

Success in Doing Business in **Russia**

POTENTIAL, OBSTACLES AND PRACTICE

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Contents of the presentation:

1. What is the **theory** of doing business in Russia;
2. What is the **image** of Russia in the West and what is the **reality**;
3. The **opportunities** and the **risks** on the Russian market;
4. Steps to take for a **successful** market entry;
5. How do you increase your chances of success (**Do's** and **Don'ts**);
6. Conclusion and answers to your questions.



A. The theory of doing business in Russia:

1. ?
2. ?
3. ?
4. ?
5. ?
6. ?
7. ?
8. ?
9. ?
- 10.?



**Умом Россию не понять,
Аршином общим не измерить:
У ней особенная стать -
В Россию можно только верить.**

1886 Fedor Tiutchev



B. The theory of doing business in Russia:

1. ?
2. ?
3. ?
4. ?
5. ?
6. ?
7. ?

8. So we do it as it's done back home.



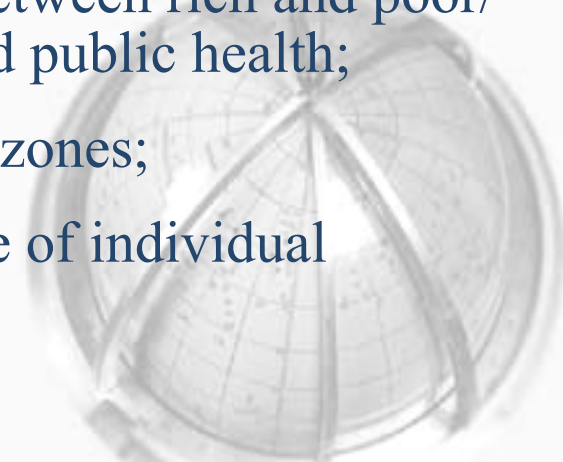
A. The image of Russia in the West is mainly negative:

1. Mafia – Oligarchs - Polonium (Abramovich, Berezovsky);
2. Cold;
3. Russian bear;
4. Risks and danger;
5. Unreliable;
6. But also positively; culture!
7. However: Fear is leading!



B. Relevant is that Russia is a country with:

1. More than **50%** of her external trade with the EU;
 - Oil and gas income contribute 15-20% to GDP;
2. A **stable political system**. After the recent Parliamentary elections (2007) and Presidential elections (2008), no great policy changes are expected for the next two years;
3. Economic: **Oil and Gas** / Increasing purchasing power and real disposable income / Growth in many sectors;
4. Growing **wealth** but also growing difference between rich and poor/
Neglect of crucial sectors such as education and public health;
5. 17 million squared kilometres surface / 11 timezones;
6. Specific Eurasiatic **Slavonic culture** / No sense of individual responsibility / Pride;
7. Many **successful foreign businesses!!**



A. What are the opportunities on the Russian market?

1. Population of **142 million**. (8th in the world);
2. GDP 2007 = EUR 883 bln / Yearly growth between **6% – 7%**;
3. Disposable income grows with **10%** per year;
4. 30% of economy in grey sector and not accounted for;
5. 15% of population has **high purchasing power** (21 million people);
6. 75% of household income is spent on **consumption**;
7. Income is concentrated in **large cities** in Western Russia;
8. 150.000 **millionaires** and 101 **billionaires**;
9. The aggregate net worth of Russia's 100 richest businessmen rose to U.S. \$577 bln in 2007 from \$248 bln in 2006;
10. Growing **demand** for consumption goods, innovative products, value-added services and modern equipment and technologies;
11. Big quantitative potential but strong qualitative **competition**.

B. Economic and market trends:

Economy:

1. Average GDP growth of **6,8%** between 1999 and 2007; **5% (2008-2011)**;
2. High natural resource commodity prices are a **blessing** for economic stability;
3. WTO accession will lead to: lower import tariffs, increased FDI and more competition and efficiency.

