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Russia Business Outlook 2013-16

Any slowdown in Russia hurts European results



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Executive summary

- In terms of better business results Russia continues to pull further away from from CEE, European and global markets
- This puts local managers under more scrutiny from global and European headquarters
- But it also allows some scope for pushback in budget negotiations: European headquarters are now wary of imposing too aggressive targets on Russia in case anything goes wrong
- As Russian sales get bigger, more managers will report to European or global headquarters and less so into a CEE cluster
- The Russian market is highly profitable for most companies
- Brands are holding up well but companies have to work harder to maintain and grow them
- The "normalisation" of business demands on managers continues and more emphasis is now being placed on receivables and cash management
- More executives are worried about the consequences for their companies in Europe and globally if the Russian business slumps in the future
- In the CEE region (and Europe) for many companies "staying above zero in sales" is a challenge; this is not the case in Russia
- Russia is the biggest market in Europe for reporting corporate double-digit sales growth
- Some companies report a single-digit sales outlook for 2013, but predominantly high-single digits
- The Russian economy is slowing but not as badly as other markets
- Russian exports were finally contaminated by global trends and were negative in 4 of the last 6 months
- In the medium and long-term shale gas could be a threat to the Russian economy
- The rate of inflation slowed in October/November and year-end inflation looks set to finish below 7%
- Unemployment has stabilised at a low rate (5.3%) and many towns report labour shortages
- The rouble outlook is stable with moderate risks on both the up and down sides
- The 2012 harvest disappointed at about 71mn t, down on the bumper crop of 2011
- The proportion of companies reviewing their route to market has exploded upwards
- Companies are re-allocating CEE staff to international and Russian projects as work slows done in CEE offices
- Some companies are asking their staff to transfer to Moscow just when more senior Russian managers want to work in the West
- Ukraine experienced a very poor third-quarter economically and more western companies report deteriorating business
- The drop in estimates for GDP growth in Ukraine for this year has been very sharp and 2013 will continue to be challenging
- Executives are satisfied with business in Kazakhstan while Azerbaijan is a small but fast-growth market

Companies are running out of good markets: Russia is something like "last man standing"

> "If the Russian market slows down sharply for whatever reason, then quite honestly I don't know what I (and other CEE mangers) will do. It's the market that's keeping the rest afloat. If it drops we are in deep trouble".

The Russian market for some companies is softening a little bit but there is thankfully enough growth (for now) to compensate for some (but not all) of the downturns in other markets across the CEE region. CIS markets are generally good but Ukraine is slowing sharply and Belarus remains mixed.

> But it is brutally clear that for some 75% of companies operating in the CEE region most markets have softened further in the last 9-15 months and some winning markets in the region have also wobbled (Poland, Turkey, Ukraine). Russia was the best market in the region and has proven the most resilient in the last year.

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Executives are fast running out of good markets in the CEE region and globally; they are like generals who are depleting a strategic reserve. In the CEE region the core CEE markets and South-east Europe are depressed in sales and profit and for most companies sales at best are growing 1-3%; for many growth is flat and in some sectors such as B2B, where financing is in short supply, 30-40% of firms are reporting negative sale growth in 2012 and predict more of the same for 2013 in core CEE.

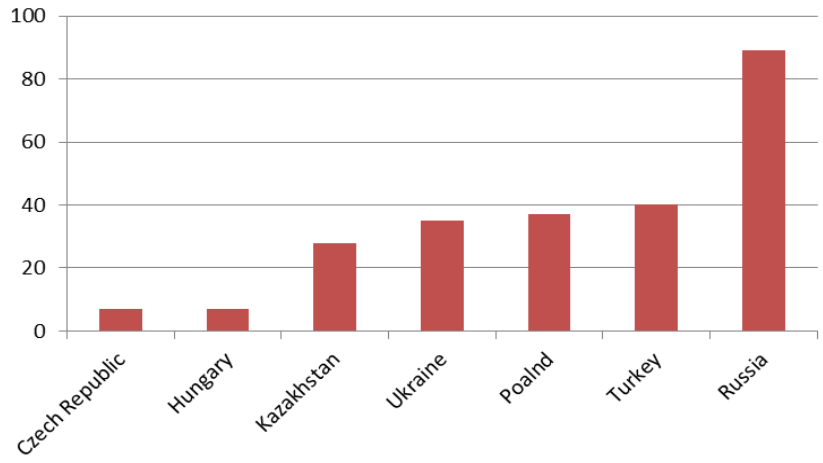
We have long maintained that the Top-3 markets in the CEE region are Russia, Turkey and Poland and this remains valid. But Turkey has seen GDP growth tumble from almost 9% in 2011 to probably less than 3% this year and Poland reported a bleak third quarter economically and the final months of 2012 are unlikely to see an improvement. When you combine this with the disappointing results coming out of Ukraine, another priority market, then you understand the increasing dependence on the Russian market.

