



Success in Doing Business in Russia

POTENTIAL, OBSTACLES AND PRACTICAL APPROACH

April 2007

This presentation treats:

1. Significance of Russia for us;
2. The potential and obstacles of the Russian economy;
3. A practical approach to success on the Russian market;
4. Conclusion and answers to your questions.



A. Our perception

- Mafia – Oligarchs;
- Cold;
- Russian bear;
- Risks and danger;
- Unreliable;
- But, a positive exception: culture!



B. Russian reality

1. Politics:

- Parliamentary (2007) and presidential (2008) elections (but no great changes expected);

2. Society:

- Growing difference between rich and poor / Neglect of crucial sectors;

3. Cultural:

- Eurasian – slavic / No sense of individuality / Pride;

4. Economic:

- Oil and Gas / Purchasing power / Growth in many sectors.



C. The significance of Russia for us:

- Necessary partner that wants to (and should) be treated as equal.

WHY?

- Geopolitical significant area that moves more and more towards China and India;
- A market and a source of natural resources that we cannot ignore (over 50% of Russia's foreign trade is with the EU).

D. Demographic and geographic figures

- 143 million people;
- 17 million km² (roughly 400 times the Netherlands);
- 11 time-zones;
- Natural resources:
 - Oil = 13% of total world explored resources;
 - Gas = 34% of total world explored resources;
 - Oil, natural gas, metals and timber account for more than 80% of exports and 32% of governments revenues.



E. Economic environment

- High world energy prices boost growth;
- GDP 2006 = € 564 bln (Netherlands = € 471bln) / growth 2006 = 6.6% / 2007 = 6% (est.);
- Inflation 9.8% (2006);
- 30% of economy in grey sector and not accounted for;
- Negotiations on WTO accession in its final stage;
- Average salary 2006 was \$437 (27% higher than in 2005);
- Increase in purchasing power;
- 6.6% unemployment (2006) and 16% of the population (23 million) lives below the official subsistence level of \$95.

A. Potential

- A market of 143 million consumers with strong demand both for modern technology and equipment, consumer and industrial goods:
 - 15% of population has high purchasing power;
 - Income is concentrated in large cities in Western Russia;
 - 75% of household income is spent on consumption;
 - Real disposal income rises 10% per year;
 - 103.000 millionaires and 53 billionaires;
 - The aggregate net worth of Russia's 100 richest businessmen rose to U.S. \$248 bln in 2006 from \$141 bln in 2005;
 - Foreign capital inflow (2006): \$ 41 billion.
- **There are many successful foreign businesses active in Russia!!**



B. Developing Sectors of the Economy

- Oil & gas, energy;
- Agribusiness;
- Manufacturing;
- Services;
- Trade.

Fastest growth

- Retail sector;
- Automotive and automobile;
- Packaging;
- Construction materials;
- Telecom & IT;
- Logistics.



C. Will Russia remain stable?

- Continuing income from oil and gas;
 - (Account for 20% of GDP)
- Low level of consumer credits and mortgage lending (The Russian owns his house, car, dacha);
- Consumptive spending can be easily (temporarily) reduced by the Russian consumer;
- Consumption over democracy (small risk of political instability).

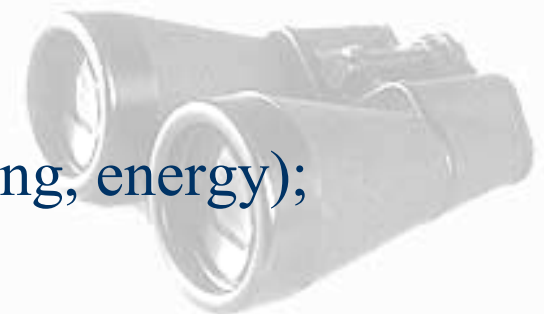
D. What do you hear from Moscow's Expats?

- Returns higher than anywhere else:
 - Stock market 2006 ↑↑ 71%;
 - Gazprom capitalization from \$30 bln to \$300 bln in 3 years;
 - Upgraded country ratings (BBB, BAA2).
- It takes determination, flexibility, stamina and hard work but success in Russia is very well possible;
- The foreign media are much too negative;
- Russia is not more difficult than China;
- B*R*IC.