Markets:

1. Retail sector;
2. Oil & gas, energy;
3. Agribusiness;
4. Automotive and automobile;
5. Packaging;
6. Construction materials;
7. Telecom & IT;
8. Manufacturing;
9. Logistics Services & Trade.

C. Risks:

Political:

1. Medvedev's presidency may lead to some unrest as shifts occur in balance of power. But: bread over democracy.

Regulative and administrative:

1. Changing and ambiguous **legislation**;
2. Difficult but not impossible to enforce contractual and ownership rights;
3. Bureaucracy.

Economic and financial:

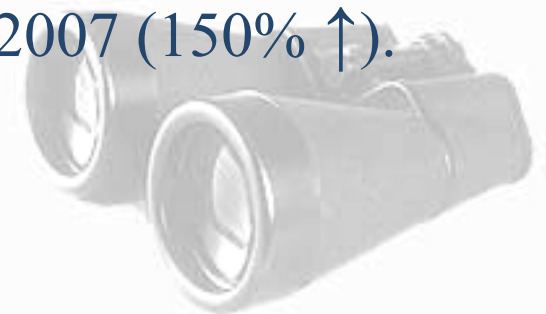
1. Underdeveloped banking system. Financing is expensive and scarce;
2. Underdeveloped SME and absence of strong bourgeoisie / middle class;
3. High and increasing **costs** (10+ % per year). Moscow is now the most expensive city in the world;
4. Underdeveloped **infrastructure** (gas, electricity, water and heat).

HR:

1. Difficult to find good **staff**. Check backgrounds, networks and loyalties.

D. Will Russia remain stable?

1. Continuing **high prices** for oil and gas;
 - Account for 15-20% of GDP.
2. Low level of consumer **credits** and mortgage lending (The Russian owns his house, car, dacha);
3. Consumptive **spending** can be easily (temporarily) reduced by the Russian consumer;
4. Consumption over **democracy**;
5. Foreign **investments** reached \$90 billion in 2007 (150% ↑).