If the Russian market were to sink appreciably, then it would have a deeply negative impact on regional corporate results and even global ones given that Russia has out-performed most BRIC markets this year as well with India and Brazil slumping sharply and China in the process of a managed slowdown.

Russia is pulling away from other CEE and global markets:

What is your priority market in the next 3 years?

(executives have 3 choices hence more than 100%)



Recently the global CEO of one of the world's largest industrial conglomerates told me during a presentation in Germany that:

> "Our business in the USA is growing at 1-3% and in the Eurozone sales are down 2% while CEE sales are up 2%. Our sales growth in Russia is very, very, very good and we will be posting new contracts over $75mn in that market in the last weeks of 2012".

When I mentioned this comment to the regional CEE Managing director of a major European FMCG company, the executive echoed those remarks when he said: "I too can say that our business is very good, three times over!"

The global CFO of one of the largest machinery companies in the USA said two months ago:

> "Our sales in the USA are up 2%, in the Eurozone were down -3% while in most of the CEE region we are growing at +2.5% and in Russia growth has fallen from +35% to +18%"

Russia is increasing in importance.

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In terms of growth performance across sectors in the CEE region, Russia ranks as follows:

	2012	2013
All sectors	1	1
Consumer products	2	1
Food & beverages	2	1
B2B	1	1
IT	2	3
Pharmaceuticals/health	1	2

Source: CEEMEA Business Group, Business Benchmarking Survey, June 201

Russia is still the double-digit sales growth market as we can see from the figures in the table below. However, about 37% of companies are expecting single-digit sales in 2013 and these are often in the consumer products and pharmaceutical sectors. But a key point is that single-digits in Russia often mean high single digits and usually on large volumes unlike in the rest of the CEE region.

Predicted percentage sales growth in 2013 by market

(all sectors combined)

	Flat/negative	Low single digits	High single digits	Double digits
Russia	6	12	27	53
Turkey	3	15	41	40
Poland	22	18	30	9
Kazakhstan	6	16	24	52
Ukraine	16	27	29	28
Belarus	20	22	34	25
Czech Republic	27	52	16	4
Romania	18	46	20	14
Hungary	38	50	13	0
Slovakia	30	48	14	9

1) We think that the figures for Ukraine are optimistic s because our survey was taken in early October just before bleak economic data came in. In recent interviews, the large majority of companies are worried about the business outlook in Ukraine in 2013.
2) Poland is becoming a single-digit growth market for almost everyone and the numbers presented here could come under more pressure given the second half economic and business results in Poland in 2012

To repeat, in sectors where some/many companies are now reporting single-digit sales growth, then in Russia this is invariably at the higher end of the scale at 7-9% and often on large volumes with reasonable or excellent profit levels. In many core CEE markets single-digit sales growth usually means 1-3%.

Sales comparisons by business sector in 2013

	USA	Eurozone	China/India	CEE	Russia
Consumer products	1-3%	-3% to +2%	8-10%	1-4%	7-15%
Food & beverages	1-2%	-4% to +2%	6-10%	0-3%	6-16%
B2B	0-3%	-4% to zero	10-14%	-2% to +3%	13-25%
Pharma/health	1-4%	zero to +2%	10-12%	1-6%	8-15%
IT	3-4%	zero to +3%	12-20%	6-12%	12-28%

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How big is Russian business?

Some 4-5 years ago when most CEE markets were booming, Russia often represented about 25% of regional CEE sales for the average manufacturing company and Poland for about 20-22%. But since then as Russia has survived or done well while other markets have tumbled badly, then the portion of total CEE sales taking place in Russia has risen to 35-40% for the large majority of companies. For the big players with sales over $1-2bn in Russia, the market now accounts for 45-55% of regional sales. For some service companies and some executive search firms, Russia is reasonable for 65-70% of business activity.

