



Russia's Investment Climate

# 2012

A Survey of Current and Potential Investors





# Russia's Investment Climate 2012:

## A Survey of Current and Potential Investors

September 2012





The mission of the Council is to assist Russia in forging and promoting a favorable investment climate based on global expertise and the experience of international companies operating in Russia.

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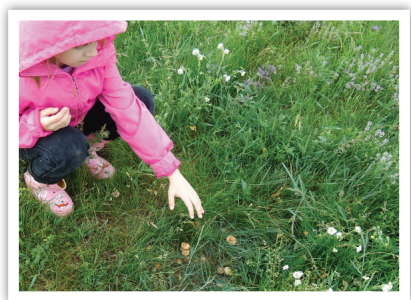
# Introduction

The Foreign Investment Advisory Council (FIAC) commissioned Ketchum to conduct an independent survey of the opinions and attitudes of current and potential foreign investors in Russia and to determine how sentiments have changed relative to 2007, the last time the survey was conducted. Over the past five years, a significant number of high-profile events occurred in Russia that have the capability of significantly impacting the opinions of current and potential investors. Over 100 investors, a statistically significant representation, were surveyed and provided data to inform this report.

In late 2008 and early 2009, Russia experienced its first recession after 10 years of economic growth. Stable growth resumed in late 2009 and 2010. Despite the deep but brief recession, the economy has not been as seriously affected by the global financial crisis as much of Europe, largely because of the integration of short-term macroeconomic policies that helped the economy survive.

In 2011 Russia's gross domestic product grew by 4.2 percent, the world's third highest growth rate among leading economies, third only behind China with 9.5 percent and India with 7.8 percent growth. Russian foreign direct investment (FDI) soared to \$18.4 billion in 2011, a 33 percent increase from 2010, with finance and manufacturing receiving the most capital. Total foreign investment, including loans and flow of capital into the equity market, surged 66% last year to \$190.6 billion, according to the Federal Statistics Service in Moscow.

Russia has a lot to offer foreign investors—from the size of its consumer market to the skilled labor force and availability of natural resources. Also, Russia's accession to the World Trade Organization (WTO) has had a positive impact on investors with almost all respondents (84%) indicating that WTO membership is a persuasive factor for new investment in Russia.



# Methodology

During April and May 2007, FIAC, conducted a survey among current and potential investors to gauge opinions about the investment climate in Russia. In 2012, FIAC commissioned Ketchum to conduct a survey to understand the current foreign investment climate and how sentiments have changed relative to 2007. The survey was developed by FIAC and Ketchum Global Research and Analytics (KGRA), and was designed to replicate, where possible, the HART Research survey of 2007 to allow for comparisons.

The survey was administered online by Braun Research March 15 – April 18, 2012 to a targeted list of company executives with interest in foreign investment. The list contained current and potential investors in Russia, and included both FIAC member organizations and non-members. Over 100 investors, a statistically significant representation from a variety of industries, were surveyed and provided data to inform this report.

In addition to the survey, a global media audit conducted by Ketchum informed this report. The goal of the media audit was to better understand how the foreign investment in Russia was being portrayed in top tier global media outlets and compare those findings with the results of the survey. KGRA reviewed a representative sample of more than 300 news stories published in top tier international newspapers, wires and broadcast reports from January 1, 2011 through January 31, 2012.

A sample of the global outlets included in the media analysis are Agence France Presse (AFP); Asahi Shimbun; Associated Press (AP); BBC; Bloomberg; CNN; Dow Jones; Financial Times (all editions); Handelsblatt; International Herald Tribune (IHT); Nikkei; Reuters; The Economist; The Guardian (U.K.); The New York Times; The Times (London); The Wall Street Journal (all editions); and The Washington Post. A quantitative algorithm and scorecard was created to analyze the articles looking at key metrics such as tone, topic, messaging and reach. The analysis provided insights on how relevant media are reporting the current investment climate of Russia which were compared with the results of the surveys.

# Key Findings

## **Investors find Russia to be an attractive investment destination.**

Companies that invest in Russia are highly satisfied. They feel the investment climate has improved since 2007 and remain keen on continuing to invest.

## **Investors are most attracted to a growing, wealthier middle class; ROI; and natural resources.**

The three most attractive aspects of investing in Russia have not changed since 2007. The order of importance has changed – with the Russian consumer market driving investment followed by the return on investment and availability of natural resources.

## **Perception has shifted as more investors feel Russia does a great deal to attract foreign investment.**

In 2007, only 8% of investors felt Russia went out of its way to recruit and attract foreign investment. In 2012, 35% of investors feel Russia does a great deal.

## **WTO Accession has had the most positive impact on the investment climate.**

Investors (84%) said the fact that Russia is closer to becoming a member of the World Trade Organization is a persuasive factor for new investment in Russia.

## **Negative factors impacting investment remain.**

Investors overwhelmingly felt bureaucracy and red tape (75%); corruption (64%); and lack of infrastructure (37%) have had the most negative impact on the investment climate.

## **Media coverage in 2011 appears to have had a minimal impact on investors' decisions.**

Nearly half (48%) of overall coverage of the investment climate was neutral. Negative coverage (24%) was not as prevalent as positive (28%) or neutral business announcements and investment opportunities. Investors are more reassured (50%) about the investment climate based on media coverage over the past 12 months.





