



BUSINESS CLIMATE SURVEY

Russia

Swedish Trade Council
June-August 2008





AGENDA

- Summary
- Introduction and methodology
- General business climate
- Establishment and operation conditions
- Legislation
- Economical and financial
- Trends and future outlook



SUMMARY

- The number of Swedish companies is growing and the majority are to be found within the service and production sector
- Russia climbed to Sweden's 13th largest export market in 2007 from 14th rank in 2005
- Almost 50 % of the respondents have a turnover of more than 91 M EUR and one in three have a significant part of the revenue in Russia
- Swedish businessmen enjoy a good reputation and are perceived very positively
- Finding business partners is rather easy though less so for service companies than for producing companies
- Knowledge of the Russian language is an advantage since Russian businessmen are lacking English proficiency
- Information is very hard to obtain and authorities are most reticent sources of information
- Daily business runs into corruption and bribes to obtain proper certification is a common occurrence
- Establishing a company can be a complicated task and the use of a sub-supplier facilitates the establishment procedure
- Renting and/or buying office, factory, warehouse and industrial land is difficult though renting office space is comparatively easy



SUMMARY

- The custom procedure is not satisfyingly, inferior and need improvement
- The certification process is rather complicated and described with demanding bureaucracy
- Rail roads are relatively well functioning while roads are not satisfactory. The well established rail road system is convenient for domestic travelling
- Telephone, mobile and internet are working satisfyingly while ordinary mail is much in need of improvement
- Local management is difficult to find followed closely by development and sales personnel
- It is not favourable to outsource production to Russia since the productivity yield is low in proportion to salary costs
- One in three believe the legislation to be non favourable since changes occur unpredictably
- Governmental actions influence the operation and different opinions exist regarding how contracts are followed
- Refunding of VAT is working rather well, almost half of the respondents find the VAT refunding working well
- A majority find that payment terms are followed rather well
- The accounting system are causing problems since there are considerable differences in accounting principles



SUMMARY

- Company taxation is rather favourable and one in three find the taxation system beneficial or very beneficial
- International currency transactions are working comparatively well closely followed by the local payment system
- The export volumes to Sweden's neighboring market Russia is comparable in size with the export to far east China
- Swedish export to Russia is higher than the Danish and Norwegian export but much lower than Finland's export
- Russia is Sweden's fourth largest import market, comparable with Swedish import from USA
- Swedish export to Russia is mainly represented by engineering products while import is dominated by fuels
- The profitability for Swedish companies is growing as well as the perception for Swedish businessmen
- Most difficulties from three years ago show improvement though finding a business partner is close to unchanged
- The legal system show improvement though corruption is still close to same level
- Future growth potential looks promising and so does profitability
- A majority plan to expand the business to the regions since the regions are expected to demonstrate the highest growth



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BUSINESS CLIMATE SURVEY

The Swedish Trade Council in Russia conducted in cooperation with OAO Swedbank the Business Climate Survey during June-August 2008.

The main purpose has been to scrutinize and analyze the current business climate in Russia as well as to compare the results with previous survey which was carried out in November 2005. The business climate survey cover areas such as the Russian law system, the economical and financial situation, establishment and trade conditions as well as the investment climate.

The survey is based on answers from questionnaires and interviews carried out with a large number of Swedish companies established in Russia. The web based questionnaires was sent out to 98 Sweden related companies in Russia and 52% answered to the questionnaire. The survey was also complemented by 15 personal interviews with carefully selected Swedish businessmen who have long experience of doing business in Russia and have good insight in the Russian business environment. The following two slides describe the respondents.

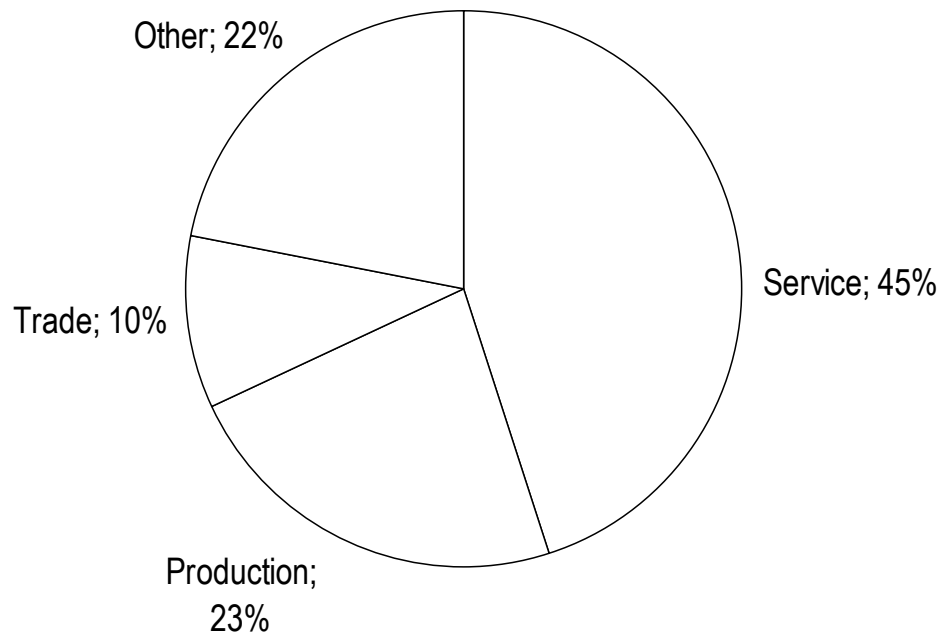


THE NUMBER OF SWEDISH COMPANIES IS GROWING

- the majority are to be found within the service and production sector

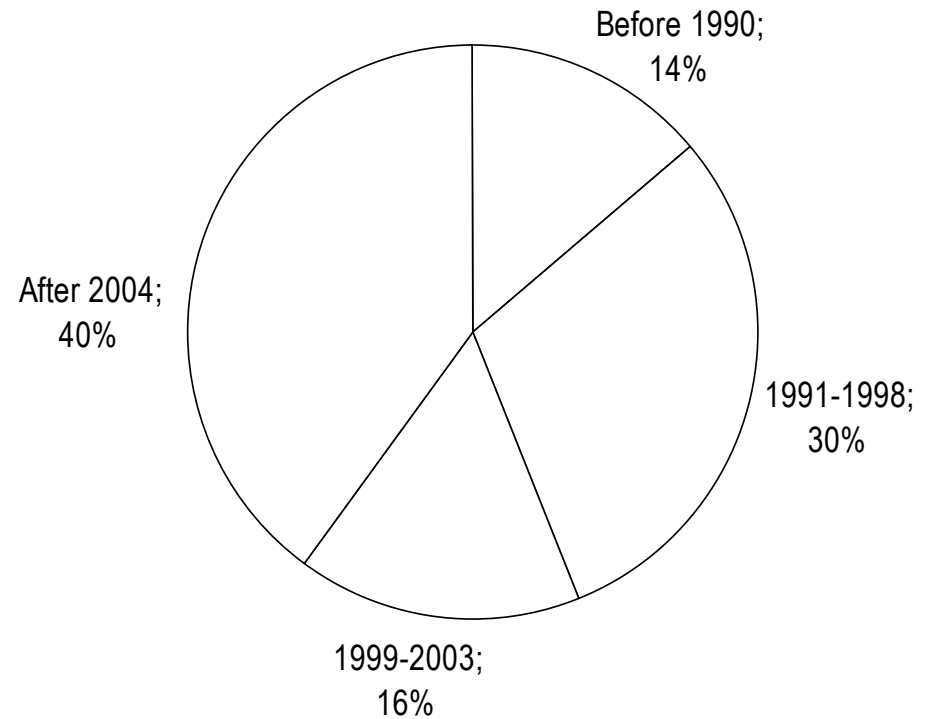
Respondents by sector

Percent



Companies established on the market

Percent

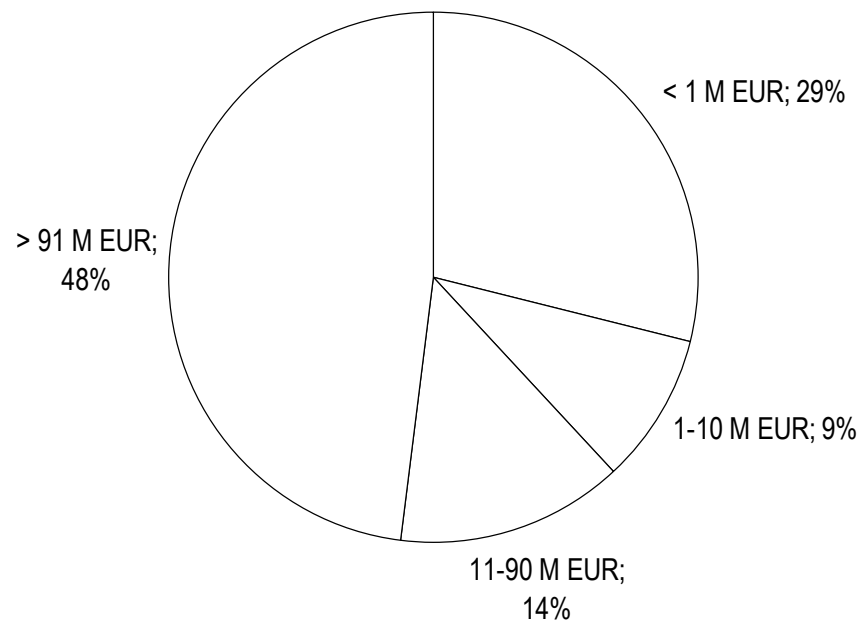




ALMOST 50 % HAVE A TURNOVER OF MORE THAN 91 M EUR - one in three have a significant part of the revenue in Russia

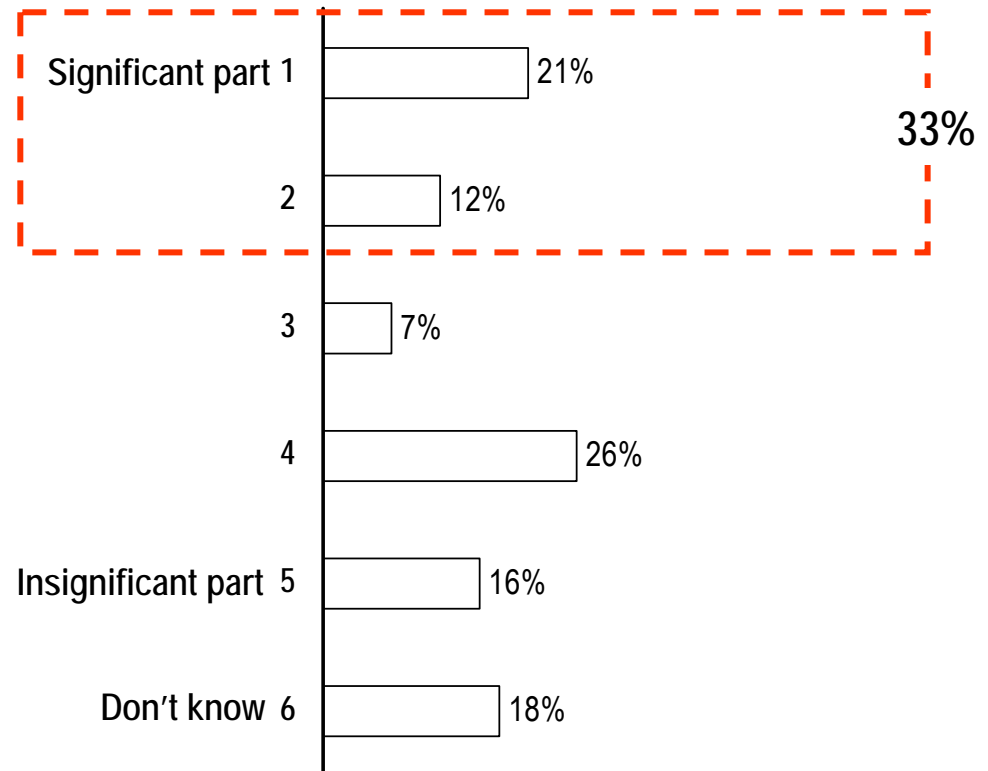
Respondents by turnover

Percent



What part of the total revenue is your revenue in Russia?

Percent





AGENDA

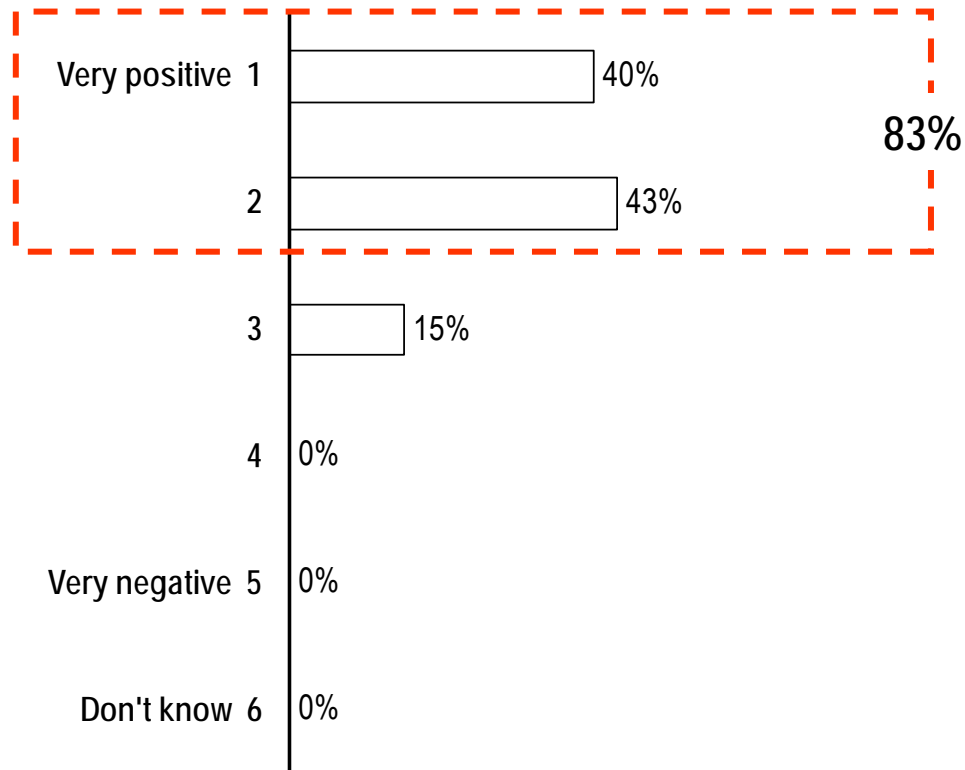
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SWEDISH BUSINESSMEN ENJOY A GOOD REPUTATION - and are perceived very positively

How are you perceived as a Swedish businessman?