One remarkable figure shows just how important the market is: in 2013 some 75% of companies are planning to expand their head-count in Russia; the number for the Czech Republic is 6%

With Russia now accounting for a larger portion of CEE and overall European business the consequence is:

> If your Russian business sneezes, then your European business catches a cold

This of course means that more pressures are being exerted on MDs managing Russia and the CIS. As one experienced MD of a large consumer company commented last month in Moscow:

> "We are a multi-billion dollar business in Russia and growing at 14% top line for heaven's sake. But our global HQ is pushing for 20-28%. This is not feasible and frankly insane.

But there is plus side to this additional pressure and exposure of running a bigger and more strategic market as one experienced MD of a European consumer products company revealed to me in Moscow last week:

> It's not so bad being so important. Yes, there is pressure but now European management is also frightened of demanding a crazy, unrealisable budget target. If Russia misses budget, I am in trouble but so is the CEE MD and the European VP. We all have a common interest in making sure targets are sensible.

This is a very good point. Several years ago when the Moscow-based MD produced a budget, he/she alone was in trouble; now all European managers want to make sure that Russia meets budget and is not stretched too far. The responsibility is now shared.

The size also impacts on reporting structures. We have long commented that Russia will increasingly report directly to global headquarters and this is happening, but slowly. One MD of a US B2B company commented last week in Moscow over breakfast:

> When I took on the role of VP for Russia, one of my conditions for taking the position was that I would report directly to global headquarters and not some European or CEE cluster. This market for my company needs strategic focus and I need to have contact with the US HQ directly and quickly. I also insist that top management visit the country at the very least once per annum and other senior managers are regular visitors

What one food/FMCG company is thinking

Remarks by the CEE regional Managing Director of one European food/FMCG company reflect what we have said in this and earlier papers. This MD reports very strong sales in Russia given that they only entered the market 5 years ago and are relatively small. The executive commented just last week that:

> We are growing top line sales in 2012 at 32% but as we gain in size and the market has become more competitive, I am planning for sales growth of 15-22% per annum over the next 2-3 years.

To put this in context this company's sales in 2012 are: +1% globally, +7% in Asia, + 3.8% in CEE, minus 2% in Europe, and as we noted +32% in Russia.

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He noted that, "We entered the market just before the 2009 crash but since then the recovery has been quick and the sales and profit results have been excellent". His company is also one of a multitude reporting solid profit levels. The manager remarked that, "All our categories are performing well or even better but I am especially pleased that our premium brands are holding up strongly. This generates more brand awareness and of course boosts our profits".

This manager understands why his sales will fall (market size, competition, more demanding consumers) and he is therefore looking at other "growth opportunities" but when he and I conversed, we agreed that the number of markets offering such opportunities is diminishing. He has decided to look for expansion in Ukraine which is comprehensible but could be challenging in the short-term as consumption will be under downward pressure in this market for the next 12-18 months. This company is "getting nothing out of Belarus" while Azerbaijan is "nice to have" but small in volume. This executive repeated that Russia is and will be the star market but that he also has a lot of faith in Turkey where the desserts market is growing well despite the focus on indigenous products such as baklava.

The executive made two clear points:

> Trying to get sales growth out of the core CE markets is very hard work. "We are growing at 1-3% in those markets. But it is a struggle to keep it at zero"
>
> The thing that keeps me awake at night is: what happens if Russia starts to slow down badly? (As we note above, very many companies would see their CEE regional strategy implode with negative consequences for pan-European business results).

The B2B sector is still good despite some recent economic trends

If there is a weaker sector in Russia for western and local companies, then it is the B2B sector which has been affected by slower industrial and investment trends and also by the recent slowdown in exports and weaker reported Russian corporate profits. But it is still holding up.

Regarding potential threats, one Russia/CIS manager of European B2B company warned:

> We must be careful that we do not repeat what we've done across Europe and CEE: in those markets business is brutal and we have all tried to cut prices and margins to hold on to at least some business. We are not in this situation in Russia, but I am fearful that if there is a downturn in Russia our sector would repeat those mistakes.

We have often noted that many B2B companies saw their sales growth fall from an annual average of 33% in 2010 and 2011 to lower figures of 14-18%. But there is still a minority of companies in this sector with sales increasing 20-35% and much depends on the scale of existing business, market share and which sub-sectors one is delivering to: automotive, aerospace, etc.