E. Successful in Russia I

- Independent Media (publishing);
- Baruch (clothing);
- AMS (advertising);
- Direct Star (telemarketing);
- Impress Media (real estate related publishing);
- Feadship and Dutch yacht builders (luxury and super yachts);
- Stroymoda (office partitioning and furniture – Ahrend);
- KPV Story (construction);
- Juralink (legal services);
- Provimi;
- The Lighthouse Group (B2B services, publishing, energy);
- Etc.



E. Successful in Russia II

- ABN AMRO, ING, Rabobank;
- Campina;
- Unilever;
- Shell;
- Frans Maas;
- Akzo Nobel;
- Heineken;
- Philips;
- Tebodin;
- Etc.



F. Obstacles

- Lack of qualified staff;
- Poor physical infrastructure (gas, water, electricity, heat);
- Poor enforcement of contractual and ownership rights;
- Administrative and legislative ambiguity (bureaucracy);
- Small SME sector and weak financial sector (enabling environment);
- Lack of management skills in many sectors;
- Strong entrenched “informal” networks between legislative, executive, judiciary and business and protectionist attitude;
- Corruption;
- Unbalanced economy.



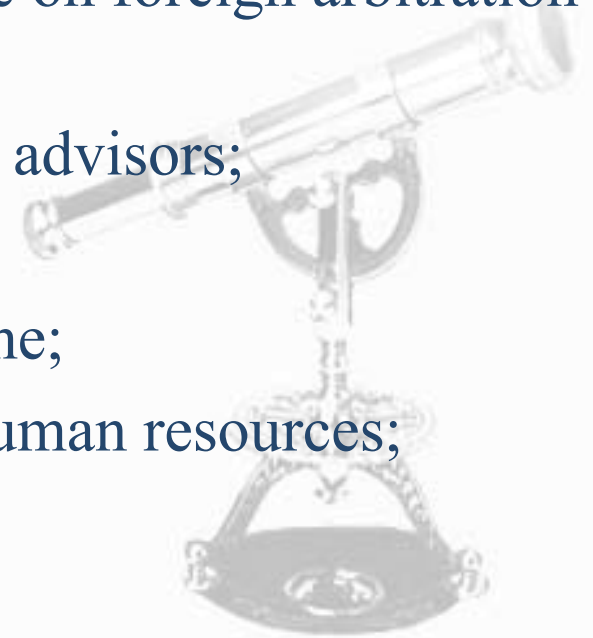
A. What is the secret of success of foreign companies in Russia?

- They are there and they are committed;
- They like it;
- They understand Russia and its potential;
- They are ready to be flexible;
- They are entrepreneurial.



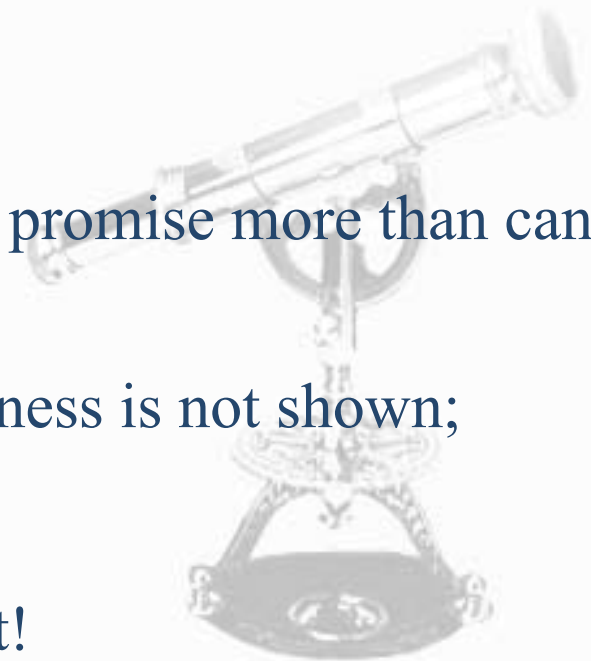
BI. Do's

- Enjoy Russia!
- Gain some knowledge of Russian language and culture;
- Do your homework and know the market;
- Stay in control (of finances and management);
- Divide the shares/interests off-shore and agree on foreign arbitration to create win-win situations;
- Use experienced local (general, tax and legal) advisors;
- Limit your exposure;
- Understand that success in Russia requires time;
- Dedicate and commit sufficient financial & human resources;
- Be flexible;
- Understand the Russian perspective!



BII. Understand the Russian perspective

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



C. Don't

- Underestimate the market or your Russian business partner;
- Think Russia is Europe;
- Think Russia is cheap;
- Hurry;
- Think it's easy to find the right staff;
- Let yourself in with corruption (payments on the basis of contracts or through third parties);
- Compromise on your business ethics;
- Give immediate exclusivity to distributors;
- Be inflexible;
- Forget to register your trademark.