# Survey Participants

## Details about the Current Investors Sample

More than 75% of representative companies have global sales over \$1 billion, including 20% that have sales over \$100 billion. A variety of industries and sectors were represented with nearly 40 Fortune 100 companies disclosing their participation in the survey. In 2011, 61% invested over \$50 million in the Russian market; 16% invested \$500 million or more. More than 77% say they invested the same amount or more in Russia in 2011 than in 2010.

Approximately 38% of representative companies are headquartered in the US; 48% in Western Europe; 7% in Asia. This is on track with the current foreign direct investment mix in Russia. More than a third (36%) of representative companies entered the Russian market before 1991.

## Details about the Potential Investors Sample

Almost half (40%) of potential investors said there is a “fairly good chance” their company would consider investing in Russia within the next 3 years. In terms of entry strategy, potential investors indicated they would prefer to open a representative or branch office, acquire a local company, or pursue a JV partnership with a local company.

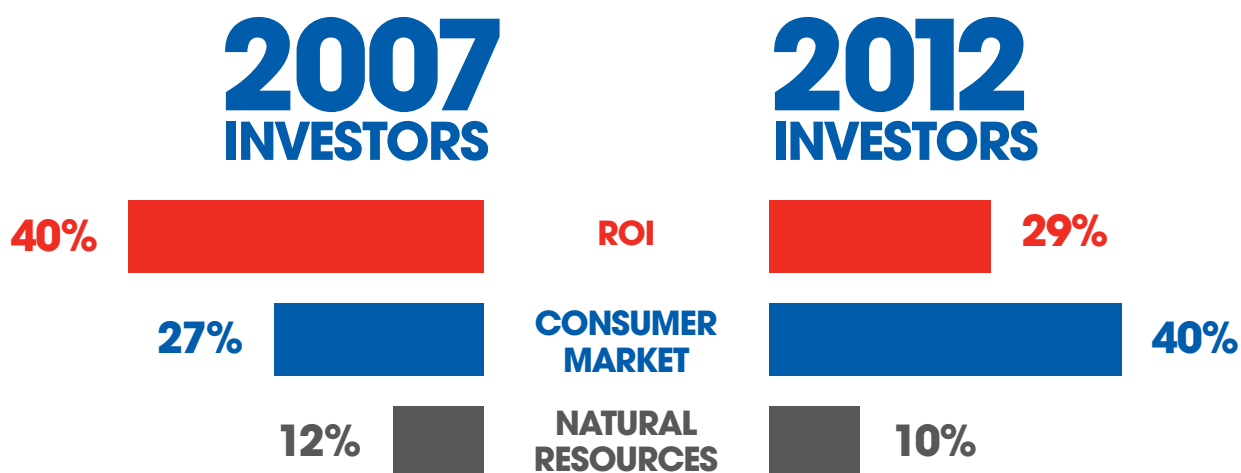
## Industries Represented in Survey Sample

<b>Professional services, consulting</b>	<b>19%</b>
<b>Consumer goods</b>	<b>15%</b>
<b>Banking, insurance, and other financial services</b>	<b>13%</b>
<b>Production of industrial goods and machinery</b>	<b>13%</b>
<b>Retail and wholesale trade, hospitality, and other consumer services</b>	<b>11%</b>
<b>Telecommunications, IT</b>	<b>10%</b>
<b>Oil and gas</b>	<b>7%</b>
<b>Other</b>	<b>12%</b>

# Factors Impacting Investment Decisions

## The Three Most Attractive Aspects Impacting Investment

While the most attractive aspects for investing in Russia have not changed since 2007 (return on investment, consumer market and resources), the order of importance has. In 2007, investors in Russia saw a return on their investment as the most attractive aspect of investing in Russia. Currently, the consumer market is the biggest attraction at 40% (up from 27% of in 2007). The remaining changes to the biggest three attractions include the potential return on investment in Russia – 29% currently, down from 40% in 2007 – and Russia’s energy and natural resources – 10% currently; 12% in 2007. All other factors garner less attention.



## The Strength of the Consumer Market

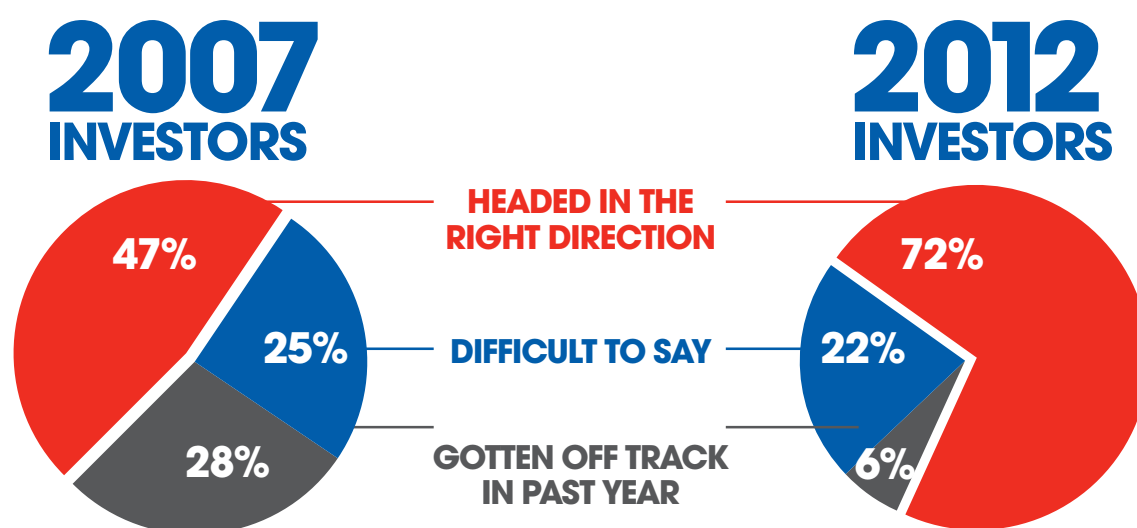
The middle class in Russia has tripled in the last five years to more than 10 million households. Russia has a much smaller population than China, Brazil or India, but each person has substantially more economic consumption power. Current investors note the Russian consumer market as the main driver for their investment and they are focusing their efforts on marketing and advertising (59%) as well as distribution and sales (51%) of their company’s products.