The sectoral average numbers were echoed by one senior country manager of a major western industrial conglomerate who reported last week that:

> In 2011 our sales grew by 42% but these numbers benefitted from one very large project: when we take that out our sales were rising just over 30%. This year we are growing the business at very nice double digits and our budget for the next 3-4 years is to grow at about 18-22%.

Given this company's positive exposure to many business/industrial sectors, these budget numbers look feasible.

As we noted in one of our earlier reports: Russia is still a market where some companies can double the business in 5 years i.e. by growing at about +20% per annum for 5 years. But we stress that this no longer applies to everyone: there are many companies in pharmaceuticals, consumer products and B2B who, given the scale of their business, are growing at 8-15%. But for companies still relatively small or looking to expand

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and invest in the market this rather old cliché of "doubling the business in 5 years" is not baloney. Achieving such a target is possible in very few countries of the world and Russia is one of them.

Russia is one of the markets where construction ,new facilities, distribution centres, and warehousing are strong. Manufacturing firms and their partners in project management support this view especially when other markets are seeing shrinkage and downsizing in this activity. But we also know that construction costs and projects are expensive in Russia: the cliché is that such construction is 40-50% more expensive than in Sweden (!). One very experienced manager setting up major facilities in Russia well east of Moscow reported that: "We have been able to keep project costs at 20% higher than in the west and we think that is a good rate. We have good western project facilitators and management companies but obtaining good "linked-up" construction/logistics facilities is still a challenge in this market.

Yes, Russians want VALUE as well as premium-brand

We have commented before that since the 2009 crash even strong, quality conscious, and resilient Russian consumers want value when they are buying your brands. Downtrading did take place in Russia but not as deeply as in other CEE and global markets and consumers have traded back up relatively strongly. But the regional Managing Director of another European FMCG company remarked last week in Vienna that:

> Our brands are doing very well across the region and we are proud of that. But we are well aware of the need for affordable innovation and products when incomes are strained across Europe. But our quality brands are holding up and especially in Russia which we understand. However, to sell these brands we have to be much more skillful with our sales and marketing strategies and explain in detail what the value is and why consumers should spend more for our branded products.

This is a view we have long held that: to sell brands, your local sales and marketing team are more challenged than they were 4-5 years ago in the pre-crisis days when Russian consumers were less discerning and less demanding. In addition, when companies turn to offering affordable innovation and products to consumers, once again sales and marketing teams have to "think outside the box" and utilise different campaigns and approaches to consumers from the marketing strategies for high-quality and high priced brands.

In summary: sales and marketing teams everywhere and especially in Russia are being challenged more to
1) sell and explain branded products and
2) introduce and explain affordable products without undermining the brand

Competition is just increasing

To summarise the comments of several regional managers from different sectors who have spoken with me in recent days, competition is rising from many sources at the same time:

1) Western companies are desperate for growth and are re-investing in Russia and focusing on the market. West-West competition is getting tougher from the "regular" competitors.
2) New western companies are arriving in Russia looking for that "growth magic".
3) Some SME type companies are also arriving on the scene and some of these are owned by private equity.
4) New competitors from the Middle East, CEE and also Brazil and Turkey are cropping up more.
5) Chinese competitors are getting stronger across the whole CEE region and in Russia. Several B2B companies now note that Chinese companies are entering the Russian market and they are competing across all business sectors not just in cheap consumer products. Companies such as Siemens and ABB are having to respond to cheaper, "good-enough-to-have Chinese products" with affordable and innovatory products of their own: this applies to piping, turbines and medical equipment for example.
6) But we also want to underscore the rise of local champions. This is at the forefront of competitive concerns of many regional and country managers. Over time such companies are regrouping, getting smarter and expanding.