Percent



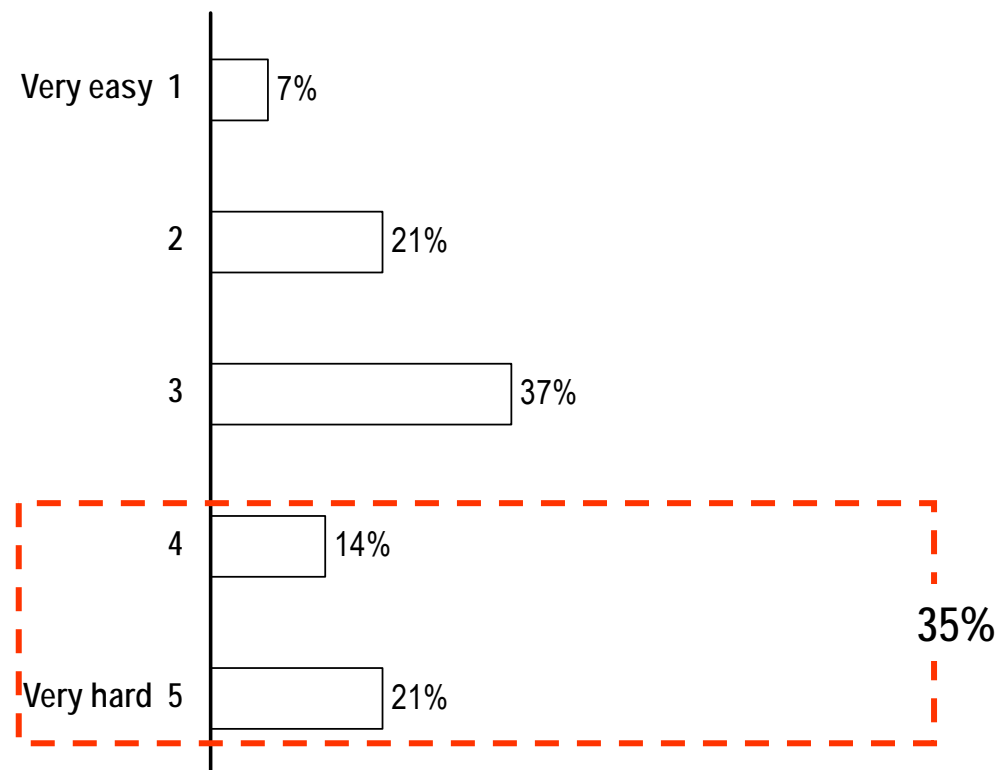
- 83% of the respondents believe that Swedish businessmen are perceived positively
- Swedish businessmen are also perceived as honest, professional and represent high quality products and services. However also associated with long decision making processes.



FINDING BUSINESS PARTNERS IS RATHER DIFFICULT - though less so for service companies than for producing companies

How do you estimate the possibility to find reliable business partners?

Percent



- One in three respondents believe that its rather difficult to find reliable business partners
- Smaller companies compared with larger companies believe that its harder to find reliable business partners
- Service companies are experiencing more difficulties compared with producing companies
- A broad network and personal contacts are crucial for successful business in Russia

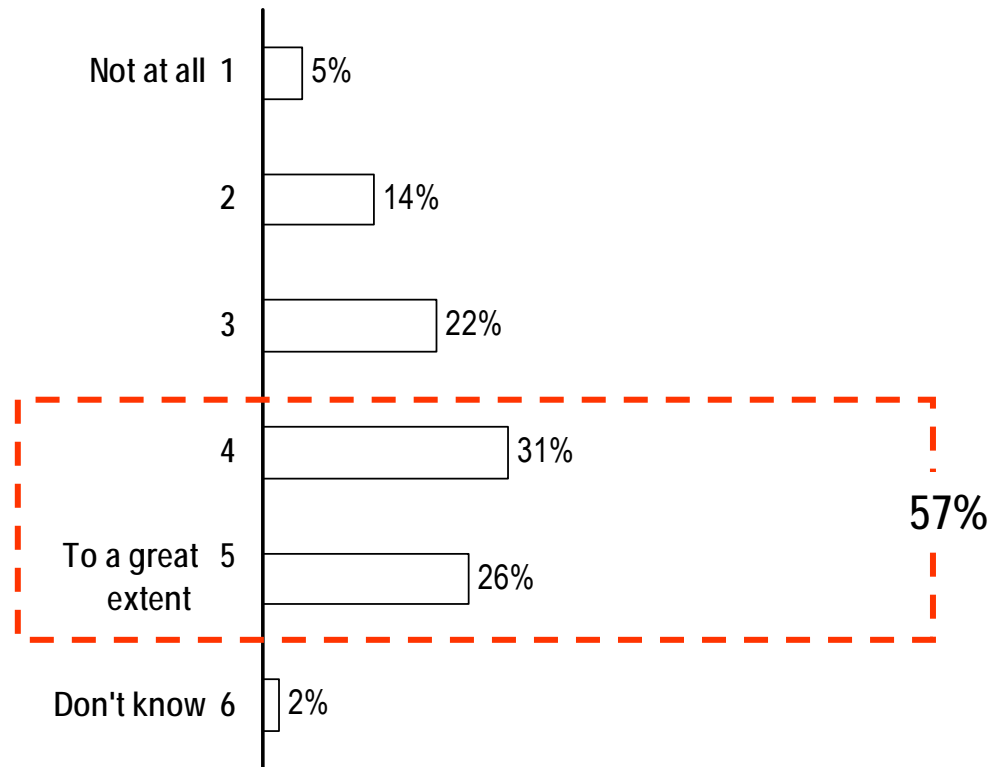


KNOWLEDGE OF THE RUSSIAN LANGUAGE IS AN ADVANTAGE

- Russian businessmen are lacking English proficiency

Does your experience show limited language skills among Russian business people?

Percent



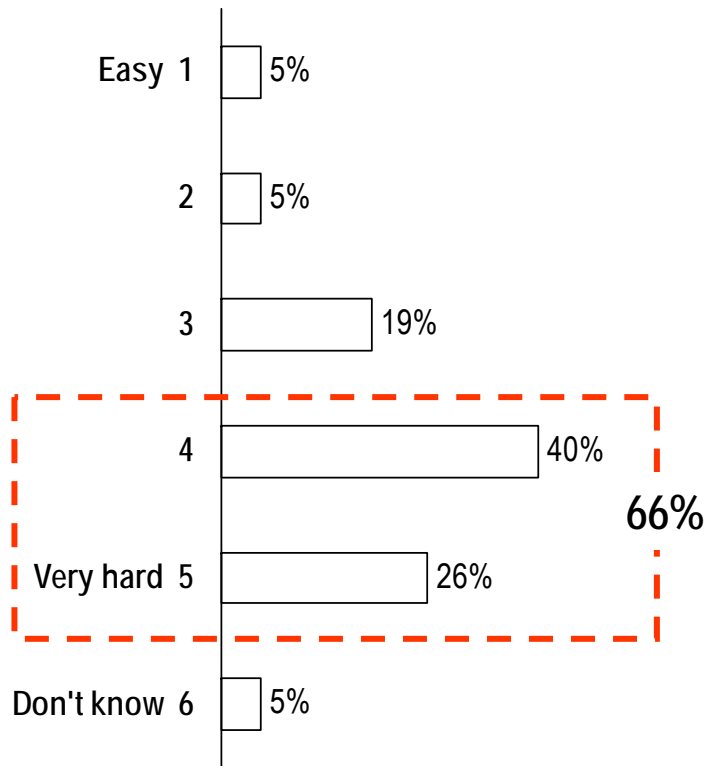
- Russian businessmen do not have sufficient knowledge of the English language
- Interpreters are usually needed during business meetings
- Knowledge of the Russian language makes a big difference, you also demonstrate your interest for the Russian language and culture
- The younger generation has better English language skills compared with older generations

INFORMATION IS VERY HARD TO OBTAIN

- authorities are most reticent sources of information

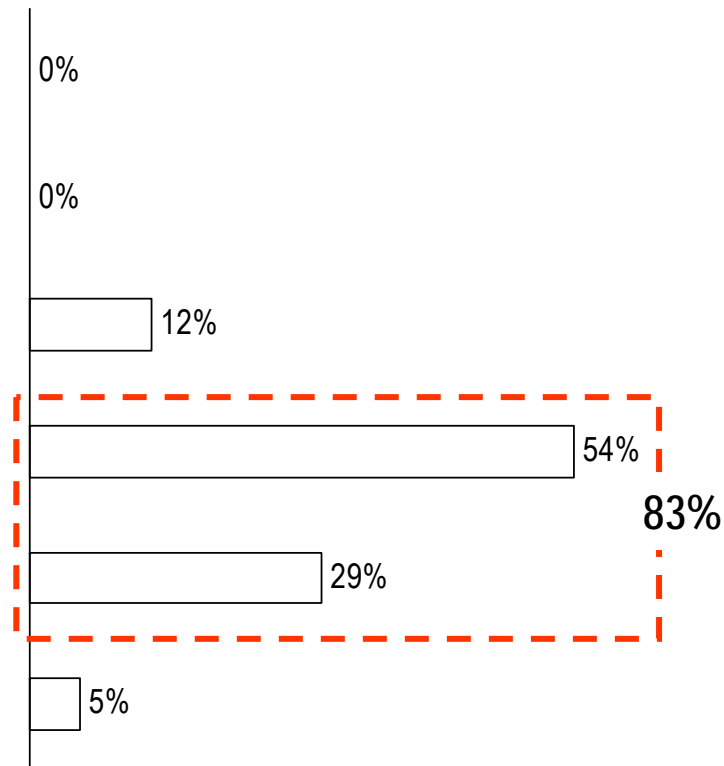
How do you estimate the gathering of financial information about local companies?

Percent



How do you estimate the gathering of information from the authorities?

Percent



- 66% of the respondents believe that its hard or even very hard to obtain information about local companies
- 83% of the respondents believe that its hard or even very hard to obtain information from the authorities
- Bureaucracy is a bottleneck that influence daily business

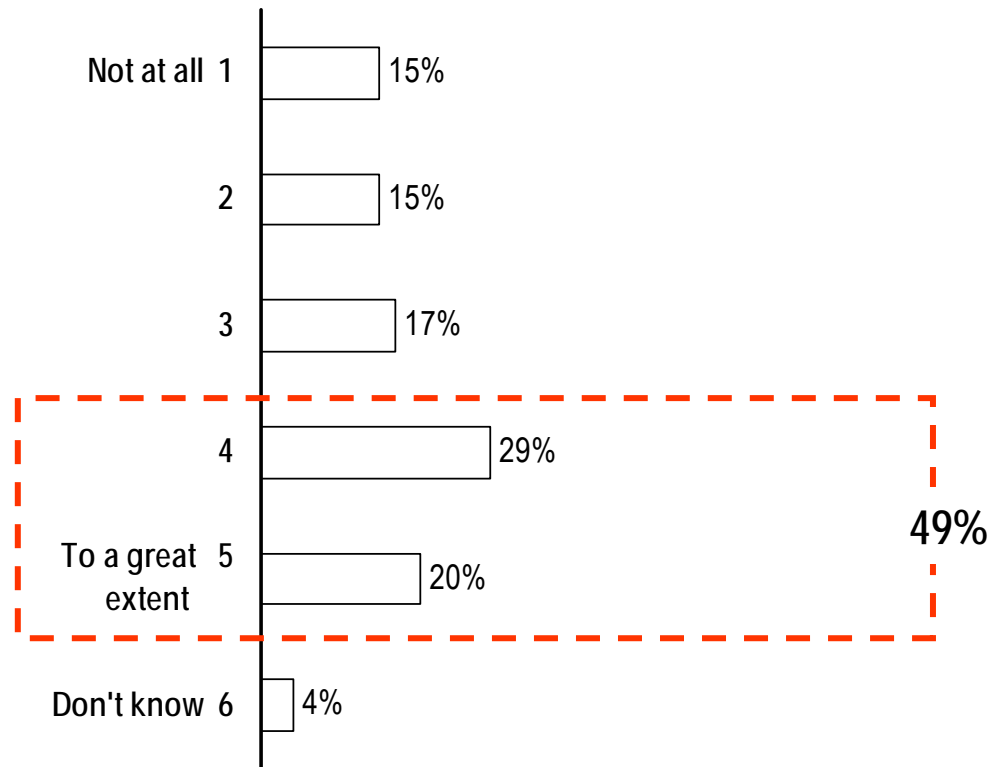


DAILY BUSINESS RUNS INTO CORRUPTION

- bribes to obtain proper certification is a common occurrence

Is the corruption noticeable for your operation?

Percent



- A majority of the respondents find corruption influencing their daily business
- Service companies are more exposed to corruption than producing companies
- Corruption is seen in both larger and smaller companies
- Bribes are very common and especially noticeable in contact with authorities



QUOTES ABOUT THE BUSINESS CLIMATE IN GENERAL

“The service standard is low compared with Sweden, it’s hard to get clear messages from the authorities. Visa and work permits are now more complicated to obtain.”

