- Strategically, do you remain Russia-oriented or do you also prioritise foreign markets?

- VIY Growth Fund I, one of VIYM's platforms, was established for investing in rapidly growing medium and low capitalisation firms. It has an 80% fund capital mandate for Russia. As for the second platform – our hotel-focused VIY Greater Europe Hospitality Fund – we have a diversified range of geographies, including Western and Eastern Europe as well as Russia.

However, just as our colleagues, we too are experiencing certain fundraising problems during this investment cycle. And given the length of the industry cycle, the best among us will attract new instruments within 18 months. This means that once everyone has used up their funds, the industry's new cycle will not see investment capital until the beginning of 2018.

- The eternal question – where is the money?

-The money is there, where it has always been – the key market players are institutional investors, above all, those from the Gulf and from Asia. But American investors are also interested in international expansion. Given our current macroeconomic climate, the main question is whether we are now in a position to make them an offer that would be more favourable than the offers they can get in developed or other developing countries.

The citizen of Londongrad

Andrey Yakunin – the eldest son of Vladimir Yakunin, RZhD ex-president (2005-2015). Born in 1975, graduated from Economics Faculty of SPSU, holds an MBA degree from London Business School and Columbia University. In 2006, together with the Israeli entrepreneur Yair Ziv, he established a company called Venture Investments & Yield Management (VIYM), which specialises in managing private equity funds that invest in hotel real estate and real sector companies. As of today, VIYM operates two funds – VIY Greater Europe Hospitality Fund and VIY Growth Fund I – with assets totalling EUR 200 million. Andrey Yakunin lives in London and has a dual citizenship – Russian and British.

- From the standpoint of capital procurement, how well or how badly is Russia doing at the moment? How bleak is Russia's foreign investment outlook?

- I think, it's enough to take a look at Russia's stock indices in order to get a rough picture. Listed assets are always a good indicator of what will happen with unquoted investments. If we take a look at the volume and dynamics of indices, we will see that the market for quoted instruments has still not recovered. The funds that combine both short and long equity selling have also not recovered. Thus, until they recover we should not expect capital procurement and recovery in the unquoted investment sector. Otherwise, it would contradict the 25-30-year history of industry development.

- To what extent, would you say, is it justified to speak of a Chinese interest in Russia's real sector? Do you cooperate with Chinese partners? Would you be able to say what their interests are?

- First of all, the fact that we are an active player in the hotel industry means that we have certain interrelations with China. If we consider the hotel industry growth rates even in Saint-Petersburg, we will notice that China is one of the most rapidly growing players in the market, and this trend will persist. Does this mean that China might eventually be interested in this industry? I am sure it does. In fact, this has already happened indirectly, for Rezidor is the largest hotel operator in Russia. In April, the Chinese HNA company acquired the controlling stake of Carlson Rezidor, thus gaining access to Russia's hotel market leader. I cannot think of an example where Chinese managers would neglect the bigger picture and concentrate instead on smaller, local projects. We can characterise what we see in the following way: the Chinese investment machine is very well tuned and follows a certain rule with regards to access to new sectors, whereby priority is always given to intergovernmental agreements – or at least to those that have been made with governmental institutions. This brings together investors from the largest funds and companies, all of which are connected to state funding. Only then is the market opened for private investors who operate in the price segment that we have discussed earlier. One example of this is the recent agreement between the Russian Direct Investment Fund and the Chinese Inventis Investment Holdings, regarding the creation of a joint investment platform in Russia, with the intention of fully realising the increasing investment, technological, trade and economic potential of Sino-Russian partnership.

- Let me ask you a personal question: when did the mass media stop using the phrase "Vladimir Yakunin, RZhD president, and his son Andrey, who deals in affiliated businesses"? Did this in any way impact on your business? Were you personally affected by the pressure of your surname? And what is the situation like today?

- I think this is a very difficult question. To give the easiest answer, I'd say that I have always been a PEP, politically exposed person (in this case, a relative of a politically exposed person) and I remain a PEP until this day. Thus, from the point of view of constant scrutiny by credit and finance watchdogs, nothing has changed for me since my father resigned. Everyone is quite adept at bringing up the word "daddy" in the context of my business – and no-one quite knows how to drop the association. This is an objective factor which I always have to take into account when I do business.

At the same time, because of this factor, we run regulated managing funds in Luxembourg. Neither the EU credit and finance institutions nor the regulators think that this factor should prevent us from working in a professional, regulated community.

Nevertheless, some media outlets still actively refer to this factor in their reports. I, personally, hope that our business will eventually leave a tangible legacy, but I realise that we need time for that.

At the very least, we have “The Lions Palace”, which was virtually crumbling down before we got involved. I am proud that we took part in renovating this architectural masterpiece and I genuinely hope that in some 50 to 70 years’ time somewhere there will be a reminder saying that Andrey Yakunin participated in the restoration of this landmark. Similarly, it will be fair if in 50 to 70 years my father is remembered for his successful contributions to some of the projects that are being carried out at the moment.

- Talking about “Lions Palace”, did you win the lawsuit against certain media outlets which claimed that your investment company had special preferences during the restoration of this landmark? There is also information according to which some high-ranking government officials get special accommodation in this hotel. Can you please clarify this situation?

- People often ask me this question. Before answering it, I would like to say that neither I, nor VIYM, nor any other party that participated in the restoration process, received any compensations from the President Administration. It has always been a commercial project that excluded any participation on the part of the government.

Now, about the project itself. We rented the building – which was in a deplorable state – for a relatively low price (when compared with its current price), because no-one else was ready to invest in the reconstruction of a rented historic building. You have to keep in mind that the reconstruction had to comply with strict regulations and was constantly under scrutiny.