The majority of current investors (82%) find the fact that Russia has a large domestic consumer market with expanding consumer credit, increasing levels of saving, rising real personal incomes, and ranking in the top third of countries in per capita GDP to be a persuasive factors for new investments.

# Factors Impacting Investment Decisions

## Direction of Economic Policies and Laws

The percentage of investors who feel Russia is headed in the right direction in terms of economic policies and laws that encourage foreign investment increased since 2007. Almost three-fourths (72%) of current investors believe that Russia is heading in the right direction, compared with 47% in 2007. It is important to note that sentiment was strong in 2007 regardless, with a two to one margin response that Russia's economic policies and laws were headed in the right direction (47%) rather than the wrong track (25%).



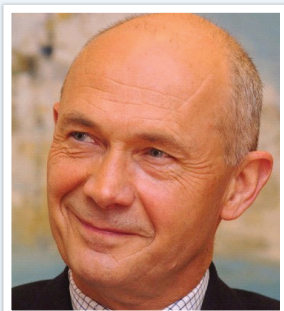
## Spotlight on Economic Policies and Laws

Among the economic policies implemented by the Russian government to encourage foreign investment include the creation of the Russian Direct Investment Fund (RDIF). RDIF was formally established on June 1, 2011. Russia's government has committed to provide \$2 billion to the RDIF annually for five years. The formation of the RDIF is part of a broader initiative underway to modernize Russia's economy. This includes additional efforts to improve the investment climate, promote the development of innovation-driven industries and transform Moscow into an international financial center. All of these economic policies have contributed to the increase in the investor sentiment that Russia's economic policies and laws are heading in the right direction.

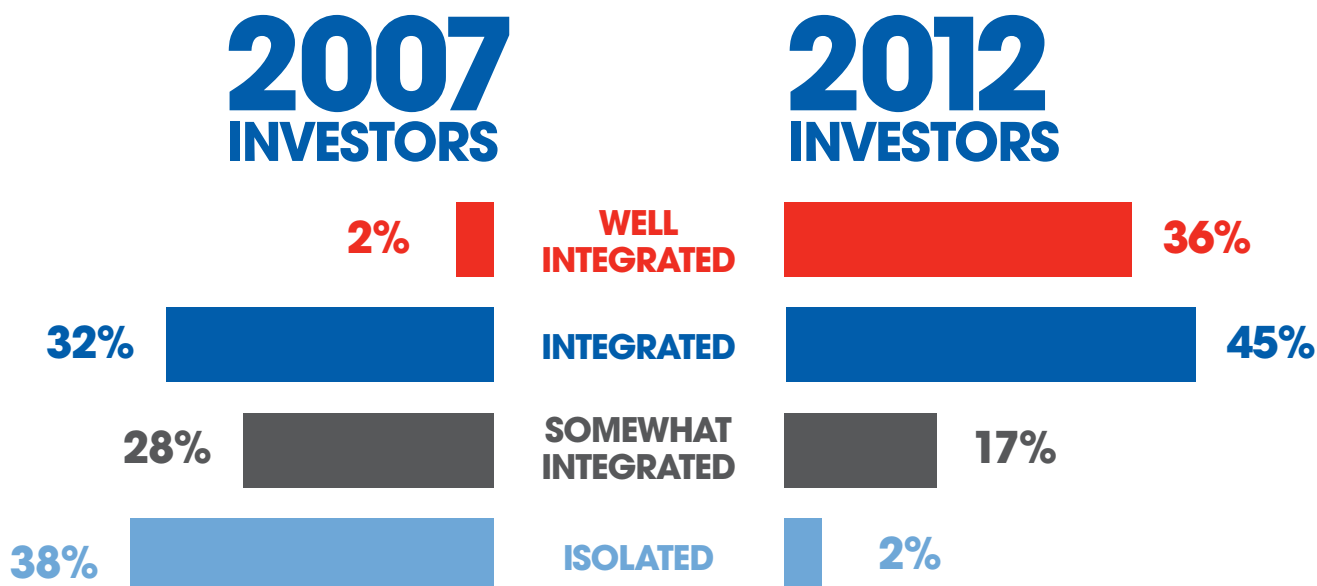
# Factors Impacting Investment Decisions

## Russia's Integration into the Global Economy

Investors believe that Russia has become more globally integrated than in 2007 up to 36% from 2%. Russia's accession to the World Trade Organization is a contributing factor to the sharp increase in investors' perceptions that Russia is more globally integrated.



