<u>Viktoria Seelich</u>

Market Analysis on the Russian Market:

From the Perspective of a German Company Producing Acrylic Glass or Polycarbonate and Consider to Enter the Russian E-Commerce Marketplace

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For my

friend Gagan Deep Singh

and my daughter Lilija

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List of Abbreviations

ASEAN	The Association of Southeast Asian Nations
AFTA	The African Free Trade Area
BCG	Boston Consulting Group
BRIC	Brazil, Russia, India and China
B2B	Business to Business
B2C	Business-to-Customer
CAGE	Culture, Administration, Geography and Economy
CIS	Commonwealth of Independent States
EDI	Electronic Data Interchange
EMS	Express Mail Service
EU	European Union
EZT	Elektronischer Zolltarif
FDI	Foreign Direct Investment
FLE	Foreign Legal Entity
FOM	Фонд Общественное Мнение = Fund of Public Opinion
GDP	Gross Domestic Product
GLOBE	Global Leadership and Organizational Effectiveness Research Program
HQS	Highly Qualified Specialist
HRM	Human Resource Management
IDV	Individualism versus Collectivism
IMF	The International Monetary Fund
IVR	Indulgence versus Restraint
JSC	Joint Stock Companies
JV	Joint Ventures
LLC	Limited Liability Company
Ltd.	Limited
LTO	Long Term Orientation

M&A	Mergers and Acquisitions
MADB	Market Access Database
MAS	Masculinity
MERCOSUR	The Southern Common Market
MNC	Multinational Companies
NAFTA	The North American Free Trade Agreement
OAO	Open Joint-Stock Company
OECD	Organization for Economic Co-operation and Development
OSEC	Office Suisse d` Expansion Commerciale
PDI	Power Distance Index
PESTEL	Political, Economical, Social, Technological, Environmental and Legal
PET	Polyethylene Terephthalate
PETG	Polyethylene Terephthalate Glycol
PMMA	Polymethyl-Methacrylate
PVC	Polyvinyl Chloride
RO	Representative Office
SEO	Search Engine Optimization
SMS	Short Message Service
SWOT	Strengths, Weaknesses, Opportunities and Threats
UAI	Uncertainty Avoidance Index
VAT	Value Added Tax
WTO	World Trade Organization
WOS	Whole Owned Subsidiary

1 Introduction

In the globalized world, various national and international institutions strive for and follow the trend towards a greater economic, cultural, political and technological interdependence. This denationalization has resulted in increased free flow of goods, services, money, people and ideas across the national borders.[1] Recently more and more companies are using the benefits of available possibilities to undertake a foreign direct investment (FDI). It has been observed that the inward FDI flow worldwide has increased from US$207,455 million per year in 1990 to about US$1,243,771 million per year in 2010.[2]

The main reasons behind the companies undertaking FDI are to capture new markets, to benefit from low costs of labour, to avoid import restrictions, to generate advantages in costs of transportation, to promote investment from the host countries and to be independent from the insecure variations of exchange rates.[3] With FDI, the organizations aim to increase the volume of business and market share, thereby hedging against the risk of possible clustering of economic activities and from facing market saturation or threats of competition in the short-run or rather in the middle-term and thus to be able to persist in the market as a profitable undertaking.[4]

The aforesaid reasons are enough to ascertain why it is recommendable for a company to have a look for investment beyond the borders. Nowadays it is possible to select between a wide range of countries irrespective of the fact that they are completely different and far away from the host country of business.

"The emerging markets are an increasingly important source of growth as they offer a growing number of accessible consumers to investors. This rebalancing offers more investment opportunities and favors large emerging economies."[5] One of these emerging economies is Russia.

From 1993 onwards the investment appeal of Russia has grown steadily reaching its highest level of 75,002 million US Dollar in 2008. During the world crisis it lost half of the FDI (inward) flow but stabilized in 2010 by attracting nearly the same FDI val-

[1] Wild et al. (2010), page 34.
[2] UNCTAD [08.03.2012], (a).
[3] Schierenbeck (2003), page 42.
[4] Bächthold (2007), page 59.
[5] "Growing opportunities Russia FDI Report 2011", page 3.

ue as that of pre-crisis time.[6] This signifies a positive outlook for FDI in Russia but there is lack of information on the various business opportunities. From this background, the present thesis work will focus on the Russian Federation.

The thesis “Market Analysis on the Russian Market: From the Perspective of a German Company Producing Acrylic Glass or Polycarbonate and Consider to Enter the Russian E-Commerce Marketplace” screens and evaluates the Russian market for a German company which produces acrylic glass (polymethyl-methacrylate, PMMA) or polycarbonate and contemplate to enter the Russian e-commerce marketplace. Moreover it brings an understanding of modern Russia to the highest level so as to maximize the potential of such a company there.

At the moment there are no surveys which are openly published or are available free of cost in the sphere of e-commerce concerning acrylic glass and polycarbonate in Russia. Even there is no official and relevant data, neither in German nor in Russian language, focusing the Russian market for doing business in the field of the particular plastic materials. The regions of interest for such plastic materials are also not known within the Russian Federation. Furthermore, there are no surveys about the market competition and potential customers for the mentioned products.