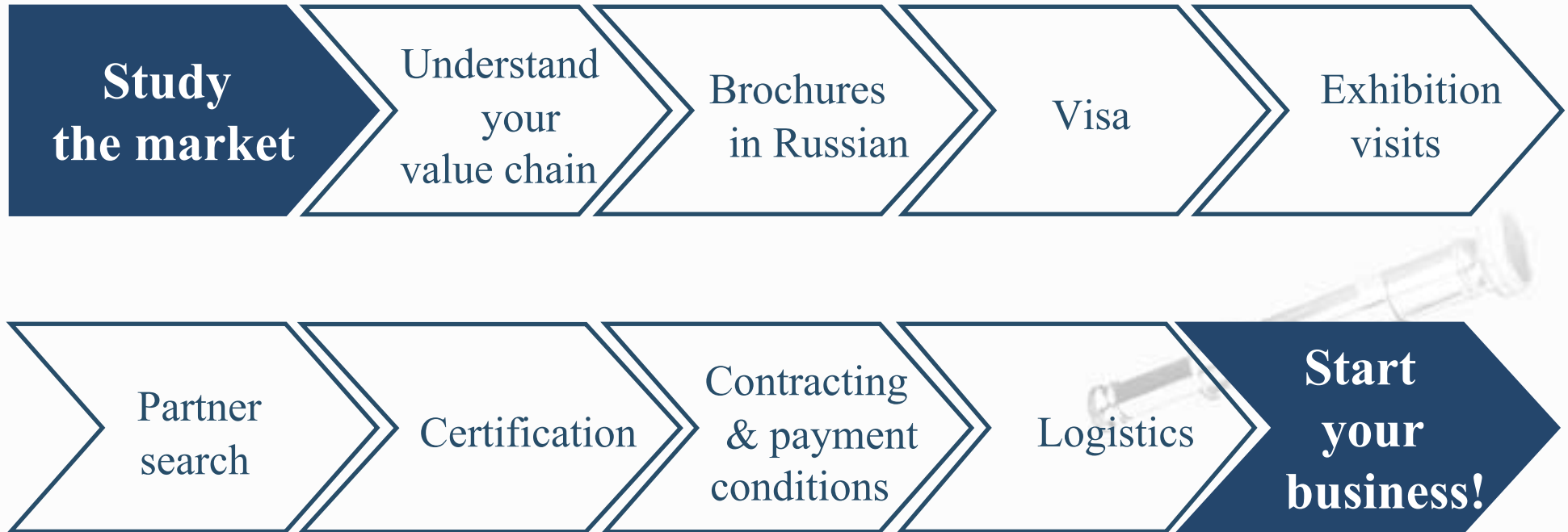


E. What do you hear around Moscow's Expat kitchen tables?

1. Returns higher than anywhere else;
 1. **Stock market** 2006 ↑↑ 70%, 2007 ↑↑ 19%;
 2. Gazprom capitalization from 30 bln \$ to 300 bln \$ in 3 years;
 3. Upgraded country ratings (Fitch: BBB+, Moody's: BAA2);
2. It takes determination, flexibility, stamina and hard work but **success** in Russia is very well possible;
3. The **foreign media** are much too negative;
4. Russia is not more difficult than **China**;
5. **RIC.**



A. Steps to take for a successful market entry:



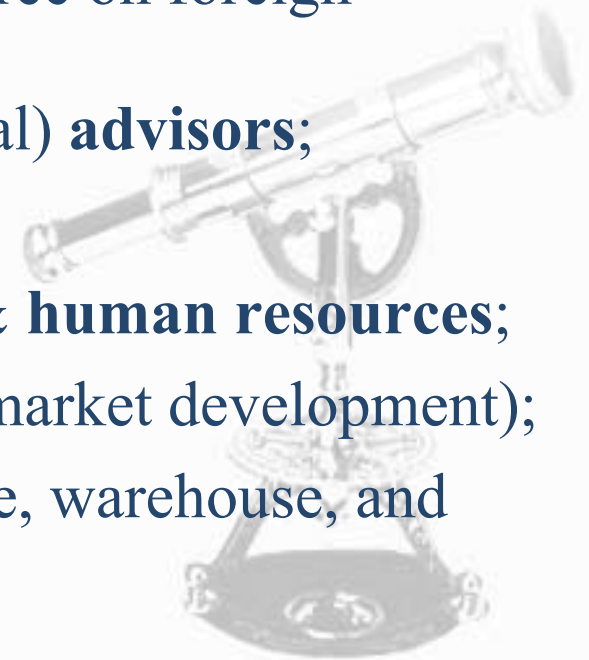
A. What is the secret of success of foreign companies in Russia?

1. They are there and they are **committed**;
2. They **like** it;
3. They **understand** Russia and its potential;
4. They are ready to be **flexible**;
5. They are **entrepreneurial**.



B. Do's:

1. **Enjoy** Russia!
2. Do your homework and **know** your market;
3. Gain some knowledge of the Russian language and **culture**;
4. Stay in **control** (of finances and management);
5. Divide the shares/interests off-shore and agree on foreign arbitration and create **win-win** situation;
6. Use experienced local (general, tax and legal) **advisors**;
7. Limit your **exposure** and risks;
8. Dedicate and commit sufficient **financial & human resources**;
9. Be **flexible** and **patient** (e.g. bureaucracy, market development);
10. Think well about the **location** of your office, warehouse, and production;
11. Understand the Russian **perspective**!