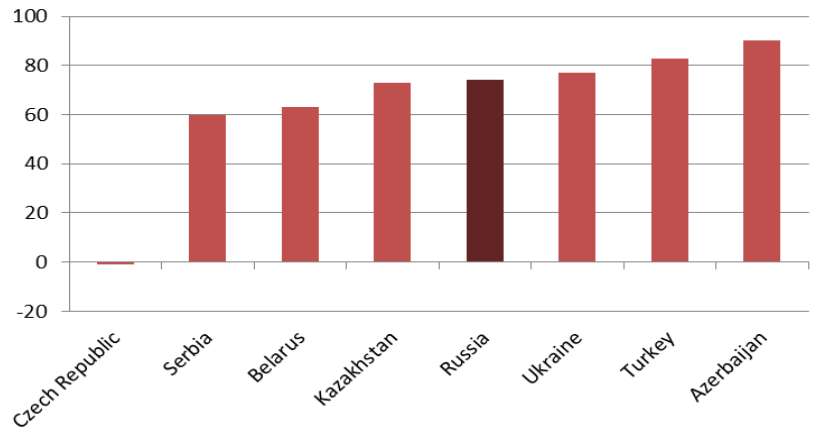
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How Russia compares in the operating environment

Route to market

We have noted in several earlier papers that upgrading the route to market in the broadest sense (distributors/warehousing/logistics/point of sale etc.) is a high priority for a growing numbers of companies in consumer products, pharmaceuticals and IT as well as B2B. Business in several big markets is relatively good (Russia, Kazakhstan, Ukraine, and Turkey), many of which have a large geographical size as well. Companies are asking: do we have the right distribution system for our fast-growing market, do we have too many or too few distributors, should we do more or less ourselves, should we have split distribution with the Russian partner managing logistics etc. while we do more of the consumer interaction and branding? And many other related questions.

The proportion of companies reviewing their route to market



Normalisation of business has created new demands. Recently Moscow-based managers have commented that they are being asked to improve:

- Top-line
- Bottom line
- And market share

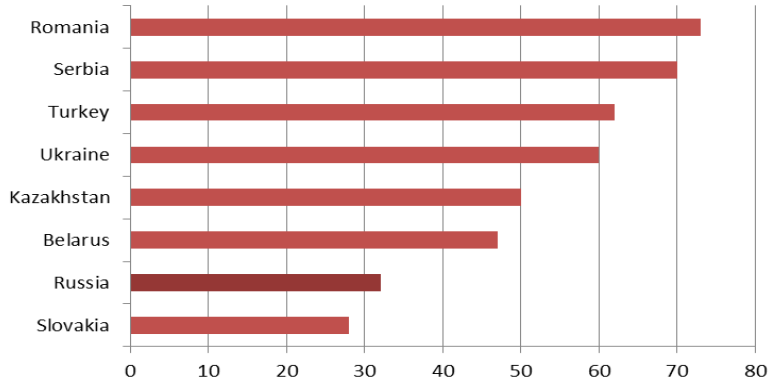
And this has entailed relatively less emphasis on top-line sales growth as “you can’t do everything at once”. As global business has weakened further this year, more emphasis is placed on:

- Tight cash management and days outstanding

As markets around Russia become more strained, regional and global CFOs want cash in the bank and increasingly well managed receivables, especially when cash management is getting harder in a growing number of markets.

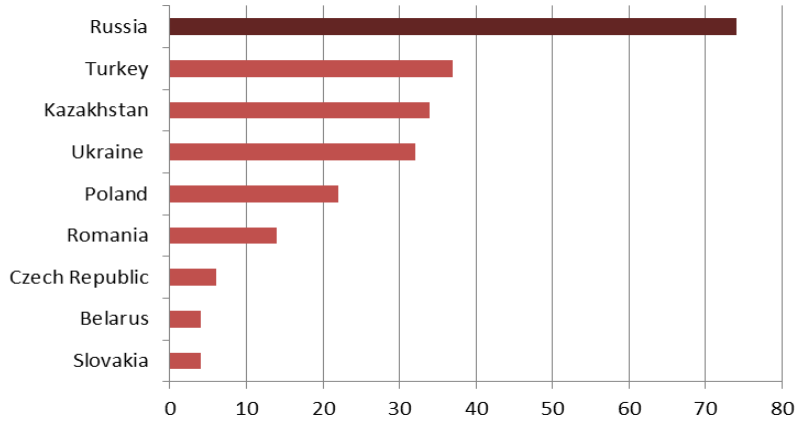
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Are you experiencing worsening issues with receivables (not necessarily bad debt)?