“Well established network and contacts are extremely important. Decisions are often made based on personal contacts and not on objective factors such as price, quality and others.”

“The authorities are created for the benefits of the authorities and not those who address them .”

“The business is very much effected by bureaucracy. The organization in Russia is much heavier than the same ones in Europe; needs many more people to run the business.”

“The time perspective is much more short term thinking in terms of decision making and perspectives in Russia. Businessmen make decisions with perspective of 5-10 years”

“Bribes are less common than in the past, though they happen more in everyday life.”



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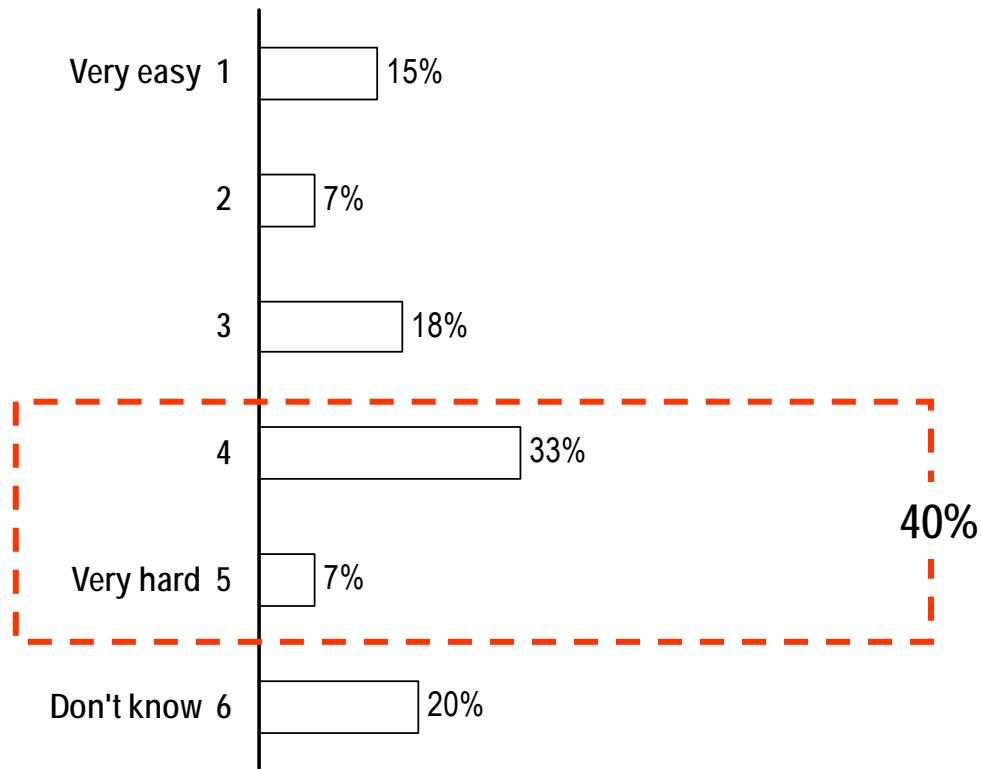


ESTABLISHING A COMPANY CAN BE A COMPLICATED TASK

- the use of a sub-supplier facilitates the establishment procedure

How difficult was it to establish your company?

Percent

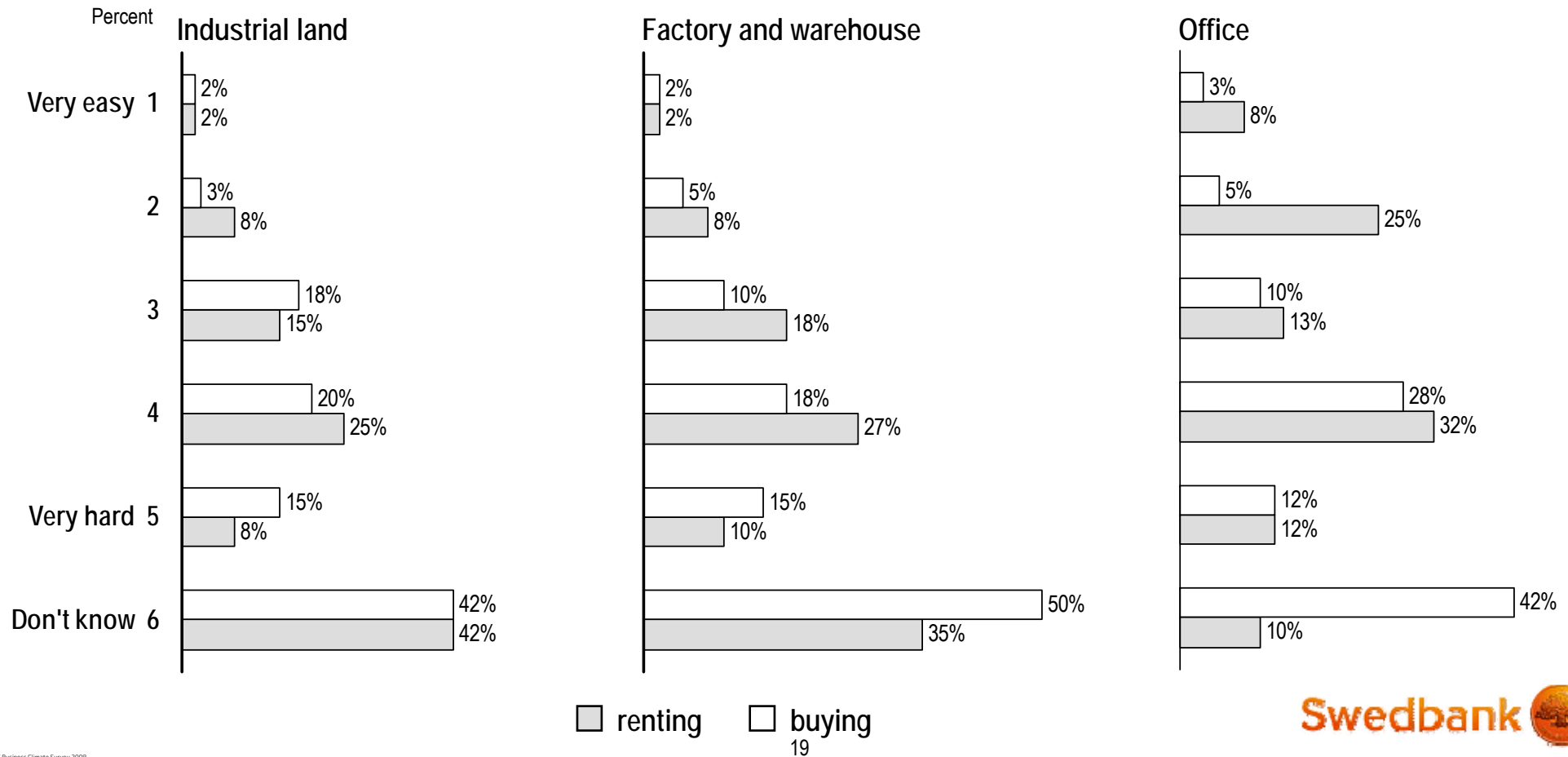


- 40% of the respondents found it hard or even very hard to establish the company
- The establishment procedure is complicated and time consuming since the process follows a strict order and documents have to be official i.e. with apostils, translated into Russian etc
- Swedish companies do underestimate the demanding procedures

RENTING AND/OR BUYING OFFICE, FACTORY, WAREHOUSE AND INDUSTRIAL LAND IS DIFFICULT

- though renting office space is comparatively easy

What is your judgment on renting/ buying the following objects?



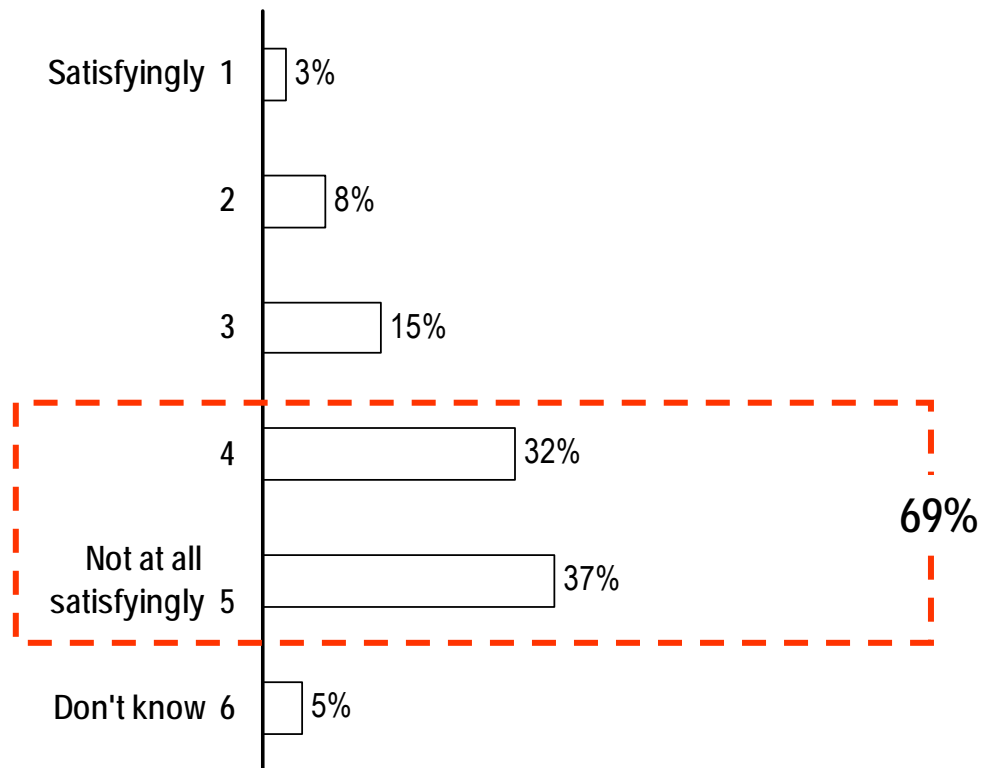


CUSTOM PROCEDURE IS NOT SATISFYINGLY

- custom procedure is inferior and need improvement

How do you think the custom processes work?

Percent



- The majority of the respondents find the custom procedure non satisfyingly
- The custom procedure is often described with bureaucracy, delays and corruption
- All documents has to be accurate in order to get custom clearance and to cross the Russian boarder
- The procedure is time consuming and small mistakes are unproportionally punished with time delays
- Swedish companies are recommended to cooperate with brokers

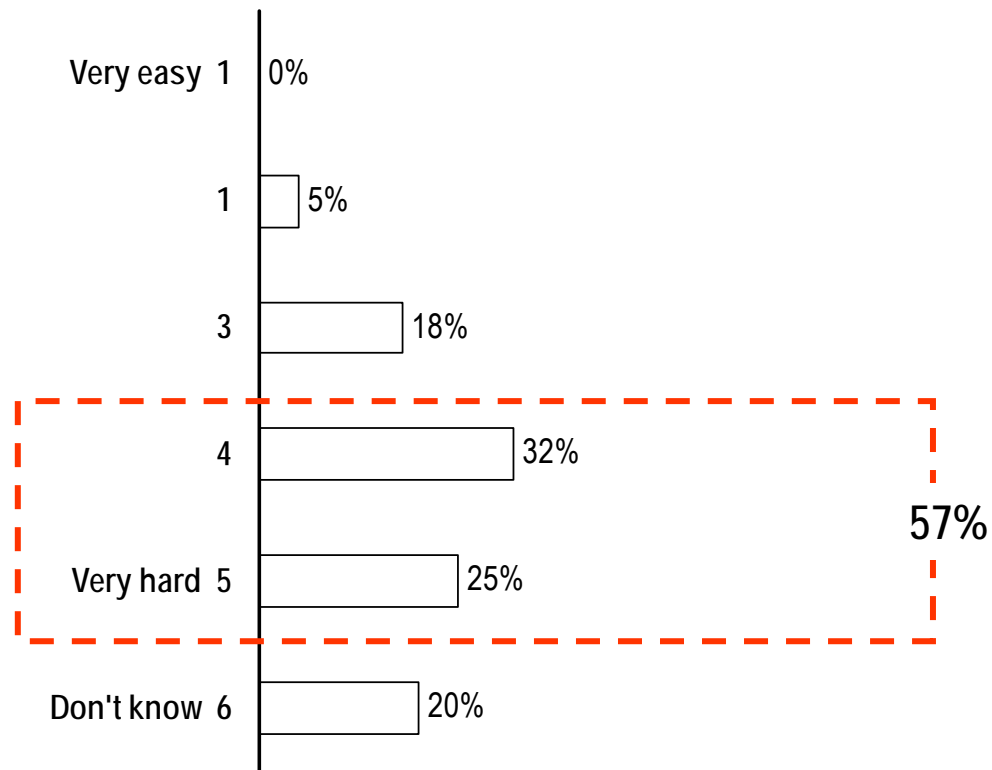


CERTIFICATION PROCESS IS RATHER COMPLICATED

- certification process is described with demanding bureaucracy

How do you think the process of product certification is?