D. Practical issues to be considered when starting up in Russia

- Movement of capital and equipment subject to certain restrictions;
- It is difficult to attract external financing for Russian projects;
- Prepare for different bureaucratic procedures;
- Don't forget your visa;
- Don't forget to have your passport on you at all times.



E. Practical issues II – 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 cost 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. Problems with exports

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

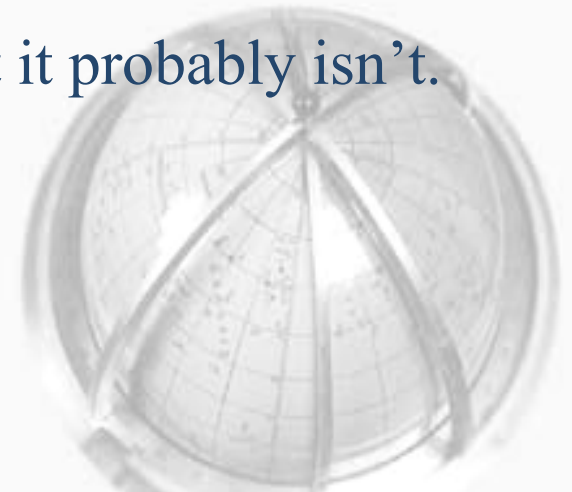
Therefore important:

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



G. Russian partner

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



Conclusion and questions – Why Russia??

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

BUT

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

POLL SHOWS FOREIGN MANAGERS MORE OPTIMISTIC ON INVESTING IN RUSSIA

An opinion poll by PBN Company of top managers, board members and shareholders of 155 international companies either investing in Russia or considering such investment shows optimism. Most respondents believe that 2005 was favorable for foreign investment in the Russian economy, 94% of the companies surveyed plan to expand their operations in Russia in the next three years and 91% plan to increase their investment in Russia, up from 78% and 71% last year, respectively.

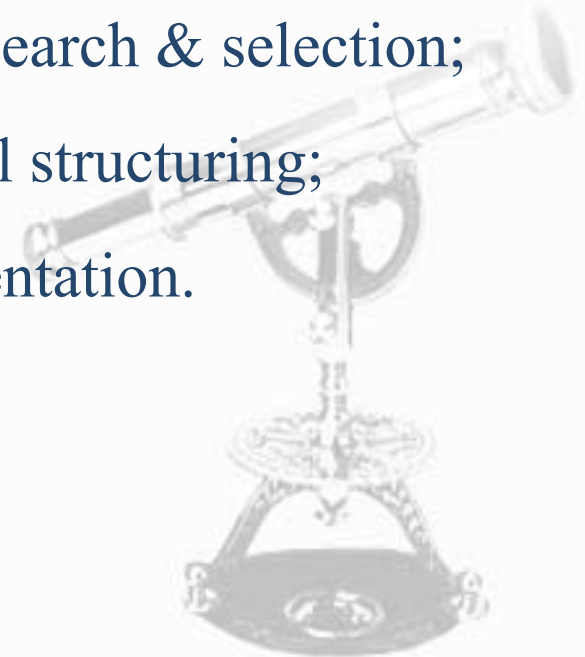
In addition, more than half of respondents believe that the investment climate in Russia's regions has improved, while 14% claim that it has become worse. The PBN company conducted the opinion poll for the Russian government's council on foreign investment and Russia's Economic Development and Trade Ministry.

Approach to Russian Market

- Step-by-step approach;
- Practical;
- Local assistance/partner;
- Limited investment size;
- Low-key.

Typical steps to be taken

- Information gathering;
- Business case development;
- Partner search & selection;
- Financial structuring;
- Implementation.



Tax environment

- | | | |
|----------------|---|--|
| • Profit Tax | 24% | over profit (17.5% to regional budget, but up to 4% reduction is possible) |
| • Income Tax | 13% | over personal income |
| • Social Taxes | 26% (max) | over pay-roll (medical, social, pension) |
| • VAT | 18% | over turnover |
| • Property tax | 2,2% (max) | over property |
| • 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

- Representative office – (vaste inrichting);
- Limited liability company (OOO) – “BV”;
- Closed Joint Stock Company (ZAO) – “BV”;
- Open Joint Stock Company (OAO) – “NV”

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