C. Understand the Russian perspective:

1. Be aware of cultural **differences** and language barriers;
2. Building of **trust** and personal relationships is key;
3. Informal communication **networks** are most important;
4. Relatively **short term** vision;
5. Vertical **authority**;
6. During first contacts the Russian partner may promise more than can be delivered (without bad intent!);
7. Russian businessmen can be imposing. **Weakness** is not shown;
8. The external appearance is very important;
9. Russian businessmen think, speak and act **fast!**



D. Don't:

1. Be **afraid** of Russia;
2. **Underestimate** the market or your Russian business partner;
3. Think Russia is **Europe**;
4. Think Russia is **cheap**;
5. Think it is easy to find the right **staff**;
6. Let yourself in with **corruption** (payments on the basis of contracts or through third parties);
7. Give immediate **exclusivity** to distributors;
8. Forget to register your **trademark**;
9. Forget your **visa** and do not forget to have your passport on you;
10. Think **transfer** of goods and money is easy.

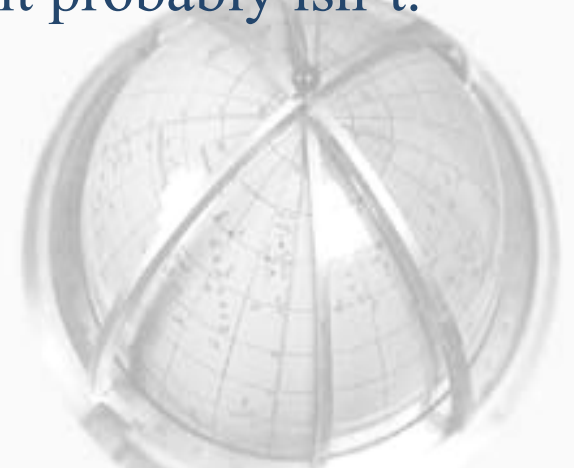


E. Don't forget the regions:

1. **Support** from local administration. Willingness for cooperation and openness for contacts and communication;
2. **Tax incentives** for investors;
3. Lower **costs** of resources compared to Moscow and Moscow region (on average 20% cheaper);
4. Comparable infrastructure and facilities;
5. Young, educated, eager and relatively cheap **workforce**;
6. Facilitating fast document transaction. **Fast** preparation and execution of decisions, resolutions and documents.

F. Russian Partner:

1. Choose your partner carefully:
 1. Good **management**;
 2. Strategy and growth **prospects**;
 3. Decent company **infrastructure**;
 4. Sufficient **transparency** (tax, legal, finance, etc.);
 5. Common **sense**; if it doesn't seem right it probably isn't.
2. When in doubt: use advisor;
3. When still in doubt: Don't continue!!



G. Problems with exports:

1. Customs;
2. Certification and documents;
3. DDP-deliveries without local representation;
4. Need to compete with grey imports.

Therefore important:

1. Good and trustworthy agent/partner/consultant;
2. Good transport company experienced in working with Russia;
3. Solid preparation and uniformity of documents;
4. Conservative payment conditions.



Conclusion and Questions – Why Russia??

- The **economy** will continue to grow;
- Consumer **spending** will continue to grow;
- The growth **potential** in the coming years in a wide number of sectors is high;
- Proximity to the market / cheap resources / specialist industries;
- Many of your colleagues / **competitors** are already there.

BUT

- Traditional problems will continue to exist so prudence and good preparation is advisable.

Tax environment:

- | | | |
|-----------------|---|--|
| 1. Profit Tax | 24% | over profit (17.5% to regional budget, up to 4% reduction is possible) |
| 2. Income Tax | 13% | over personal income (with |
| 3. Social Taxes | 26% (max) | over pay-roll (medical, social, pension) |
| 4. VAT | 18% | over turnover |
| 5. Property tax | 2.2% (max) | over property |
| 6. Dividend tax | 15% (30% to individuals)-(cross-border) and 9% (national) | |

Profit Repatriation

Dividends (or distributions of net profit for Limited Liability Companies) are payable annually, semi-annually or quarterly. In practice, profits are often repatriated through a number of techniques such as: transfer pricing mechanisms, service charges, royalties and interest payments. This is, however, coming under increasing official scrutiny.

Main forms of legal presence in Russia:

1. Representative office;
2. Limited Liability Company (OOO);
3. Closed Joint Stock Company (ZAO);
4. Open Joint Stock Company (OAO).

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