Percent



- The majority of the respondents believe that the process is hard or even very hard
- The custom procedure is often described with bureaucracy, delays and corruption
- Swedish companies are recommended to cooperate with agents

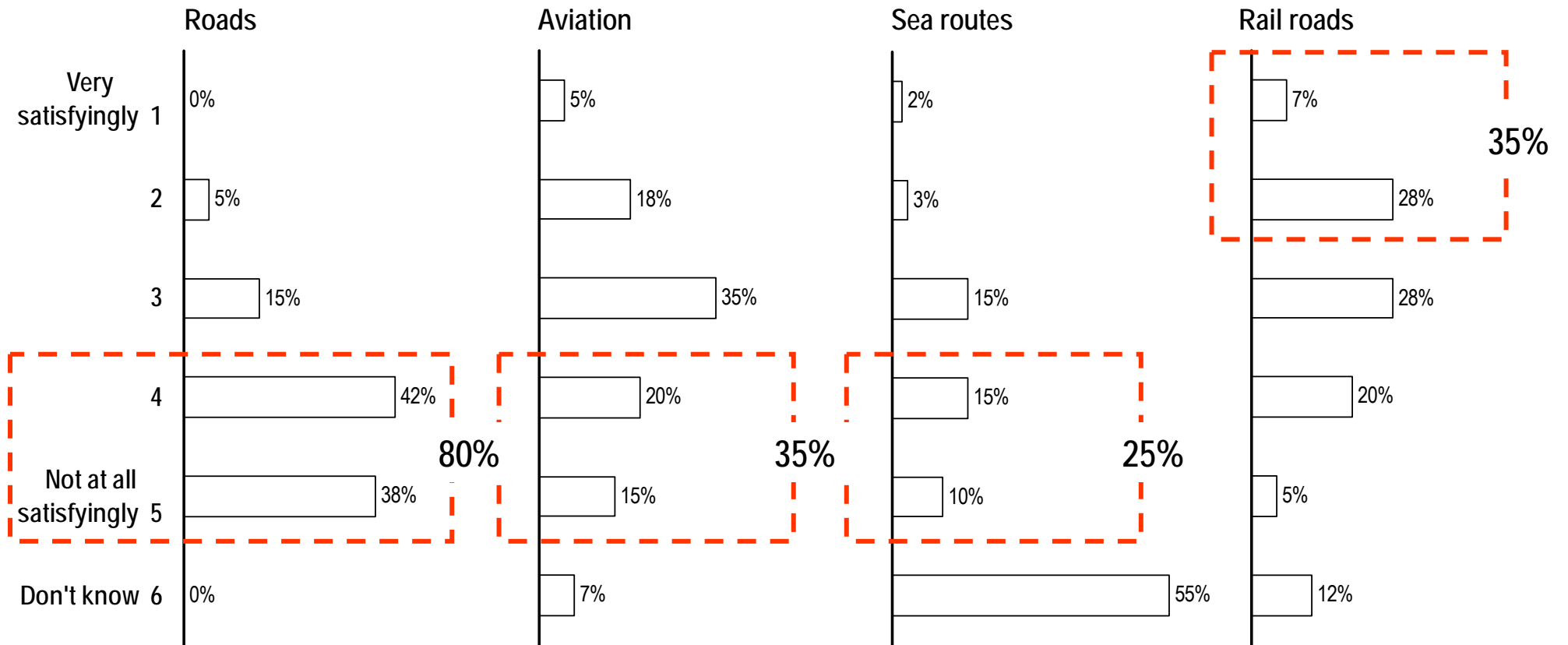


RAIL ROAD SYSTEM IS CONVENIENT FOR DOMESTIC TRAVELLING

- roads are not satisfactory

How do you think the infrastructure works?

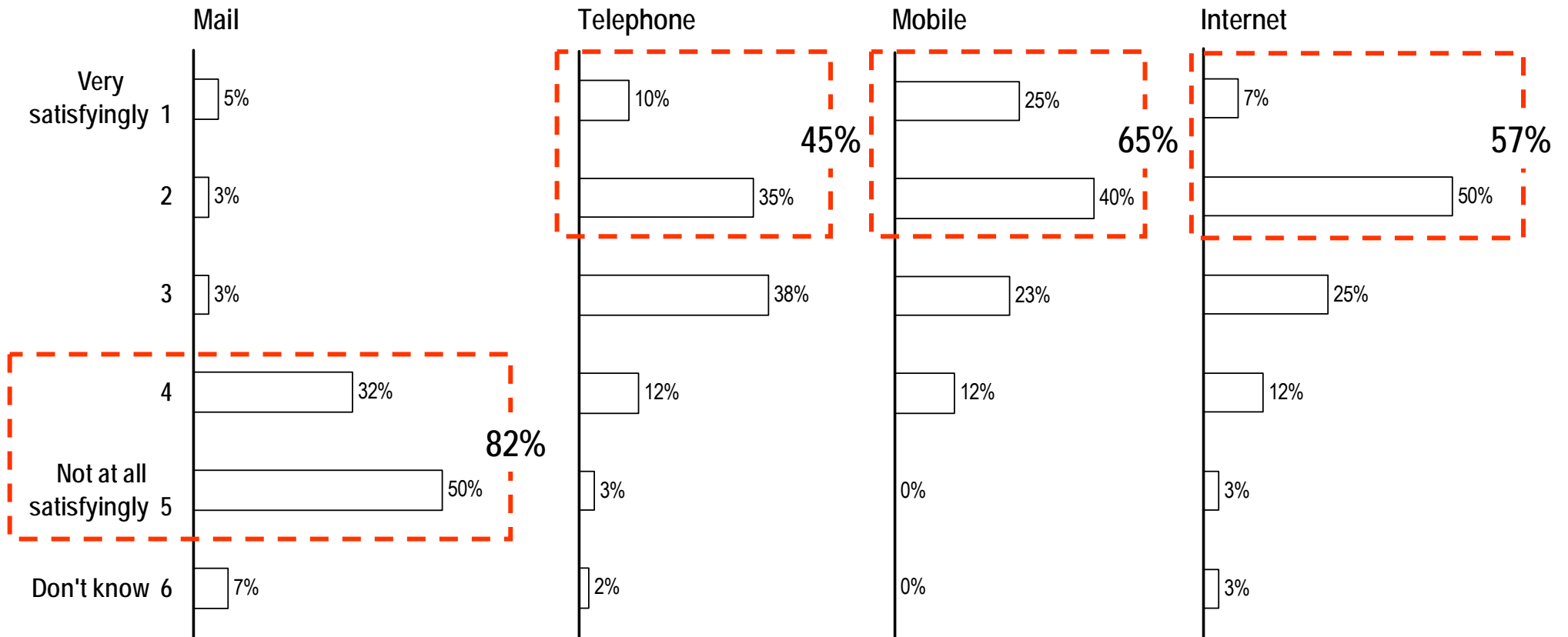
Percent



TELEPHONE, MOBILE AND INTERNET ARE WORKING SATISFYINGLY - ordinary mail though is much in need of improvement

How do you think the infrastructure works?

Percent



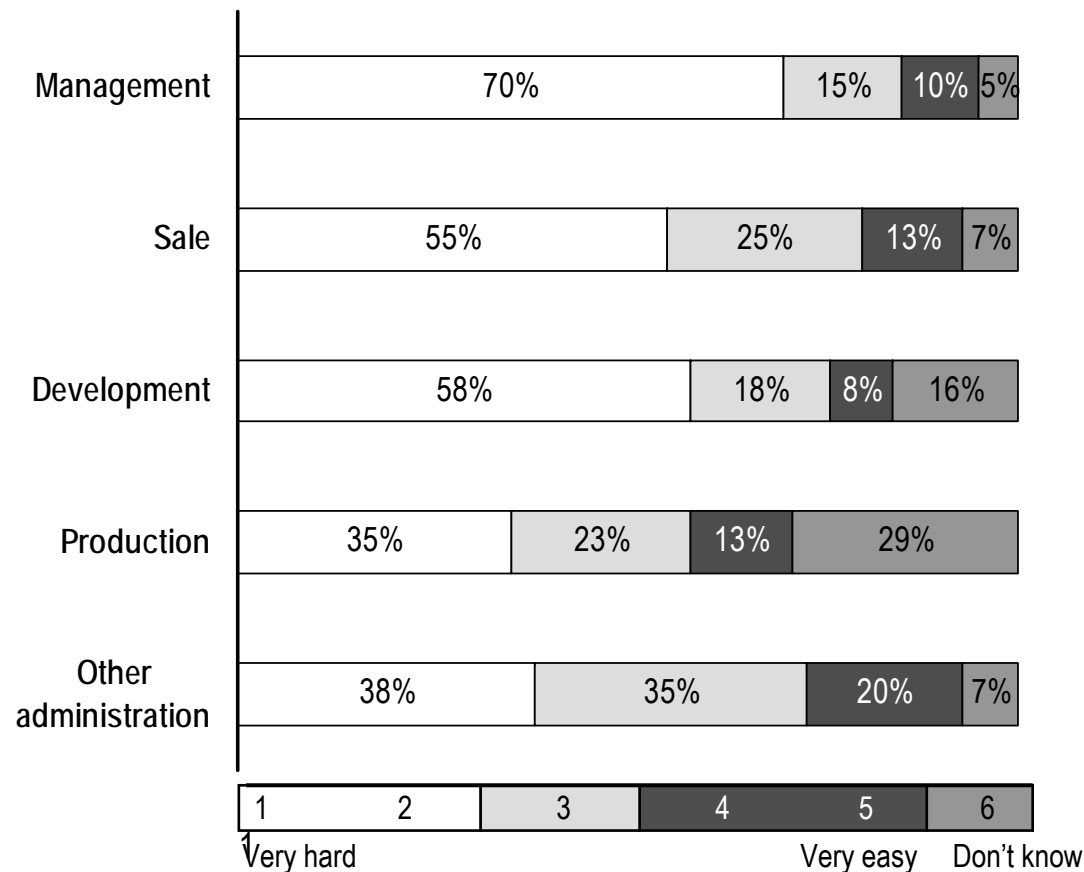


LOCAL MANAGEMENT IS DIFFICULT TO FIND

- followed closely by development and sales personnel

How do you think the availability of local manpower is?

Percent

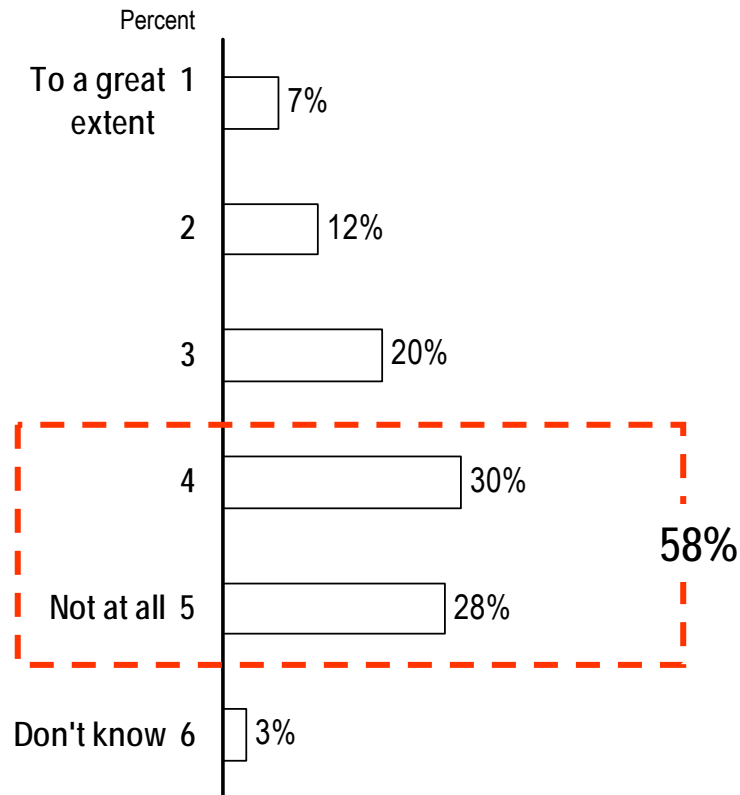


- A majority believe that its hard or even very hard to find management personnel, closely followed by development and sales personnel
- A majority believe that other administration personnel is rather easy to find
- The Russian labour market is rather flexible and has high staff turnover, personnel needs incentives

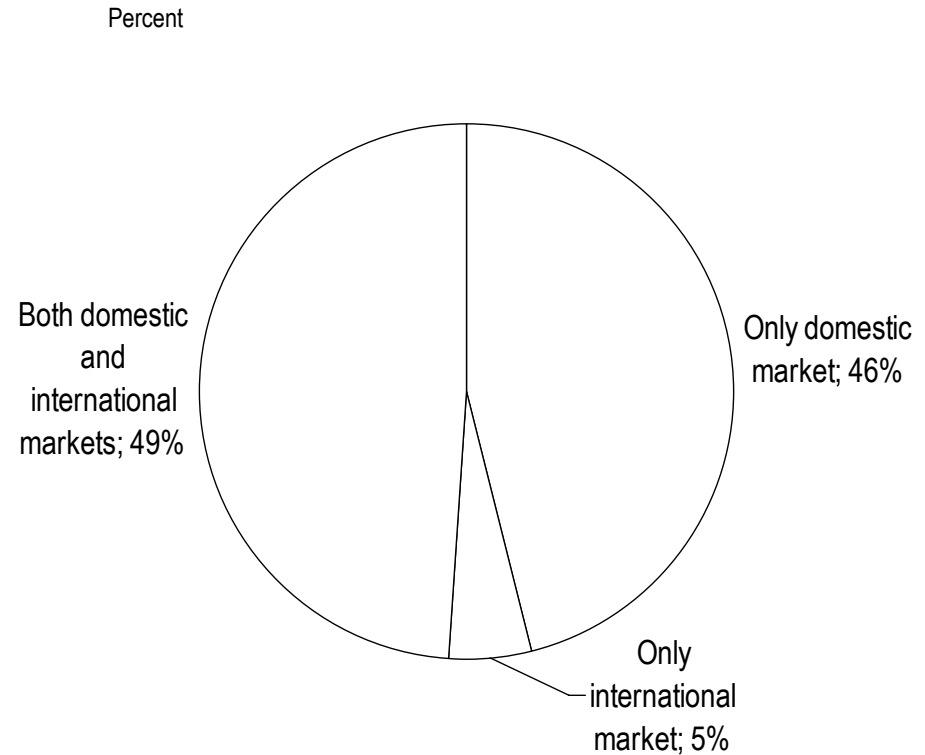


IT IS NOT FAVOURABLE TO OUTSOURCE PRODUCTION TO RUSSIA - the productivity yield is low in proportion to salary costs

Is the salary level compared to the productivity a reason to move the production to Russia?



What market does the production supply?