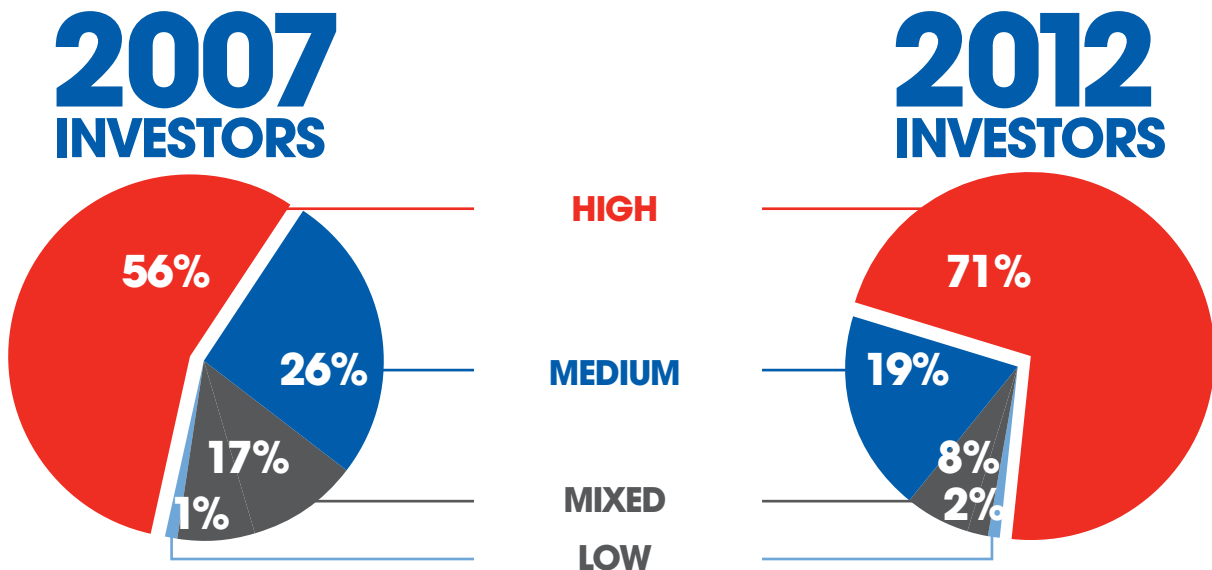
**Pascal Lamy**, the WTO director general, said that the agreement would “cement the integration of Russia into the world economy” and that it “affixes the WTO quality label to the Russian Federation.” Likening Russia's long journey to membership to a marathon, he also warned that “once you cross the finish line, attention immediately changes to the future, to implementation.”



# Foreign Investors' Attitudes Towards Russia's Investment Climate

## Investor Satisfaction

Companies that invest in Russia are highly satisfied. They feel the investment climate has improved since 2007. Investors recognize the challenges of bureaucracy, red tape and corruption, but they remain keen on continuing to investment. Most current investors are highly satisfied (71%) with their decision to invest in Russia. Very few (2%) report a low level of satisfaction.



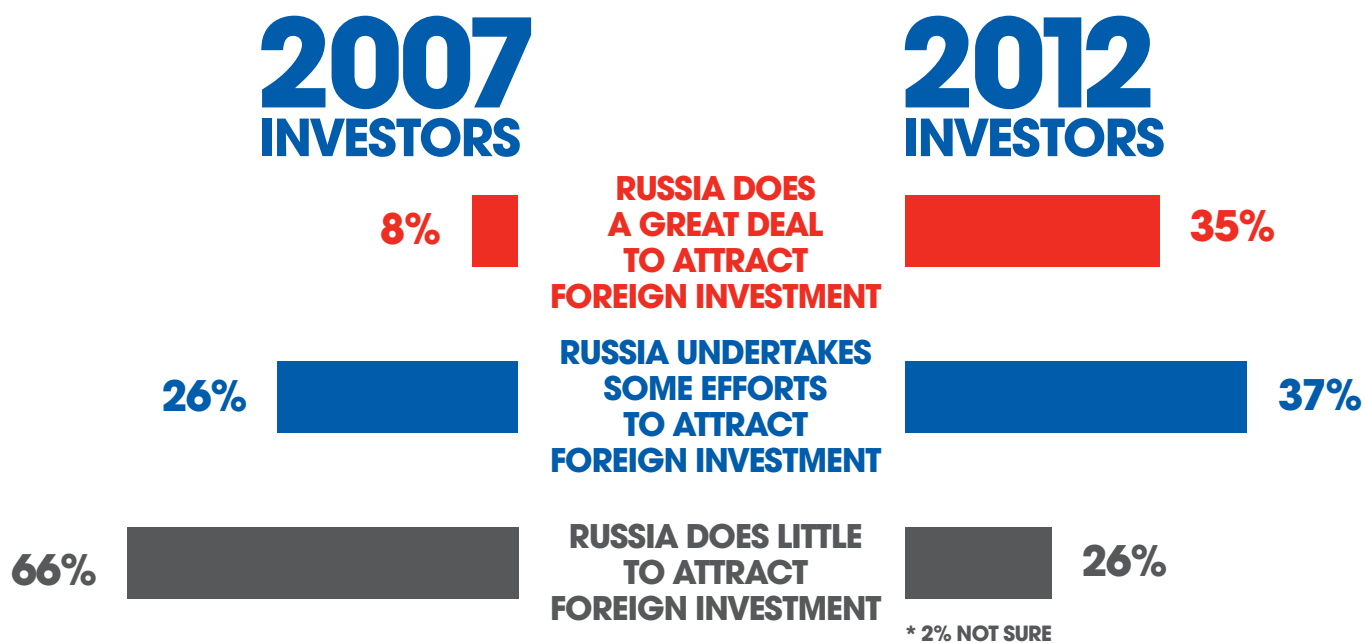
### High Level of Satisfaction Leads to Increased Investment