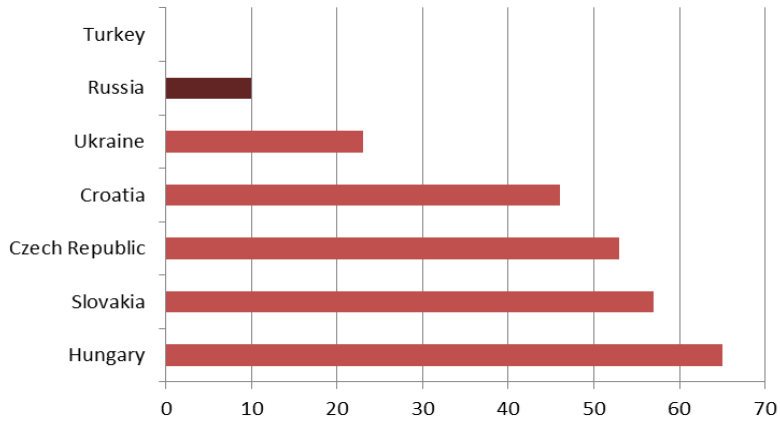


Latest trends in human resources and talent management

In 2013 where do you plan to hire new staff?



In 2013 where do you plan to cut staff?



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Trends and recent comments from executives related to HR

- Money motivates younger, junior people more than it does senior, experienced managers.
- But the money factor does still play a very significant part in recruiting and retaining strong talent.
- How much money? One owner of several enterprises and businesses said of salaries in core CEE: "The markets are down and companies are struggling. We are communicating to staff in core CEE that salaries cannot keep rising at 3-4% and they have to be flat or negative even". Of course this is a sharp contrast with Russia where salaries are rising on average by inflation +/plus 1-5% or even inflation plus/+ 1-10%. These are averages while the top performing managers salaries can rise 20%+ according to one senior HR director.
- Western companies should appreciate that currently Russian salaries are rising in nominal terms across the economy at 14-16% (which is inflation plus 8-9%). This is for blue and regular white collar workers in Russian companies and in government posts. So Russian staff will be benchmarking what they receive from you to this nominal rise across the economy.
- There is an open debate as to what extent a "glass ceiling' exits preventing Russia mangers rising to the top in Russia and abroad: in Poland 90% of MDs are locals (or non-western) whereas in Russia the number is well below 50%. Some Russians argue that their own nationals are often not yet "sophisticated and diplomatically trained" enough for the highest level of western corporate politics and western insiders do better.
- Related to this point, the country manager of one major US B2B company remarked to me a few weeks ago: "Because the business is so important, we are bringing in senior expatriates to manage several aspects of the business. This leap-frogging over our local Russian staff is causing disgruntlement and I can understand why. I am advising European headquarters to rethink some of these transfers or at least to assure our Russian staff that promotion opportunities will be available for them in the near future".
- Staff does want better work/life balance and this applies especially to young top talent.
- With business stagnating in several CEE and SEE markets, more companies are telling their staff that there is no future with domestic business and that they have to turn to international or Russian projects to avoid lay-offs. They are being told that this work can take place in Bucharest or Zagreb or that they will have to transfer to Moscow.
- A counter trend is that more senior Russian staff are now asking to work abroad on their Russian projects. The very experienced regional director of one executive search company said:

  > As we interview top Russian managers the size of the pay packet and the total package is a key criterion. But we are hearing more Russian interviewees stating that they want to work for western companies in the West. This is becoming very important for some of them and they are even willing to take a real cut in remuneration if their location is in the West.

- Refusals: a small number of companies have pointed out that Russian staff are now turning down the western company's offer at the very end of the interviewing process when a final offer has been made. In some case this is after 5 heavy-weight interviews with senior western staff and even with interviews taking place at headquarters
- As one HR executive commented: "Often the candidate is interviewing you and keeping you on a back burner even for a very senior and highly-paid position. The candidate then waits until the end to judge the outcome and may have 2-3 offers in his/her pocket already".
- These points are accurate but at the same time some companies note that retention is currently a little easier as some staff are concerned about future risks in the economy and are impacted by negative global sentiment which keeps them in their posts. One senior manager of a major B2B company said that "We are seeing that our staff are more cautious about jumping ship at the moment".
- This executive went on to make an excellent point about the generations of staff: "We think that the cream of our staff are often aged about 35-45 years because they have remnants of the strong Soviet educational system, they have seen tough times as well as good ones, they have experience and they know us and their jobs. We think these people are "gold dust" and you have to do everything you can to hold on to them".