QUOTES ABOUT ESTABLISHMENT IN GENERAL

“The best option is to find a local person who shares the same views and culture. It’s easier to make a Russian person a good manager than to take a Swede and make him a good Russian manager”

“I would in an early stage of establishment hire a Swede for 6-24 months, let him pave the ground and there after replace him with Russian management.”

“Will definitely need a Swedish representative in order to control the activities and report back to Sweden”

“Local presence is crucial in order to become successful in Russia. To have production near the market is an advantage.”

“Registering a company is more time consuming than you can predict. It’s more or less impossible to execute the process from Sweden.”

“To be successful with your establishment in Russia you need full commitment from the mother company’s top management and board of directors.”



QUOTES ABOUT OPERATIONS IN GENERAL

“Since Russia is booming and prices and salaries are increasing rapidly, you need to adapt to the constant changing market terms. It’s important to understand the need for higher salaries.”

“We offer good salaries for key personnel, otherwise they will ask for salary increase once a year, and a Christmas bonus.”

“Be determined, put time and effort, work 100%. Face and accept that things are different. It makes sense to come here, lots of possibilities though high competition. Don’t be afraid!”

“There are no unions for collective negotiations, they are instead held on individual level.”

“In Sweden it’s much more of collective decision-making, while in Russia one manager makes the decisions.”

“Don’t come to Russia if you are looking for cheap labour force. There are other countries that are better at providing that”



AGENDA

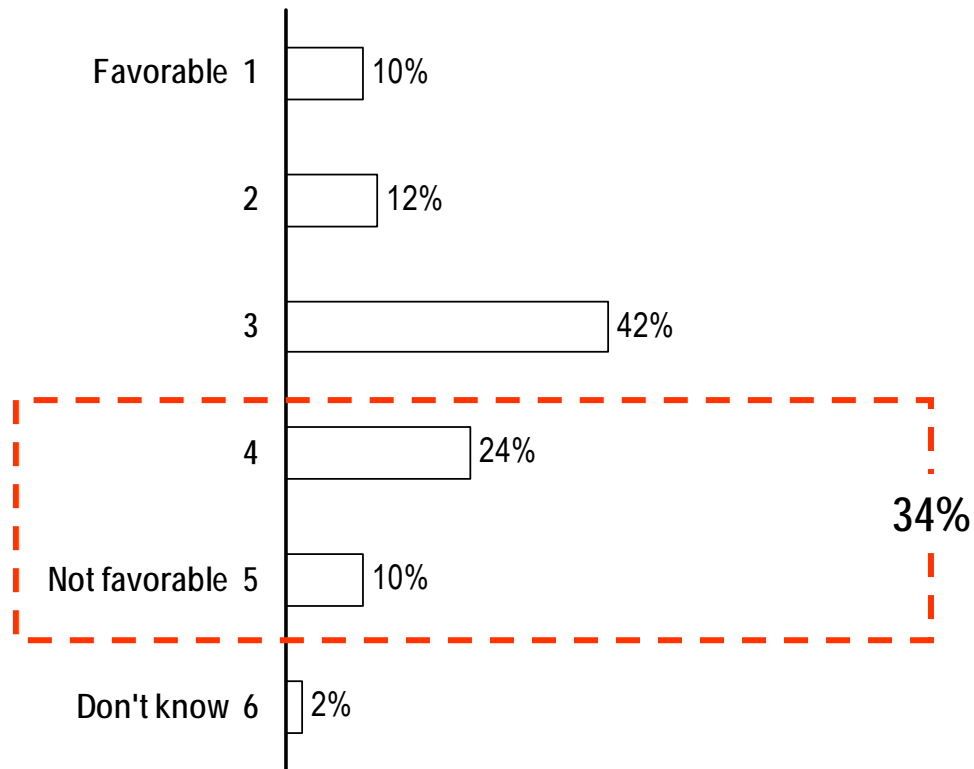
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ONE IN THREE BELIEVE THE LEGISLATION TO BE NON FAVOURABLE - changes occur unpredictably

Do you think that Russia has a legislation that is favorable for your operations?

Percent



- One in four find the legislation to be favorable for their operations
- Small and large changes occur unpredictably and are implemented with short notice
- To be compliant with law is sometimes difficult and time consuming

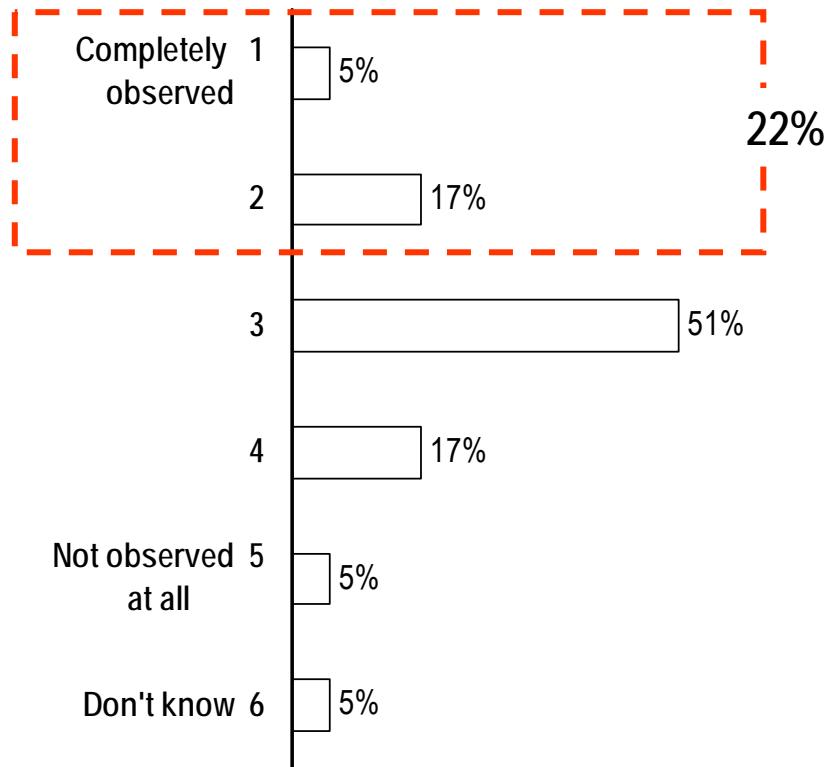


GOVERNMENTAL ACTIONS INFLUENCE THE OPERATION

- different opinions exist regarding how contracts are followed

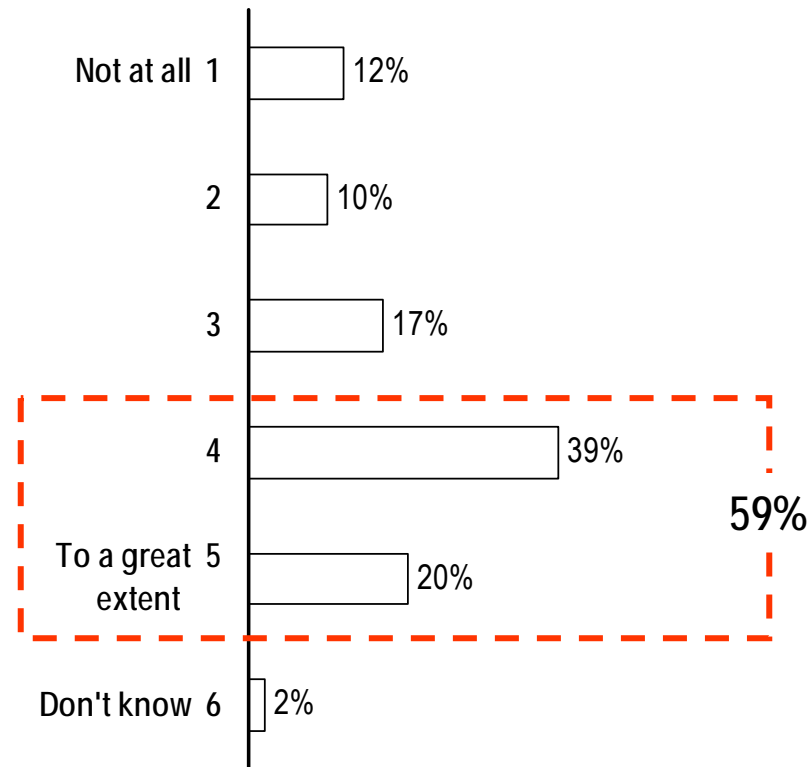
To what extent do you think the law of contracts is observed?

Percent



Do you think governmental actions influence the operation?

Percent





QUOTES ABOUT LEGISLATIONS IN GENERAL

“Contract has to be written in Russian so be prepared to have bilingual documents. Be ready for long negotiations and many changes before you get your contract signed.”

“It’s important to evaluate the partner you are working with: how serious, enthusiastic and financially stable the company is. Though financial figures are difficult to obtain.”

“You should not rely on verbal agreements. You don’t have an agreement until it’s on paper.”



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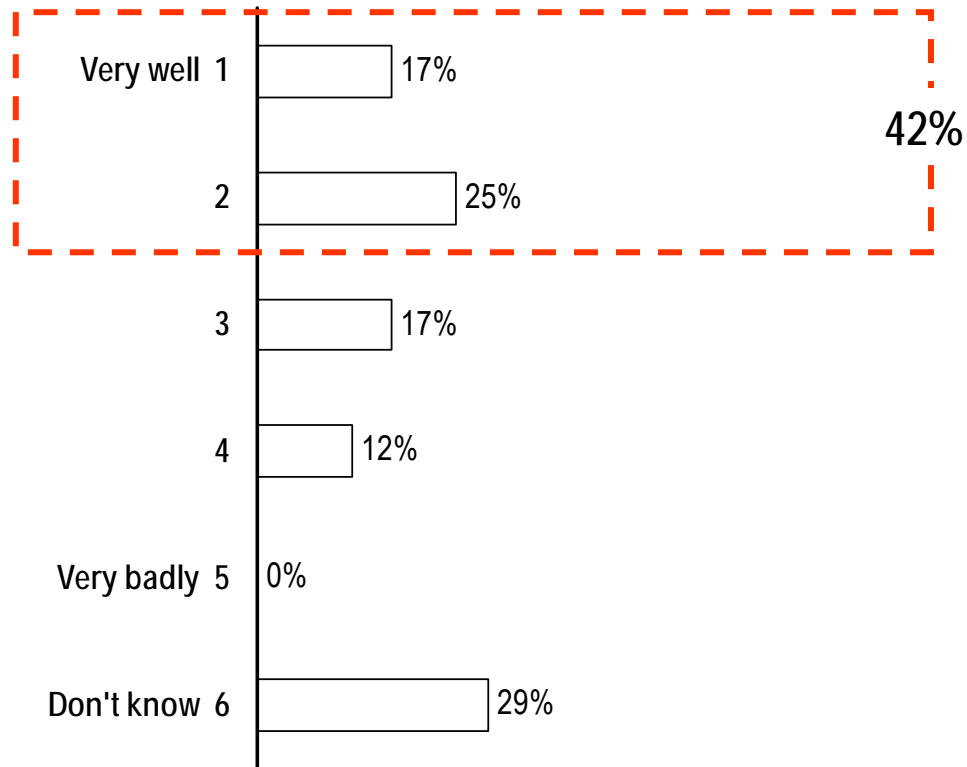


REFUNDING OF VAT IS WORKING RATHER WELL

- almost half of the respondents find the VAT refunding working well

How do you think the refunding of VAT works?

Percent



- VAT is reported on a monthly basis and strict reporting routines must be followed
- Similar system as in Sweden with in and outgoing VAT
- The VAT is normally 18%

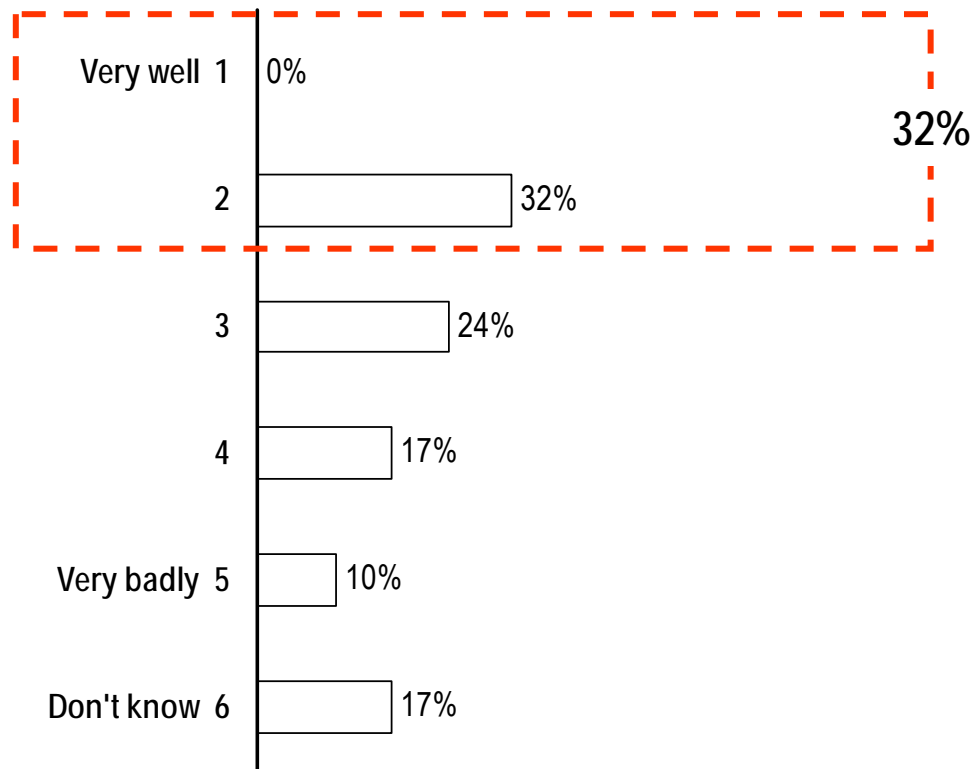


PAYMENT TERMS ARE FOLLOWED RATHER WELL

- a majority find that the payment terms are followed well

How do you think payment terms are followed?