The main task of this thesis is to make a market attractiveness study involving the analysis of conditions for a foreign investment. To accomplish the same, analytical tools like the PESTEL (Political, Economical, Social, Technological, Ecological and Legal) analysis, CAGE (Cultural, Administrative, Geographical and Economical) framework, Porter’s Five Forces Analysis and the Online Marketplace analysis will be conducted. These methods will help in matching the needs of a company to a structured and tailored overview about the macro and micro environment of the chosen country.

The market attractiveness study which has its main focus on acrylic glass is divided into four main parts. Chapter 2 starts with a general overview of the Russian macro environment including the examination of political, legal, economical, technological, social, and cultural factors. In chapter 3 the e-commerce market and its future potential is highlighted. Chapter 4 focuses on the microenvironment, whereas chapter 5 deals with the entry modes. Chapter 6 describes the recommendations for a successful market entry and the optimum timing for an entry and the last chapter summarizes the findings of the whole thesis.

Due to the focus on the phase before entering a market, the following contents are outside the scope of this thesis; a deeper examination of tax regulations in the Russian Federation, determination of potential logistics partners and strategy implementation.

[6] UNCTAD [03.03.2012], (b).

2 Macro Environment Analysis

The choice of the right location of business is a fundamental decision governing the success of a company. This decision holds its importance not only in the startup stage of a business but also in the expansion stage. Considering the major impact of location on the business, it is crucial to carry out an accurate analysis of the macro environment.[7] The macro environment is defined as the part of the environment constituted by various agencies and forces which are external to a company and to which a company must respond.[8]

Global movements in culture, society, demography, politics, international law, economics and technology are able to change the conditions both in favor and against the countries, industries and organizations. International enterprises have their business in several national environments. Each of these countries has varied range of environmental influences at the macro, industry and market levels. Since, the national trends will differ from those taking place in the global environment in terms of pace, size and direction and a company has to monitor the macro environmental situation in each country of operation.[9]

A useful framework to structure such an analysis is a combination between two tools. The first tool is the so called PESTEL analysis[10] as it involves the evaluation of background factors which are influencing the competitive environment. A survey even confirmed that the factors analyzed in the PESTEL analysis are significant for decision making while going international. In this survey the global investors determined transport and infrastructure (63%), telecommunications infrastructure (62%) and the transparency of the political, legal and regulatory environments (62%) as the crucial factors.[11] The Second tool is the CAGE[12] distance framework. In this context, the distance between the countries is an important aspect for success or failure of an investment.[13]

The following chapter will analyze the social, cultural, political, legal, economical and technological environment and summarize the findings in a SWOT (Strengths, Weaknesses, Opportunities and Threats) and CAGE framework.

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[7] Thommen and Achleitner (2003), page 93.
[8] Stonehouse et al. (2004), page 142.
[9] Stonehouse et al. (2004), page 144.
[10] Rugman and Collinson (2009), page 387; Lynch (2009), page 82.
[11] "Growing opportunities Russia FDI Report 2011", page 3. *(multiple answers were possible)*
[12] Ghemawat (2001), page 1ff.
[13] Ghemawat (2001), page 1ff.

2.1 Social and Cultural Environment

Lynch (2009) counts changes in lifestyle, shifts in values or culture, attitudes to work and leisure and the demographic changes and distribution of income to the socio-cultural item. He recommends exploring and justifying with evidence three or four well-thought items instead of a lengthy ‘laundry list’ of items.

Consequently, the starting section will highlights demographic changes, distribution of income and cultural issues concerning the business environment.

2.1.1 Country and Demography

Before analyzing the social and cultural conditions in Russia a short and concise overview about Russia’s country profile is being provided.

Russia is a vast country located in North Asia and extends from the Arctic Ocean south to the Black Sea and from the Baltic Sea east to the Pacific Ocean.[14] It spans over nine time zones were by 2010 there were even eleven.[15] With a total area of 17 million sq km it is the world’s largest country and therefore it is almost twice as big as Canada. While being both, the capital and the largest city of Russia (over 11.5 million inhabitants[16]), Moscow is also the political and financial center of the country. St. Petersburg, on the coast of the Baltic Sea, is Russia's main seaport[17] with 4.84 million inhabitants it is the second biggest city of the country. There are ten other cities with a population of over one million people such as Novosibirsk (1.47 mill.), Yekaterinburg (1.35 mill.) and Nizhny Novgorod (1.25 mill.).[18]

From tundra in the North to semi-arid desert in the South and full range of forests and grasslands from West to East, Russia offers a diverse topography. The same applies for the climate. The greater part of the country has a continental climate, but there are also arctic and sub-arctic zones in the North and subtropical areas in the South resulting in a large variation in the climate within the country.[19]

Russia has abundant natural resources, including vast deposits of petroleum, natural gas, coal, and iron ore. Many of these reserves are located far from inhabited areas and Russia's harsh, cold climate makes it difficult to take advantage of many of the country's valuable resources.[20]

After that, continuing the analysis with looking briefly to the Russian society in terms of demography and selected social indicators.

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[14] CIA – The World Factbook, [09.03.2012].
[15] RiaNovosti [09.03.2012], (b).
[16] GKS [03.03.2012], (a).
[17] CIA – The World Factbook [09.03.2012].
[18] GKS [03.03.2012], (a).
[19] “Doing business and investing in the Russian Federation”, page 6.
[20] CIA – The World Factbook [09.03.2012].