The project required considerable funding from day one, for the reconstruction and restoration of the historical and architectural value of the building are not cheap.

The payments to Four Seasons, the managing company, were already being made even before the actual launch of the hotel, so that the company could prepare the building for its main function – that of a “world class hotel”. On top of that, we had to comply with all the standards (regarding engineering, room and public space equipment etc.) set by Four Seasons. This is a standard Four Seasons policy and it is rather expensive.

Now that the building has been “brought back to life”, we have to pay annual fees for using it. Taking into account its location, the total area of the building and other factors, the total amount is a hefty one. We regularly pay our managing company, Four Seasons, to ensure that the premium standards of one of the world’s best hotels are always maintained. We also have monthly rewards for our personnel and we always pay them, regardless of the market situation and the hotel revenue.

The standard cost recovery period for such hotels is at least 8 years from the launch date. So far we have spent a lot on this project. On top of that, our investments were in dollars, whilst the returns will be made over an extended period of time, in roubles, at an exchange rate that is half of what it was when we started this project.

- Can you please tell us a bit more about your work on other Saint-Petersburg-based projects? What about Nikolskiye Ryady?

- Despite various rumours, I am convinced that we will bring this project to full completion. Neither I, nor my team have any doubts about it. We are looking for gaps in the market. Therefore, we are planning to open a mid-range priced hotel that would have 250 rooms and a youth hostel with 150 rooms. Pre-empting questions from the citizens of Saint-Petersburg, I would like to assure you that we have preserved all of the original arches that could still be salvaged.

The legislative side of this project – as it concerns the regulations around such redevelopments –was not an easy one. While we do not write or choose the laws that regulate the industries in which we operate, we have no other choice but to abide by these laws. It would be rather strange to complain about the lack of private equity investments given the strict legislative measures introduced by regulators, which often make it difficult for projects to be implemented (or indeed sometimes make project implementation pointless).

For us, the benefit of this particular project is the novelty. We are the “trailblazers” of the Russian hotel industry. We brought Four Season and Holiday Inn into Russia, and we are now planning to introduce an international hostel operator to the Russian market.

- Your company had a whole number of development projects, both residential (“Vodoley” in Sestroretsk) and those oriented at the industrial sector. What do you think of these sectors now? Are you interested in investing in industrial parks? Alternatively, the Resort region is building cultural and tourism clusters. Would you be interested in investing into hotel or residential real estate in that region?

- **The** current VIYM strategy is aimed at creating and managing investment portfolios which involve direct investments in hotel real estate in the Greater Europe area, along with investments in the rapidly growing medium and low-capitalisation firms based in Russia and CIS. At the same time, we are always happy to consider new initiatives. As I said, we are one of the few funds that has open limits for three to four projects and we are actively considering various options.

- Let me ask you about your public activities. You are the head of SPSU Alumni Association. What do you need it for?

– The answer is simple – I find it interesting. As soon as the university recognised the necessity of having an organised alumni network we started to look for those who would be interested in helping us. If we analyse the statistics, we will notice that there are at least 50 thousand social media users that are following SPSU events. As of today, we have 20 thousand people participating in this project. They share ideas about how to expand the network. One couldn’t dream about this even a few years ago.

One of significant achievements to date has been this year’s launch of the first grant program. As soon as we launched the program we realised that what the participants valued about it the most was the opportunity for direct communication between the students on the one hand and seasoned experts on the other. As such, the Association decided to launch a mentorship programme together with EY. Among the latest events organised by the Association was the Knowledge Fair, which was held on October 1. We managed to bring together three generations of SPSU alumni.

We also have a number of global tasks. One of them is the careers centre. It is obvious that the University should care about the quality of students’ future careers. It is also important to track their career paths for up to five to ten years after their graduation. This would allow the University to illustrate to prospective students what their potential career trajectory could feasibly look like after a given number of years. Therefore, significant efforts will be put into creating relationships between faculties and potential employers.

The group's second task has to do with tackling the lack of information. This is particularly important for students and graduates with science degrees. Following the latest developments and contributions that our recent graduates make to world of science is not just a matter of curiosity. Many of them become famous scientists. If we manage to make them contribute to the life of the University in any way, either by working as University fellows or by publishing their works via the SPSU press, this would help us to better position our alma-mater in both national and international rankings.

Communications support in the field of scientific cooperation is one of the areas that I am particularly interested in.

Finally, we have a project called "Address book" – it aims to pool contacts and promote cooperation between the 250 thousand SPSU alumni that are scattered all around the world.

- What else do you do when you are not busy with your business?

- Together with a team of like-minded enthusiasts I am trying to promote the Russian direct and venture investments market, both domestically and abroad. I am also focussed on creating a regulatory environment that would attract capital into the country. This is all done under the auspices of the National Alternative Investment Management Association (NAIMA) – a non-for-profit partnership.

We stood at the birth of this association in 2013. As of today, there are 25 participants at NAIMA, among which are leading direct and venture investment funds, consulting companies, governmental development institutes and private entities.

– Some media outlets are not very fond of you and your projects. Why do you think that is the case?

– We should not simplify the reality. First of all, I would like to note that a lot of business-oriented magazines turn to us for commentaries and ask us to explain some of our business-decisions instead of simply copying the unverified information that their colleagues publish. We are always open to a constructive dialogue with journalists who value the facts and who want to hear the story from its primary source.

As for the media industry in general, we have to remember that it follows certain rules and, as a famous entrepreneur once said, "good news doesn't sell". Although all of us (including the government, society and business) are interested in creating a positive image of the reality.

If we all make an effort to form this image, then, perhaps, one day even the most critical media outlet, instead of publishing a regular "horror" story, will publish positive news that will inspire us all towards fruitful work.

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