Percent



- One in three find the payment terms working well
- Payment terms are normally between 30-60 days

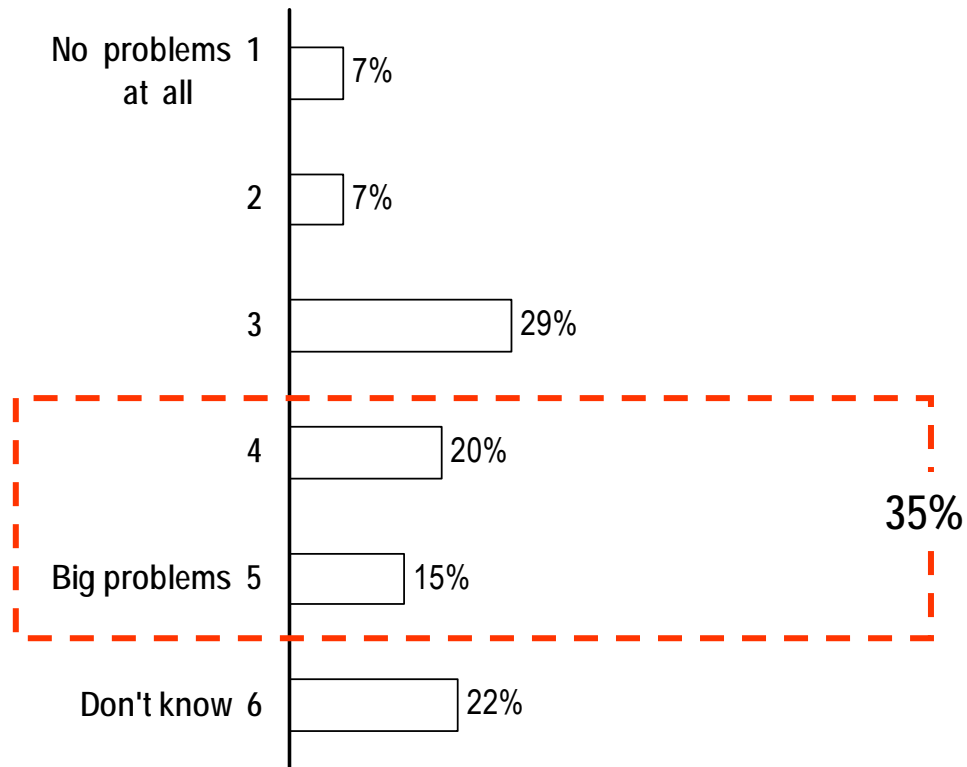


THE RUSSIAN ACCOUNTING SYSTEM (1C) IS CAUSING PROBLEMS

- there are considerable differences in accounting principles

Do differences between the Swedish and Russian accounting systems cause problems for the operation?

Percent



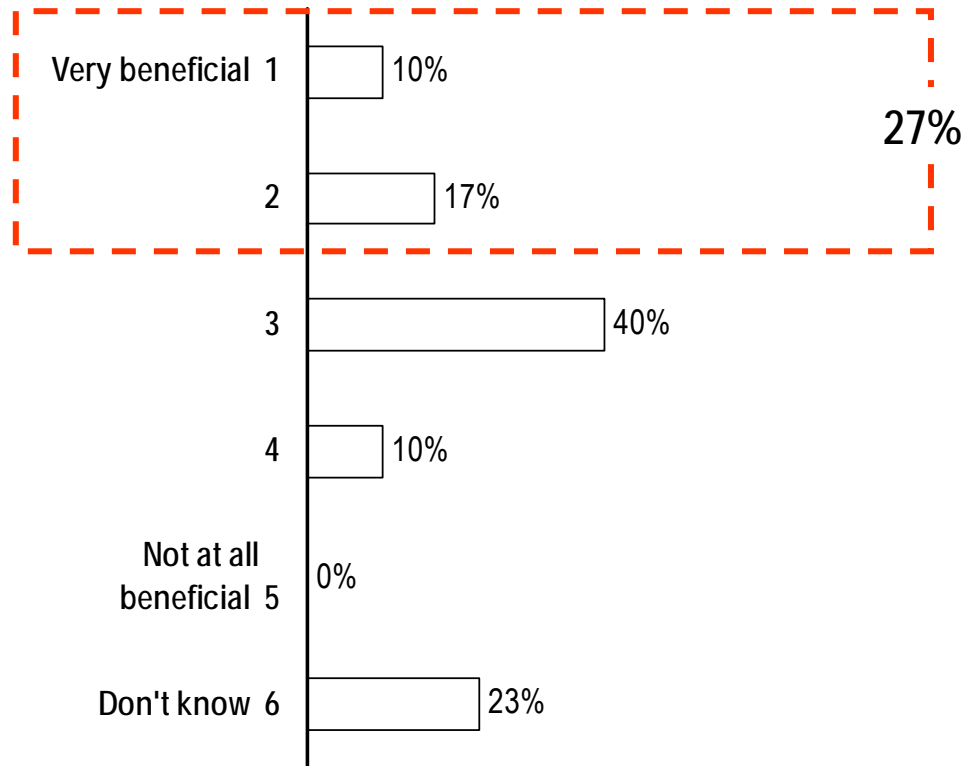
- One in three believe the accounting system to be associated with problems
- Each transaction is followed by strict documentation and should be archived



COMPANY TAXATION IS RATHER FAVOURABLE - one in three find the taxation system beneficial

What do you think about the company taxation?

Percent



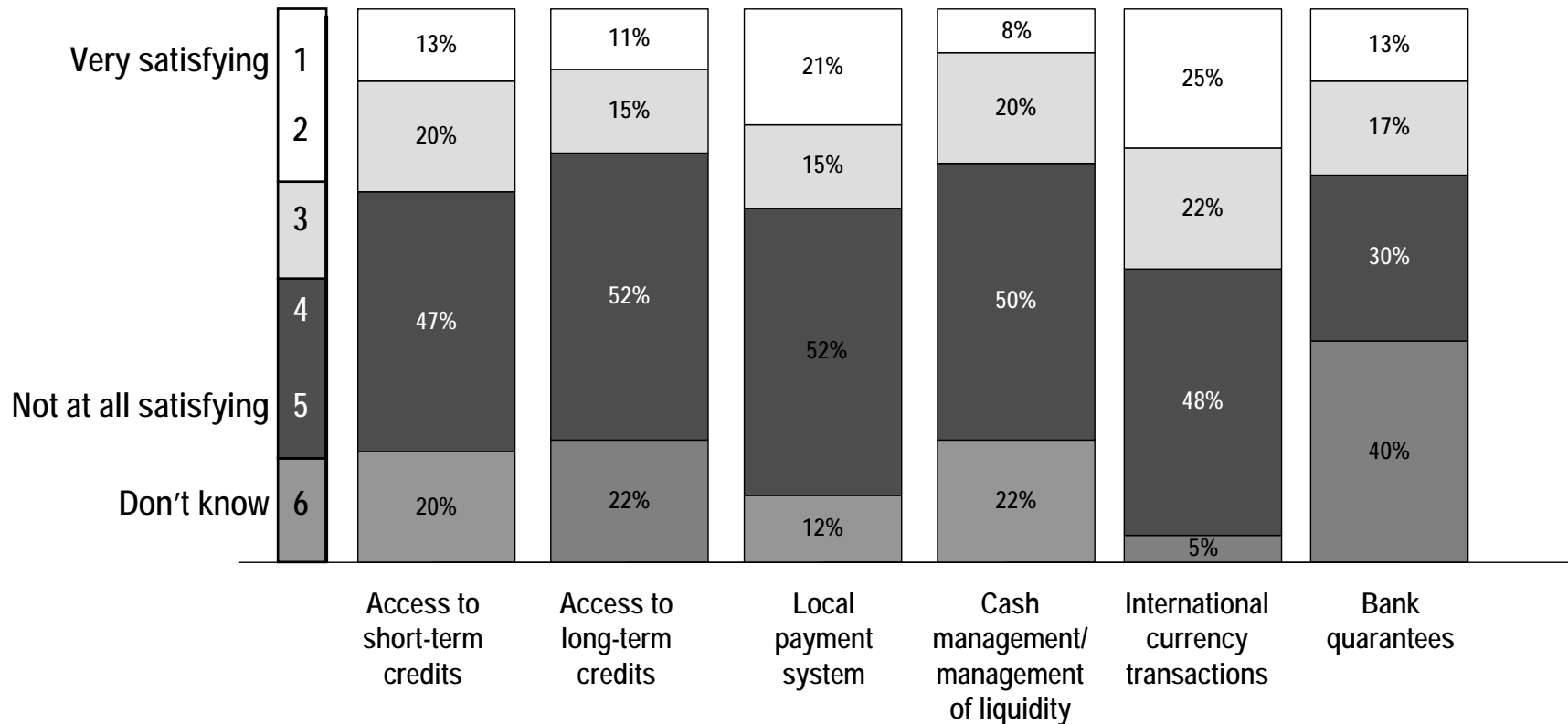
- The company profit tax is 24 %
- The income tax is flat rate with 13 %
- The social tax is degressive starting from
 - 26 % (≤ 280.000 RUB/Year)
 - 10 % (281.000-600.000 RUB/Year)
 - 2 % (≥ 601.000 RUB/Year)

CHALLENGING TO WORK WITH BANKS

- but international currency transactions are working comparatively well

How do you think the bank system works?

Percent





QUOTES ABOUT ECONOMICAL AND FINANCIAL IN GENERAL

“Many work with pre-payments and Russians know that if they don't pay they don't get things.”

“Cash flow is much more of an important issue for European companies than for businessmen in Russia.”

“Usually suppliers ask for pre payment and buyers ask for credit.”

“Pre-payment and short term credits are still obstacles for efficient business.”

“The Russian accounting system is adjusting towards international standards.”



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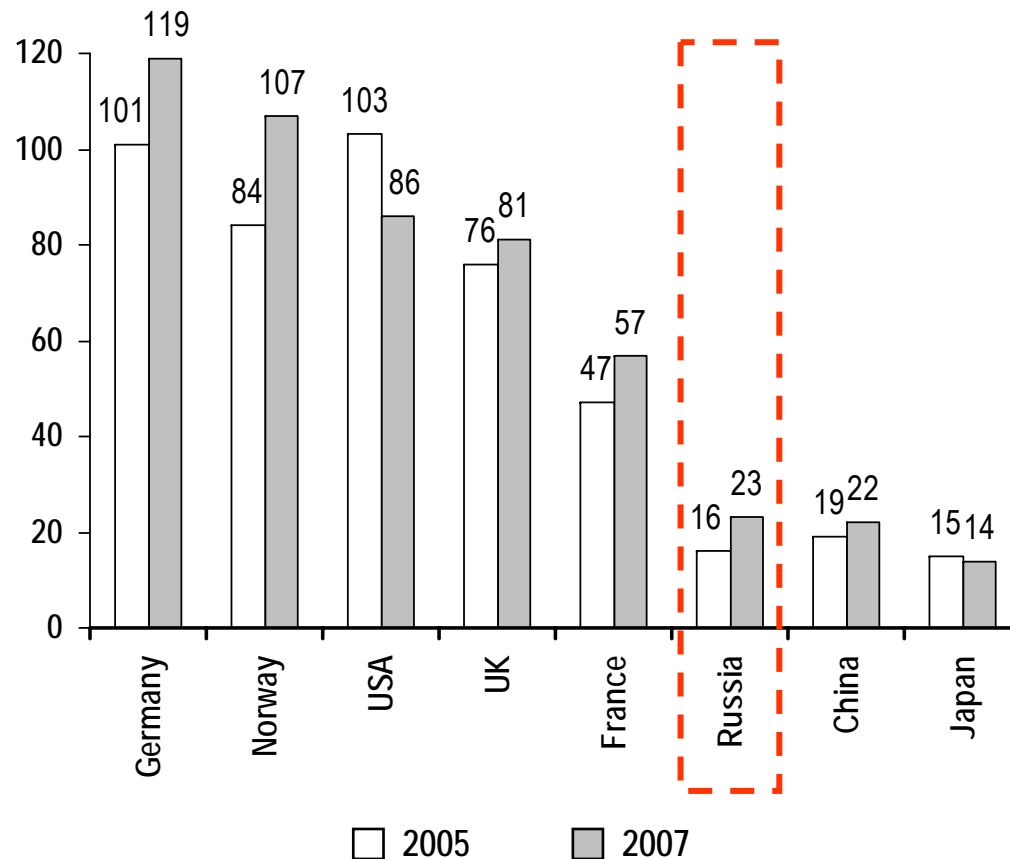
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SWEDISH EXPORTS TO RUSSIA IS GROWING - though comparable with export to far east China