Current investors are highly satisfied and keen to expand their investments in Russia as one-third (34%) of the respondents surveyed invested more in Russia in 2011 than in 2010. Current investors feel increasingly confident that they understand the market and are able to leverage consumer demand, availability of natural resources, skilled labor, convenient geographic location and the variety of opportunities that are expected to come with Russia's accession to the WTO.

# Foreign Investors' Attitudes Towards Russia's Investment Climate

## Evaluation of Efforts to Recruit Foreign Investment

In 2007, whatever sense the Russian government had of their effort to attract foreign investment, two thirds of investors did not recognize those efforts. In 2007, only 8% of investors felt Russia went out of its way to recruit and attract foreign investment. In 2012, 35% of investors feel Russia does a great deal. This data highlights the importance of the Russian government effectively communicating its commitment to attracting foreign direct investment.



### Opportunity to Enact Policies to Further Strengthen the Investment Climate

Investors believe that the government can and should play a positive role in changing the investment climate for the better. With changes in the Government and the Kremlin this year, there is a strong opportunity to enact policies that clearly and credibly address investors' concerns about bureaucracy and corruption and reinforce their positive impressions about smart macroeconomic policies.



# Foreign Investors' Attitudes Towards Russia's Investment Climate

## Positive Investment Factors

Russia's accession to the World Trade Organization has had the most positive impact on the investment climate. Other factors positively impacting the investment climate in Russia are the macroeconomic situation (51%) and access to qualified personnel (37%).



**Alan Mulally**, president and CEO, Ford Motor Company. "The completion of Russia's negotiation to join the WTO will create far more certainty and protection for investors and exporters while generating new opportunities in what is soon expected to be the largest auto market in Europe. With one of the fastest growing economies in Europe, Russia represents a strong market for Ford products as we grow our global business. Russia's membership in the WTO will be good for trade, good for jobs, and good for investment."

- Ford Statement on Russia's WTO Agreement 10 November 2011

## 2012 INVESTORS

### WTO ACCESSION



### MACROECONOMIC SITUATION



### ACCESS TO QUALIFIED PERSONNEL



# Foreign Investors' Attitudes Towards Russia's Investment Climate

## Negative Investment Factors

Some of the biggest barriers to a strong investment climate in Russia cited by investors are largely attributable to the government. Investors overwhelmingly felt bureaucracy and red tape (75%); corruption (64%); and lack of infrastructure (37%) have had the most negative impact on the investment climate.

## 2012 INVESTORS

### BUREAUCRACY AND RED TAPE



### CORRUPTION



### POOR, WORN INFRASTRUCTURE



## Addressing Investors' Concerns

In responses to various questions – whether viewing Russia on its own or comparing it to other countries – investors consistently expressed serious concern with the level of corruption in society; bureaucracy and red tape; fair interpretations and application of laws; and protection of property rights. Perhaps more so than ever before, Russia must make consistent and credible efforts in addressing corruption, rule of law and bureaucracy if is to create a strong, competitive and attractive investment climate over the long term.