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- How long does it take to hire someone? Providing the Russian candidate does not turn you down (!), executive search companies are reporting that the process from first interview to the hiring decision is stretching out to 3-4 months. The regional MD of one executive search firm explained this: "Western companies are looking at the Russian market in a more serious manner and HR positions are now taking on increasing importance. Internal processes are more rigorous and often more senior western managers are being brought into the selection/decision procedures".
- A few companies report that they are losing staff to the new, rising Chinese companies. These companies behave a bit like the big, Russian, "oligarch" companies and offer staff 40-60-80% more in salary terms and this distorts the HR market of course.
- On the salary front, western headquarters often still "don't get it". Several country and regional managers have approached me in recent weeks complaining that they are engaged in arduous and difficult internal debates about Russian salary increases. It is easy to understand that companies globally are managing costs tightly in challenged markets and want to do the same in Russia. But I sympathise with local managers who have to go through this arduous and indeed time-wasting process. IF HQ is happy with the results from Russia, then it has to pay for it. The Russian market is hot, business is pretty hot and salaries are commensurate. You can't get something for nothing. Russia is 'exceptional" in its salary criterion.

Economic summary

The general dynamics of our October-November reports remain the same:

> The Russian economy is slowing down to some degree and a few sub-sectors are weakening. But in comparison with other European and global economies, the economic and business results are still either good or very good

Macro-economic data 2009-16

	2009	2010	2011	2012	2013	2014	2015	2016
GDP	-7,9	4,3	4,3	3,7	3.8	4,1	4,4	4,8
Retail sales	-5,5	6,3	7,2	5,8	5,5	4,8	4,9	4,8
Real wages	-2,8	4,4	4,9	7,4	4,5	4,3	4,4	5,0
Disposable income	1,0	3,7	2,8	3,4	3,6	3,9	4,2	4,0
Inflation (year-end)	8,8	8,7	6.1	6,7	5,6	5,4	5,0	5,0
Unemployment rates	7,9	7,6	6,5	5,6	6,1	5,6	5,6	5,3
Gross fixed investment	-17,9	5,6	6,8	6,0	6,6	6,8	7,1	7,3
Industrial output	-10,8	8,3	4.7	3,9	4.7	5,4	5,7	6,2
FX reserves ($bn)	447	485	490	510	545	575	600	620
Rouble/$ (year-end)	30,3	30,4	32,1	31,3	31,2	30,9	30,6	30,0
Rouble/Euro (year-end)	43,4	40,0	41,5	40,8	40,0	39,3	38,4	38,0
Budget balance (% of GDP)	-6,3	-3,5	-0,2	-1,0	-0,3	-0,5	0,0	0,2
Current-account balance (% of GDP)	3,8	4,9	4,9	4,0	2,9	2,8	2,5	2,5

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Consumer-related statistics: by year and monthly

	2009	2010	2011				2012*									
	year	year	Q1	Q2	Q3	Q4	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct
Disposable income	1.0	3.7	-3.0	-2.8	1.3	2.3	2.0	3.1	2.6	2.1	3.6	4.6	2.2	7.2	3.8	n/a
Real wages	-2.8	4.2	0.6	3.3	4.3	4.4	9.1	13.3	9.0	10.4	12.4	12.9	8.1	7.3	4.0	5.2
Real retail sales	-5.5	4.4	5.1	5.7	7.5	9.0	6.8	7.7	7.3	6.4	6.8	6.9	5.4	4.3	4.4	3.8
Unemployment	8.3	7.6	7.4	6.5	6.2	6.3	6.6	6.5	6.5	5.8	5.4	5.4	5.4	5.2	5.2	5.3
Industrial output	-10.8	7.3	5.9	5.1	5.1	3.4	3.8	6.5	2.2	1.3	3.7	1.9	3.4	2.1	2.0	1.8
Fixed investment	-17.9	5.6	-3.2	4.7	7.6	8.4	15.6	15.1	4.9	7.8	7.7	4.7	3.8	2.3	-1.3	4.9
Consumer prices	8.8	8.7	9.5	9.5	8.1	6.6	4.2	3.7	3.7	3.6	3.6	4.3	5.6	5.9	6.6	6.5
Budget deficit (running)	-5.9	-4.0	-3.4	-2.2	-0.9	0.4	0.5	0.3	0.2	0.3	0.1	-0.1	0.0	0.3	-0.1	-0.5
Notes: * month compared with same month of previous year																

If the oil price stays between $95 and $103 per barrel (which is the consensus opinion and close to the the Russian government's budget target), then Russian GDP growth will fluctuate between around 3.7% and 4.2% for the next 3 years and growth in retail sales, disposable income and real wages will all fluctuate between 4-6% or even up to 7%; industrial and investment growth will trend at about 3-4% and 6-7% respectively and we presume the budget will go into a small deficit as the government continues with some social and infrastructure spending.