Export from Sweden by destinations, 2005 and 2007

billion SEK



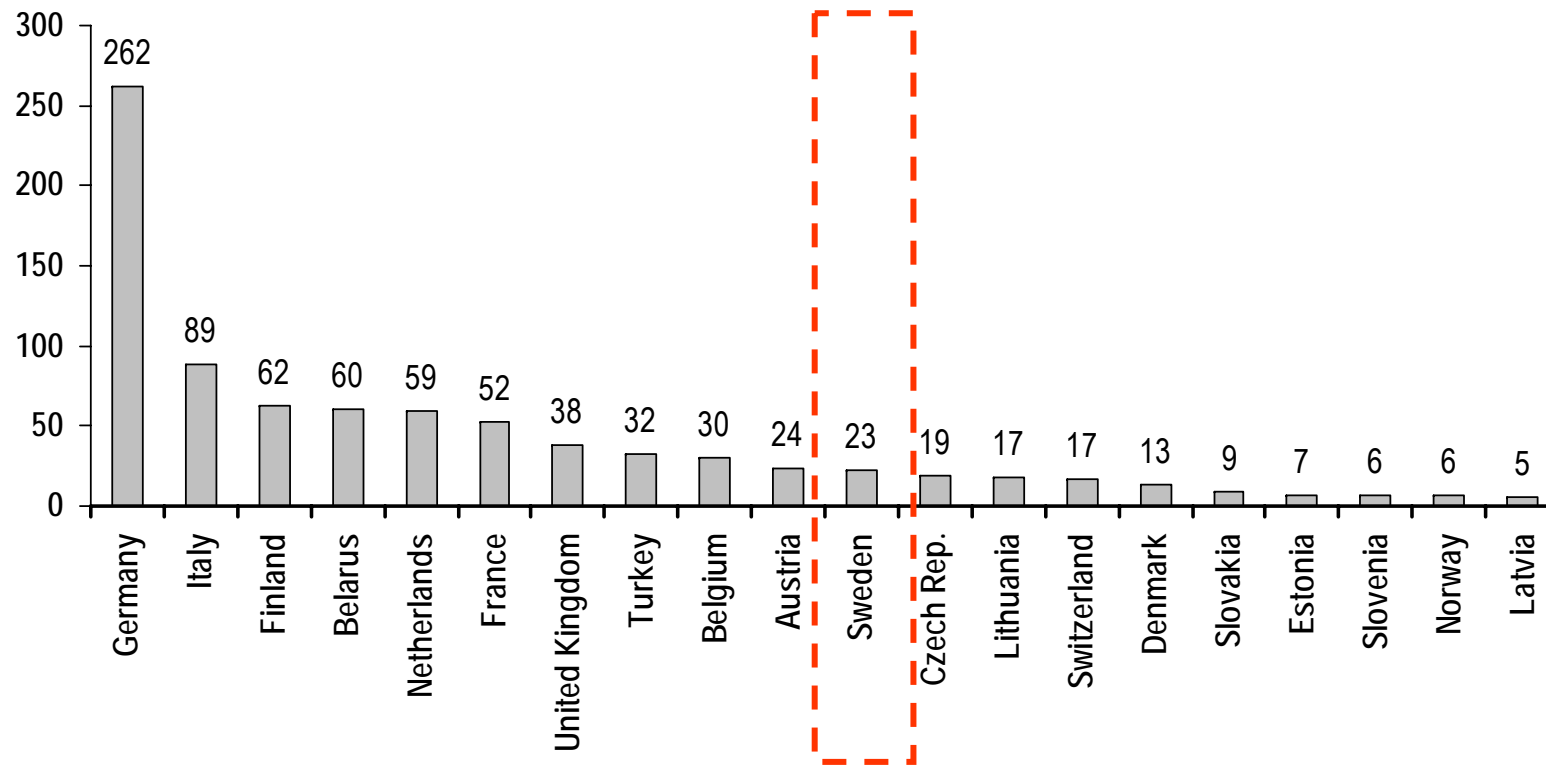
- The share of Swedish exports to Russia compared to total exports increased from 1,6% in 2005 to 2,0% in 2007
- Russia climbed to Sweden's 13th largest export market in 2007 from 14th rank in 2005



SWEDISH EXPORTS TO RUSSIA IS HIGHER THAN DANISH AND NORWEGIAN EXPORTS BUT MUCH LOWER THAN FINISH EXPORT

Export from European countries to Russia 2007

billion SEK*



* Exchange rate 2007 used: 1 SEK= 6,76 USD

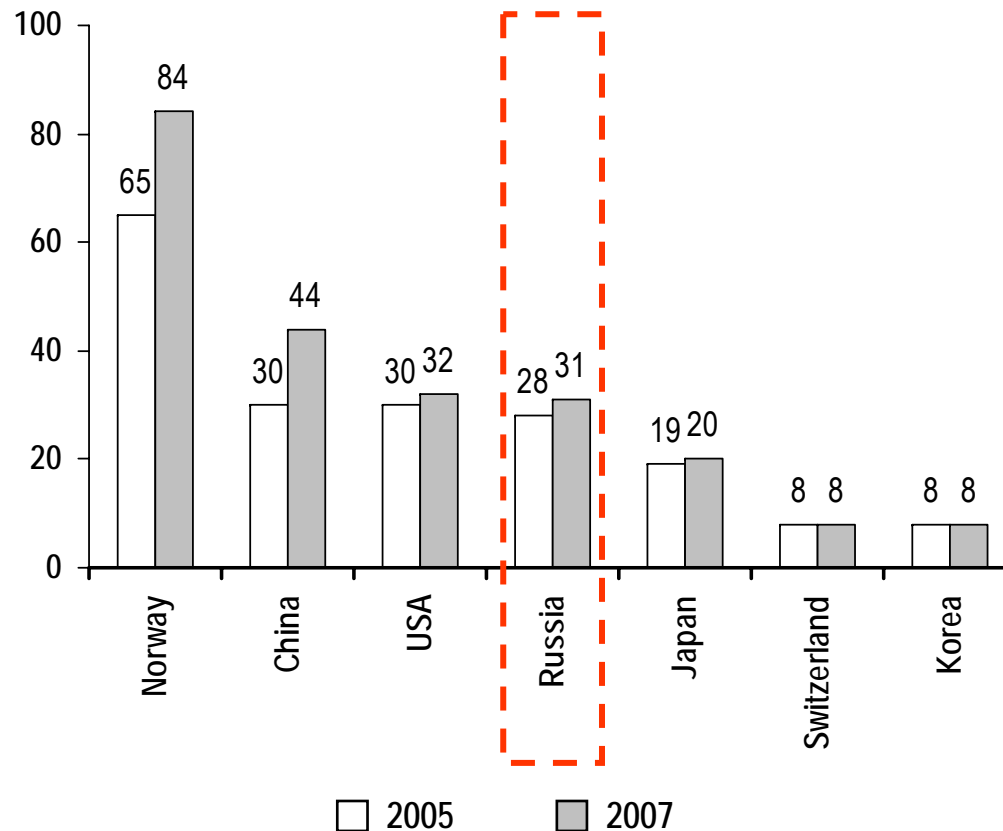
Source: UN Comtrade, SCB/Riksbanken



RUSSIA IS SWEDEN'S FOURTH LARGEST IMPORT MARKET - comparable with Swedish import from USA

Import to Sweden by countries, 2005 and 2007

billion SEK



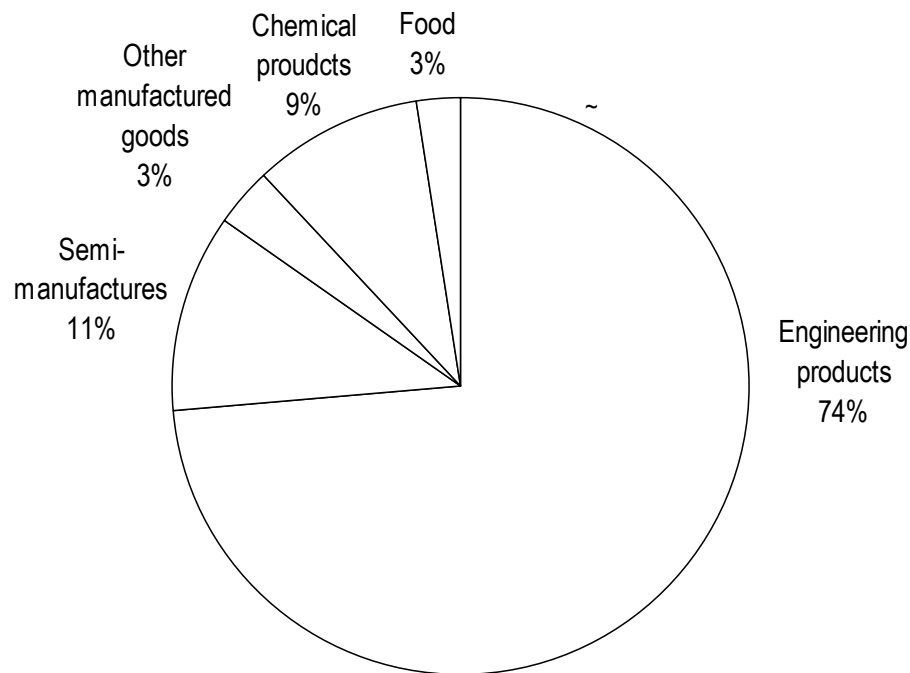
- Russia kept the rank as Sweden's 4th largest import market in 2007
- However, the share of Swedish imports from Russia compared to total imports decreased from 11,3% in 2005 to 10,5% in 2007



SWEDISH EXPORTS TO RUSSIA IS MAINLY ENGINEERING PRODUCTS - imports from Russia is dominated by fuels

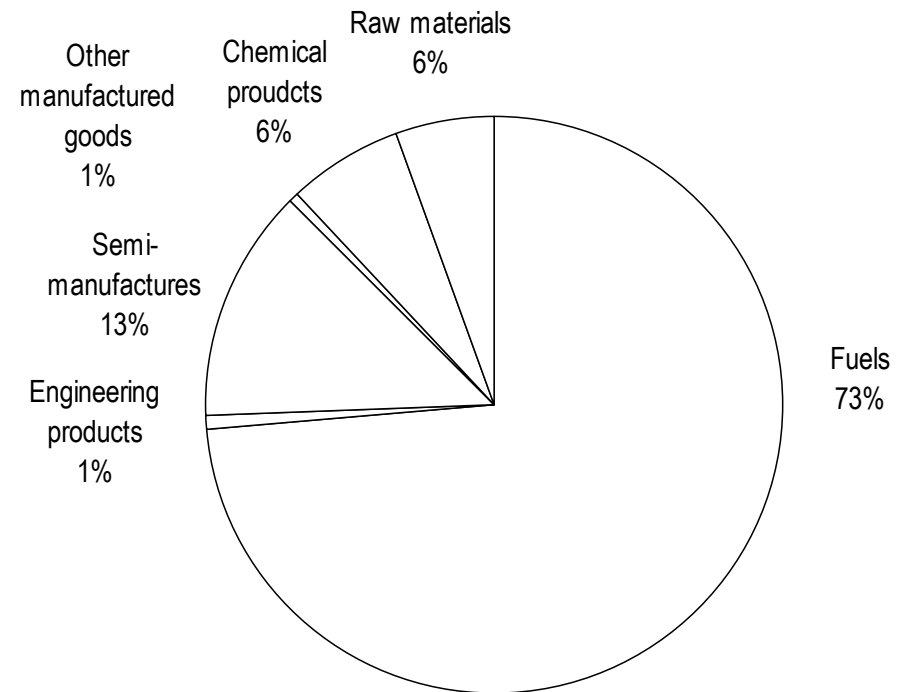
Swedish export to Russia by product category, 2007

Percent, 100% = 22 710 million SEK



Swedish import from Russia by product category, 2007

Percent, 100% = 31 358 million SEK

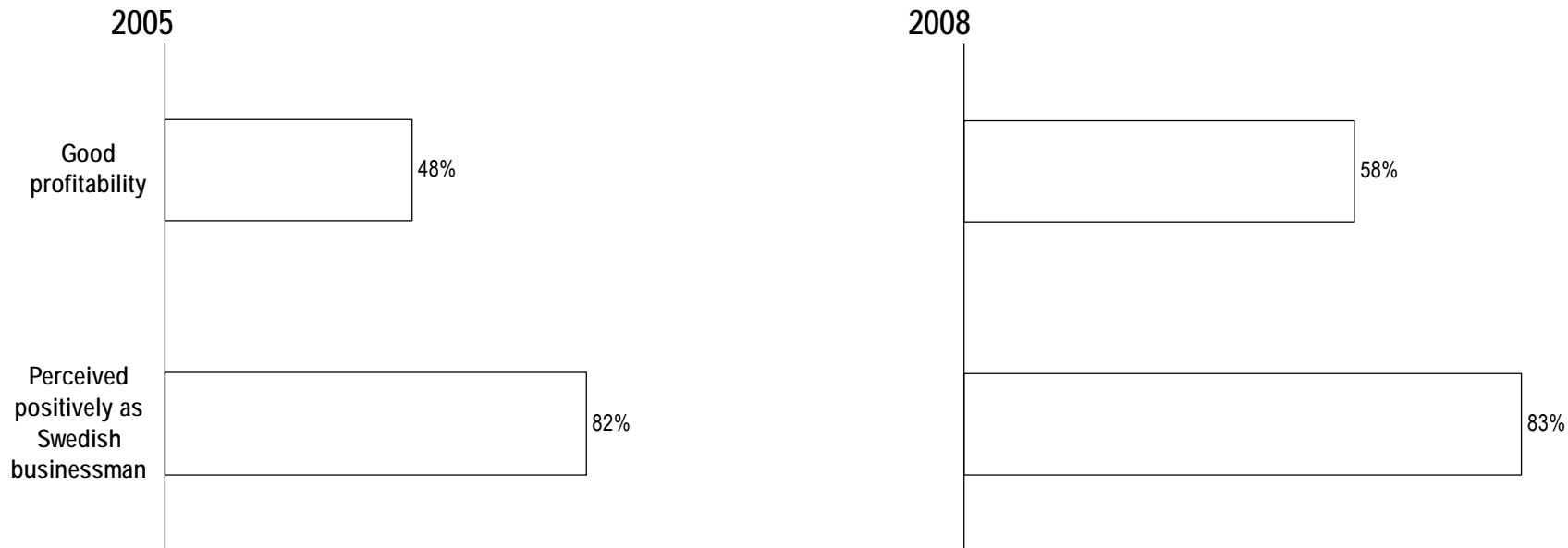




THE PROFITABILITY FOR SWEDISH COMPANIES IS GROWING - as well as the perception of Swedish businessmen