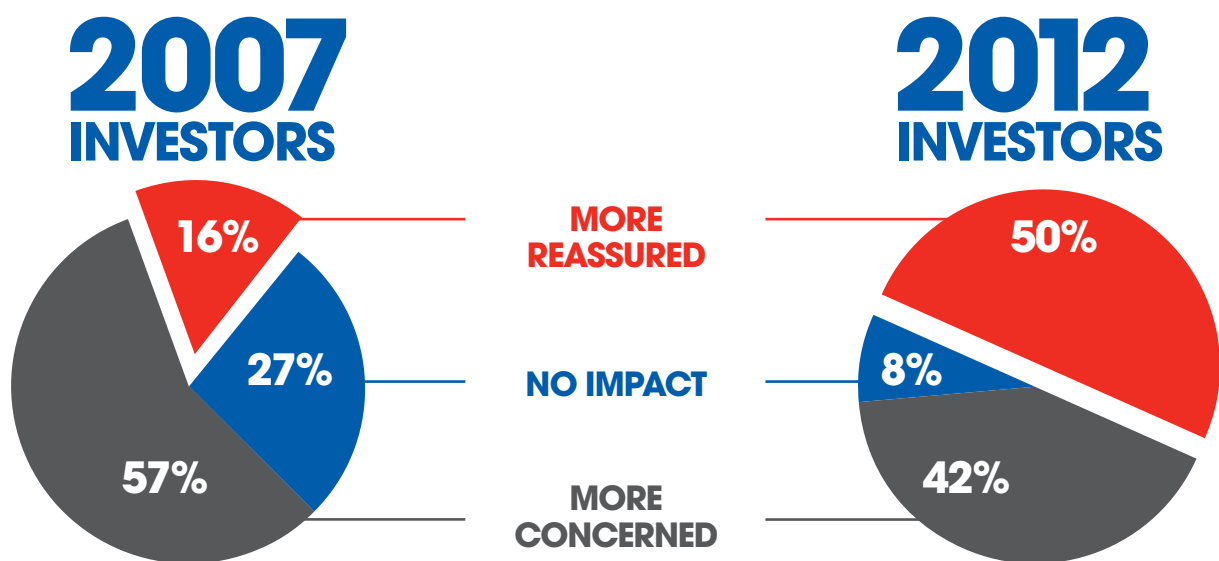




# The Impact of Media Coverage on Investors' Attitudes

## Impact of Media Coverage

When respondents were asked how the news coverage they have read and heard over the past 12 months has impacted their feelings about Russia's investment climate, half of all 2012 investors (50%) felt more reassured. As compared to 2007, only 16% of investors felt more reassured by media coverage.



## Russia Bolstered by Global Economic Crisis

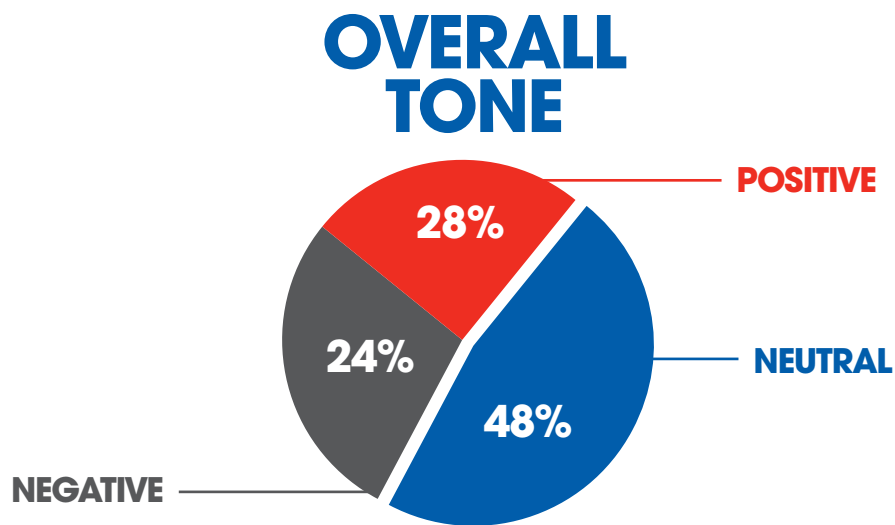
Media coverage of discussions about the economic uncertainty in the developed world often included mentions of Russia. Russia's accession to the WTO was the primary driver of those conversations, with promoters and adversaries both comparing Russia with the rest of the developed world. Those speaking positively about Russia focused on the investment opportunities available in Russia (as well as other emerging markets) in a time when the Eurozone is facing financial uncertainty and crisis, thereby reassuring investors about opportunities in Russia.

At the same time, Russia's reputation also appeared to be bolstered in the media by initiatives such as Skolkovo and the Sochi 2014 Winter Olympics. These events were referenced with regard to Russia's innovation and infrastructure and the importance that the government has placed on them.

# The Impact of Media Coverage on Investors' Attitudes

## Tone of Media Coverage

In general, media coverage appears to have a minimal impact on investors' decisions. Nearly half (48%) of overall coverage of the investment climate was neutral. Negative coverage of protests was not as prevalent as positive or neutral business announcements and investment opportunities.



Overall, media coverage was neutral and the political protests have had minimal impact on investment decisions.

## Topics Driving Media Coverage

- **WTO Accession.** A large portion of the positive coverage stemmed from coverage of Russia's accession to the WTO.
- **Business announcements.** A majority of all coverage was neutral to positive due to the heavy media coverage of financial results and business investments (Sochi 2014 investments, auto and pharmaceutical industry successes).
- **Elections, protests and capital outflows.** Three out of five negative posts concerned financial issues and the Duma elections. Negative media coverage spiked in September 2011 ahead of the presidential elections but more directly ahead of the Duma elections.



# Russia's Key Strengths

## Positive Messages about Russia

Respondents were asked to review a number of pro-investment messages about Russia and rate the most persuasive messages. Respondents indicated Russia has a host of strong pro-investment messages that it can deliver to improve the investment climate as a majority of the surveyed investors rated all of the messages as extremely or quite persuasive reasons for investing. The most persuasive message (80%) is that Russia is “poised to become member of World Trade Organization: compete as equal in world markets, and further integrate into global trade system.”