> With those provisos the message is steady as she goes: nothing too exciting but hugely better than 120 other economies in the world

The global slowdown has impacted the Russian economy and we estimate that GDP this year will finish at about 3.7%. The downward estimates for Russia GDP growth this year have been much smaller than those for other markets.

Russia has been less hurt by a drop in exports compared with other countries which have seen export growth collapse to almost zero or low single digits. But it looks like Russian export growth will fall to +5% this year and be only 3-5% next year. Russian exports were contaminated by global trends during the summer when year-on-year exports were actually negative for three months and then turned upwards again in autumn (this followed the trend with Chinese exports). Energy prices have held up and the reason that Russian exports are decelerating is that the Eurozone is taking less volume of energy from Russia even though the oil price is stuck at about $108.

Rising inflation and less government spending/subsidies means that real wage growth is slowing along with retail sales: in October retail sales were at a two-year low of 3.8% year-on-year growth and real wages grew by only 5.2%. This was expected and we have flagged this outcome constantly throughout 2012. But the numbers remain relatively good.

Industry, manufacturing and investment all slowed through the summer-autumn period this year due to global trends, weakening exports and also weaker profits in Russian corporates (which could have been impacted by high nominal wage growth of 14-15% or due to some mis-reporting). Investment growth popped up again in October to 4.9% after a fall in September but we need to see if this was due to inventory restocking.

> The bottom line: B2B companies could face some downward pressure in the next year compared with other sectors but ought to be able to maintain double digit sales growth based on these economic numbers.

As in Ukraine, poor agricultural results in the late autumn brought down the harvest figures: 2010 was a disastrous drought year and 2011 was a bumper crop of 94mn t but 2012 has shrunk to a weak 71mn t and thus the agricultural sector is down by 20-25% this year but we reiterate that 2011 was a bumper year for comparison purposes.

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Russia is distinguished as being one of about 5-10 markets globally where new credit is rising in double digits (along with China, India, Brazil, Turkey, and almost in Poland). Here again though we are likely to see a slowdown in the coming months: consumer credit rose in 2012 by 28-35% and corporate credit increased by 17-23%. We estimate that this growth will slow to about 20% and 15% respectively in 2013.

Russia like several other markets (including Ukraine) is looking like a twin-track economy with better results in consumer spending, income and retail sales and wages whereas industrial production, exports and investments are slowing more sharply.

Inflation has stabilized after jumping up from the 20-year low points of this spring (3.6% in May) and climbed to 6.6% in September but stabilised at 6.5% in November. It now appears certain that year-end inflation will remain below 7% and we expect a 2012 average inflation rate of about 5%.

As inflation ticks up, real wages growth is slowing from bumper high levels of 12% this summer to a still good 5.2% in October. The consumer figures likely foretell a softening in this sector and a lot now depends on the Christmas season.

The rouble looks fairly stable as long as the oil price remains within our confines of $95-103 per barrel and the Euro/dollar trading range remains in a band between1.26 and 1.33. We will need to monitor what impact shale gas will have on energy prices in the mid-term. Liquidity has been kept tight for some 15 months now since the rouble tumble of October 2011; if and when the central Bank loosens liquidity perhaps starting in 2013, then that could hurt the rouble a bit. Interest rates will probably come down in the first quarter of next year but this will not have a large impact on the rouble. Global factors will be more important and the Russian Central Bank has consistently warned that it would use the rouble as a buffer in any deteriorating global environment so there are some downside risks. But if the global economy continues to bumble along at current sub-par levels, we see the rouble staying in a range of 30.5 and 31.8 to the US dollar and 39-41 to the Euro for the next 15 months with occasional spikes of volatility. The rouble currency basket will also stay close to its current levels of 35.0 to 36.5 given the above provisos.

The numbers and comments in this section lead us to conclude that:

> We do not anticipate any big bounce back in GDP growth in 2013-14 (unless there is an upward spike in oil prices), rather “just” steady stabilisation at about 3.6 to 4.0% range.

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