Conclusions

Percent



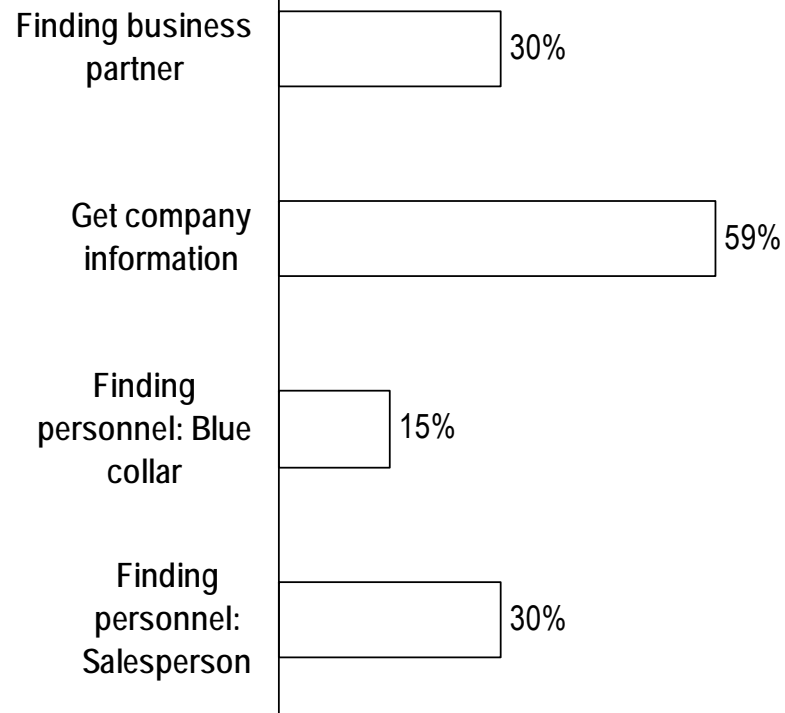


MOST DIFFICULTIES FROM THREE YEARS AGO SHOW IMPROVEMENT - though finding business partner is close to unchanged

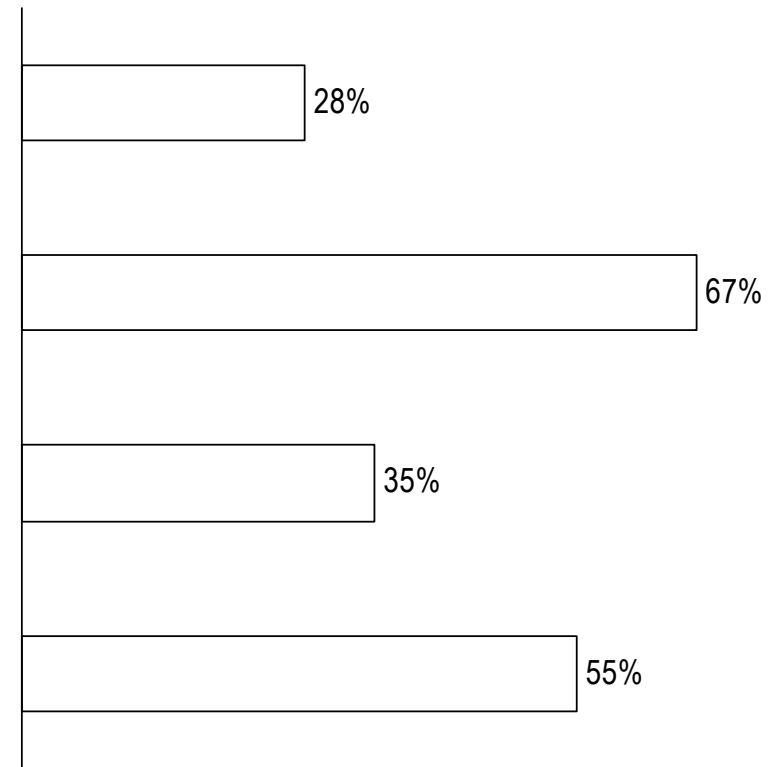
Difficulties observed

Percent

2005



2008



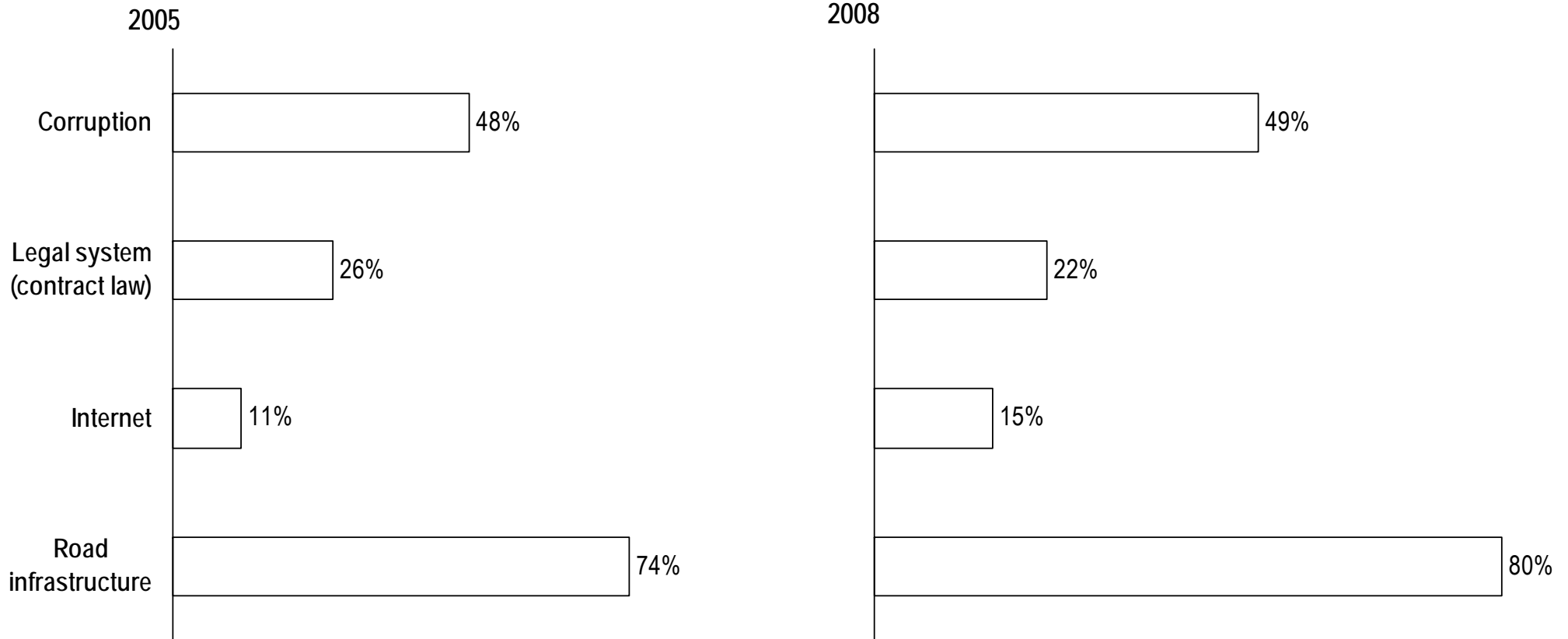


THE LEGAL SYSTEM SHOW IMPROVEMENTS

- though corruption is still obvious

Difficulties observed

Percent

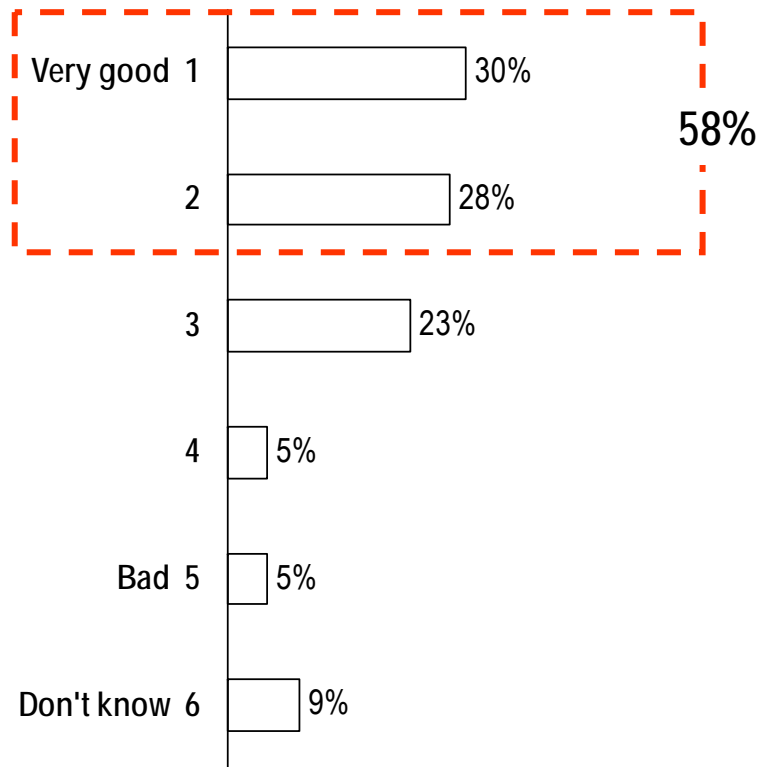




FUTURE GROWTH POTENTIAL LOOKS PROMISING - and so do profitability

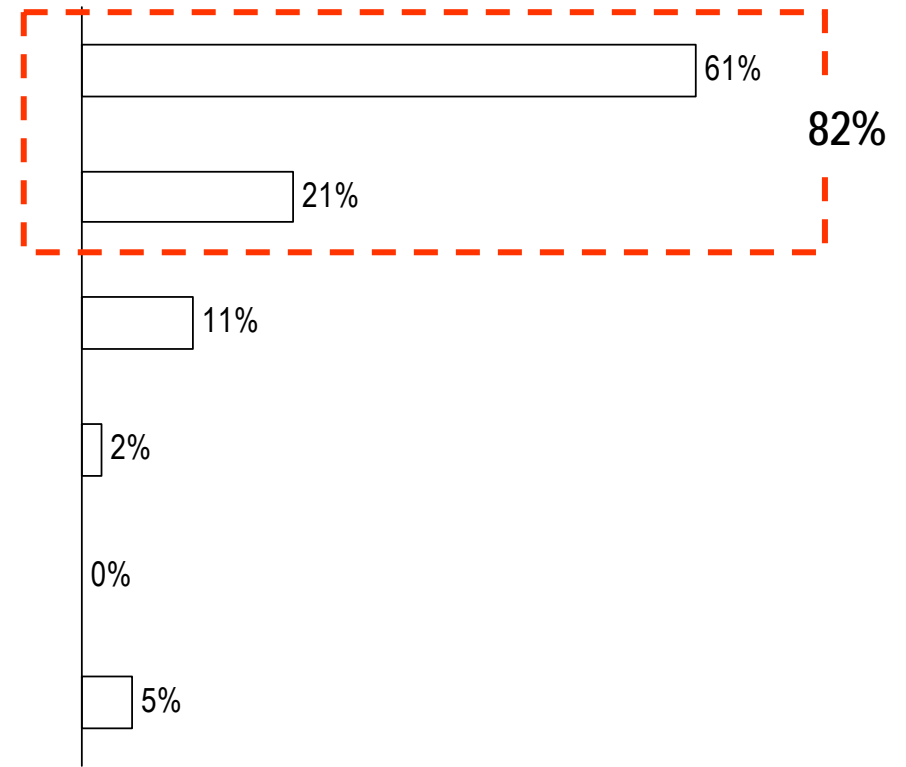
If possible, how do you estimate the profitability in comparison with other markets?

Percent



How do you estimate your company's future growth potential on this market?

Percent

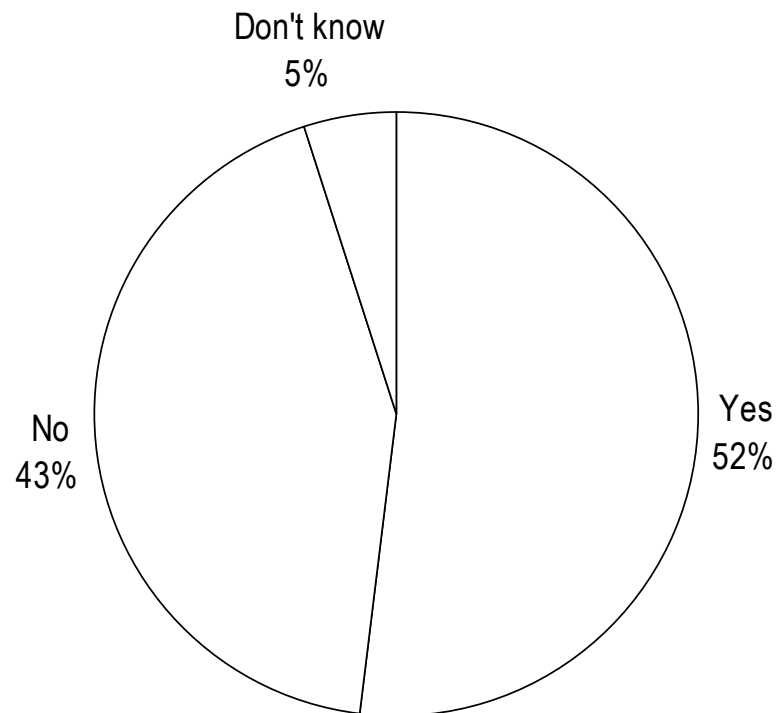




A MAJORITY PLAN TO EXPAND BUSINESS TO THE REGIONS - and the regions are expected to demonstrate the highest growth

Do you have plans to expand the business outside the larger cities/regions?

Percent



- A majority plan to expand their business to the regions
- 13 cities have more than one million inhabitants
- 65 % of the service companies and 50% of the production companies plan to expand their business to the regions



QUOTES AND CONCLUSIONS ABOUT TRENDS AND FUTURE

“The regions are expected to demonstrate high growth and will be important for future business in Russia. Sweden is increasing the export to Russia and is expected to continue the growth.”

“The Russian middle class is growing rapidly and is expected to drive the economy:”

“The Russian industries are investing in modern equipment in order to facilitate domestic refining.”