**2007**  
INVESTORS

**2012**  
INVESTORS

### POISED TO BECOME MEMBER OF WTO



### CURRENT FOREIGN INVESTORS RATE HIGHLY AS PLACE TO INVEST



### STRONG BASE OF TECHNOLOGICAL AND SCIENTIFIC POTENTIAL DRIVEN BY STRONG EDUCATION SYSTEM



### READY SUPPLY OF AFFORDABLE ENERGY



# Russia's Key Strengths

In addition to the aforementioned positive message about Russia's accession to the WTO, messages about the large consumer market (78%), growth in GDP (68%) and the highly educated work force (65%) are also extremely persuasive to investors. While the percentage of support for each of these messages may appear to have dropped slightly since 2007, the investors still find the messages to be quite strong, with more than two-thirds of investors responding that each of the messages are extremely persuasive. The decline from 2007 to 2012 is because investor sentiment shifted to supporting messages regarding Russia being poised to become a member of the WTO. However, these other messages still remain quite convincing and resonate with investors.

**2007**  
INVESTORS

**2012**  
INVESTORS

## LARGE CONSUMER MARKET



## STABLE ECONOMY WITH SUSTAINED GDP GROWTH



## HIGHLY EDUCATED WORK FORCE, HIGH PRODUCTIVITY



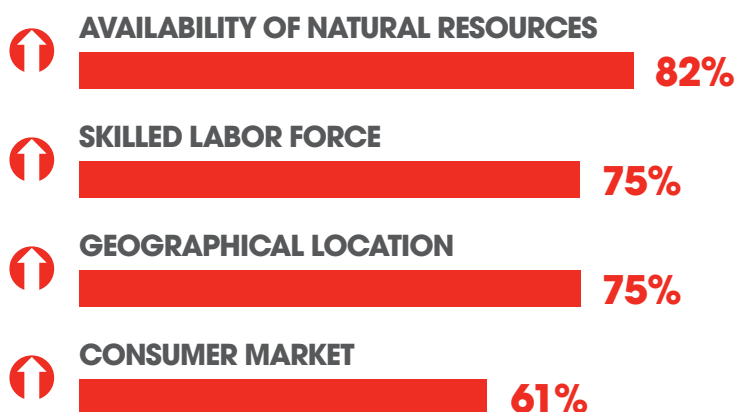
## GOVERNMENT HAS EFFECTIVELY TRANSITIONED TO CAPITALIST MODEL



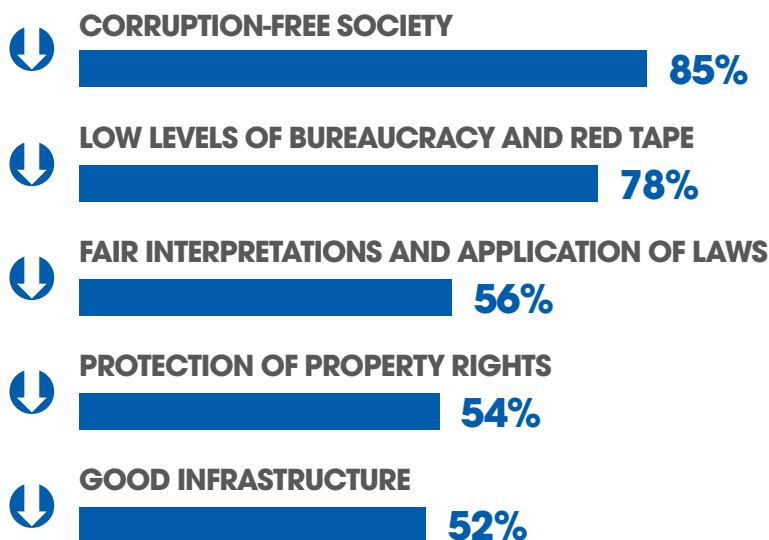
# Russia Compared to Other Emerging Markets

Russia is similar to other emerging markets in several ways, but can differentiate itself by focusing on its strengths and downplaying the weaknesses.

## Four areas where investors believe Russia is well ahead of other emerging markets:



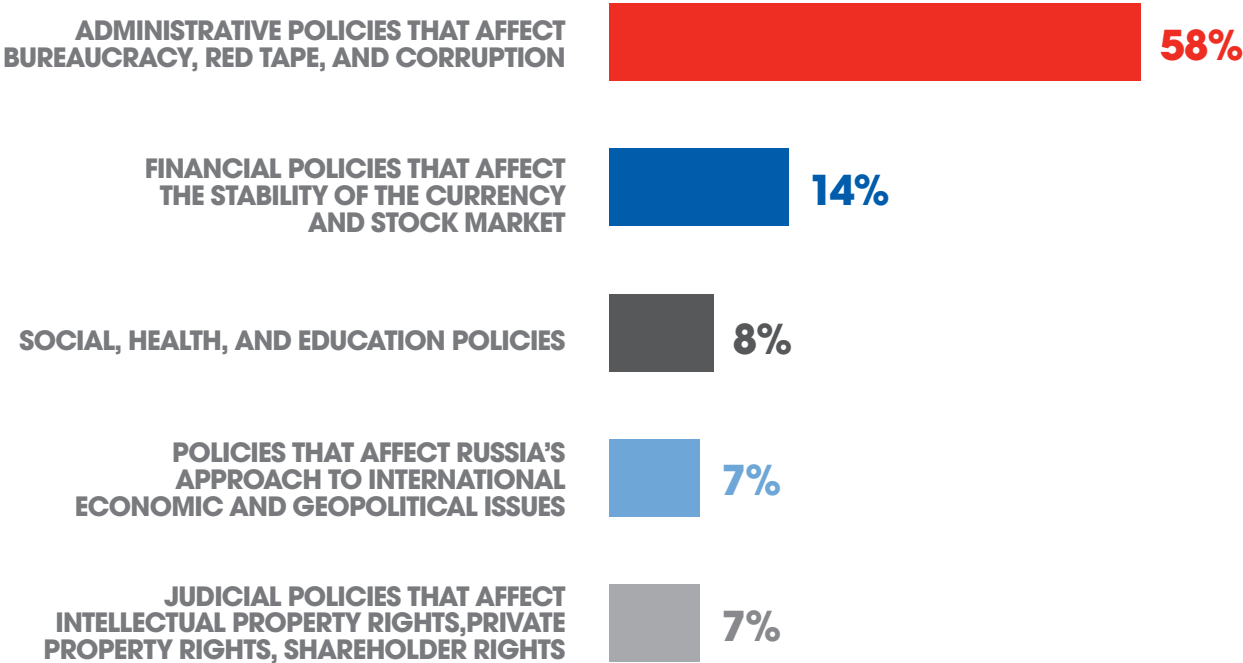
## Primary areas where Russia lags well behind other emerging markets:



# Recommendations

When asked which one area the Russian government should focus on first if it wants to improve the country's investment climate, a majority (58%) of investors agreed the government should focus on improving administrative policies that affect bureaucracy, red tape, and corruption.

## 2012 INVESTORS



In order to improve these factors, the government should continue to make clear and consistent efforts to improve the business environment as well as showcase market opportunities. The key to implementing the recommendations that follow is to show measurable results and progress on a specific timeline.



# Recommendations

## Suggested Roadmap

In order to continue to improve the investment climate in Russia, the following policy, government, and communications recommendations should be implemented.

	Near term	Long term	Ongoing
Policy and government initiatives	<ul style="list-style-type: none"> <li>Enforce existing legislation aimed at cutting red tape, bureaucracy and corruption.</li> <li>Ease short-term visa regime for business and scientific cooperation.</li> <li>Clarify the course and scope of economic and regulatory reform aimed at modernizing and diversifying Russia's economy.</li> <li>Make Skolkovo a physical and virtual platform for business and scientific collaboration in Russia.</li> <li>Support consumer market with higher level of broadband penetration.</li> <li>Demonstrate support for fundamental sciences, language and business education to sustain high level of domestic workforce.</li> <li>Ease the process of setting up new businesses, including access to infrastructure and domestic credit markets.</li> </ul>	<ul style="list-style-type: none"> <li>Demonstrate support for internal consumer markets – including tech innovation in key industries like energy, mining, transportation.</li> <li>Leverage R&amp;D presence and investment of the biggest global corporate players in Russia to support development of highly skilled and productive domestic business workforce.</li> <li>Ensure major universities and Skolkovo power business and technology innovation clusters, support international exchange programs.</li> <li>Ensure college graduates have good foreign language and management skills.</li> </ul>	<ul style="list-style-type: none"> <li>Invest in better public services and infrastructure.</li> <li>Create a number of global FDI and R&amp;D partnerships with the largest companies, where Russia plays a unique role.</li> <li>Create a stable and business-friendly environment to encourage FDI and thus improve long-term economy growth prospects.</li> <li>Encourage largest Russian companies to invest in R&amp;D and innovation to support domestic demand and the market.</li> <li>Guarantee protection of IP rights, introduce more robust anti-corruption measures and enforce anti-piracy laws.</li> </ul>
Communications	<ul style="list-style-type: none"> <li>Devise and execute briefings by government representatives with financial and media community showcasing readiness for FDI.</li> <li>Celebrate Russian corporate success by introducing a pool of “ambassadors” to present Russian business success stories abroad.</li> <li>Leverage the Sochi Olympics to promote Russia's innovation and growth.</li> <li>Create and implement a six-year plan to track progress against World Bank's Ease of Doing Business scorecard.</li> </ul>	<ul style="list-style-type: none"> <li>Encourage higher levels of participation and engagement of senior government officials in high profile investment in Russia (i.e. launches of investment projects, production facility openings).</li> <li>Show that Russia is open for business and FDI.</li> <li>Focus PR efforts on Russia's main asset and differentiator - its people - highly educated workforce able to support global businesses in favourable geographic location development.</li> </ul>	<ul style="list-style-type: none"> <li>Demonstrate steps taken to remove long-standing structural impediments to growth and foreign investment.</li> <li>Clearly indicate Russia's long term commitments to improvement of business environment, targets and goals for FDI.</li> <li>Showcase ongoing progress in terms of economic diversification, and the creation of favorable business environment for domestic and foreign players alike.</li> <li>Work in tandem with FIAC and foreign business organizations to promote investment</li> <li>Promote the office of the investor ombudsman.</li> </ul>

## What Does Success Look Like?

- Russia's economy is well diversified and is one of the major FDI destinations globally.
- Russia is praised for being a strategic global partner for the largest international companies, moving up to 20th place in the World Bank's “Ease of Doing Business” survey.
- Russia becomes an exporter of intellectual services and high tech products, based on its tradition and the ability of its workforce to deliver on the world's most challenging projects. There are both internal and external markets for Russian industrial products and services.
- Moscow is viewed as a major global financial center.
- Russia gains renown for a number of identifiable business successes and high return on FDI investment.



# Notes





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